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Trade Compliance for Transportation & Logistics Providers

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Trade compliance has long been an area of risk and uncertainty for the transportation and logistics sector. It is difficult for many providers to conceptualize, in practical terms, their duties and obligations when asked to perform global services. Service providers hold a vulnerable place in the supply chain by virtue of being other than the sellers and buyers who have direct tangible contact with cargoes, their sources, and their end uses. The risk associated with this role occasionally arises in the form of highly publicized prosecutions and industry guidance from which few parties are immune, whether domestic U.S. or foreign, whether air or ocean providers, or even cross-border motor carriers, and whether large global conglomerates or smaller niche players.

Very recently the international trade compliance risks for the transportation and logistics business yet again drew attention. The U.S. Department of the Treasury (among other agencies) issued a "Sanctions Advisory" as stark reminder of the economic sanctions risk exposure that exists for the global industry. On May 14, the agencies published "Guidance to Address Illicit Shipping and Sanctions Evasion Practices" with particular focus on illicit shipping in the maritime segment. In short, the United States continues in its concerns over global threats to national security and its willingness to extraterritorially enforce restrictions.

The key takeaway from this advisory is that transportation and logistics providers should develop risk-based sanctions (and other) compliance programs emphasizing due diligence and adherence to policy. Specifically, Treasury recommends that industry "continually adopt business practices to address red flags and other anomalies that may indicate illicit or sanctionable behavior." Certainly the stakes could not be higher with criminal and civil penalties looming for domestic and foreign operators, and yet piloting a reasonable path forward is complex and time consuming. In times like these a simple level-set on the fundamental risks for industry and basic best practices can serve well to plot that course. The paragraphs that follow outline the high-level considerations for three principal compliance regimes as well as high-impact compliance considerations.

Treasury Enforcement of OFAC Sanctions. The Treasury Department's Office of Foreign Asset Controls (OFAC) administers approximately 30 different sanctions programs against countries and persons. Those programs generally prohibit the transfer of property or funds, including participating in or facilitating such transfer, to restricted parties. All U.S. persons must comply, including any non-U.S. entities owned or controlled by a U.S. person as determined under the country-specific sanction (See 31 CFR 535.329). A service provider's mere participation in a restricted transaction

has been an area for exposure in recent years. Traffic involving Cuba and Iran have been a unique area of difficulty for industry due to the swift evolution of U.S. policy over the last decade.

State Enforcement of the ITAR. The Department of State's Defense Directorate of Trade Controls (DDTC) enforces the International Traffic in Arms Regulations (ITAR) found at 22 CFR Parts 120 to 130. Those export controls restrict the import, export, and temporary import or export, of defense articles, technical data, and defense services. The ITAR applies to any items designated on the United States Munitions List (USML) found at 22 CFR 121.1 including firearms, ammunition, missiles, explosives, training equipment, military electronics, optics, and spacecraft systems. The DDTC requires registration of certain actors involved in the trade of arms, including, from time to time, service providers, particularly where their activities may be considered brokering of defense articles and services. Unlawful brokering and participation with knowledge of violations have been areas of exposure for service providers in recent years.

Commerce Enforcement of the EAR. The Department of Commerce's Bureau of Industry and Security (BIS) enforces the Export Administration Regulations (EAR) found at 15 CFR Parts 730 to 780. Those export controls principally restrict the export and reexport of items and technology, including participating in or facilitating such export, based on item, country-specific embargoes, and end users. Items under control include any nonmilitary goods, software, or technology that are physically located in the U.S. or of U.S. origin, of foreign origin but containing more than de minimis U.S. content, or of foreign origin but a direct product of U.S. technology or software. The EAR applies to U.S. persons, but also foreign subsidiaries that are controlled, directly or indirectly, by a domestic entity (15 CFR 760.1). Importantly for transportation and logistics providers, one of the Ten General Prohibitions found in the EAR makes it unlawful to proceed with transactions with the knowledge that a violation has occurred or is about to occur (General Prohibition Ten, found at 15 CFR 736.2). General Prohibition Ten has appeared as a specific area of enforcement against service providers in recent years.

Compliance Best Practices and Red Flags. The penalties for violation of these and other U.S. regulatory regimes, including the Foreign Corrupt Practices Act (FCPA), anti-boycott restrictions, and even U.S. customs compliance, which has become an area of exposure for operators, extend well beyond negative headlines that yield harm to commercial reputations. Significant civil penalties, criminal fines, and even jail time can follow misconduct and careless acts. There is neither a one-size-fits-all approach to international trade compliance nor any real benefit in adopting compliance programs and practices that will not be followed. Rather, the task for each transportation and logistics operator is to assess risk for the operation and tailor an appropriate program together with training and process controls. The tactical elements of a strong compliance program include: developing internal leadership and subject matter expertise on trade controls; sticking to process fundamentals, such as denied parties screening; and watching for the gamesmanship among shippers that can cause liability for even the most well-meaning of operators.

Watching for gamesmanship is of course the front line of trade compliance risk mitigation for transportation and logistics providers. An awareness of weaknesses and "red flags" helps personnel to remain vigilant and to escalate issues where they arise. Perhaps the best example of this tactic is found in the "Know Your Customer Guidance" published by the Department of Commerce in Supplement No. 1 to Part 732 of the EAR. That guidance amounts to: (1) deciding whether "red flags" exist; (2) inquiring further if necessary; (3) avoiding self-blinding against bad facts; (4) training

sales and operations staff; (5) reevaluating situations as new facts are learned; and (6) consulting with the respective agencies or counsel before proceeding if "red flags" or other risks cannot be resolved. A few important "red flags" for transportation and logistics providers to guard against as part of trade compliance programs include:

- The customer is reluctant to offer information about the end use of a product.
- The product's capabilities do not fit the buyer's line of business.
- The product ordered is incompatible with the technical level of the country to which the product is being shipped.
- The customer has little or no business background.
- Deliveries are planned for out-of-the-way destinations.
- A freight forwarding is listed as the product's final destination.
- The shipping route is abnormal for the product and destination.
- Packaging is inconsistent with the method of shipment or destination.

Remember, Voluntary Disclosures Are Available. The reality of international transportation and logistics is that it is a hard, fast-paced, fact-specific, multifaceted business. Real or potential violations can arise for even the most well-meaning of operators. Exposure for these and similar regimes can often extend five years in the past, which is a relatively long tail to consider when a history of violations is found. Those instances present opportunities to update compliance programs, retrain personnel, and implement meaningful corrective actions to mitigate present and forward-looking risk. They also offer a chance to consider voluntary self-disclosures to the agencies having jurisdiction, which are available for the regulatory regimes described here and others that maybe implicated. Giving notice to an agency should not be taken lightly, but it can serve as a pathway for closing out a file with mitigated financial exposure (and often little or no exposure). Self-disclosures are discretionary for most regulatory regimes, although ITAR compliance is one important exception where the remedial action is considered obligatory.

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