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Exporters Beware: U.S. Government Significantly Steps Up Enforcement Efforts

Earlier this year, a Minnesota company was hit with \$800,000 in criminal and civil penalties for omitting certain facts in license applications submitted to the U.S. Department of Commerce's Bureau of Industry and Security (BIS) for the export of seismic testing equipment to India. These penalties were assessed for violations of the Export Administration Regulations (EAR), which impose licensing requirements and other controls on the export of controlled goods, software and technology. Last year, the maximum penalty would have been \$122,000 for the same infractions.

The increased penalties resulted from the enactment of the International Emergency Economic Powers Enhancement Act ("IEEPA Enhancement Act") on October 16, 2007, which raised the maximum civil penalty from \$50,000 per violation to the greater of \$250,000, or twice the amount of the transaction that is the basis of the violation.¹ The law also raised the maximum criminal penalty for violations of U.S. export control laws from \$50,000 to \$1,000,000 and imposed a maximum jail sentence of 20 years.

The U.S. government has signaled that it will pursue a wide range of violations of U.S. export laws with greater vigor than ever before. In addition to bringing more criminal cases for export control violations, the government has indicated that it will start enforcing even relatively minor violations of export laws, such as late or inaccurate filing of export data required by the U.S. Census Bureau. In response to this enforcement crackdown, companies can prevent violations of export control laws and reduce the risk of exposure to the enhanced export penalties by reviewing, updating and improving their export compliance programs.

IEEPA Enhancement Act

The dramatic increase in potential civil and criminal



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penalties under the IEEPA Enhancement Act marks a major change in the enforcement landscape for companies involved in U.S. export transactions. The new IEEPA penalties apply not only to EAR violations detected by BIS, but also to various economic sanctions programs established and enforced by the Office of Foreign Assets Control (OFAC).

When IEEPA was originally passed in 1977, the maximum civil penalty was only \$10,000 per violation. Other than an inflation adjustment raising the maximum penalty amount to \$11,000, the first time that export penalties were increased was in 2005, when the civil penalties were raised to a maximum of \$50,000 per violation.² In the belief that even this amount was insufficient to deter violations of export control laws, BIS and other agencies involved in export enforcement pressed Congress to increase the penalties. The result of this effort was the IEEPA Enhancement Act with its \$250,000 maximum for civil penalties and escalation of criminal penalties. Even after this latest legislation, BIS is still seeking even higher penalties. A bill now pending in Congress, the Export Enforcement Act (S. 2000), would increase the maximum civil penalties for violating export control laws to \$500,000 per violation and increase the criminal penalties on companies violating export laws to the greater of \$5 million or ten times the value of the exports involved.

Exporters should also be aware that IEEPA Enhancement Act civil penalties may be applied retroactively. Under current law, BIS and OFAC have the discretion to apply the increased civil penalties on violations that occurred prior to the October 16, 2007 effective date of the IEEPA Enhancement Act. For example, a company planning to file a voluntary self-disclosure for a violation that occurred prior to that effective date could be subject to the increased penalties.

Stepped-Up Justice Department Export Enforcement

Other departments of the U.S. government, including the U. S. Department of Justice (DOJ), have stepped up enforcement of criminal penalties for violating export control laws. Last year, DOJ and several partner agencies launched the Export Enforcement Initiative. Led by DOJ's National Security Division, the initiative is now training law enforcement officers, federal prosecutors and others to work in task forces to investigate and prosecute illegal exports and technology transfers. As a result of the new initiative, U.S. attorneys are better equipped to prosecute criminal cases involving export controls, which has resulted in more

such cases being brought. For example, according to DOJ statistics in fiscal year 2007 there was more than a 50 percent increase in defendants charged with violating the primary export control laws compared to the previous year.

Recent Cases

While only a small number of cases brought under the enhanced penalty provisions of the IEEPA Enhancement Act have been closed to date, it is clear that BIS and DOJ are moving aggressively to use their new powers, oftentimes pursuing parallel civil and criminal cases involving the same export violations.

For example, BIS assessed increased IEEPA penalties in the amount of \$400,000 against MTS Systems Corporation, the Minnesota company noted above. BIS charged MTS Systems with violating U.S. export law because its application to export seismic testing equipment to India failed to mention that the equipment would be used to test nuclear power plant components. The company also failed to mention in a second export license application that a U.S. restricted party in India provided funding for the sale or the possibility of a nuclear end-use. For each violation, BIS assessed a \$200,000 civil penalty – 80 percent of the maximum under the IEEPA Enhancement Act.

In a companion criminal case, DOJ obtained a sentence of two years probation and a criminal fine of \$400,000 against the same company for the same misrepresentations discussed above in its license applications. The plea agreement also required MTS Systems to implement and maintain a model export compliance program and sponsor an export compliance conference. This case is just one example of DOJ's expanded role in export enforcement.

As part of a similar multi-pronged attack, BIS assessed a civil penalty of \$132,791 against Engineering Dynamics, Inc. for violating export laws. The company was charged with conspiring with its agent in Brazil to sell Iran a U.S.-origin engineering software program for designing offshore oil and gas structures. The civil penalty assessed was equivalent to 53 percent of the maximum penalty under the IEEPA Enhancement Act. Furthermore, OFAC imposed an additional penalty of \$132,791 on Engineering Dynamics for violating OFAC's Iranian Transactions Regulations.

These civil penalties were supplemented with criminal penalties assessed against Engineering Dynamics' corporate owners and officers and the co-conspirator in Brazil for the

same transaction. In the criminal case, DOJ obtained a guilty plea by two owners and officers of the company for one count of conspiracy to violate U.S. export laws by exporting engineering software to Iran through Brazil without proper government authority. Each of these defendants will face a maximum of five years in prison and a \$250,000 fine when they are sentenced in August 2008.³ The Brazilian co-conspirator was recently sentenced to 13 months in prison, while also being ordered to pay \$100,000 in fines and to forfeit more than \$109,000 in profits for his role in the prohibited exports to Iran.

Other Enforcement Initiatives

Another area of stepped up enforcement is the mandatory filing of Electronic Export Information (EEI), previously known as Shipper's Export Declarations (SEDs). The U.S. Census Bureau recently issued a new rule requiring exporters to submit export data electronically on the Automated Export System (AES) prior to exporting goods from the U.S.⁴ The new regulation will go into effect on July 2, 2008 but will not be enforced until September 30, 2008. It imposes criminal penalties for knowingly failing to file EEI or for knowingly submitting false export information, while increasing civil penalties for filing mistakes or late filings. This new regulatory scheme transforms what used to be routine paperwork requirements into a new area for export enforcement.

Previously, the Census Bureau allowed exporters to submit export data either by filing paper SEDs or by transmitting the data electronically. As a result of the new rule, exporters, freight forwarders and carriers may only file such data electronically and must do so within stated time frames prior to exportation. The time frames depend on the mode of transportation used to carry the goods out of the U.S. For example, exporters must file EEI for ocean cargo with the exporting carrier 24 hours prior to loading of the cargo on the vessel at the port of export, while EEI for truck shipments must be filed one hour prior to arrival of the outbound truck at the U.S. border crossing.

Under the new regulation, exporters, forwarding agents and carriers are subject to civil penalties of \$1,100 per day or a maximum of \$10,000 per violation for filing failures or delays. Exporters may also face criminal penalties of up to \$10,000 or up to five years imprisonment (or both) for knowingly submitting false or misleading export information through AES.⁵

The Census Bureau has indicated that BIS and the Department of Homeland Security (DHS) – including Customs and Border Protection (CBP) – will have enforcement authority over export violations under the new rules, such as filing errors made via AES. The escalated penalties and enhanced enforcement authority under the new regulation require a new level of due diligence by exporters, freight forwarders and carriers in submitting export data.

Export Compliance Programs

As U.S. export enforcers intensify their enforcement activities, there is a greater need for companies to increase their compliance efforts. An effective internal compliance program can help prevent companies from committing violations of export control laws and regulations, and can also help to substantially reduce penalties when violations occur. According to BIS's penalty enforcement guidelines, the presence of an effective compliance program is a mitigating factor to which BIS accords "great weight" in determining penalty amounts.

BIS's Office of Export Enforcement has set out nine specific factors that are considered in assessing whether a compliance program is effective, such as the existence of a customized training program for personnel and management, compliance manuals, centralized oversight, and evaluation plans that prompt remedial measures for violations.⁶ BIS will also consider such factors as to whether a party's export compliance program was effective in uncovering a problem (thus suggesting that the program will help prevent further violations), and whether the party has taken steps to correct deficient internal procedures that may have led to the violation.⁷

Conclusion

The U.S. government now has greater discretion and capacity than ever before to enforce U.S. export laws and to apply higher penalties for export control violations. It is clear that companies having effective compliance programs can reduce their exposure to penalties for export control violations. It is increasingly important, therefore, for companies and their management -- working with export compliance experts as appropriate -- to understand the laws that apply to the export of their products and to enhance their export compliance programs.

¹ Pub. L. 96-110, 50 U.S.C. § 1705.

² USA Patriot Improvement and Reauthorization Act of 2005, Pub. L. 109-177, March 9, 2006.

³ DOJ has agreed not to impose the increased IEEPA criminal penalties retroactively.

⁴ See Foreign Trade Regulations: Mandatory Automated Export System Filing for All Shipments Requiring Shipper's Export Declaration Information; Final Rule, 73 Fed. Reg. 31,548 (June 2, 2008).

⁵ 15 CFR § 30.71 (effective July 2, 2008).

⁶ www.bis.doc.gov/complianceand enforcement/pec_program.pdf.

⁷ See 15 CFR Part 766, Supplements 1 and 2.

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