Fried Frank International Trade and Investment *Alert*™

BIS Proposes Revised Penalty Guidelines for Civil Enforcement Cases

On December 28, 2015, the U.S. Commerce Department's Bureau of Industry and Security ("BIS") published a proposed rule that would amend BIS guidance regarding civil enforcement cases under the U.S. Export Administration Regulations ("EAR"). This proposal is an effort to make the civil penalty process more predictable, transparent, and aligned with guidelines issued by the Department of the Treasury, Office of Foreign Assets Control ("OFAC"). The proposed rule would amend the factors BIS considers when deciding whether to settle allegations of EAR violations and when setting penalties in civil enforcement case settlements.[1] Comments on the proposed rule are due by February 26, 2016.

BIS and OFAC both currently derive statutory authority for enforcement of penalties from the International Emergency Economic Powers Act ("IEEPA"), under which each agency can impose civil monetary penalties of up to $250,000 or twice the value of the transaction, whichever is greater. In 2009, OFAC put into place revised enforcement guidelines to create more transparency and predictability in the penalty process regarding economic sanctions violations (the "OFAC Guidelines"). The proposed BIS rule, which closely mirrors the OFAC Guidelines, provides a framework of factors that BIS will consider in each case to determine whether to impose monetary penalties, and if so, how much. We do not expect the proposed guidelines to materially affect the size of civil penalties imposed by BIS, and the agency has stated that it does not expect to increase the number of cases that result in a monetary penalty. Rather, the new guidelines would aid exporters in estimating the range of potential penalties, especially for export violations that implicate both the EAR and OFAC sanctions programs.

Civil Monetary Penalties

Under the proposed guidelines, BIS would apply the aggravating, general and mitigating factors set forth below to determine whether a civil monetary penalty is appropriate based on the facts and circumstances of the case. In some instances, BIS may determine that a warning letter is sufficient; in others, BIS may determine that the penalty must be more significant in order to accomplish BIS's goals, including deterrence.[2]

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1 The new guidelines would not apply to civil administrative enforcement cases for violations under part 760 of the EAR – Restrictive Trade Practices and Boycotts, which will continue to be governed by Supplement No. 2 to Part 766.

2 In general, penalties for settlements agreed to after litigation has been commenced will be higher than those described in the Guidelines.

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Base Penalty Amount

Under the proposed rule, if BIS decides that a civil monetary penalty is appropriate, it then would determine whether the violation should be characterized as egregious or non-egregious and whether the respondent voluntarily self-disclosed the alleged violation. These two factors would determine the "base penalty amount," which is the starting point from which BIS may adjust civil penalties. In this quadrant system, there would be significantly higher penalties for egregious cases and for failure to voluntarily self-disclose. Since "egregious" is not a defined term, BIS would characterize the violation by reference to all of the factors set forth below, giving particular weight to the aggravating factors. BIS would also reserve the discretion to charge multiple violations for a single transaction (e.g., an unlicensed export, reporting the incorrect ECCN and export authorization on export documentation, recordkeeping violations).

The base penalty amounts are shown in the table below and reflect the explicit intent of BIS to encourage voluntary self-disclosure. The proposed rule notes that "[w]ith respect to VSDs generally, OEE will issue warning letters in cases involving inadvertent violations and cases involving minor or isolated compliance deficiencies, absent the presence of aggravating factors." In fact, the vast majority of voluntary self-disclosures – about 97% – do not result in monetary penalties.

	Non-Egregious	Egregious
Voluntary Self-Disclosure	One-half of transaction value (capped at $125,000 per violation)	One-half of applicable statutory maximum
No Voluntary Self-Disclosure	Applicable schedule amount (capped at $250,000 per violation)	Applicable statutory maximum

As noted above, the "statutory maximum" is currently $250,000 or twice the value of the transaction. The proposed rule defines the "transaction value" as the U.S. dollar value of the transaction, which BIS would determine based on commercial invoices, bills of lading, signed Customs declarations, or similar documents. At times, BIS would consider the market value of the items that were the subject of the transaction and/or the economic benefit derived by the respondent from the transaction. If the transaction involved a lease of U.S.-origin items, BIS would look to the value of the lease to determine the transaction value.

The "applicable schedule amount" refers to the following graduated series of penalties based on the underlying transaction values:

Transaction Value	Schedule Amount
less than $1,000	$1,000
$1,000 – $10,000	$10,000
$10,000 – $25,000	$25,000
$25,000 – $50,000;	$50,000
$50,000 – $100,000;	$100,000

Transaction Value	Schedule Amount
$100,000 – $170,000	$170,000
$170,000 or more	$250,000

Following BIS's determination of the base penalty amount, BIS would consider a number of factors to determine whether to adjust the penalty amount upward or downward. The ultimate penalty amount will never exceed the statutory cap.

Aggravating Factors

The first set of aggravating factors would be willfulness, recklessness and concealment. The degree of each of these would determine the degree of aggravation factored into the penalty calculation. BIS would consider a respondent's failure to exercise a minimal degree of caution in avoiding conduct that violates the EAR and the respondent's deliberate efforts to mislead law enforcement.

The second set of aggravating factors would be awareness of conduct at issue, with a focus on supervisory or managerial level staff. This factor, which previously was not listed as its own factor but is in the proposed rule, would capture situations in which the respondent took no action to address a violation despite the respondent knowing, or having reason to know, of the violation. Here, BIS would consider, among other things, whether business processes were designed to avoid the respondent learning of violations and whether senior management had implicit or explicit knowledge of the conduct.

The third set of aggravating factors would be harm to regulatory program objectives, which would take into account the destination involved in the transaction, the end use and end user of the product and the sensitivity and control level of the items involved. BIS would view each of these facts with an eye to whether the conduct, in purpose or effect, substantially implicated national security or other essential interests protected by the U.S. export control system.

General Factors

General factors, which could either be mitigating or aggravating depending on the circumstances, include an assessment of the individual characteristics of a respondent, including the respondent's commercial sophistication, exporting experience, volume and value of export transactions, particularly as compared to the total volume of the respondent's business, and regulatory history, with a focus on the last five years. BIS has helpfully stated that it will not take into account past violations of an acquired entity if the acquirer took reasonable steps to uncover, remediate and disclose such violations. BIS also will consider whether the transaction was in support of other illegal conduct.

Also included in General Factors is an assessment of the presence and adequacy of a compliance program, including a determination of whether or not the respondent had an effective risk-based BIS compliance program in place at the time of the apparent violation that complied with BIS standards. The role of a compliance program in detecting and addressing the violation may be considered a mitigating factor.

Mitigating Factors

As noted above, the remedial response of the respondent, and the role of its compliance program in such response, may be considered mitigating factors if the respondent took corrective action in response to the

apparent violation. This may include the implementation of new and more effective internal controls designed to prevent future occurrences and informing senior management.

Demonstration of exceptional cooperation with regulators may result in a 25% to 40% reduction of the base penalty amount. In order to qualify for such a significant reduction, the respondent must have provided substantial additional information regarding the apparent violation and/or other apparent violations caused by the same course of conduct. BIS also will consider whether respondent entered into an agreement with regulators to toll the statute of limitations, where applicable.

With voluntary self-disclosures specifically being taken into account in the determination of the base penalty amount, it would no longer be listed separately as a mitigating factor. However, cases involving voluntary self-disclosure may still warrant mitigation of the penalty amount due to exceptional cooperation with regulators.

BIS also would consider whether, had a license been sought in advance, one likely would have been approved. A respondent's penalty may be reduced by up to 25% if BIS concludes that a license application likely would have been approved. In addition, if the alleged violation is the respondent's first, the penalty may be reduced by 25%. While mitigating factors may be combined for a more significant reduction in penalty, such reduction will generally be limited to a reduction of 75% of the base penalty amount.

Other Relevant Factors

In addition to the above, BIS may consider as relevant in certain circumstances whether (i) a single transaction gave rise to multiple violations, (ii) multiple unrelated violations could warrant a stronger enforcement response, (iii) there are corresponding enforcement actions taken by other agencies in response to the conduct at issue, and (iv) the action taken by BIS is likely to have a deterrent effect on others. The proposed rule also includes a catch-all category, providing BIS the flexibility to consider factors not enumerated therein.

Key Takeaways

While the guidelines set forth in the proposed rule are not yet in place, their content already is a useful guide to help exporters anticipate the approach BIS is likely to take to settlement and penalty determinations in the future. Given how closely the BIS guidelines align with the OFAC Guidelines, enforcement decisions by OFAC under the OFAC Guidelines may also provide guidance on what to expect from BIS in the coming years. We expect the BIS guidelines to provide greater predictability and transparency to the process, which will allow exporters to proceed in a more informed manner. As the proposed rule makes clear, it continues to be of great importance to maintain a well-functioning compliance program, to voluntarily self-report when a violation is detected and to take corrective action to guard against future violative conduct.

If you have any questions regarding the proposed rule or how it may impact your business, please reach out to the contacts listed below.

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