

Internal Compliance Programmes –

Day to Day Operational
Challenges & Best Practices
13th January 2011

METI & OSETC Joint Seminar – Manila



Agenda

- Introduction
- Company Obligations
- METI's Notice
- Challenges & Best Practice

Why am I here?

- To understand the export controls law that each individual as well as each company must comply with
- To grasp the key elements that you and your company must address in order to allow your company to conduct its business in a sustainable & compliant manner

***You have a part to play in fulfilling your company's vision
i.e. to comply with the export control laws & regulations***

– A Good Corporate Citizen

Key Takeways

- To be prepared for export compliance operational challenges and understand industry best practice
- To appreciate export compliance as a real concern; not simply a paper exercise
- To connect your day-to-day operational work with export compliance practices

Brief Introduction to Export Controls

What are Export Controls?

- Laws and regulations established to curb the proliferation of weapons of mass destruction and their means of delivery
- National export control regimes based on international agreements
- Export licenses are required to export controlled products or technology
- Customs authorities typically act as the appointed enforcement agencies for Export Controls
- Accountability of **exporters of record** when dealing with controlled goods / technology

What are Strategic Goods? (Strategic Items)

Goods relating to the –

Development, Design, Production, Stock Piling or use of:

- Chemical, biological, radiological & nuclear (CBRN) weapons
 - Conventional arms & military equipment
- & their delivery means (systems)

Commonly known as:-

Weapons of Mass Destruction “WMD”

Common Misconception

*“My company is not in the arm industry.
Export controls do not concern me and my business at all.”*



What are Strategic Goods?

(also known as Strategic or Controlled Items / Products / Commodities)

Types of goods covered under export controls

Scope of goods controlled:

- (1) Hardware**
- (2) Software**
- (3) Technology** relating to design, development and production of weapons of mass destruction (“WMD”)

Dual-use items (civilian and military uses)

Munitions (conventional military weapons and WMD)

Other products under “Catch-all” provision

What are Strategic Goods? (Strategic Items)

Apart from munitions / weapons , strategic goods also include dual-use goods, e.g.

| Dual-use Item | Military Use | Civilian Use |
|-------------------------|---------------------------------------|--|
| Titanium Alloy | Gas Centrifuge for Uranium Enrichment | Watches, Eye-glass Frame |
| Carbon Fibre | Missile Components | Golf Club Shafts, Fishing Rod, Bicycle |
| Triethanolamine | Chemical Weapons | Shampoo |
| Freeze-drying Equipment | Biological Weapons | Instant Coffee |

Which industries are likely to be affected?

| | | | |
|------------------------|---------------------|--|-------------------|
| Aerospace | Automotive | Advanced Engineering | Bioscience |
| Chemicals | Defence | Electronics & Telecom (components & complete products) | Hi-Tech Equipment |
| Information Technology | Medical Instruments | Pharmaceutical | R&D |

Export Controls Landscape

| Country (Region) | Member of Int'l Export Control Regimes | Government Agency Responsible | Export Control legislation | Enforcement |
|------------------|--|-------------------------------|----------------------------|---|
| Australia | √ | MOD | √ | √ |
| China | Δ | MOFCOM | √ | √ |
| EU | √ | EU | √ | √ |
| HKG SAR | X | TID | √ | √ |
| India | X | MOCI | √ | Δ |
| Indonesia | X | X | X | X |
| Japan | √ | METI | √ | √ |
| Korea | √ | MKE | √ | √ |
| New Zealand | √ | MOFAT | √ | √ |
| Malaysia | X | MITI | √ | By July 2011 |
| Pakistan | X | MOFA | √ | Δ |
| Philippines | X | OSETC | X/Δ | X |
| Singapore | X | MOF/SC | √ | √ |
| Taiwan | X | MOEA / MOF | √ | √ |
| Thailand | X | MOC / MOFA | √/Δ | X |
| US | √ | DOC /DOE | √ | √ |
| Vietnam | X | X | X | X |
| Legend: | √ = Yes | Δ = Maybe / Partial | X = No | (status as of 1 st Dec 2010) |

Note: (1) Malaysia Parliament passed the Strategic Trade Bill 2010 in April [Likely to be implemented by Jul 2011]
 (2) Thailand Ministry of Commerce (Dept of Foreign Trade) is currently drafting a Dual-Use List and preparing a legislation
 (3) Vietnam has set up a "Task Force" to study the implementation of their export controls regime
 (4) A "Senate Bill" has been filed in the 15th Congress of the Philippines

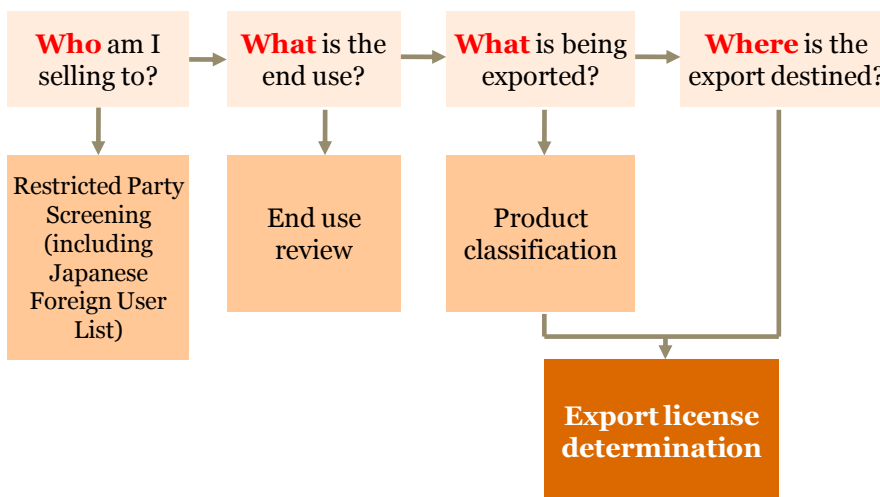
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Company Obligations

Core obligations – key elements to conduct screening



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Catch-All Control (or unlisted items)

Almost all Export Controls Regimes incorporate such provisions:-

Captures goods that are not listed in the Control List where you have any reason to **“suspect”** or **“know”** that they will be / are used in the production of WMD or conventional weapons

- Export license is compulsory
- Applicable to hardware, software & technology

Company-wide Effort & Challenge

* Remember: Most export control regimes cover both the export of physical goods and the export of “transfer of” technology

| Various Function in a Typical Organisation | |
|--|----------------------------------|
| Sales | Customer screening, end use |
| Engineering (+ R&D) | Product Classification |
| Human Resources & Administration | Nationality & Office Security |
| Information Technology (IT) | IT Security |
| Legal | Contracts |
| Finance | Payment & bankers |
| Procurement & Outsource | Supplier & vendor |
| Operations (Logistics & Shipping) | Export License & end-destination |

Company's Obligation

Exporting is a privilege, not a right!

It is mandatory to comply with the export control legislation of the countries from which a company exports

METI Minister's Official Request to All Japanese Companies & their Subsidiaries [company self management]

(NOTICE issued on 3rd March 2006)

1. Company-wide (including overseas subsidiaries) awareness on the importance of Export Controls
2. Top management is responsible for establishing the company's export control organization and implementing export control compliance program
3. Headquarters should ensure:
 - overseas subsidiaries are aware of the export control guidance and
 - that they establish and implement the relevant export compliance rules and procedures

NOTE:-

Latest update on Japan Export Controls:

(1) Strengthening of penalty: imprisonment (10 years max) & fine (10 million yen max)
– effective 1st Nov '09

(2) Compliance Standard for Exporters: all exporters must maintain an export control system
– effective 1st Apr '10

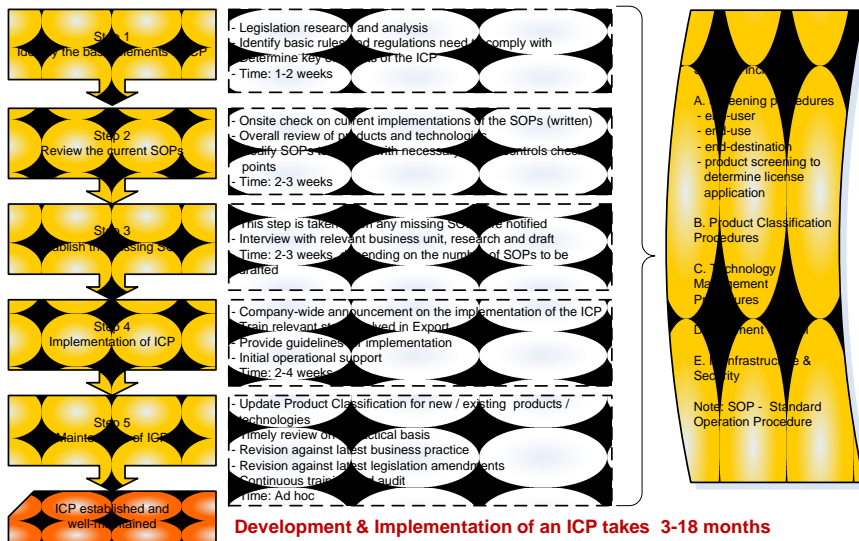
Internal Compliance Program (“ICP”)

What is ICP?

- Export controls SOP across all business functions
- Prerequisite for trade facilitation licensing schemes in most countries
- Capture analysis, decisions, accountability and implementing procedures
- Level of detail dependent on complexity of company’s business operations
- One size does not fit all
- Scalable and organic in nature

Note: SOP – Standard Operation Procedure

Developing an ICP



What is an ICP? (examples of key elements)

1. Management Commitment
(Statement Policy – communicate to & accessible by all staff)
2. Assigned, empowered & authorized responsible compliance officer/team
3. Establish an effective product classification procedure
(Product Classification Table – accessible by all relevant staff)
4. Establish an effective screening procedure
(end-user, end-use and end-destination of export)
5. Well monitored Order Processing & Shipping Procedures
(transaction screening & export licensing determination system)
6. Set up a training program on export control for all staff & business partners

What is an ICP? (examples of key elements)

7. Conduct regular internal review of the company's export compliance performance
8. Establish an effective document filing system
(min 5 years of record keeping)
9. Set up an emergency notification system to manage any reports of dubious transactions or export control violations
(about to occur / already occurred)
10. Periodic review / revision of the ICP as per business and political arena changes
(at least once per year)
11. Written guidance / instruction to subsidiary & business partners

Primary Challenges Faced by Companies Implementing an ICP

Resources

- Lack of a dedicated trade compliance / export controls resource
- Underestimating time to develop
- Underestimating time and barriers to implement

Migration & Operational integration of existing foreign ICP

- Common issue for multi-national companies
- Customisation underestimated

Alignment of business partner

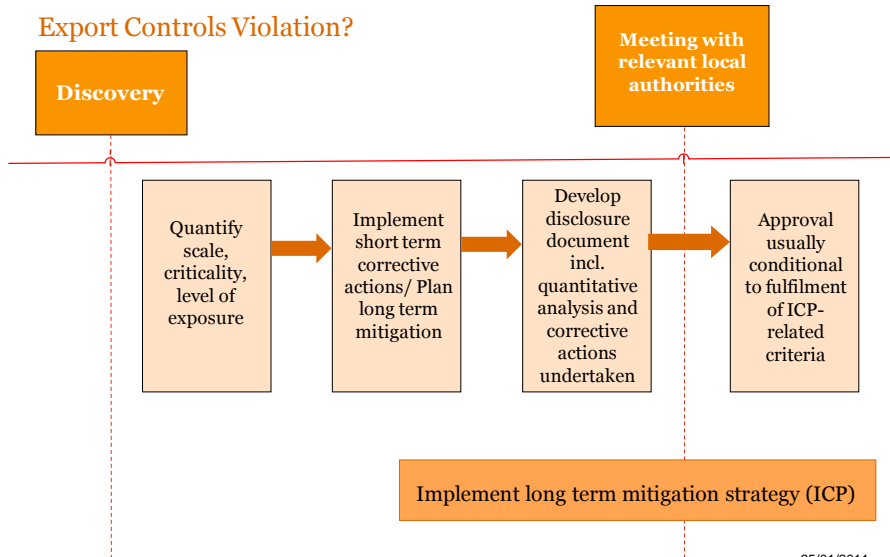
- Understanding of commercial constraints
- Definition of roles and responsibilities
- Could apply to 3PL, Subcontractors, Customers, Suppliers, etc

Managing Your Company's Export Controls

- **Assess your company's services:-**
 - a. products and technologies (goods) – are they controlled?
 - b. customers (end-user) – are they listed in Denial List Party?
 - c. end-use (application) – any WMD related?
 - d. end-destination – any embargoed /sanction country?
- **Set up internal screening procedures for above 4 key elements (a-d); recommend to set up an *ICP* as Best Practice**
- **Company wide announcement on *ICP* compliance and training on the screening procedures**
- **Communicate & educate the business partners on *ICP* compliance**

Best Practice - Voluntary disclosure

Export Controls Violation?



What Often Goes Wrong?

Failure to obtain the relevant Permit and / or comply with the Permit conditions (or Permit validity expires)

Ineffective end-user, project, research program screening

Unlicensed technology transfers – overseas meetings, cloud computing, samples, prototypes, spare parts, hand carry etc.

Deemed exports / re-exports (extra territorial effect?) – Use of Asian subsidiary to circumvent US/EU controls

Record keeping lapses

Incorrect declarations – classification of goods, end user / destination

Failure to or delays in voluntary disclosure

Why Does It Go Wrong in Asia?

1. **Overreliance on HQ based compliance and resources**
2. Only US, EU and Japan have export controls
3. Only a paper exercise
4. I am not an arms dealer
5. Export controls is not my problem
6. **Our Freight Forwarder /Distributor is taking care of it**
7. No revenue involved = no perceived value
8. **No resources or lack of resources (no in-house expertise)**
9. Changes to national legislation not well publicised
10. No support and commitment from top management
11. Mixed messages from governments
12. **Lack of consistency between national control regimes**

What Does it Take to Create and Operate an Effective ICP?

Key factors:

| | | |
|---|--------------------------|------------------------|
| Buy-in from top management (or other stakeholders) | Export controls resource | Awareness and training |
| Localisation | - Dedicated | - Logistics |
| Periodical review & audit | - Sufficiently senior | - Sales/marketing |
| | - Empowered | - R&D |
| | - Financial (budget) | - Business partners |
| | | - etc |

Summary

1. Growing issue in Asia
2. Serious risk exists regardless of enforcement environment
3. ICP is a strong mitigation factor
4. Now is a good time to act
5. PwC Regional support

Thank you

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