Export Controls and Sanctions

RECENT DEVELOPMENTS

US export controls and sanctions laws have undergone a number of important developments in the first quarter of 2011. This Review covers key issues related to:

- Cloud computing
- Cuba sanctions
- Export control certifications for certain visa applications
- Trade agency reorganization
- US export controls against India
- Conflict minerals reporting
- Application of export controls to academic research, and
- Libya sanctions.

US and non-US companies, alike, should be aware of these issues and the potential impact on their global operations.

CFIUS Disapproval of Huawei-3Leaf Systems Deal Puts New Focus on US Controls Over Cloud Computing Technology

The US Committee on Foreign Investment in the United States (CFIUS) recently blocked Chinese telecommunications company Huawei Technologies Ltd. (Huawei) from acquiring the cloud computing-related technology of, and hiring employees from, insolvent US firm 3Leaf Systems. On February 18, 2011, Huawei issued a statement that it would not contest CFIUS's recommendation that Huawei withdraw its application to CFIUS for national security clearance of the transaction. The CFIUS action may signal an important development in US control of cloud computing technology and US regulation of foreign investment.

The parties did not seek CFIUS approval before the transaction. According to a Huawei statement, no CFIUS approval was sought because Huawei had timely sought and received approval for its acquisition of 3Leaf Systems technology from the US Bureau of Industry and Security (BIS) in the US Department of Commerce. CFIUS did not agree that the BIS actions satisfied the government's concerns with the technology transfers, and it later asked Huawei to submit the deal for national security review.

The CFIUS action came after Senators Jim Webb and Jon Kyl and three other lawmakers wrote Commerce Secretary Gary Locke and Treasury Secretary Timothy Geithner to question the Administration's stance on the Huawei-3Leaf Systems deal and its regulation of cloud computing. In their February 10, 2010, letter, the legislators asked for a description of "the technology classification process as it relates to the export of resource virtualization or cloud computing technology." They also asked for a description of "the review taken by the Commerce Department that allowed a foreign

company, with close ties to the Chinese military, to obtain an export license for this technology."

The CFIUS action and the focus by members of Congress on these issues come as the Department of Commerce is developing its policies on cloud computing. On January 11, 2011, the Department issued guidance stating that "the service of providing computational capacity through grid or cloud computing is not subject to the Export Administration Regulations (EAR), since the service provider is not shipping or transmitting any commodity, software or technology subject to the EAR to the user." The Department had issued earlier guidance consistent with this position in January 2010.

CFIUS does not issue policy guidance, and its recommendations on the Huawei transactions are not public. However, the disapproval of Huawei's actions may signal that CFIUS views foreign acquisition of US cloud computing technology as raising heightened national security concerns. For the Department of Commerce, though its guidance apparently has not directly dealt with acquisition of the technology for creating and maintaining a cloud computing network, rather than its operation, the CFIUS action and congressional pressure may encourage the Department to tighten its review of cloud computing-related activities. ◆

Certain Cuba Sanctions Restrictions Lifted

On January 28, 2011, the US Treasury's Office of Foreign Assets Control (OFAC) amended the Cuban Assets Control Regulations, 31 C.F.R. Part 515 (CACR or Cuba sanctions). The amendments implement policy changes announced by President Obama on January 14, 2011 to continue outreach efforts to the Cuban people. The amended regulations took effect immediately and among other things, authorize general licenses for (i) certain transactions with Cuban nationals who are permanent residents outside of Cuba, (ii) travel to Cuba in connection with educational and religious activities, and (iii) remittances to Cuba.

Prior to the amendments, the Cuba sanctions broadly prohibited transactions with Cuban nationals no matter where they resided. The amended regulations establish a new general license that authorizes persons in the United States to engage in certain transactions with individual nationals of Cuba who are permanent residents outside of Cuba. The general license is subject to the requirement that US persons obtain from the Cuban national at least two documents issued to the individual by the government authorities of the new country of permanent residence. However, all property in which a Cuban national has an interest that was blocked prior to the later of the date on which the individual took up permanent residence outside of Cuba or January 28, 2011, remains blocked.

The amendments to CACR also add general licenses for certain educational and religious activities that had previously required specific licenses from OFAC. A specific license will still be required for any educational or religious activities not authorized under the new general licenses. The new general license for educational activities authorizes accredited US graduate and undergraduate degree-granting academic institutions to engage in travel-related transactions incident to certain educational activities. Students traveling under the general license must carry a letter on official letterhead, signed by a designated representative of the sponsoring US academic institution, stating that the study in Cuba falls within the scope of the general license.

Similarly, the new general license for religious activities authorizes religious organizations located in the United States, including members and staff, to engage in travel-related transactions that are incident to religious activities in Cuba. Under the general license, travelers must engage in a full-time program of religious activities, and donations to Cuba or Cuban nationals are not authorized. In addition, individuals traveling under the general license must carry a letter on official letterhead, signed by a designated representative of the US religious organization, stating that the travel is within the scope of the general license.

Finally, the amended regulations add three general licenses related to remittances to Cuba subject to certain restrictions. These new licenses authorize (i) remittances of up to $500 per quarter to any Cuban national, except prohibited officials of the Government of Cuba or prohibited members of the Cuban Communist Party, to support the development of private businesses, among other purposes; (ii) unlimited remittances to religious organizations in Cuba in support of religious activities; and (iii) remittances to close relatives who are students in Cuba pursuant to an educational license for the purpose of funding transactions authorized by the license under which the student is traveling. ◆

New Export Control Certification Required For Non-Immigrant Worker Visas

Companies seeking visas for their foreign national workers must now certify whether such workers need a deemed export license to access controlled technology and technical data. Effective February 20, 2011, companies petitioning for certain non-immigrant visas for their employees must certify on Form I-129 that they have reviewed US export control regulations and determined that: (i) a license is not required from either the Department of Commerce or the Department of State to release technology or technical data to the beneficiary or (ii) if an export license is required, the company will not release controlled technology to the foreign worker unless and until it has received a license or other authorization to do so. This certification is only required for H-1B, H-1B1, L-1, or O-1A visas.

A deemed export occurs when controlled technology or technical data is released to foreign persons in the United States. A release of technology includes making it available to a foreign person through visual inspection or oral exchange and making it available by practice or application under the guidance of persons with knowledge of the technology. Such releases are deemed to be an export to the foreign person's country of nationality and may require an export license from the Commerce Department or the State Department prior to release.

To determine whether technology or technical data is controlled for export, it must first be classified under the Commerce Control List (CCL) found in the Export Administration Regulations (EAR) or the US Munitions List (USML) contained in the International Traffic in Arms Regulations (ITAR). The CCL contains a list of dual-use items that are controlled for export because they have both commercial and military applications. The USML controls items that are directly related to defense and military use. If the technology or technical data is described on the CCL, a license may be required prior to its release to a foreign person in the United States, depending upon such foreign person's most recent country of citizenship or nationality. If the technology is listed on the USML, a license will be required prior to release to any foreign person in the United States. However, the EAR and the ITAR do not control technology or technical data that are "publicly available" or in the "public domain," as those terms are defined by the applicable regulations.

Understanding the deemed export rules, classifying technology under the EAR or the ITAR, and determining whether a license is required to release technology to a particular foreign employee are likely to pose challenges to company personnel unfamiliar with US export controls. ◆

President Announces Trade Agency Reorganization Initiative

On March 11, 2011, President Obama issued a memorandum assigning a US Chief Performance Officer with the responsibility of leading an effort to create a plan for the restructuring and streamlining of certain federal government agencies. The US Office of Management and Budget's Deputy Director for Management will serve in this role. The reform effort springs from the President's January 25, 2011 State of the Union Address calling for increased competitiveness and innovation through government reform. This effort will focus first on the executive departments and

agencies supporting trade, exports, and overall US competitiveness. A new Government Reform for Competitiveness and Innovation Initiative will review the federal agencies and programs involved in trade, exports, and competitiveness by analyzing their scope and effectiveness, areas of overlap and duplication, and cost. Although the memorandum does not specifically identify the agencies falling under this Initiative, they likely will include the Office of the US Trade Representative, the Commerce Department's International Trade Administration, the Department of Energy, the USDA Foreign Agricultural Service, the Small Business Administration, the Export-Import Bank, the Overseas Private Investment Corporation, the US Trade and Development Agency, and the Office of Foreign Assets Control.

The President's memorandum requires consultation with the relevant leaders and staff of the departments and agencies, external organizations, and government reform experts on suggested improvements in effectiveness and efficiency. President Obama requested that the Chief Performance Officer submit recommendations within 90 days for presidential and congressional action to restructure and streamline federal government programs focused on trade and competitiveness. This schedule would call for the proposal by around mid-June. The President identified the following principles as guidance for the recommendations: (i) efficient and effective facilitation of US competitiveness; (ii) transparent, understandable, and easily accessible agency programs and requirements; and (iii) reduced inefficiencies and overlapping responsibilities or functions. US companies with international operations should carefully monitor such changes and their potential impact on business efficiencies. ◆

United States Eases Export Controls Against India

On January 25, 2011, the US Commerce Department's Bureau of Industry and Security (BIS) lifted restrictive export controls on trade with India in the civil space, defense, and other high technology sectors. BIS's new rule implements the November 8, 2010 bilateral understanding between President Obama and Prime Minister Singh of India to expand the two countries' strategic and commercial partnership. Companies doing business with India should be aware of BIS's new rule and its impact on potential trading opportunities.

INDIAN ENTITIES REMOVED FROM THE ENTITY LIST

The new rule removes the following Indian defense and space-related entities from BIS's Entity List.

- Bharat Dynamics Limited (BDL)
- Defense Research and Development Organization (DRDO) subordinate entities:
  - » Armament Research and Development Establishment (ARDE)
  - » Defense Research and Development Lab (DRDL)
  - » Missile Research and Development Complex
  - » Solid State Physics Laboratory
- Space Research Organization (ISRO) subordinate entities:
  - » Liquid Propulsion Systems Center
  - » Solid Propellant Space Booster Plant (SPROB)
  - » Sriharikota Space Center (SHAR)
  - » Vikram Sarabhai Space Center (VSSC).

Removing these nine Indian entities from the Entity List eliminates the additional dual-use licensing requirements for exports to entities on the List. Exporters, however, must still obtain all necessary authorizations otherwise required under BIS's Export Administration Regulations (EAR) for shipments to these entities.

INDIA REMOVED FROM THREE COUNTRY GROUPS

BIS's new rule removes India from EAR Country Groups listing countries with certain export restrictions imposed for reasons of nuclear nonproliferation (Country Group D:2), chemical & biological weapons (Country Group D:3), and missile

technology (Country Group D:4). India's removal from these groups eliminates certain licensing requirements for items such as medical products containing certain pathogens and toxins, and certain rocket systems and unmanned aerial vehicle end uses. In addition, with the removal of India from Country Groups D:2, D:3, and D:4, two license exceptions are now available for exports to India. Specifically, License Exception Baggage (BAG) is available for exports and re-exports of unaccompanied baggage to India, and India now is an eligible destination for reexports under License Exception Additional Permissive Reexports (APR).

INDIA ADDED TO ONE COUNTRY GROUP

The new BIS rule adds India to Country Group A:2 of the EAR. Country Group A lists member countries of the Missile Technology Control Regime (MTCR). Although India is not an MCTR member, its placement on the Country Group A:2 list recognizes India's commitment to adhere to the MCTR's export control requirements.

Conflict Minerals Reporting Requirement

The recently enacted Dodd-Frank Wall Street Reform & Consumer Protection Act amended the Securities Exchange Act of 1934 by including a new provision requiring companies filing with the US Securities and Exchange Commission (SEC) to disclose whether their products use conflict minerals. The Act defines such conflict minerals as "columbite-tantalite (coltan), cassiterite, gold, wolframite or their derivatives" and other minerals determined by the US Secretary of State to be financing conflict in the Democratic Republic of the Congo (DRC). Conflict minerals are commonly used in cell phones, laptops, electronic, medical and other high-tech products.

While the law does not prohibit companies from using conflict minerals, it aims to discourage such activity by requiring certain companies that use conflict minerals necessary to their manufactured products' functionality or production to annually disclose to the SEC whether any such minerals originated in the DRC or an adjoining country. If so, then the company must submit a certified report to the SEC describing:

- The due diligence measures taken on the source and chain of custody of the minerals, including an independent private sector audit of the report.
- The products manufactured or contracted to be manufactured that are not "DRC conflict free," the country of origin of the conflict minerals, and the facilities used to process the conflict minerals. "DRC conflict free" means the product does not contain minerals that directly or indirectly finance or benefit armed groups in the DRC or a neighboring country.

The law further requires that companies post the information disclosed to the SEC on their website. The SEC is expected to issue implementing regulations for this provision in April 2011. These regulations should provide further clarification how the conflicts mineral reporting requirement will be applied. In the meantime, companies subject to this new provision should prepare for the requisite due diligence, product evaluations, and supply chain reviews. Non-subject companies also should ready themselves for cooperating with business partners who file with the SEC. Companies also should note that the new law does not otherwise widen the existing US sanctions prohibiting certain business transactions with DRC individuals and entities on the Office of Foreign Assets Control's List of Specially Designated Nationals and Blocked Persons (SDN List.) ◆

Court of Appeals Upholds Conviction of Professor for Export Control Violations

In January 2011, the US Court of Appeals for the Sixth Circuit upheld the 2008 convictions of John Reece Roth for multiple violations of US export control laws in connection with research he conducted while a professor

of electrical engineering at the University of Tennessee at Knoxville. *United States v. John Reece Roth*, 628 F.3d 827 (6th Cir. 2011). In 2010, the US District Court for the Eastern District of Tennessee sentenced Roth to four years in prison for these violations.

Roth was convicted of violating the Arms Export Control Act and associated provisions of the International Traffic in Arms Regulations (ITAR) for unlawfully exporting defense articles and defense services without a license. He had been working on an Air Force contract for the development of plasma actuators for use in controlling the flight of military drone aircraft. Roth took certain technical data associated with that work with him on his laptop computer while traveling to China to lecture at universities there. He also disclosed technical data to two students at the University, one a national of China and the other a national of Iran, who worked with him on the contract.

On appeal, Roth argued that the technical data were not defense articles or defense services because the contract contemplated that the plasma actuators would be tested on commercial aircraft before being used on military aircraft. The Court of Appeals, citing a Seventh Circuit ruling, *United States v. Pulungan*, 569 F.3d 326, 328 (7th Cir. 2009), held that the designation of items as defense articles or defense services was not subject to judicial review, but that the court could review whether the information in question about the plasma actuators fell within the ITAR definition of technical data. The Court of Appeals held that the information did constitute technical data because the ultimate use for which the plasma actuators were being developed was military.

Roth also argued on appeal that the convictions resulting from his travel to China with technical data on his laptop were erroneous because he never opened the electronic file while traveling and could not have known its contents until after his return to the United States. The Court of Appeals rejected this argument, holding that Roth knew that the information loaded on his laptop included export-controlled technical data, and that taking the technical data to China was a violation of law even if Roth did not show the data to anyone while he was in China.

The *Roth* case underscores how crucial it is that universities, faculty members, and student researchers be familiar with the application of US export control laws in the context of academic research and consulting. Universities should have in place export control policies that are disseminated to relevant faculty, staff, and students. Appropriate training programs and other safeguards should be instituted to ensure that the policies are effectively implemented. Faculty members should take principal responsibility for export control compliance associated with research and consulting projects that they lead, including responsibility for compliance by students and staff working under their supervision.

As the *Roth* convictions demonstrate, exportation can occur by means of disclosure to foreign nationals even if the nationals are located in the United States, but it can also occur by means of travel with technical data on a laptop even if those technical data remain under the traveler's control. Such activities are commonplace in the academic setting, but they are fraught with potential export control violations and should be undertaken with close attention to the export control laws. ◆

The United States, United Nations, European Union and United Kingdom Impose Sanctions on Libya

For an overview of the sanctions imposed by the UN, US, EU and UK at the end of February 2011, see Mayer Brown LLP's Legal Update of March 1, 2011.

The various sanctions programs continue to develop and additional individuals and entities have been sanctioned. Most recently, on April 8, 2011, OFAC issued General License No. 4, which provides guidance with respect to investment funds in which there is a blocked, non-controlling, minority interest of the Government of Libya. ◆

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