

I.E. Canada Controlled Export Webinar Series

Session 2 – Economic Sanctions: Mitigating Your Legal and Reputational Risk

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Growing Impact of Canadian Trade Controls

- ▭ what's driving this?
 - ▭ since 9/11, new emphasis of Canadian authorities on security (vs. government revenues)
 - ▭ more recently, increased penalties, enforcement by U.S. authorities
 - ▭ pressure from U.S. affiliates, suppliers and customers (and U.S. government)
 - ▭ penalty exposure
 - ▭ operational exposure
 - ▭ reputational exposure
- ▭ Canadian companies are now more concerned than ever before about whom they deal with, where their products and technology end up, and who uses their services

What Are Canada's Trade Controls?

- ↪ export and technology transfer controls
 - ↪ Import Control List
 - ↪ Export Control List, Area Control List
 - ↪ new brokering controls
- ↪ **economic sanctions**
 - ↪ **Special Economic Measures Act**
 - ↪ **United Nations Act**
 - ↪ **Freezing Assets of Corrupt Foreign Officials Act**
 - ↪ **Justice for Victims of Corrupt Foreign Officials Act (Sergei Magnitsky Law)**
 - ↪ **Criminal Code (“terrorist groups”)**
 - ↪ **blocking orders and anti-boycott laws and policies**
- ↪ domestic industrial security
 - ↪ Defence Production Act, Controlled Goods Program
- ↪ other legislation of potential concern
 - ↪ anti-bribery law (Corruption of Foreign Public Officials Act, US FCPA, UK Bribery Act)
- ↪ “compliance convergence”

Canada's Economic Sanctions Regime

- ▭ Special Economic Measures Act and United Nations Act can include:
 - ▭ ban on providing goods, services, technology
 - ▭ assets freezes – cannot deal with listed individuals, companies, organizations
 - ▭ ban on facilitation
 - ▭ monitoring and reporting obligations
- ▭ Freezing Assets of Corrupt Foreign Officials Act
 - ▭ Ukraine and Tunisia
- ▭ new Justice for Victims of Corrupt Foreign Officials Act (Magnitsky Law)
- ▭ application to persons in Canada and Canadians outside Canada
- ▭ permit process and enforcement (GAC, CBSA and RCMP)
- ▭ **also, Criminal Code – terrorist groups**

Canada's Economic Sanctions Regime

- consequences of non-compliance
 - criminal penalties
 - fines in an amount that is appropriate in the opinion of the Court
 - up to 10 years imprisonment
 - CBSA detention and seizure
 - operational costs
 - reputational costs

Economic Sanctions: Jurisdictions of Concern

Burma/Myanmar

Central African Republic

Democratic Republic of Congo

Eritrea

Iran

Iraq

Lebanon

Liberia

Libya

North Korea

Russia

Somalia

South Sudan

Sudan

Syria

Ukraine (including Crimea)

Venezuela

Yemen

Zimbabwe

Rise of Targeted or “Smart” Sanctions

- ▭ designated or listed individuals and entities, and the entities they own or control, regardless of where you are or they are
 - ▭ country sanctions regulations
 - ▭ Criminal Code – terrorist entities
 - ▭ Al-Qaeda and Taliban
 - ▭ October 2017 Magnitsky Law
 - ▭ involvement in gross violations of human rights
 - ▭ significant corruption
- ▭ mandatory disclosure to RCMP/CSIS

Challenges with Economic Sanctions

- measures take effect immediately – no consultations
- measures change often, in response to developing international events
- measures are “layered”
 - multiple Canadian regulatory regimes
 - measures in the country in which you’re doing business
 - US extraterritorial measures

Challenges with Economic Sanctions

- ↪ significant differences in Canadian administration and guidance on economic sanctions vs the United States and other countries
 - ↪ no FAQs, guidelines, rulings, opinions
 - ↪ limited consolidation of blacklists
 - ↪ no formal voluntary disclosure process
 - ↪ no deferred or non-prosecution agreements

Key Issues in Interaction With US and Other Regimes

- ▭ key recommendations of Canada's House of Commons Foreign Affairs Committee
 - ▭ properly resource and reform the structures for sanctions regimes
 - ▭ comprehensive, publically available, written guidance for public and private sectors regarding interpretation of sanctions regulations
 - ▭ produce and maintain a comprehensive, public and easily accessible list of all individuals and entities targeted by Canadian sanctions containing all information necessary to assist with proper identification
 - ▭ independent administrative process by which designated individuals and entities can challenge in a transparent and fair manner
 - ▭ clear rationale for the listing and delisting of persons

Canada's Autonomous Sanctions: Iran

- ▭ starting in 2010, escalating Special Economic Measures Act measures against Iran culminating in broad trade embargo (May 29, 2013):
 - ▭ included prohibitions against
 - ▭ exporting, selling, supplying or shipping goods, wherever situated, to Iran, to a person in Iran, or to a person for the purposes of a business carried on in or operated from Iran
 - ▭ importing, purchasing, acquiring, shipping or transshipping any goods that are exported, supplied or shipped from Iran, whether the goods originated in Iran or elsewhere
 - ▭ making an investment in an entity in Iran
 - ▭ providing or acquiring financial services to, from or for benefit of a person in Iran
- ▭ over 600 entities and individuals had been designated under Canada's *Special Economic Measures (Iran) Regulations*

Canada's Autonomous Sanctions: Iran

- ▭ effective February 5, 2016, broad trade embargo measures have been removed, leaving **only**:
 - ▭ SEMA prohibitions on activities involving 202 listed persons
 - ▭ SEMA prohibitions on supplying any Schedule 2 items and related technical data
 - ▭ United Nations restrictions
 - ▭ export and technology transfer controls

Canada's Autonomous Sanctions: Iran

- ▭ prohibitions against dealings with listed persons (now 202)...
- ▭ it is prohibited for any person in Canada or any Canadian outside Canada to
 - ▭ (a) deal in any property, wherever situated, that is owned, held or **controlled by** a listed person or by a person acting on behalf of a listed person; [used to be “held by or on behalf of”]
 - ▭ (b) enter into or facilitate any transaction related to a dealing referred to in paragraph (a);
 - ▭ (c) provide any financial or related service in respect of a dealing referred to in paragraph (a);
 - ▭ (d) make any goods, wherever situated, available to a listed person
or to a person acting on behalf of a listed person; or
 - ▭ (e) provide any financial or related service to a listed person **or to a person acting for the benefit of a listed person.**

Canada's Autonomous Sanctions: Iran

- ↯ prohibitions on supplying Schedule 2 items and technology...
 - ↯ it is prohibited for any person in Canada or any Canadian outside Canada to export, sell, supply or ship any of the goods listed in Schedule 2, wherever situated, to Iran, to a person in Iran, or to a person for the purposes of a business carried on in or operated from Iran
 - ↯ it is prohibited for any person in Canada or any Canadian outside Canada to transfer, provide or disclose to Iran or any person in Iran any technical data related to the goods listed in Schedule 2
- ↯ Schedule 2 has 41 categories, including:
 - ↯ aluminum and aluminum alloy products - piping, tubing, fittings, flanges, forging, castings, valves, any unfinished products in any form and any waste or scrap that are made of aluminum and its alloys that are not specified in the *Export Control List*
 - ↯ stainless steel valves, piping, tubing and fittings - any valves, piping, tubing and fittings that are made of stainless steel type 304, 316 or 317 and that are not specified in the *Export Control List*
 - ↯ gold, silver, platinum, palladium, ruthenium, rhodium, osmium and iridium - in addition to specific items made of those metals referred to in these Regulations, all raw, semi-finished or finished forms of those metals or their alloys.

Canada's Autonomous Sanctions: Iran

- ▭ prohibitions against “facilitating” a violation:
 - ▭ it is prohibited for any person in Canada or any Canadian outside Canada to do anything that causes, facilitates or assists in, or is intended to cause, facilitate or assist in, any act or thing prohibited by sections 3 or 4 (prohibitions on dealings with listed persons and prohibited items)
- ▭ requirement to report to RCMP or CSIS:
 - ▭ every person in Canada and every Canadian outside Canada must disclose without delay to the Commissioner of the Royal Canadian Mounted Police or to the Director of the Canadian Security Intelligence Service
 - ▭ (a) the existence of property in their possession or control that they have reason to believe is owned, held or controlled by or on behalf of a listed person; and
 - ▭ (b) any information about a transaction or proposed transaction in respect of property referred to in paragraph (a)

Canada's Autonomous Sanctions: Iran

- ↯ exemptions for listed person restrictions
 - ↯ pension payments to any person in Canada or any Canadian outside Canada;
 - ↯ certain transactions related to diplomatic missions, international organizations with diplomatic status, United Nations agencies, the International Red Cross and Red Crescent Movement, or with certain Canadian NGOs
 - ↯ the transfer of any accounts, funds or investments held on behalf of a Canadian by a listed person on the day on which that person's name was listed to any person who is not a listed person
 - ↯ loan repayments made by a listed person on loans entered into before the day on which that person's name was listed to any person in Canada or any Canadian outside Canada who is not a listed person
 - ↯ the exercise of a right by a person who is not a listed person with respect to a listed person's property that is subject to a lien, a mortgage or security interest, a hypothec or prior claim, or a charge
 - ↯ financial services required in order for a listed person to obtain legal services in Canada with respect to the application of any of the prohibitions

Canada's Autonomous Sanctions: Iran

- ↯ exemptions from goods and technical data restrictions
 - ↯ equipment, services and software that facilitate secure and widespread communications via information technologies, or the provision or acquisition of financial services in relation to such equipment, services and software, provided that an export permit has been issued in respect of any ECL goods
 - ↯ goods used to purify water for civilian and public health purposes, or the provision or acquisition of financial services in relation to such goods; and
 - ↯ any activity, or the provision or acquisition of financial services in relation to an activity, that has as its purpose
 - ↯ the safeguarding of human life,
 - ↯ disaster relief, or
 - ↯ the provision of food, medicine and medical supplies.

Canada's UN Sanctions: Iran

- ↯ Canada's United Nations Act Iran regulations amended in accordance with UN Security Council Resolution 2231
 - ↯ list of designated persons (and regular reporting for FS firms)
 - ↯ very long list of prohibited goods and technology
 - ↯ prohibitions on provision of property and financial services in connection with prohibited items
 - ↯ uranium mining restrictions
 - ↯ shipping and aircraft restrictions
 - ↯ sourcing ban on arms and related materials
 - ↯ prohibitions against facilitation

Export Controls: Iran

- ▭ export and technology transfer controls under Export and Import Permits Act
- ▭ Notice to Exporters No. 196 (Feb 5, 2016): **policy of denial** for transfer of certain Export Control List items:
 - ▭ certain Group 1 dual-use (cybersecurity, sensors, special materials, aerospace and propulsion, etc.)
 - ▭ all Group 2 (munitions), Groups 3 and 4 (nuclear)
 - ▭ certain Group 5 (strategic items)
 - ▭ all Group 6 (missile technology, GPS)
 - ▭ certain Group 7 (chemical weapons materials, containment facilities, human toxins)
 - ▭ exceptions for items for civil aircraft

Canada vs United States Sanctions: Iran

- ↪ new “disconnect” between US and Canadian sanctions against Iran
 - ↪ re-exports/re-transfers of US-origin items to Iran
 - ↪ US takes jurisdiction with as little as 10% US-origin – differs from ECL 5400 test applied by Canadian authorities
 - ↪ Iranian visitors / temporary resident employees access to US technology
 - ↪ are you US-owned or controlled?
 - ↪ OFAC General License H authorizes certain transactions for US-owned foreign entities – now revoked with authorization to wind down until November 4, 2018
 - ↪ involvement of US persons – use of recusals
 - ↪ other US touchpoints

Prosecutions: *R. v. Yadegari*

- ▭ July 6, 2010, first successful prosecution under the Iran sanctions regulations under United Nations Act
- ▭ attempted shipment to Iran through Dubai dual-use pressure transducers
- ▭ could be used in heating and cooling applications as well as in centrifuges for enriching uranium
- ▭ Ontario provincial court judge found that Yadegari “knew or was wilfully blind that the transducers had the characteristics that made them embargoed”
- ▭ also violations of Customs Act, Export and Import Permits Act, Nuclear Safety and Control Act, and Criminal Code
- ▭ sentenced to 51 months imprisonment (slight reduction on appeal)

Prosecutions: *R. v. Lee Specialties Ltd.*

- ↯ first prosecution under *Special Economic Measures Act*
- ↯ attempted shipment of 50 Viton O-rings to Iran (\$15 total value)
 - ↯ although dual-use, these were prohibited goods listed on Schedule 2 to the Iran SEMA regulations
 - ↯ multiple changes in account and shipping addresses
- ↯ detained by CBSA
- ↯ April 14, 2014 guilty plea and \$90,000 penalty

Russia / Ukraine Economic Sanctions Measures

- ↯ designated person restrictions on range of activities involving over 300 listed entities and individuals
- ↯ broad prohibitions – asset freeze
- ↯ financing prohibition
 - ↯ debt financing prohibition (30 or 90 days maturity)
 - ↯ equity financing prohibition
- ↯ prohibitions against supply of listed goods or related financial, technical or other services for use in
 - ↯ offshore oil exploration or production at a depth greater than 500 meters;
 - ↯ oil exploration or production in the Arctic; or
 - ↯ shale oil exploration or production

Russia / Ukraine Economic Sanctions Measures

- ▭ prohibitions on any dealings with Crimea region of Ukraine, including:
 - ▭ investment and related services
 - ▭ importing, purchasing, acquiring, shipping or otherwise dealing in goods exported from the region
 - ▭ exporting, selling, supplying, shipping or otherwise dealing in goods destined for the region;
 - ▭ transferring, providing or communicating technical data or services;
 - ▭ providing or acquiring financial or other services related to tourism

Russia / Ukraine Economic Sanctions Measures

- ▭ export control policy (GAC Export Controls Division)
 - ▭ no permit if material benefit to Russian military

Justice for Victims of Corrupt Foreign Officials Act (Sergei Magnitsky Law)

- ↪ came into force October 28, 2017 - broad prohibitions against engaging in activities involving listed foreign nationals
- ↪ adds new grounds for imposing sanctions:
 - ↪ “gross violations of internationally recognized human rights”
 - ↪ “acts of significant corruption”
- ↪ current listings of foreign nationals
 - ↪ Russia – 30
 - ↪ Venezuela – 19
 - ↪ South Sudan – 3
 - ↪ Myanmar - 1
- ↪ importance of screening all counterparties and all individuals and entities who own or control them

The Cuban Conundrum

- ↯ problem, whether or not you trade with Cuba
- ↯ Canada's expanding economic relationship with Cuba
 - ↯ Canada is one of Cuba's largest trading partners
 - ↯ Canadian exports to Cuba - machinery, agrifood products, sulphur, electrical machinery, newsprint
 - ↯ Canadian imports from Cuba - ores, fish and seafood, tobacco, copper and aluminum scrap and rum
 - ↯ Canada is one of Cuba's largest source of foreign direct investment
 - ↯ Canadian FDI - nickel and cobalt mining, oil and gas, power plants, food processing

The Cuban Conundrum

- ▭ expanding extraterritorial reach of U.S trade embargo
 - ▭ 1962 – imposition of full trade embargo under Trading With the Enemy Act
 - ▭ 1975 – elimination of general license allowing trade by foreign non-banking entities
 - ▭ had to apply for specific license and demonstrate independent operation re decision-making, risk-taking, negotiation and financing
 - ▭ 1990 – Mack Amendment proposed outright prohibition on issuance of licenses to foreign affiliates of U.S. firms
 - ▭ 1992 – Cuban Democracy Act
 - ▭ 1996 – Helms-Burton Act extends aspects of Cuban embargo to Canadian companies that have no connection with U.S. entities

Current U.S. Measures vs. Cuba

- ▭ Cuban Assets Control Regulations
 - ▭ administered by U.S. Treasury' Office of Foreign Assets Control
 - ▭ prohibition on foreign entities owned or controlled by U.S. persons from doing business with Cuba

- ▭ Export Administration Regulations
 - ▭ administered by the U.S. Department of Commerce's Bureau of Industry and Security
 - ▭ requires that a re-export license be applied for where U.S. content is 10% or more

- ▭ Helms-Burton Act
 - ▭ Title III – private right of action vs. “traffickers” in “confiscated property” (right suspended)
 - ▭ Title IV – bar on entry in the United States for traffickers, their spouses and minor children

Canadian Response to U.S. Trade Embargo of Cuba

- ↪ diplomatic
- ↪ NAFTA/WTO?
- ↪ primarily FEMA and the 1996 FEMA Order

The Foreign Extraterritorial Measures Act

- ▭ 1996 “blocking” order
 - ▭ obligation to notify Canadian Attorney General of certain communications
 - ▭ prohibition against complying with certain U.S. trade embargo measures
- ▭ penalty exposure: up to \$1.5 million and/or 5 years imprisonment

The Notification Obligation

“Every Canadian corporation and every director and officer of a Canadian corporation shall forthwith give notice to the Attorney General of Canada of any directive, instruction, intimation of policy or other communication relating to an extraterritorial measure of United States in respect of any trade or commerce between Canada and Cuba that the Canadian corporation, director or officer has received from a person who is in a position to direct or influence the policies of the Canadian corporation in Canada.”

The Non-Compliance Obligation

“No Canadian corporation and no director, officer, manager or employee in a position of authority of a Canadian corporation shall, in respect of any trade or commerce between Canada and Cuba, comply with an extraterritorial measure of United States or with any directive, instruction, intimation of policy or other communication relating to such a measure that the Canadian corporation or director, officer, manager or employee has received from a person who is in a position to direct or influence the policies of the Canadian corporation in Canada.”

FEMA Enforcement Experience

- ↯ there has never been an attempted prosecution of the Canadian blocking order
- ↯ no case law or administrative/prosecutorial guidelines
- ↯ no guidance from the Canadian government
- ↯ numerous investigations - American Express, Eli-Lilly, Heinz, Red Lobster, Wal-Mart and others
- ↯ Wal-Mart's Cuban pyjamas
 - ↯ nationalistic sensitivities

Critical FEMA Conflict Points

- ↯ training programs
- ↯ compliance manuals
- ↯ communications and instructions
- ↯ server accessibility
- ↯ meetings and telephone conversations
- ↯ M&A due diligence
- ↯ contracts – e.g., supply agreements with U.S. companies, intercompany agreements, purchase orders, etc.
- ↯ end-use certificates

Managing the Relationship Between U.S. and Canadian Export Controls and Trade Sanctions

- cannot simply adopt U.S. trade control policies for Canadian operations
- export control and trade sanctions compliance manuals and any related directives should be “home grown”

Managing the Relationship Between U.S. and Canadian Export Controls and Trade Sanctions

- when potential conflicts arise:
 - case-by-case analysis, very context-specific
 - addressing exposure of U.S. citizens in Canada
 - involvement of Canadian and U.S. counsel

- cultural - sovereignty issues particularly sensitive

Canada's Boycott Policy

- ▭ October 21, 1976 federal policy; does not prohibit compliance with international economic boycotts
- ▭ identifies “unacceptable” activities taken in connection with such boycotts
 - ▭ requiring a firm or individual to engage in discrimination based on race, nationality, etc. of another Canadian firm
 - ▭ refusing to purchase from or sell to another Canadian firm
 - ▭ refusing to sell Canadian goods to any country or refraining from purchasing from any country
 - ▭ restricting commercial investment or other economic activity in any country
- ▭ sanction is denial of government support and assistance in such transactions

Provincial Discriminatory Business Practices Legislation

- ▭ Discriminatory Business Practices Act (Ontario)
- ▭ prohibits refusing to engage in business with others where:
 - ▭ refusal is an account of on “attribute” (e.g., geographical location) of the others or of a third person with whom the others do business; and
 - ▭ refusal “is a condition of the engaging in business” of the company making the refusal and another person
- ▭ prohibits entering into a contract in which one party refuses to engage in business with another person on account of an attribute of that other person or of a third person with whom that person conducts business
- ▭ prohibits seeking or providing negative statements of origin
- ▭ requires reporting of requests to engage in discriminatory business practices

Provincial Discriminatory Business Practices Legislation

- penalty/sanction exposure
 - cause of action for damages against person who contravenes
 - banned for providing goods or services to Ontario government for five years
 - up to \$100,000 fine

Potential “Red Flags”

- ▭ Canadian Border Services Agency advises that your transactions or potential customers may require particular scrutiny in the following circumstances
 - ▭ little is known of the customer, lack of information from normal commercial and trade sources on finances and corporate principals
 - ▭ customer reluctant to disclose end-use/end-user information
 - ▭ customer requests unusual payment terms or currencies

Potential “Red Flags”

- ▭ customer does not wish to use commonly available installation and maintenance services
- ▭ order amounts, packaging, or delivery routing requirements do not correspond with normal industry practice
- ▭ the performance/design characteristics of the items are incompatible with the customer’s line of business or stated end-use
- ▭ customer provides only a “P.O. Box” address or has facilities that appear inappropriate for the items ordered

Potential “Red Flags”

- ▭ orders for parts are inappropriate or inconsistent with apparent legitimate needs of customer (e.g., no indication of prior authorized shipment of system for which parts are required)
- ▭ customer is known to have, or is suspected of having, unauthorized dealings with problem countries
- ▭ know your customer -- do not “self-blind”

Best Practice #1 – Screening for Designated Persons

- ▭ prohibition against dealings involving designated or listed persons
- ▭ screen for any involvement in the activity – customer, borrower, ultimate user, agents, vendor, creditor, broker, service provider, research partner, collaborator
 - ▭ and the individuals and entities that own or control them
- ▭ limited consolidation of lists by Canada
- ▭ practical necessity of using a third party screener
 - ▭ due diligence on screener

Best Practice #2 – Contract Clauses and Certifications

- ↪ trade control clauses for agreements with vendors, customers, agents and other counterparties
 - ↪ they are not designated person nor owned or controlled by same
 - ↪ compliance with trade controls and certifications
 - ↪ controls in place to prevent and detect violations
 - ↪ end-use certification
 - ↪ indemnification for contravention of trade control clauses or law
 - ↪ notification of investigations or inquiries, cooperation

Best Practice #3 – “Home Grown” Compliance Policies

- ▭ trade control compliance in the shadow of the United States

- ▭ Canadian sanctions can be more onerous than those of the United States – e.g., Russia/Ukraine, Belarus, Burma, North Korea

- ▭ conflicts
 - ▭ Cuba
 - ▭ potential employment and human rights violations

Best Practice #4 – Keeping Your Bank Happy

- ↯ in absence of guidance from Canadian government, banks have become the “front line” and may have greater exposure than customers
- ↯ keep banks apprised of transactions involving high risk jurisdictions in order to avoid delays and frozen funds
- ↯ banks concerns may extend beyond Canada, and beyond legal requirements – may be de-risking markets and sectors
- ↯ be prepared to demonstrate that you’ve implemented policies and controls
- ↯ coordinate sanctions permit and license applications with the bank

Best Practice #5 – Using Voluntary Disclosure Mechanisms

- ▭ in certain circumstances, can be an effective tool

- ▭ coordinate with multiple government depts
 - ▭ RCMP (plus mandatory disclosure of dealings with designated persons)
 - ▭ Global Affairs Canada Economic Law Division
 - ▭ Canada Border Services Agency
 - ▭ other (e.g., GAC Export Controls Division, Canadian Nuclear Safety Commission)

Core Elements of Your Economic Sanctions Compliance Program

- ▭ basic components should include:
 - ▭ corporate compliance manual
 - ▭ screens and lists
 - ▭ appointment of compliance officers
 - ▭ internal audit procedures
 - ▭ correction / voluntary disclosure process
 - ▭ training programs
 - ▭ contracts
 - ▭ conflict procedures



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