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### Are you ready for the next big change in international trade?

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By Lindsay Bernsen Wardlaw

Without an effective international arbiter of trade-related complaints to hold them back and with little interest in a dispute resolved primarily through military might, governments are turning to their national trade regulations to influence foreign affairs and manage international crises.<sup>[1]</sup>

New tariffs, sanctions, export controls, and import bans all have a profound impact on businesses. Your organization may suddenly need to replace a vital source of supply because the supplier is blacklisted, the supply is tainted by forced labor, or the use of the supply confers problematic export control or sanctions jurisdiction on the product it will be incorporated *into*. Or your organization may be able to keep using the same source of supply—but only by paying steep tariffs on each shipment. Or perhaps you may lose access to certain customers or markets, or you may have to reduce your service offerings, open accounts at a new financial institution, or change your pension plan investments.

Whatever the nature of the change, your organization must be ready to enact new regulatory requirements immediately. In the United States (US), for example, trade-related federal government agencies may—and often do—rely on their national security and foreign policy missions to issue far-reaching mandates that take effect the same day they are published or very shortly thereafter.<sup>[2]</sup>

We do not know what new events or conflicts might prompt trade action in 2023, but some trends are already in motion: US prohibitions on transactions (including exports, imports, and intangible exchanges of ideas or transfers of funds) with entities in Russia<sup>[3]</sup> and China<sup>[4]</sup> will likely become even more stringent<sup>[4]</sup>, as will US safeguards on the technology and equipment necessary to develop and produce artificial intelligence,<sup>[5]</sup> semiconductors,<sup>[6]</sup> and quantum computing.<sup>[7]</sup> Persuaded by Russian aggression in Ukraine, surveillance and human rights concerns, and US pressure on semiconductors, other governments across the world appear increasingly likely to adopt lockstep or complementary measures.<sup>[8]</sup>

The European Union (EU) is making dramatic changes to its import taxation regime, including implementing a Carbon Border Adjustment Measure<sup>[9]</sup> and Foreign Subsidies Act.<sup>[10]</sup>

And though we often focus on the effect of new *restrictions* on business, loosening trade-related constraints without fully removing them also increases compliance costs as businesses try to navigate what is permitted and what is prohibited. In 2023, the United States may also lift some constraints on Iran and Venezuela—if those governments become more amenable to US interests and international human rights norms.

Finally, we can expect that the United States will continue to push the limits of its jurisdiction to control imports

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and exports that traditionally have not been subject to its laws while the EU and other partner governments contemplate the use of secondary sanctions to discourage backfilling and sanctions evasion.

## **Preparing the company for change**

How can your organization prepare to transition smoothly to compliance with new requirements while minimizing the impact on business?

There are two stages of preparation.

First, you should develop a landscape of the organization's sales, procurement, and research touchpoints. By developing and periodically refreshing this landscape, the organization should be able to rapidly identify the impact of new or revised sanctions, export control, or customs regimes. Second, you should develop the tools necessary to respond to a specific trade-induced business crisis.

### **Stage one: Understanding your risk**

If you know where your organization's goods and information flow to and from and the customs and export control classifications assigned to those items, then you will know which new trade measures affect you and how to respond rapidly.

Though some of this information overlaps with information your organization may already gather to support periodic securities filings, other facts may seem overwhelming to gather at first, especially in companies with a very large operations or sales footprint. Work with counterparts across the business to determine the approach to information-gathering that is most viable for your organization. Once you understand the big picture, you can always dig deeper into the details.

### **Geographic risk**

Many trade measures apply to imports, exports, or other transactions with a particular country or region. So start by aggregating information about the countries where your organization has development, procurement, and sales. Interconnections between these countries are critical—between which countries do you exchange goods or information internally or externally during development or manufacturing? Where are your most vital inputs imported from, and where are your most essential markets?

Then, dig deeper into your supply chain. Where do the raw or semi-finished materials used in your inputs come from? What are the labor conditions there? If you have limited visibility into your supply chain, you may need to rely on publications from industry associations or government reports to assess the likeliest sources of supply. Your quality function may also have insights to share.

Look also at your distributors. Do they have a regionally delimited scope? What do they buy from your organization, and what countries do they sell to?

Finally, make sure you have a sense of which country's regulators have jurisdiction over your business operations. For example, transactions may be subject to US or EU jurisdiction if they are managed by US or EU personnel; rely on overhead or shared functions and resources, including IT resources, that are based in the US or EU; or use US or EU currency.

### **Counterparty risk**

Some trade controls are specific to a given counterparty or end-use. You should also consider assembling a list of

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your most essential suppliers, customers, and agents by volume. What industries do these customers serve? Take special note of customers who provide goods or services to government and military end-users. In addition, for those in high-risk jurisdictions, like Russia or China, consider using a due diligence tool to gain insight into your counterparty's ownership and control. Ownership or control by a restricted party imparts additional sanctions and export control risks.

## **Product and input risk**

Trade controls also apply directly to certain goods, services, and technology. For this reason, you should understand the customs and export control classifications of your organization's primary inputs and products. How many items that are actively imported or exported are unclassified? If you do not already have a strategy for classifying unclassified items, consider prioritizing the classification of goods exported to or imported from high-risk jurisdictions. Does your organization know whether it is developing projects involving sensitive, export-controlled technology? If it is, who collaborates on these projects—and where are those parties located?

## **Stage two: Developing a crisis management task force and response plan**

Once you understand your exposure, you can quickly assess if a new measure impacts your business. But you also want the ability to agilely respond.

Many elements of your business may be affected by new restrictions and will need to be consulted in your response. Before a crisis hits, connect potentially affected parties by creating a cross-functional trade crisis task force. The same colleagues who helped you understand your trade-related exposure may be good candidates for membership on the task force, but, in any case, ensure the task force is well-resourced and has the authority necessary to act and communicate on trade-related issues.

Working with this task force:

- Ensure you have a functioning restricted party screening system and that your vendors, customers, banks, and agents are all screened through this system. If you do not already use a background check system for new hires that includes restricted party screening, consider screening employees as well. Counterparties and transactions—like perhaps warranty work, imports of returns, and exports of prototypes or samples—that are not automatically screened should be subject to periodic manual screening.
- Develop a transactional sales review process that links trade compliance with other major transactional stakeholders to assess destination, counterparty, and bank risk; payment term and project restrictions; end-use and diversion risk; and reputational risk. Keep the platform and process flexible so that new trade programs can be incorporated as needed. Make sure to consider a centralized recordkeeping repository to record the results of these reviews.
- Draft an end-use/end-user certificate and supplier certification template that can be supplemented or modified to incorporate new concerns. Ensure your organization is familiar with these certificates and the intervals at which they should be requested. Create a recordkeeping repository for completed certifications.
- Draft a communication plan for the company and its management that you would use to explain new trade measures.
- Use protective contractual provisions, like force majeure provisions, to address the risk that you will be unable to complete a transaction due to changed regulatory requirements. Ensure that this language captures new sanctions, new export controls, new restricted party designations, and new determinations

that the counterparty uses forced labor or is located in a region deemed to use forced labor. You should be able to terminate the contract or delay performance or payment on this basis with minimal consequence. You should also ask your counterparty to confirm that it is currently compliant and not sanctioned. Finally, you should flow down compliance requirements that apply to your organization, seek indemnification for government fines or penalties, require assistance cooperating with government investigations, and obtain the right to audit your counterparty's compliance. Keep track of which contracts have the updated provisions and which are still in the queue for revision.

- Discuss any trade-related jurisdictional nexus discovered in the landscaping exercise with affected businesses.
- Monitor regulatory change and changes to the company's risk profile, including changes that affect jurisdictional nexus.

## Responding to crisis

Now you are ready to identify and respond to regulatory change.

When the moment arrives, immediately inform the business that you are aware of new measures, that you are determining their effect, and that you will provide further information as needed.

Using your landscape, work with the task force to determine if any supply, sale, or other transactions must be changed to avoid violation or should be changed to mitigate costs (such as moving sourcing from a country subject to antidumping, countervailing, or other remedial or punitive duties).

If the business is affected, is the prohibition comprehensive or targeted? To meet targeted restrictions, double-check the scope and effectiveness of your restricted party screening and due diligence, update and circulate your end-use/end-user or supplier certifications, and invoke the relevant provisions of your contacts. To meet comprehensive restrictions, you may have to develop a plan to wind down your sales or business operations for a particular market. Banking, payroll, asset, and infrastructure disposition may all be affected by the structure of the trade compliance measures, so consult your counsel carefully.

This article was designed to help you carve an immense challenge into digestible pieces, but, in practice, this will be a time-consuming project. Every organization will face unique hurdles. Remember, if you need assistance at any stage of this process, help is out there.

## Takeaways

- Trade requirements will continue to change, and businesses must be ready to respond quickly—even if they are cut off from major customers, suppliers, markets, or collaborators.
- Readiness requires understanding your organization's geographic, end-user/end-use, and item-based risk. In short: What do you make, what do you need to make it, and where/to whom does it need to go?
- Readiness also requires pre-coordination with leaders from potentially affected functions, like sales, procurement, finance, tax, facilities, engineering, research and development, and IT.
- Among other things, this coordination should include a review (or development) of your organization's restricted party screening measures, transactional review procedures, end-use/end-user certificates, supplier certificates, and contractual protections. Make sure you understand when these tools apply currently and how you could modify them to expand their scope, revise their controls, or add review stages

if needed.

- If you know when you are affected by new measures and have connected with the right parties within your organization, then you are as ready as you can be. Monitor the law, communicate the changes, and use your updated tools—or make new ones!

**1** Simon Lestor, “Ending the WTO Dispute Settlement Crisis: Where to from here?” International Institute for Sustainable Development, March 2, 2022, <https://www.iisd.org/articles/united-states-must-propose-solutions-end-wto-dispute-settlement-crisis>; Mark L. Busch, “The World Trade Organization shines a spotlight on US trade policy,” *The Hill*, December 10, 2022, <https://thehill.com/opinion/international/3766204-the-world-trade-organization-shines-a-spotlight-on-us-trade-policy>. See also remarks by National Security Advisor Jake Sullivan, October 13, 2022, <https://www.whitehouse.gov/briefing-room/speeches-remarks/2022/10/13/remarks-by-national-security-advisor-jake-sullivan-on-the-biden-harris-administrations-national-security-strategy> (explaining the U.S. strategy to “shape the rules of the road” when it comes to foundational technologies over the next decade and describing new semiconductor export controls as “premised on straightforward national security concerns”).

**2** New regulatory rules, like those involving international trade, that relate to a “military or foreign affairs function of the United States” are exempted from the rulemaking requirements of the U.S. Administrative Procedures Act. 5 U.S.C. 553(a)(1). The agency governing dual-use export controls, the U.S. Department of Commerce’s Bureau of Industry and Security (BIS), regularly relies on this authority. In 2022, it often released rules for public inspection that were effective the same day—well before the date of official “publication.” (See examples in the Russia and China context below.) Likewise, the Office of Foreign Assets Control (OFAC), the U.S. sanctions agency, regularly releases sanctions designations that are effective immediately. In 2022, OFAC emphasized its expectation of immediate compliance by issuing a finding of violation to a bank that failed to adhere to a new sanctions designation within hours of its publication. U.S. Department of Treasury, “The U.S. Department of the Treasury’s Office of Foreign Assets Control Issues Finding of Violation to MidFirst Bank,” news release, July 21, 2022, <https://home.treasury.gov/policy-issues/financial-sanctions/recent-actions/20220721>.

**3** See, e.g., Implementation of Sanctions Against Russia Under the Export Administration Regulations (EAR), 87 Fed. Reg. 12,226 (effective Feb. 24, 2022, published Mar. 3, 2022); Expansion of Sanctions Against the Russian Industry Sector Under the Export Administration Regulations (EAR), 87 Fed. Reg. 12,856 (effective Mar. 2, 2022, published Mar. 8, 2022); Further Imposition of Sanctions Against Russia With the Addition of Certain Entities to the Entity List, 87 Fed. Reg. 13,141 (effective Mar. 3, published Mar. 9, 2022); Imposition of Sanctions on ‘Luxury Goods’ Destined for Russia and Belarus and for Russian and Belarusian Oligarchs and Malign Actors Under the Export Administration Regulations (EAR), 87 Fed. Reg. 14,785 (effective Mar. 11, 2022, published Mar. 16, 2022); Expansion of Sanctions Against Russia and Belarus Under the Export Administration Regulations (EAR), 87 Fed. Reg. 22,130 (effective Apr. 8, 2022; published Apr. 14, 2022); Expansion of Sanctions Against Russian Industry Sectors Under the Export Administration Regulations (EAR), 87 Fed. Reg. 28,758 (effective May 9, 2022, published May 11, 2022); Export Administration Regulations: Revisions to Russia and Belarus Sanctions and Related Provisions; Other Revisions, Corrections, and Clarifications, 87 Fed. Reg. 34,131 (effective June 2, 2022, published June 6, 2022); Implementation of Additional Sanctions Against Russia and Belarus Under the Export Administration Regulations (EAR) and Refinements to Existing Controls, 87 Fed. Reg. 57,068 (effective Sept. 15, 2022, published Sept. 16, 2022).

**4** See, e.g., Implementation of Additional Export Controls: Certain Advanced Computing and Semiconductor Manufacturing Items; Supercomputer and Semiconductor End Use; Entity List Modification, 87 Fed. Reg. 62,186 (effective Oct. 7, 2022, published Oct. 13, 2022).

**5** BIS announced in a 2018 Advanced Notice of Proposed Rulemaking that it would be considering export controls

on emerging technologies, including items and technologies associated with artificial intelligence (AI), like AI chipsets and AI cloud technologies, as well as neural networks, deep learning models, and expert systems. Review of Controls for Certain Emerging Technologies, 83 Fed. Reg. 58,201 (Nov. 19, 2018). Since then, it has added controls for training a deep convolutional neural network to automate geospatial analysis, and it has requested comments on the impact of controls on brain-computer interfaces on the development of AI, but it has not added any other direct controls on artificial intelligence. Addition of Software Specially Designed To Automate the Analysis of Geospatial Imagery to the Export Control Classification Number 0Y521 Series, 85 Fed. Reg. 459 (Jan. 6, 2020); Request for Comments Concerning the Imposition of Export Controls on Certain Brain-Computer Interface (BCI) Emerging Technology, 86 Fed. Reg. 59,070 (Oct. 26, 2021). While it is unclear exactly what form additional controls will ultimately take, a Georgetown scholar has recommended implementing controls not on programs but on chips that are sufficiently advanced to run AI and the equipment to manufacture those chips. (Carrick Flynn, *Recommendations on Export Controls for Artificial Intelligence*, Georgetown Center for Security and Emerging Technology, February 2020, <https://cset.georgetown.edu/publication/recommendations-on-export-controls-for-artificial-intelligence>). Even without crafting item-specific controls, the U.S. government is taking measures to restrict AI-related exports. In December 2022, BIS added “major artificial intelligence (AI) chip research and development, manufacturing and sales entities” with “close ties” to the Chinese government, defense industry, or military to the BIS Entity List, creating a licensing requirement, with a presumption of denial, for all items subject to the Export Administration Regulations. Additions and Revisions to the Entity List and Conforming Removal From the Unverified List, 87 Fed. Reg. 77,505 (Dec. 16, 2022).

**6** Certain semiconductor manufacturing equipment is already listed on the U.S. Commerce Control List, and BIS’s November 2018 announcement on controls on emerging technologies also listed microprocessor and advanced computing technologies such as systems-on-chip, stacked memory on chip, and memory-centric logic. Review of Controls for Certain Emerging Technologies, 83 Fed. Reg. 58,201 (Nov. 19, 2018). In 2022, BIS targeted exports of previously uncontrolled semiconductor manufacturing equipment and restricted it for export to China in particular. Implementation of Additional Export Controls: Certain Advanced Computing and Semiconductor Manufacturing Items; Supercomputer and Semiconductor End Use; Entity List Modification, 87 Fed. Reg. 62,186 (Oct. 13, 2022). The rule also included controls on supercomputers that could be used for development of artificial intelligence.

**7** BIS also included quantum computing and encryption in its 2018 list of emerging technologies for which it would be evaluating potential controls. Review of Controls for Certain Emerging Technologies, 83 Fed. Reg. 58,201 (Nov. 19, 2018). Like with artificial intelligence items, the U.S. government has begun to impose geographic and end-user-based controls even without creating a traditional item-based control. In 2022, OFAC specifically prohibited exports of quantum computing services to Russia, and BIS prohibited the export of certain otherwise uncontrolled quantum computing items to Russia. Implementation of Additional Sanctions Against Russia and Belarus Under the Export Administration Regulations (EAR) and Refinements to Existing Controls, 87 Fed. Reg. 57,068 (Sept. 16, 2022); OFAC, Determination of September 15, 2022, made pursuant to Executive Order (E.O.) 14,071, “Prohibitions Related to Certain Quantum Computing Services.” BIS also added seven Russian entities to its Entity List in 2022 for, among other things, “their involvement in the development of quantum computing technologies, which would further enable Russia’s malicious cyber activities, or are otherwise important to Russia in developing advanced production and development capabilities.” Additions of Entities to the Entity List, 87 Fed. Reg. 60,064 (Oct. 4, 2022).

**8** For example, the United States coordinated with over 30 partner countries to implement “substantially similar” export controls on Russia. See EAR, Supplement No. 3 to 15 C.F.R. 746, “Countries Excluded from Certain License Requirements of § 746.8.” It is also negotiating with the major semiconductor-producing nations of the world to implement complementary controls on semiconductor exports. Reid Whitten and J. Scott Maberry, “The New Containment: How the Semiconductor Industry Came to Be at the Heart of the Technological Cold War,” *National Law Review*, December 21, 2022, <https://www.natlawreview.com/article/new-containment-how->

semiconductor-industry-came-to-be-heart-technological-cold-war.

**9** The European Council and the European Parliament agreed to the Carbon Border Adjustment Mechanism on December 13, 2022. Between October 1, 2023, and the end of 2025, the EU will phase in a certification and payment scheme for imports of carbon-intensive goods (cement, iron and steel, aluminum, fertilizers, electricity, and hydrogen). European Commission, Taxation and Customs Union, “Carbon Border Adjustment Mechanism,” last accessed January 5, 2023, [https://taxation-customs.ec.europa.eu/green-taxation-0/carbon-border-adjustment-mechanism\\_en](https://taxation-customs.ec.europa.eu/green-taxation-0/carbon-border-adjustment-mechanism_en).

**10** The European Council adopted the EU’s Foreign Subsidies Regulation (already adopted by the European Parliament) on November 28, 2022. The regulations allow the European Commission to investigate and remedy allegedly distortive foreign subsidies and impose notice and approval requirements for certain M&A and public procurement transactions. European Council, “Council gives final approval to tackling distortive foreign subsidies on the internal market,” news release, November 28 2022, <https://www.consilium.europa.eu/en/press/press-releases/2022/11/28/council-gives-final-approval-to-tackling-distortive-foreign-subsidies-on-the-internal-market>.

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