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Disclosure Strategy After BIS Export Control Policy Update

By **Eric Sandberg-Zakian, Blake Hulnick and Lisa Ann Johnson**
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On June 30, Assistant Secretary of Commerce for Export Enforcement Matthew Axelrod issued a memorandum announcing a revised approach to administrative enforcement by the U.S. Department of Commerce Bureau of Industry and Security.[1]

The revised approach, which BIS had foreshadowed by announcing a series of policy reviews over the last several months, could complicate the calculus companies have long employed in deciding whether to disclose past export violations to BIS voluntarily.

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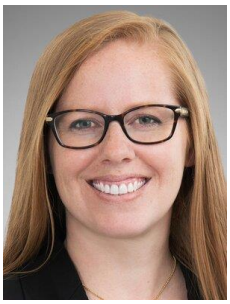
Citing, among other factors, an increasing threat from nation states including China, Russia, Iran and North Korea, Axelrod announced four significant enforcement policy changes that should resolve some administrative violations more quickly, but could significantly increase the cost and legal exposure resulting from others.

Even in cases that are resolved without monetary penalties, BIS may seek compliance commitments, which may be costly to implement and result in prolonged engagement with the agency.



Lisa Ann Johnson

These changes come on the heels of related developments, including a policy change to make public administrative charging letters before cases are resolved, as well as increased emphasis on trade controls enforcement from other agencies, including the U.S. Department of Justice.

Taken together, the changes indicate export controls violations are presenting companies with increasing risks, and should prompt companies to undertake a careful revaluation of how they decide whether to voluntarily disclose past violations as a means of reducing legal exposure.

Policy Changes Announced

The four policy changes announced in the Axelrod memo are intended to focus the Commerce Department's enforcement efforts on cases that "do the most harm to our national security."[2]

First, in making penalty assessments, BIS will place greater emphasis on applying the aggravating factors in the existing BIS enforcement guidance in the Export Administration Regulations.

The Axelrod memo suggests that a more uniform application of the aggravating factors should increase the number of cases treated as egregious, a formal categorization that, under the agency's enforcement guidance, results in substantially higher penalty amounts.[3]

In some cases — especially those involving high-volume, low-dollar transactions — the difference between egregious and nonegregious treatment can mean the difference between relatively small penalties and bet-the-company legal exposure.

Second, BIS is ending its long-standing practice of entering into no-admit, no-deny settlements. In order to benefit from the reduced penalties available through settlement, companies will now be required to admit the underlying factual conduct. The agency asserts that such admissions are helpful learning tools for industry because they help companies understand the facts underlying enforcement cases more clearly and adjust their compliance programs accordingly.

Third, in cases that BIS determines did not result in serious national security harm but are still sufficiently serious to merit more than a warning letter or no-action letter, BIS will offer settlements with compliance commitments instead of monetary penalties. The Axelrod memo explains that these remedial measures will be enforced, at least in some cases, through the imposition of temporary denial orders conditioned on training or other compliance requirements.

Such orders — which are a bit like the export control equivalent of a deferred prosecution agreement — have the potential to result in significant reputational harm if counterparties view the subject of the order as posing compliance risk or misunderstand the effect of the suspended order. While it is difficult to make firm predictions, it seems BIS may intend to pursue these compliance-commitment-only settlements in a subset of the cases previously settled favorably with only warning letters.

Fourth and finally, BIS is creating a dual-track approach to voluntary disclosures, offering resolutions within 60 days of final submission for cases involving only minor or technical infractions, but, for cases involving potentially more serious violations, BIS will now assign both an enforcement agent and an Office of Chief Counsel attorney to investigate the disclosure.[4]

In the most serious cases, the DOJ's National Security Division Counterintelligence and Export Controls Section will assign prosecutors to investigate as well.

As Axelrod noted in his remarks — and as National Security Division guidance makes clear — a voluntary disclosure to BIS does not qualify as a voluntary disclosure to the DOJ, which maintains its own, separate program for voluntary disclosures of trade controls violations that may have been committed willfully — i.e., with knowledge the violation was unlawful, the required mental state for a trade controls crime.[5]

Separate from the four changes announced on June 30, BIS also recently revised the regulations concerning the treatment of charging letters, and now will make public formal charging letters as soon as they are finalized in an effort to better inform the regulated public and deter violations sooner.[6] The agency will continue in most cases to provide respondents with nonpublic draft precharging letters for settlement negotiation purposes, however.

These changes come as other federal agencies increase their focus on export controls enforcement and BIS expands its field operations. For example, Deputy Attorney General Lisa Monaco continued to emphasize the role of U.S. trade controls as a top priority in federal criminal enforcement in a June 16 speech,[7] calling sanctions the new Foreign Corrupt Practices Act and underscoring the leniency available under the National Security Division's voluntary disclosure program.

This builds on the DOJ's March 2 announcement of Task Force KleptoCapture, an interagency law enforcement task force dedicated to enforce the sweeping sanctions, export restrictions and economic countermeasures that the U.S. has imposed against Russia. At the same time, BIS has opened an additional U.S. field office and has increased the number of former prosecutors in its Office of Chief Counsel.[8]

Implications for Voluntary Disclosures

Companies routinely use voluntary disclosures to BIS as a means of reducing possible exposure associated with export controls violations; BIS received about 400 voluntary disclosures in 2021.[9]

Companies disclose a variety of different kinds of violations, ranging from isolated and inadvertent record-keeping and licensing oversights to more serious issues, such as exports to restricted parties on BIS' entity list; exports of more sensitive, dual-use items with military or intelligence significance to tightly controlled markets like China; exports to broadly sanctioned markets such as Russia and Belarus or fully embargoed countries and regions such as Iran, Syria, North Korea, Cuba, and the Crimea, Donetsk, and Luhansk regions of Ukraine; or intentional violations of the export controls rules.

The new BIS guidance may up end existing expectations for how voluntary disclosures will be treated and will present exporters and their advisors with a new strategic landscape to assess.

In the past, BIS has penalized comparatively few cases, especially when voluntarily disclosed. In addition, DOJ prosecutors have become involved in a small fraction of voluntarily disclosed export control cases.

Thus, companies have typically considered voluntary disclosures as a reasonable path to mitigating worst-case scenarios, opting to prioritize thorough internal reviews, compliance remediation and BIS engagement to reduce dramatically the chances of large penalties and criminal investigation.

Going forward, the cost-benefit analysis that often favored voluntary disclosure may be replaced by a riskier and more bifurcated set of outcomes for export control violations: on the one hand, less serious cases that are resolved quickly without penalties, and on the other, more serious cases that may be subject to very significant penalties, collateral consequences and potentially more frequent criminal investigations.

Companies considering disclosing minor or technical infractions may benefit from the new, shorter timetable for resolution, which will likely reduce uncertainty for many companies, allowing them to implement their remedial plans and move on.

However, companies disclosing more serious violations may be exposed to more frequent and larger monetary penalties, more frequent criminal investigation, greater reputational risks stemming from the requirement to admit to bad facts and BIS' intention to publicize allegations in charging letters earlier in a case, and more burdensome settlements even when avoiding monetary penalties in favor of compliance-commitment-only resolutions.

In light of this new reality, companies may need to reconsider at least three points when deciding whether to make a voluntary disclosure to BIS.

First, companies may wish to rethink internal policies and practices regarding submission of voluntary disclosures. While it remains BIS policy to strongly encourage disclosure if a company believes it may have violated the Export Administration Regulations,[10] the increased likelihood of undesirable outcomes even when making a voluntary disclosure will have to be weighed against a generally more aggressive enforcement environment.

The Axelrod memo's stated intent to enforce aggressively and impose larger penalties applies to all cases, not just voluntary disclosures. And BIS has been expanding its investigatory capabilities, while the DOJ is shifting more resources to criminal export controls violations, as well.[11]

As a result, the risks posed by both voluntarily disclosed and nonvoluntarily disclosed export controls violations are rising, notwithstanding the significant penalty mitigation benefits that are typically associated with disclosure — i.e., a typical monetary penalty reduction of 50% under BIS' enforcement framework. Companies should undertake careful, detailed and case-specific analyses when deciding whether to disclose.

Second, companies will increasingly need to give serious consideration to making a voluntary disclosure to the DOJ when making a voluntary disclosure to BIS in light of BIS' stated intention to involve DOJ prosecutors in the National Security Division's Counterintelligence and Export Control Section more regularly in the most serious cases.

Axelrod's emphasis on increased, early prosecutor involvement suggests the DOJ will play a role in a larger number of cases and formal referrals for criminal investigation could become more frequent. As a result, companies will have to prepare for a higher likelihood of DOJ involvement, which in some cases may involve taking advantage of the DOJ National Security Division's own voluntary disclosure process.

Many companies have found this process unappealing since it was established in 2016 and even since it was revised to be more attractive to companies in 2019, in part because it offers less leniency than, for example, the similar voluntary disclosure process the DOJ Fraud Section maintains for Foreign Corrupt Practices Act matters.[12]

Now, however, companies may need to give more serious consideration to utilizing the DOJ process when making a voluntary disclosure to BIS.

Third, when circumstances permit, companies may decide to investigate more thoroughly before initiating a voluntary disclosure to BIS. Because BIS permits companies to submit an initial notification of voluntary disclosure to BIS, and then follow up with a full report six months later, with the option to seek extensions, companies often initiate voluntary disclosures quickly, at the outset of an internal investigation.

Going forward, companies may want to gather more facts before deciding whether to make a disclosure, and may seek them out by conducting more fulsome investigations, including through email review and interviews, before deciding how to best mitigate enforcement risks, including by retaining white-collar defense counsel in addition to trade controls counsel.

Of course, there are still a range of circumstances where it may be advisable to swiftly initiate a voluntary disclosure process, such as to help mitigate possible national security harm or to ensure that the company receives mitigation credit for notifying BIS of a compliance issue before the agency becomes aware of the issue through other channels.

Overall, companies and practitioners will need to closely monitor export controls enforcement developments. In particular, it will be important to assess how BIS' new enforcement approach will play out in practice, including especially how the agency assesses monetary penalties under the new policy and how significantly DOJ involvement in BIS investigations will increase.

Already, however, it is clear that the new approach has raised export control enforcement risks, and in some cases will make decisions about whether to make voluntary disclosures more challenging and more consequential.

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[1] Matthew Axelrod, Assistant Secretary for Export Enforcement, Memorandum for all Export Enforcement Employees, Bureau of Industry and Security, U.S. Dep't of Commerce, June 30, 2022, https://bis.doc.gov/index.php/documents/enforcement/3062-administrative-enforcement-memo/file. Axelrod announced the memorandum in remarks delivered at BIS' annual "Update" conference. See Matthew Axelrod, Assistant Secretary for Export Enforcement, Remarks As Prepared for Delivery, BIS' 2022 Update Conference on Export Controls and Policy (June 20, 2022), https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/3068-2022-06-30-bis-press-release-export-enforcement-policy-changes/file.

[2] Matthew Axelrod, Assistant Secretary for Export Enforcement, Remarks As Prepared for Delivery, BIS' 2022 Update Conference on Export Controls and Policy (June 20, 2022), at 6, https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/3068-2022-06-30-bis-press-release-export-enforcement-policy-changes/file.

[3] While voluntarily disclosed, non-egregious cases generally are eligible for a "base penalty" of half the transaction value (up to a capped maximum amount), the base penalty for voluntarily disclosed egregious cases may be penalized at up to the greater of the transaction value or $164,060.50 per violation (i.e., half the statutory maximum). The current statutory maximum for violations of the Export Control Reform Act of 2018 is $328,121 or twice the value of the transaction. See Commerce Department, Civil Monetary Penalty Adjustments for Inflation, 87 Fed. Reg. 157, 159 (Jan. 15, 2022).

[4] Matthew Axelrod, Assistant Secretary for Export Enforcement, Memorandum for all Export Enforcement Employees, Bureau of Industry and Security, U.S. Dep't of Commerce, June 30, 2022, https://bis.doc.gov/index.php/documents/enforcement/3062-administrative-enforcement-memo/file.

[5] See Export Control and Sanctions Enforcement Policy for Business Organizations, Nat. Security Div.,

U.S. Dep't of Justice, Dec. 13, 2019, https://www.justice.gov/nsd/ces_vsd_policy_2019/download ("It is important to note that when a company identifies potentially willful conduct, but chooses to self-report only to a regulatory agency and not to DOJ, the company will not qualify for the benefits of a VSD under this Policy in any subsequent DOJ investigation.").

[6] See Export Administration Regulations: Revisions to Russia and Belarus Sanctions and Related Provisions; Other Revisions, Corrections, and Clarifications, 87 Fed. Reg. 34,131 (June 2, 2022).

[7] Lisa Monaco, Deputy Attorney General, Remarks As Prepared for Delivery, Deputy Attorney General Lisa O. Monaco Delivers Keynote Remarks at 2022 GIR Live: Women in Investigations (June 16, 2022), https://www.justice.gov/opa/speech/deputy-attorney-general-lisa-o-monaco-delivers-keynote-remarks-2022-gir-live-women.

[8] See Peter Lichtenbaum, Eric Sandberg-Zakian, and Blake Hulnick, Export Control Compliance Amid Stricter Russia Restrictions, Law360 (March 22, 2022), https://www.law360.com/articles/1475610/export-control-compliance-amid-stricter-russia-restrictions.

[9] See Event Recap: "2022 Export Enforcement Priorities," Silverado Policy Accelerator (Feb. 24, 2022), https://silverado.org/news/event-recap-2022-export-enforcement-priorities.

[10] 15 C.F.R. § 764.5.

[11] See Peter Lichtenbaum, Eric Sandberg-Zakian, and Blake Hulnick, Export Control Compliance Amid Stricter Russia Restrictions, Law360 (March 22, 2022), https://www.law360.com/articles/1475610/export-control-compliance-amid-stricter-russia-restrictions.

[12] See Section 9-47.120 - FCPA Corporate Enforcement Policy, Justice Manual, U.S. Dep't of Justice, https://www.justice.gov/jm/jm-9-47000-foreign-corrupt-practices-act-1977#9-47.120.