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Controlling U.S. Export Controls: *A Canadian/Mexican Buyer's Guide to Negotiating a U.S. Export Control Clause*

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In recent years the U.S. government has stepped up enforcement of export control laws to minimize threats to its national security. The government's increasing scrutiny of international trade and business—including with its closest neighbors Canada and Mexico—from a national security perspective requires that U.S. businesses, ever more examine their export contracts even more carefully. Some U.S. sellers, in an attempt to reduce the potential for liability, draft export control clauses that may place substantial and costly burdens on the buyer, which could include, in some cases, requiring buyers to track their clients' sales activities, limit their own ability to distribute controlled information within their non-U.S. organization, and understand and apply the complex U.S. export control regime. Buyers need to understand to what they are agreeing to in an export control clause, knowing that in most cases there is room for negotiation.

The questions foreign buyers ask their lawyers when they first review an export control clause include: "can they ask for this?" and "is this language really required by U.S. law?" The quick answer to both is "yes, to some extent." Knowing to what extent, however, is the key to negotiating a balanced and realistic export control clause. U.S. companies *are* required to control the export of certain U.S. products and technology to avoid having them fall into the wrong hands. Anything they do in this regard beyond what is required by law will be viewed favorably by U.S. export control authorities. U.S. law does not require specific language be included in the contract, so it is easy to overreach and request from foreign buyers more than what is necessary to comply with U.S. law. There are several moving parts in an export control clause. For the foreign buyer, understanding those parts will help avoid acquiring

unnecessary costly and even impossible obligations.

Below we provide examples of some overreaching, but still fairly typical, export control clauses:

A clause that conditions all of the buyers' exports to seller's approval could read as follows:

Example 1

"BUYER understands that the SELLER's right to furnish U.S. information or technology, or the direct product thereof, is subject to the continuing approval of U.S. governmental authorities. BUYER agrees not to export technology or information provided by SELLER under this Agreement without the prior written consent of SELLER."

A clause that places the burden on the buyer to understand and comply with U.S. regulations could state as follows:

Example 2

"BUYER acknowledges that it is familiar with U.S. laws and regulations concerning the export or re-export of U.S. information and technology, or the direct product thereof, to unauthorized destinations and persons and BUYER agrees to abide by all such regulations in respect of all information or technology supplied by SELLER under this Agreement. BUYER further agrees not to export, directly or indirectly, the SELLER's technology or information to any restricted or prohibited destination under applicable U.S. regulations unless a request to do so has been submitted by SELLER and until such request is approved in writing by the appropriate U.S. Government Agency."

A more direct, but still very comprehensive, export clause could read as follows:

Example 3

"BUYER agrees not to disclose or export, either directly or indirectly, any technology or information, or the direct product thereof, acquired by it pursuant to this Agreement to any destination or person if such disclosure or export is prohibited by the laws and regulations of the United States of America. This paragraph shall survive the termination of this Agreement."

All of these clauses have space for negotiation. The objective is to reduce the burden on the buyer while still allowing the seller to comply with U.S. export regulations. The clause should not be a mechanism to limit, monitor or control the buyer's activities beyond what is strictly required to control protected information or technology. The negotiable components in export control clauses normally include:

1. the definition of the *product, technology or information that is controlled*;
2. the definition of "export";
3. the requirement of *familiarity and applicability of U.S. law*;
4. the inclusion of "indirect export"; and
5. the *survival of the export control clause* after termination of the Agreement.

Using the examples, below we provide some advice in the application of these components.

Define What Is Controlled

The parties to the agreement need to know if the product, information or technology that is the subject of exportation under the agreement (hereinafter the "subject item") is in fact controlled under the U.S. export control regime. Example 1, and more ambiguously example 2, fail to separate subject items which are legally controlled under applicable U.S. regulations from those which are not. If the seller's obligation is to protect only those subject items which are controlled under U.S. law, why is it necessary that all of the seller's technology or information be controlled under the contract? Extending control obligations on the buyer for everything the seller provides, regardless of its nature, could seriously limit what the buyer can do with the acquired product, information or technology. It is important that the contract provides specific guidance as to what is controlled and subject to the clause and what is not. Example 3 does this by only limiting re-export activity that is restricted or prohibited under applicable U.S. law, which is much more helpful. Sometimes, however, under U.S. export control laws, it is not always evident what is actually controlled and in some situations the analysis may require an opinion from the authority. The buyer, therefore, could request that the application of the clause extend only to information or technology that can be demonstrated to be controlled under U.S. law. Note

that parties may request from U.S. authorities a written confirmation as to whether a subject item is controlled under applicable regulations. This request could come at any time before or during the application of the agreement, but keep in mind that the process may be burdensome and could last several months.

Understand the Definition of "Export"

Both parties, but specially the buyer, need to have a very clear understanding of what the term "export" means and how will this affect the buyer's operations after acquiring the controlled information or technology. Buyers should be aware that U.S. regulations and case law are quite comprehensive as to what is an "export" and what is "deemed" an export. The U.S. legal terms for "export" includes activities that would not normally be considered as such in other countries. "Export" includes, for example, verbal or written transmissions or communications (phone calls or emails) with persons located in other countries, even if the recipient is a U.S. person, or transmission or communications carried out in the United States if the recipient is a foreigner. The definition covers activity such as emailing technical drawings to company personnel; presenting products or information in international trade shows; accepting foreigner visits to the factory floor or offices; and carrying replacement parts or a laptop containing controlled information on a commercial flight. If the export control clause, as in examples 2 and 3, prohibits the buyer from exporting the goods to prohibited destinations and persons, the buyer needs to be aware what and who those destinations and persons are, an effort which requires consistent review of U.S. laws, regulations and Executive Orders. Using the U.S. definition of "export," in the case of example 1, the buyer would technically have to request written consent from seller before carrying out even simple types of communication with non-U.S. persons about the acquired information, technology or product within or outside the company. Overall, it is very important for a buyer, prior to agreeing to an export control clause, to understand and clarify with the seller what "export" really means in the context of the export controls in the agreement, as the term "export" in a U.S. court will likely go far beyond what may otherwise be commonly understood in commercial practice.

Limit Requirements for Buyer to Apply U.S. Export Control Law

Export clauses, as in example 2, sometimes require the buyer to understand and apply U.S. export control laws and regulations. The obligation is practical for the seller as it is then clear that both the seller and the buyer are subject to the same obligations, and hence, in the event of a suspected U.S. export control breach, both would share responsibility.

It also ensures that the foreign buyer will rise to the level of being a U.S. person for purposes of controlling exports. But requiring a foreign buyer to be familiar with and apply U.S. export control laws to subject items could be a substantial and unnecessary burden for the foreign buyer. The U.S. export control regime is generally complex, extensive and often times ambiguous. Furthermore, it is constantly evolving. If the buyer agrees to this obligation, it needs to get ongoing representation of experienced U.S. counsel to make sure its post-contractual activities are not in breach of U.S. export controls. To avoid having to commit to the entire U.S. export control legal framework, while giving comfort to the seller, the parties could perhaps agree to specific language in an attachment that sets forth certain obligations which, based on U.S. law, may be relevant to avoid undesired export and re-export activity. The seller would disclose to the buyer any important changes to U.S. law during the term of the agreement (e.g., the addition of a prohibited destination) and incorporate these changes as necessary into the contract, in this way removing the burden and complications from the buyer of having to be up-to-date with the laws and the jurisdiction of a country that is not its own.

Define and Limit “Indirect” Exports

Clauses in examples 2 and 3 above seek to control a buyer from carrying out “indirect” exports and/or re-exports. An indirect export, in very general terms, is one carried out through a third party or buyer. By agreeing to control indirect exports, the buyer would be responsible for any sales to prohibited destinations made by its clients, buyers, intermediary sellers and/or consumers who receive subject items. If the U.S. seller is prohibiting the buyer from carrying out indirect exports, the parties need to agree what this obligation entails. If the buyer makes a sale of the subject item to a client, will the buyer be responsible for controlling what that client does with the item? How far down the chain is this requirement effective? Will the buyer need to know what its *client’s clients* do with subject items? Is the buyer in a position to monitor and control the subject item effectively in these cases? And will the buyer be liable if one of its clients ships the subject item to a prohibited destination even if the buyer applied all reasonable controls? If the buyer agrees to be responsible for indirect exports to prohibited destinations or persons, it needs to be able to actively and systematically limit, within its organization, the risk of these exports occurring. U.S. companies normally involved in exporting commonly have sophisticated export control monitoring and compliance systems in place tailored to their organization to avoid such export control risks. One option to reduce the burden on the buyer may be to limit its obligations related to indirect exports to requiring its

clients, or other persons it discloses the subject item to, to provide written confirmation that they will not disclose or resell any subject items to the list of prohibited destinations and persons. This may give U.S. seller sufficient comfort while removing from the buyer the burdensome duty of tracking and being responsible for its client’s (and potentially event its client’s clients) activities.

Limit the Survival Clause to the Obligations Effective on the Date of Termination of the Agreement

Example 3 provides that the export control clause will survive the termination of the agreement. In other words, parties will still be subject to the clause even if, for any reason, the agreement is terminated. This is a reasonable request given the potential for creating a loophole to adequate export control by allowing the buyer to disregard any control by terminating the agreement. The catch for the buyer is that, if it commits to U.S. export controls even after termination of the agreement, it needs to remain up to date in the developments of U.S. law and what it considers a prohibited destination even after the expiration of the agreement. It may be important for the buyer, then, that if the export control clause will survive the agreement, the parties agree that the export control obligations be limited to those in effect at the time of termination of the agreement, so as to avoid having said obligations expand—something that could happen in different and significant ways—after termination of the agreement. Furthermore, depending on what the actual export control obligations for the buyer are, it may be advisable to put a deadline on how long these obligations will survive, as a terminated agreement could easily become forgotten through changes in key staff, or technology and information could become old or get commingled with other information or technology, making it difficult, over time, to monitor and control, while leaving the buyer perpetually vulnerable to a lawsuit.

These are only some of the most important points to keep in mind when negotiating export control clauses. If faced with an export control clause, it is important that both parties, but particularly the buyer who is taking full responsibility for controlling the information it receives, understand the obligations it is acquiring and evaluate carefully its abilities to comply with such obligations.

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