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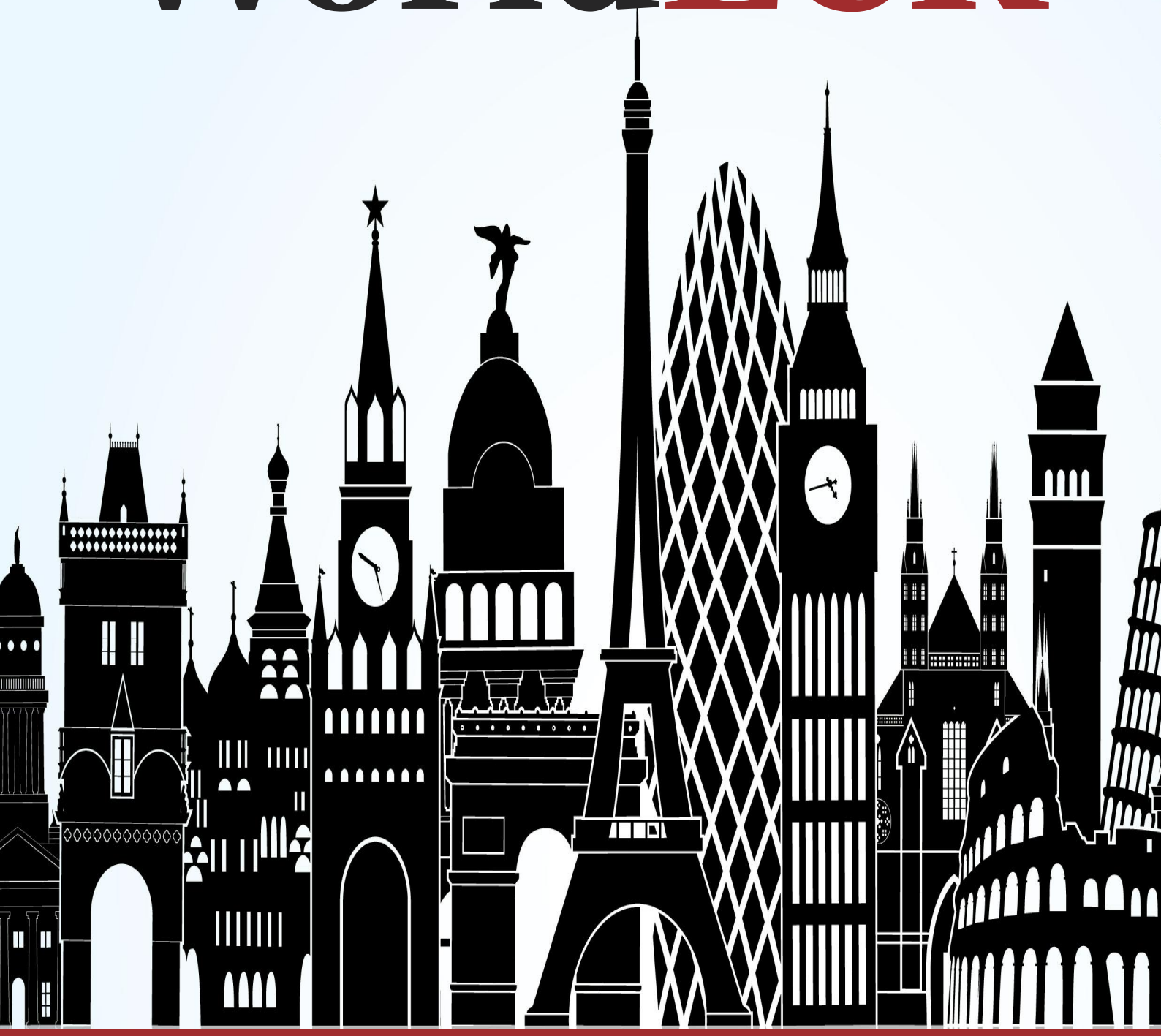

SPECIAL FOCUS

EUROPE 2015

In 2014, conflict in Ukraine put EU sanctions and export controls firmly on the European corporate compliance agenda. In this Special Focus, *WorldECR* speaks to the lawyers advising on the impact of the regulations and the challenges facing business – and the regulators – in the year ahead.

Special Focus: Europe 2015

THE EXPORT CONTROL CHALLENGE

Export controls seldom seize the headlines in the way that sanctions do, and the rhythm of practice may be more measured. Nonetheless, there are drivers for change. Amongst these are the need for greater consistency in the way the rules are applied and the European Parliament's renewed interest in their human rights and security implications. Businesses, meanwhile, have come to realise that they ignore the commercial consequences of compliance at their peril.

In EU, just as in U.S., legal practice, export controls and sanctions frequently overlap – and indeed, the issues conflate. This is unsurprising given that they are tools designed with the same policy aims: regional and international security, addressing of foreign policy concerns, and non-proliferation.

But, as Miriam Gonzalez of Dechert pointed out in the preceding article on sanctions, each possesses its own rhythm: sanctions are intended (indeed, orchestrated) to catch their targets by surprise while export controls follow the pattern of more orthodox legal regimes, arrived at by negotiation and consultation, change occurring gradually, reflecting the exigencies of the global situation, but seldom in 'real-time'.

That's not to say headaches don't attend upon the effort involved in staying up to speed. In the U.S., much ink and many tears have been shed on the process of 'reform' – the moving of some items from the USML to the CCL. In Europe the pain is around the multiplicity of ways in which EU Member States have implemented the EU regulations – in particular, the EU Dual-Use Regulation (428/2009) and the rules governing the control of exports of military technology and equipment .

In EU parlance, 'reform' is largely understood as the need to iron out (to the extent that it is possible) the discrepancies that arise in practice. As the head of export controls at a household-name European company recently told *WorldECR*:

'I'd like to see alignment on export licensing requirements and application procedures, such as end-user statement requirements that help facilitate transactions where multiple border-crossings in a more complex supply chain are the reality for most companies'

It isn't that the Commission isn't aware of the need for progress. In 2013 DG Trade published a report on a consultation it conducted in 2011

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Special Focus: Europe 2015

which 'opens the way for the preparation of a Communication outlining a long-term vision for EU strategic export controls and which may announce concrete policy initiatives for their adaptation to rapidly changing technological, economic and political circumstances'.

While tortured wording scarcely hints at rapid change, there are signs of improvement, says Fabienne Vermeeren of the Brussels office of White & Case. She points out that one major gripe has already been addressed: in December, the EU updated Annex 1 to Regulation 428/2009 to reflect changes to the Wassenaar Arrangement list (the amount of time it had taken to do so had been a frequent source of grumbles from businesses disadvantaged vis-à-vis competitors in jurisdictions which update their regimes more swiftly).

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Fabienne Vermeeren, White & Case

Further, says Vermeeren, 'In Council Conclusions published on 21 November, it was indicated that the Council would be favourable to moving to e-licensing.' It is currently possible to apply for an export licence online in some, but not all countries. The development would still mean that companies would need to apply to the relevant national authority instead of at EU level (and exporting subsidiaries of a company in different EU Member States still face different procedures and processing times), and yet, says Vermeeren, 'The mere fact that companies would be able to do this would be better than the present situation.'

Vermeeren adds that it'll be hard to weed out all the anomalies that make each Member State regime so unique: 'But there are some steps that would make things straightforward, like issuing more Union General Export Authorisations ('UGEAs'). Also, a review of the National Export Authorisations would be useful – some of these could be implemented generally at the EU level into UGEAs, while new ones might include a permit for low-value shipments, something that was mooted in the current legislation, but it didn't work. Another one could be for large projects.'

National differences such as those Vermeeren describes can be 'bewildering' for U.S. businesses navigating their way around Europe, says Sheppard Mullin's Curtis Dombek. He advises where typically 'there's a U.S. element, whether that's the parent company of the client, or a supplier, or a customer. In that cross-border setting, invariably EAR, ITAR or sanctions issues enter the legal fabric. But it's also essential to spot the EU issues,' there being, he says, 'a real dissonance between the U.S. and EU regimes that manifests itself in so many different ways.'

By way of example, he says, there are 'so many U.S. licence exceptions that don't exist in the European Union (notwithstanding various national exceptions). U.S. export control reform, he says, has created a whole set of new complexities: 'Even before reform, the USML looked very little like the control list in the EU. Now with the need to unravel components and deciding what's under the jurisdiction of the Department of Commerce 600 series, but still listed as a military item in the EU, the challenges have greatly multiplied.

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Les Carnegie, Latham & Watkins

The significant degree of commonality that is shared between the two systems itself creates pitfalls, Dombek suggests: 'The fact that if you comply with the U.S. rules 100 percent will make you will be 70 to 80 percent compliant in the EU is no comfort. Such overlap is merely an invitation to complacency!'

Having recently helped prepare, with colleagues, an export control compliance programme for a European company, Les Carnegie of the Washington, DC office of Latham & Watkins understands that all too well: "It's been an interesting collaboration. The important thing is that when you're formulating a global trade policy, it's essential to differentiate. Such a global compliance programme has to be entirely respectful of EU and U.S. activities.'

Condition precedent

Export control issues – particularly in heavily controlled industry sectors – can make or break deals. Carnegie's colleague Charles Claypoole describes recently advising a major European company where it was buying out a joint venture with a UK rival: 'The deal required the transfer of military technology from the UK to other EU jurisdictions. There were a number of complex export control issues. One related to the security classification of technology which triggered requirements for government approval. Our task was to incorporate these elements into the structure of the transaction in a way that gave our client contractual leverage in the deal.'

And yet as in so many areas of compliance, the extent to which export controls have the potential to permeate the fabric of business life is still under-appreciated in the EU (that's not to say that in the United States all those that should know, do know about, say, export controls and their application to the Cloud – nebulous even on that side of the Atlantic).

Fieldfisher's Jochen Beck has been helping clients understand the often extremely technical repercussions of commercial imperatives and change: 'Businesses aren't always initially aware of the export control

Special Focus: Europe 2015

implications of their activities,' says Beck. 'One issue we've seen come up has been companies wanting to move servers that store sensitive data abroad

'What could be useful would be a mechanism whereby one licence covers all back-and-forward data exchange for transfers between all Member States and safe countries…[perhaps] structured like a U.S. technical assistance agreement.'

Jochen Beck, Fieldfisher

(e.g. in the framework of an IT consolidation project). Companies will usually assess whether they require a licence to export sensitive data to that server, but the second question is sometimes forgotten: Do we also require a licence to re-export the data from the storage country? Looking, for example, at military information stored on a server in a EU Member State, the answer differs from Member State to Member State. While it might not be a problem to obtain the required licences, the applications, record-keeping and reporting requirements in several countries just for storing emails and data can create a huge (administrative) burden which would be aggravated if, for example, a third Member State comes into play as well. What could be useful would be a mechanism whereby one licence covers all back-and-forward data exchange for transfers between all Member States and safe countries. Such a licence could for instance be structured like a U.S. technical assistance agreement, a TAA.'

Northern exposure

Carolina Dackö of Vinge says she is probably only one of a few lawyers in Sweden for whom export controls/ sanctions advice makes up a significant part of their practice. Typically, she says, she takes a holistic approach to the issue: 'Industrial clients usually want some assistance in understanding whether they have dual-use products in their inventories. That's quite a straightforward task for small companies. But for big companies of course it's more difficult. The most important part of my role is to advise on internal organisation, because it is everyone's responsibility, at the end of the day to ensure compliance. So, for example, if you're doing a lot of R&D, how do you ensure that you're thinking about these issues early on? It's a learning curve – I'm helping companies to understand when the rules are triggered, and what to do when they are.'

Interestingly, says Dackö, export controls have become quite political in Sweden. There are in the EU no explicit rules comparable to the deemed export rules in the United States that would prevent the transfer of controlled technology to nationals of certain non-EU countries on EU soil. But Sweden boasts a large Iranian population, many of whom are pursuing their studies in the country's excellent universities. Controversy has arisen where university departments have banned Iranian students from certain courses – something that goes well against the grain of the non-discriminatory principles that are part of the bedrock of Swedish society. 'Here you're getting into deemed export territory,' says Dackö, 'It's an interesting development!'

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Carolina Dackö, Vinge

At the European level too, the political element of export controls has been sharpened – not least by the role of the European Parliament which was given equal law-making powers with the EU Council in certain key areas (which exclude restrictive measures or sanctions) and thus must approve any amendments to the export control regime for it to move forward.

For businesses, the most noticeable impact of parliament's involvement is the possibility of delay (resulting from additional scrutiny) in the implementation of change – but also that the human rights considerations will now impact on what is and isn't controlled. For example, there is a strong push being led by Dutch MEP Marietje Schaake for the EU to prohibit the export of 'information and communication technologies ('ICT') that can be used in connection with human rights violations as well as to undermine the EU's security, particularly for technologies used for mass-surveillance, monitoring, tracking, tracing and censoring, as well as for software vulnerabilities.' And while the Commission has included some categories of intrusion software in its recently published annex to the Dual-Use Regulation (reflecting the Wassenaar changes) it has also committed to a general review of measures it can take to 'catch' dangerous technologies as they emerge; this, possibly, might include the creation of its own, autonomous lists of controlled products independent of the multilateral regimes.

'I think it's quite clear,' says Gide partner Olivier Prost, 'that parliament is going to play a stronger role in the development of export controls.' Prost notes that toward the end of last year the Commission sent to parliament for debate a proposal for a regulation that would in effect limit imports of conflict minerals, broadly mirroring s.1502 of the Dodds-Frank rule.

Be careful what you wish for

Can Europe cope with more rules? It's an interesting question. Many lawyers we've spoken to for this Focus would respond by saying that the EU's institutions – both in Brussels and in the Member States – might endeavour to endow themselves with greater (and much-needed) capacity before saddling themselves with regulations that neither they nor business possess the resource to administer.

And yet, as one lawyer, mindful of Europe's many ethical and security challenges, both domestic and foreign, says, 'The pressure to take a stand, to do something, is ever present.'