Export compliance risks in the supply chain

By Darryl Anderson
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The potential impact of trade wars dominates the headlines. Savvy shippers also know that expanding markets through international trade requires knowledge of and adoption of best practices to address trade issues. Professional organizations such as the Canadian Institute of Traffic and Transportation recognize that the risks associated with compliance failure, even unintentionally, can have grim consequences. For that reason, CITT's October 2018 Canadian Logistics Conference features a session on the topic of export compliance featuring Kevin Riddell, Director, International Logistics for Tremco Incorporated. Depending on the misbehaviour, exporters can be subject to fines, audits, seizures, inspections, investigations, loss of market access and even imprisonment. This article will focus on ways to address export compliance risks in the supply chain.

Export controls overview

Export Development Canada summarizes trade "compliance" as the process used by companies to observe the laws and regulations that govern its international business operations. Many of these rules are established by national governments to manage their countries' trade with other nations (such as setting rates of duty), while others are created to fulfill the requirements of international trade agreements.

Riddell tells shippers that two key considerations shape the nature of export controls. The *Export and Import Permits Act* (EIPA) permits the Federal Cabinet to establish the Import Control List (ICL), the Export Control List (ECL), the Area Control List (ACL), and the Automatic Firearms Country Control List (AFCCL). For each one of these lists, the EIPA sets out criteria that govern the inclusion of goods, technologies or countries on the

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respective lists. Control over the flow of products and technology contained on these lists or to the specified destinations is affected through the issuance of import or export permits.

The Minister of Foreign Affairs and the Minister of International Trade traditionally divide responsibility for the EIPA. Through an exchange of letters, the Minister of Foreign Affairs has asked the Minister of International Trade to take responsibility for import and export controls implemented for economic and trade-related reasons. The Minister of Foreign Affairs retains decision-making authority for controls over military, dual-use and strategic goods and technology, while first seeking the views and recommendations of the Minister of International Trade for specific sensitive applications.

Export Control List

The Borden Ladner Gervais *Pocketbook on Canadian Export Controls* advises that residents of Canada are not permitted to export certain types of products or technologies, specific products of U.S. origin, to certain destination countries or identified terrorist individuals or groups without first obtaining an export permit. Therefore, a clear understanding of the rules that govern international trade is vital.

The Export Control List sets out a variety of items and technologies that require permits for export, regardless of their export destination. The Export Control List is organized into seven groups as follows:
- Group 1: Dual-Use List
- Group 2: Munitions List

Kevin Riddell, Director, International Logistics, Tremco Incorporated, will be speaking at the CITT Conference in October in Vancouver.

- Group 3: Nuclear Non-Proliferation List
- Group 4: Nuclear-Related Dual-Use List
- Group 5: Miscellaneous Goods
- Group 6: Missile Technology Control Regime List
- Group 7: Chemical and Biological Weapons Non-Proliferation List

Analysis of the export permits issued for both non-strategic and strategic commodities reveals that softwood lumber, clothing/textiles and logs, and munitions, dual-use, and other goods are just some of the most frequent goods covered by the regime. The major international destination of Canadian strategic export permits issues in 2017 was the United States, Europe and Asia.

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Drivers of change in export controls

On July 12, 2017, the Government of Canada circulated changes to the Export Control List. The Order came into effect on August 30, 2017. Cyndee Todgham Cherniak founding lawyer of LexSage, a boutique international trade law and sales tax firm, indicated that the ECL Order added new export controls and changed a significant number of existing export controls. Changes were made to all Groups. Additions were made to all but Group 5.

The changes to both the Export Control List and the Export Controls Guide do not take place in a vacuum. Key developments in 2017 were legislative amendments to EIPA, the Comprehensive Economic and Trade Agreement and Bill C-47: An Act to amend the *Export and Import Permits Act* and the Criminal Code (amendments permitting the accession to the Arms Trade Treaty). The changes and additions were also made in response to those consultations and changes to Canada's international obligations in/with the Wassenaar Agreement (December 2015), Nuclear Suppliers Group (June 2015), Missile Technology Control Regime (October 2015) and Australia Group (June 2015).

Riddell stresses the fact that unanticipated events such as the Saudi Arabia/Canada diplomatic row of the summer of 2018 can also test shippers' export compliance readiness and a proactive approach to compliance is required.

Export control supply chain best practices

Shippers should undertake an internal export compliance review. Riddell asserts that the internal review should check all the export products being shipped against the Export Control List or whether any of the export destinations are subject to the Area Control List or economic sanctions. "Paying special attention to US origin rule 5400 is important," said Riddell.

Firms should also implement and fine tune their internal export compliance program. The program should, amongst other things, have executive buy in, identify an export compliance manager, establish a record-keeping policy, establish an internal audit procedure, set out internal training requirements and confirm the processes relating to export permit applications.

Todgham Cherniak stated: "It is important to understand Canada's export controls and carefully review the additions and changes. The most time-consuming step is a review of one's exports and transfers to identify controlled goods and technology (including components of products to be exported or transferred). It is not just physical exports (i.e., sending something by courier, ship, air, etc. from Canada to a place outside Canada) that are covered by Canada's export controls. Transfers, in the form of server access, uploads and downloads (e.g., Dropbox) USB key/DVDs/CD-Roms, emails, telephone conversations, technical assistance and services, etc. are covered by Canada's export controls.

Another step is to update computerized systems to ensure an export permit is obtained before the export or transfer of all controlled goods or technology.

Updating compliance policies and programs and educating the critical people in an organization about the changes to Canada's export controls laws and the compliance program is a vital best practice, according to Todgham Cherniak.

It may also be necessary to contact agents and representatives outside Canada (including subsidiaries) to inform them of the changes to Canada's export controls laws and train them to follow compliance programs.

Riddell cautioned that "dual-use" lists contain products and technologies that many companies would not expect to be subject to export controls. Regardless of whether or not products and technologies are sold for military purposes, they may be subject to Canada's export control regime. Canada controls the export of "dual-use" products and technologies.

Dual-use items include products and technologies associated with a variety of advanced materials, electronics, computers, telecommunications, sensors, lasers, navigation, avionics, marine equipment and technology and propulsion. Examples of dual-use items include software and hardware that use certain types of encryption, optical switches, optical fibre, certain digital video camera technology and "heads-up display" technology.

Riddell alerts shippers to the fact that Canadian shippers may also need to concern themselves with United States extraterritorial concerns. The U.S. export control legal framework governs not just American exports, but exports of American goods or by American technology.

Riddell provided an example of the legal reach of the United States when a Canadian national was sentenced by the U.S. District Court in Seattle to serve 42 months in prison for conspiracy to export restricted goods and technology to Iran on August 20, 2018.

If a shipper's products or technologies are related to advanced materials, encryption, electronics, computers, telecommunications, sensors, lasers, navigation, avionics, marine or propulsion then there is a need to review the Export Control List to determine if their product require an export permit.

Conclusion

Political tensions or significant changes to the Export Control List or Canada's Export Controls Guide indicate to shippers that it is necessary to anticipate and understand the changes and update systems used to ensure compliance with the Export and Import Permits Act. Riddell also suggests that professional education and networking offered by CITT and others is an essential best practice for managing supply chain export compliance risk because knowledge is the backbone that supports the implementation of all other best practices.

Darryl Anderson is a strategy, trade development, logistics and transportation consultant. His blog Shipping Matters focuses on maritime transportation and policy issues.