

The Value And Limitations Of Trade Compliance Policies

By **Eric Sandberg-Zakian** (March 2, 2018, 11:16 AM EST)

Companies around the world are increasingly paying eye-popping penalties to settle allegations that they have violated U.S. economic sanctions or export controls. Last year, the Chinese telecom equipment company ZTE Corp. agreed to penalties of just under \$1.2 billion in a combined civil and criminal settlement with the U.S. departments of Commerce, Treasury and Justice in connection with an alleged conspiracy to sell products subject to U.S. export control jurisdiction to Iran. In 2014, the French bank BNP Paribas agreed to pay \$8.9 billion in a combined civil and criminal settlement with the Treasury and Justice departments for violating sanctions restricting financial transactions involving Cuba, Sudan and Iran. Some of the largest settlements involve violations that allegedly occurred over many years during which the defendants' compliance teams repeatedly missed opportunities to uncover and remediate compliance lapses.



Eric Sandberg-Zakian

It follows that getting employees to report potentially problematic transactions and ensuring that in-house attorneys and compliance professionals respond by investigating appropriately can mitigate trade compliance enforcement risk by stopping ongoing violations as soon as possible and demonstrating to regulators that the company is proactive about catching and remedying compliance lapses. However, the measures that will make a favorable impression on primary regulators in civil enforcement actions may make little difference to criminal prosecutors. Thus, in a world of increasing joint civil and criminal trade controls enforcement, taking a thorough and holistic approach to complaint reporting and investigation is crucial.

Policies on Reporting and Investigation in Civil Enforcement Cases

For many companies, messaging to employees about reporting and investigating problematic transactions starts with the corporate trade compliance policy or trade compliance manual. As the foundational document on which a trade compliance program is built, a policy or manual often articulates a commitment to identifying, preventing and remediating violations of law or policy. In the most common trade controls enforcement context — a voluntary disclosure and corresponding civil investigation by a primary regulator — the existence and content of that policy or manual is often, in and of itself, key evidence that can persuade a regulator to resolve the matter leniently.

Policies on reporting problematic transactions vary in two main respects — specificity and voluntariness. With respect to specificity, some policies simply instruct employees to look out for and report potential

violations, while other policies describe in detail the circumstances in which a report is required, the proper way to make a report, the proper internal audience for the report, and how the compliance team is expected to respond and investigate. With respect to voluntariness, some policies merely encourage employees to report and investigate problematic transactions, while others require them to do so.

Policies that provide specific instructions for reporting and make reporting and investigating mandatory offer great value. They increase the likelihood that transactions with red flags or potential past violations that come to an employee's attention will be escalated to the right compliance personnel in time to prevent a violation or remedy a shortcoming in the company's controls. In the absence of specific instructions, employees are more likely to report red flags to others in the company who are not equipped to handle them correctly. In the absence of a mandatory reporting requirement, employees are more likely to underestimate the significance of a compliance issue and fail to raise it to those who would recognize its importance.

Another advantage of specific, detailed and mandatory reporting policies is that primary trade controls regulators tend to look favorably on them. The U.S. Department of Treasury administers U.S. economic sanctions, while the departments of State and Commerce administer U.S. export controls, and all three agencies conduct enforcement investigations of possible trade controls violations. In and of itself, a policy that requires reporting of problematic transactions and details how to make a report will suggest to regulators that the company is serious about identifying and remediating violations.

Better yet, in the event of a careless or even intentional violation, a strong policy can help convince a regulator that the violation was an isolated incident perpetrated by rogue employees. Primary trade controls regulators at Treasury, State and Commerce are often reasonably sympathetic to failures by individual employees. If the company can show that ongoing violations were allowed to continue in direct contravention of corporate policy, regulators may be less likely to conclude that the company suffered from a pervasive culture of noncompliance or that senior business and compliance managers knew about but did not stop long-running violations.

Civil trade controls enforcement actions, especially those initiated by a voluntary disclosure in which the agency's primary source of facts is a narrative drafted by company counsel, often allow companies to emphasize particular mitigating factors. Although agencies can and do issue subpoenas for documents, civil trade controls investigations rarely involve large-scale email collection and production (in contrast to criminal investigations, in which such document work is the norm). Thus, when primary regulators assess the root cause of a violation and its connection to the broader corporate compliance culture, they generally rely on the company's written narrative and accompanying documents.

Under those circumstances, regulators can be expected to give great weight to a policy that requires employees to report violations, requires compliance personnel to investigate those violations, and lays out detailed instructions for how to go about reporting and investigation. Regulators may view the policy as reflective of corporate values and culture, and will generally not have access to the massive documentary and testimonial record that would be required to assess whether the company truly implemented the policy in practice, or merely issued it on paper. In sum, a mandatory and detailed reporting and investigation policy can, in and of itself, serve as a major risk mitigator in civil enforcement actions.

The Broader View of Reporting and Investigation in Criminal Enforcement Cases

Unfortunately for corporate defendants, many government investigations of serious trade controls

violations are conducted not just by primary regulatory agencies, but also by federal prosecutors from U.S. Attorney's Offices and the DOJ's National Security Division. And criminal investigations often look behind corporate policies to a fuller record of email correspondence, other company data, and witness interviews. As a result, prosecutors can generally be expected to give less weight than civil regulators to a policy that requires employees to report and investigate and details how to do so.

With a fuller record at their disposal, prosecutors will have the means and inclination to look past the paper provisions of a policy and assess how it operates in practice. Are employees aware of the policy? Do they follow it? What has the compliance department done to explain the policy and ensure it is followed? Is compliance with the policy audited? If the company discovers that someone acted in contravention of the policy, how does the company respond? In a criminal investigation, a policy is less likely to serve as a central and highly influential piece of evidence. More commonly, it is simply the starting point for an inquiry into a company's compliance practices.

In fact, in the criminal context, sometimes the existence of a policy imposing mandatory reporting and investigation obligations, and providing detail on how to go about those tasks, can even be harmful if a company does not sufficiently implement it. Prosecutors may be inclined to view an employee who fails to report as required or a compliance team member who fails to investigate as required to be acting with a problematic state of mind. It is much easier to conclude that a compliance lapse was not merely a mistake but a deliberate unlawful act if an employee also violated clear, written duties to report or investigate the lapse.

In assessing whether to pursue a criminal case against a company, prosecutors will still care about whether the culpable individuals acted as rogue employees or engaged in misconduct of a kind that was commonly tolerated or encouraged at the company. But they generally have more information at their disposal to assess the corporate compliance culture beyond a mere written policy. Thus, the specter of possible criminal trade controls investigations makes it imperative that companies not just adopt, but also fully implement reporting and investigation policies. Training, messaging, auditing and, in the case of noncompliance, discipline all must be high priorities following adoption of a policy.

A policy that is not properly implemented or reliably followed becomes a source of risk in a criminal case. That risk is especially pronounced when compliance personnel fail to undertake required investigation or do not follow the investigatory process detailed in a policy. Those employees surely knew better, prosecutors may conclude, and must have breached their duty to investigate because they were either willfully blind to compliance lapses or active participants in a broader conspiracy. Prosecutors may ask themselves (and ultimately jurors): Could these employees have been pressured not to investigate? Were they instructed to drop the investigation? How could anyone in their position have stood by and done nothing, knowing what the policy required of them, unless they were part of a deliberate cover-up?

The different role a policy can play in civil and criminal cases reflects a broader difference between the two types of enforcement actions. Establishing that an individual wrongdoer was a rogue employee is a more difficult or riskier proposition in a criminal case. Civil regulators often lack the documents and investigatory resources to refute the company's position that it did not accept or encourage the employee's wrongdoing. Prosecutors are better positioned to develop evidence to the contrary. If they do develop such evidence, a mitigating factor put forth by the company (that an individual employee acted wrongfully and in contravention of established corporate policy) may become a key piece of the government's case because it helps prosecutors carry their mens rea burden and establish that the company acted willfully (i.e., with knowledge the act was unlawful).

Put differently, once prosecutors conclude that a company did not prioritize compliance in good faith and they exercise their discretion to try to attribute bad acts by an employee to the company, the rogue employee defense can turn from a defendant's shield into a prosecutor's sword. If prosecutors believe that an employee's actions were done with the knowledge and support of the company as a whole, it is no longer helpful to prove the employee knew her actions contravened corporate policy. Instead, it can become one more piece of evidence showing a criminal state of mind by the employee and the company alike.

In a time of increasingly aggressive criminal trade controls investigations by the DOJ, companies should be aware that policies requiring, and detailing processes for, reporting and investigation cannot mitigate criminal enforcement risk. A policy, in and of itself, is likely to serve as an important mitigating factor in a straightforward civil matter before a primary regulator. In the face a more searching grand jury investigation by the DOJ, however, how the company implemented the policy will be far more important. Thus, a compliance or legal department responsible for such a policy should ensure that employees know about the policy, are trained on how to comply with it, actually do comply with it, and are disciplined if they do not. Otherwise, if a criminal investigation comes along, the policy will be of little help, and may even become a liability.

Eric Sandberg-Zakian is an associate with Covington & Burling LLP in the firm's Washington, D.C., office.

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