

US Announces Record-Setting Penalties for Violations of Export Controls and Economic Sanctions

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On March 7, 2017, the United States announced that China's Zhongxing Telecommunications Equipment Corporation and ZTE Kangxun Telecommunications Ltd. and their respective affiliates (collectively, ZTE) had agreed to a record combined civil and criminal penalty of \$1.19 billion for exporting telecommunications equipment to Iran and North Korea in violation of the Export Administration Regulations (EAR), the Iranian Transactions and Sanctions Regulations (ITSR) and the International Emergency Economic Powers Act (IEEPA).

ZTE entered into separate settlement and plea agreements with the U.S. Department of Commerce's Bureau of Industry and Security (BIS), the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC) and the U.S. Department of Justice (DOJ). In announcing the agreements, high-ranking U.S. officials, including the secretary of Commerce, the secretary of the Treasury and the attorney general, emphasized that the case and settlements are indicative of the Trump administration's aggressive approach to economic sanctions and export controls enforcement and should be taken as a signal of the administration's future enforcement posture.

The settlement marked the largest penalty ever imposed by BIS (\$661 million) and OFAC's largest settlement to date with a nonfinancial institution (almost \$101 million). If the criminal plea agreement with DOJ is approved by a federal judge, the combined \$1.19 billion in penalties would be the largest fine and forfeiture ever levied by the U.S. government in an export control case.

Background

According to the documents released by DOJ, BIS and OFAC, between 2010 and 2016, ZTE conspired to evade the U.S. embargo against Iran to obtain business deals with Iranian entities, including entities affiliated with the government of Iran, and supplied U.S.-origin equipment and software needed to build the backbone of large-scale telecommunications networks in Iran. In particular, the DOJ factual resume and the settlement documents state that ZTE exported to Iranian entities U.S.-origin items that included routers, microprocessors, servers, databases and other items listed on the Commerce Control List (CCL) and which also were subject to regulations administered by OFAC. The documents provide that to facilitate evasion of U.S. sanctions and export controls, ZTE used another controlled Chinese company acting in concert with ZTE to procure equipment and software from the United States without detection by the U.S. regulators.

In addition, the BIS settlement revealed that ZTE procured parts and components subject to the EAR and incorporated these parts and components into telecommunications items that ZTE transferred from its facilities in China to agents of a North Korea state-owned entity, knowing that the items would be shipped to North Korea without the required U.S. government authorization. In so doing, ZTE committed 283 separate violations of the EAR.

U.S. law enforcement agencies first began investigating ZTE in 2012. During the course of their investigation, the agencies determined that ZTE knowingly misrepresented that it had stopped shipments to Iran as of March 2012 and was no longer violating U.S. export control laws. According to the DOJ factual resume, ZTE also misled the U.S. government by deleting and concealing information from the outside counsel and forensic accounting firm that ZTE had retained with respect to the investigation.

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BIS Settlement

As part of the settlement with BIS, ZTE agreed to pay a penalty of \$661 million (of which \$300 million is suspended for a seven-year probationary period). ZTE also agreed to active audit and compliance requirements designed to prevent and detect future violations, and a seven-year suspended denial of export privileges.

In announcing the BIS settlement, Commerce Secretary Wilbur Ross stated: “[w]e are putting the world on notice: the games are over. Those who flout our economic sanctions and export control laws will not go unpunished — they will suffer the harshest of consequences.” He further emphasized that under President Donald Trump’s leadership, “we will be aggressively enforcing strong trade policies with the dual purpose of protecting American national security and protecting American workers.”

OFAC Settlement

ZTE agreed to pay \$100,871,266 for apparent violations of the ITSR. The total value of the 251 transactions constituting the apparent sanctions violations was \$39,622,972. However, because OFAC determined that ZTE did not make a voluntary self-disclosure and the apparent violations constituted an egregious case, both the base civil monetary penalty and the statutory maximum civil monetary penalty for the apparent violations amounted to \$106,180,280.

OFAC emphasized in its enforcement notice that “[f]rom on or about January 2010 to March 2016, ZTE’s highest-level management developed, approved, and implemented a company-wide plan that utilized third party companies to conceal and facilitate ZTE’s illegal business with Iran.” Furthermore, OFAC pointed out ZTE’s “surreptitious” and “willful” conduct, highlighting that after informing the U.S. government it had wound down its Iran-related activities, ZTE’s highest-level management decided to resume the Iran business in 2013. OFAC concluded that ZTE “systematically undermined the integrity of the sanctions program objectives.” It noted that ZTE is a sophisticated and experienced company with global operations and routine dealings

with goods, services and technology subject to U.S. laws, yet it did not have or did not enforce a sanctions compliance program.

Treasury Secretary Steven Mnuchin also underscored that the ZTE settlement should be viewed as an indication of the administration’s enforcement posture, stating that the “settlement is OFAC’s largest ever against a non-financial entity and sends a powerful message that Treasury will aggressively pursue any company that willfully violates U.S. economic sanctions laws and obstructs federal investigations of such violations.” He went on to emphasize that “Treasury will continue to coordinate its efforts with other federal agencies — including [DOJ] and the U.S. Department of Commerce — in order to prevent sensitive or controlled U.S.-origin goods from being illegally shipped or exported to sanctioned countries or parties.”

DOJ Plea Agreement

Separately, ZTE has agreed to enter a guilty plea in connection with the related criminal investigation and to pay a \$430,488,798 penalty to the United States for conspiring to violate IEEPA by unlawfully exporting U.S.-origin items to Iran, obstructing justice and making a material false statement. According to court documents, ZTE took steps to conceal information from and mislead the U.S. government. Attorney General Jeff Sessions stated that ZTE “not only violated export controls that keep sensitive American technology out of the hands of hostile regimes like Iran’s — they lied to federal investigators and even deceived their own counsel and internal investigators about their illegal acts.” And, similar to his counterparts at the Departments of Treasury and Commerce, Attorney General Sessions emphasized that the case “makes clear that our government will use every tool we have to punish companies who would violate our laws, obstruct justice and jeopardize our national security.”

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