

UNITED STATES DEPARTMENT OF COMMERCE
BUREAU OF INDUSTRY AND SECURITY
WASHINGTON, D.C. 20230

In the Matter of:

Zhongxing Telecommunications Equipment
Corporation
ZTE Plaza, Keji Road South
Hi-Tech Industrial Park
Nanshan District, Shenzhen
China

ZTE Kangxun Telecommunications Ltd.
2/3 Floor, Suite A, Zte Communication Mansion
Keji (S) Road
Hi-New Shenzhen, 518057
China

Respondent

ORDER ACTIVATING SUSPENDED DENIAL ORDER RELATING TO
ZHONGXING TELECOMMUNICATIONS EQUIPMENT CORPORATION AND
ZTE KANGXUN TELECOMMUNICATIONS LTD.

Background

On March 23, 2017, I signed an Order approving the terms of the Settlement Agreement entered into in early March 2017, between the Bureau of Industry and Security, U.S. Department of Commerce (“BIS”) and Zhongxing Telecommunications Equipment Corporation, of Shenzhen, China (“ZTE Corporation”) and ZTE Kangxun Telecommunications Ltd. of Hi-New Shenzhen, China (“ZTE Kangxun”) (collectively, “ZTE”), hereinafter the “March 23, 2017 Order.” Under the terms of the settlement, ZTE agreed to a record-high combined civil and criminal penalty of \$1.19 billion, after engaging in a multi-year conspiracy to violate the U.S. trade embargo against Iran to obtain contracts to supply, build, operate, and maintain telecommunications networks in Iran using U.S.-origin equipment, and also illegally shipping telecommunications

equipment to North Korea in violation of the Export Administration Regulations (15 C.F.R. Parts 730-774 (2017)) (“EAR” or the “Regulations”). ZTE also admitted to engaging in an elaborate scheme to hide the unlicensed transactions from the U.S. Government, by deleting, destroying, removing, or sanitizing materials and information.

Under the terms of the Settlement Agreement and the March 23, 2017 Order, BIS imposed against ZTE a civil penalty totaling \$661,000,000, with \$300,000,000 of that amount suspended for a probationary period of seven years from the date of the Order.¹ This suspension was subject to several probationary conditions stated in the Settlement Agreement and March 23, 2017 Order, including that ZTE commit no other violation of the Export Administration Act of 1979, as amended (50 U.S.C. §§ 4601-4623 (Supp. III 2015)), the Regulations, or the March 23, 2017 Order. The March 23, 2017 Order also imposed, as agreed to by ZTE, a seven-year denial of ZTE’s export privileges under the EAR that was suspended subject to the same probationary conditions. The March 23, 2017 Order, like the Settlement Agreement, provided that should ZTE fail to comply with any of the probationary conditions, the \$300 million suspended portion of the civil penalty could immediately become due and owing in full, as well as that BIS could modify or revoke the suspension of the denial order and activate a denial order of up to seven years.

The Settlement Agreement and March 23, 2017 Order require that during the probationary period, ZTE is to, among other things, complete and submit six audit reports

¹ In addition to the BIS-ZTE settlement, ZTE Corporation entered into a plea agreement with the Justice Department’s National Security Division and the U.S. Attorney’s Office for the Northern District of Texas, and entered into a settlement agreement with the Treasury Department’s Office of Foreign Assets Control. The civil penalties (including the \$661 million civil penalty imposed by BIS) and the criminal fine and forfeiture totaled, when combined, approximately \$1.19 billion.

regarding ZTE's compliance with U.S. export control laws. The Settlement Agreement and March 23, 2017 Order also include a broad cooperation provision during the period of the suspended denial order. This cooperation provision specifically requires that ZTE make truthful disclosures of any requested factual information. The Settlement Agreement and March 23, 2017 Order thus, by their terms, essentially incorporate the prohibition set forth in Section 764.2(g) of the EAR against making any false or misleading representation or statement to BIS during, inter alia, the course of an investigation or other action subject to the EAR.

On February 2, 2018, acting pursuant to the Settlement Agreement and March 23, 2017 Order, BIS requested, among other things, that ZTE provide a status report on all individuals named or otherwise identified in two letters sent by ZTE, through its outside counsel, to the U.S. Government, dated November 30, 2016, and July 20, 2017, respectively. The status report was to include, among other things, current title, position, responsibilities, and pay and bonus information from March 7, 2017 to the present. The first of those two letters, dated November 30, 2016, was sent during BIS's investigation of the violations alleged in the Proposed Charging Letter and referenced in the Settlement Agreement and March 23, 2017 Order. In that letter, ZTE described "self-initiated" employee disciplinary actions it asserted that it had taken to date and additional actions that the company said it would take in the near future because they were "necessary to achieve the Company's goals of disciplining those involved and sending a strong message to ZTE employees about the Company's commitment to compliance." The letter focused on ZTE's asserted commitment to compliance, including from the highest levels of management.

The July 20, 2017 letter, sent on ZTE's behalf during the March 23, 2017 Order's seven-year probationary period, also asserted ZTE's commitment to compliance and

claimed that the disciplinary actions taken had sent a very strong message to ZTE employees. The letter was sent “to confirm that the measures detailed by ZTE with respect to discipline have been implemented” against nine named ZTE employees identified during the U.S. Government’s investigation. The employee disciplinary actions—actions that ZTE told the U.S. Government that it had already taken—were in ZTE’s words a showing of ZTE’s “overall approach to discipline and commitment to compliance,” which the company described as “significant and sufficient to prevent past misconduct from occurring again at ZTE.” Nearly all of the employees named in the July 20, 2017 letter had been specifically identified to ZTE by the U.S. Government as individuals that U.S. law enforcement agents wanted to interview during the investigation, either because they were signatories on an internal ZTE memorandum discussing how to evade U.S. export controls, were identified on that memorandum as a “project core member” of that evasion scheme, and/or had met with ZTE’s then-CEO to discuss means to continue evading U.S. law. Three were members of the “Contract Data Induction Team” involved in extensive efforts to destroy and conceal evidence described in more detail below and in the PCL.

In sum, through those two letters, ZTE informed the U.S. Government that the company had taken or would take action against 39 employees and officials that ZTE identified as having a role in the violations that led to the criminal plea agreement and the settlement agreements with BIS and the U.S. Department of the Treasury’s Office of Foreign Assets Control. In fact, and as ZTE now admits, the letters of reprimand described in the November 30, 2016 letter were never issued until approximately a month after BIS’s February 2, 2018 request for information, and all but one of the pertinent individuals identified in the November 30, 2016 or July 20, 2017 letters received his or

her 2016 bonus.² These false statements were not corrected by ZTE even in part until March 2018, more than 15 months from ZTE's November 30, 2016 letter, approximately a year from the Settlement Agreement (which ZTE executed on March 2, 2017) and the March 23, 2017 Order, and nearly eight months from the July 20, 2017 letter. During a conference call on March 6, 2018, ZTE indicated, via outside counsel, that it had made false statements in the November 30, 2016 and the July 20, 2017 letters. As discussed below, ZTE's first detailed notification occurred on March 16, 2018.

Proposed Activation of Suspended Sanctions and ZTE's Response

On March 13, 2018, pursuant to Section 766.17(c) of the Regulations, BIS notified ZTE of a proposed activation of the sanctions conditionally-suspended under the Settlement Agreement and the March 23, 2017 Order, based on ZTE's false statements in its letters dated November 30, 2016 and July 20, 2017, respectively. The notice letter to ZTE also gave the company an opportunity to respond, which it did on March 16, 2018.

I have reviewed in detail ZTE's response. In its letter, ZTE confirmed the false statements and, as discussed further *infra*, posed certain questions in rhetorical fashion. ZTE then proceeded to summarize its response upon "discovering" the failure to implement the stated employee disciplinary actions prior to March 2018, including its decision to notify BIS of the failures. The company also described the asserted remedial steps it had taken to date, including the issuance in March 2018, of the letters of

² Some of the disciplinary actions ZTE discussed in its November 30, 2016 letter relate to employees who resigned from ZTE well before the date of that letter, including some even as far back as 2012 and 2013. ZTE asserted that such employees left the company by "mutual understanding." Including these employees allowed ZTE to inflate the number of employees listed as subject to disciplinary action, and the material provided by ZTE to date does not establish that they were, in fact, subject to such action. The false statements discussed as violations in this order do not include, however, ZTE's statements relating to the circumstances under which these employees left the company. Nor do the false statements at issue relate to an employee referenced in the July 20, 2017 letter, concerning whom ZTE did not clearly state that disciplinary action had been taken. This order also does not relate to any issues relating to the termination of four officials addressed as part of the criminal plea agreement.

reprimand that were to have been sent in 2016-2017. ZTE additionally asserted that, for current employees whose 2016 bonus should have been reduced (by 30% to 50%), it would deduct the corresponding amount from their 2017 annual bonuses “to the extent permitted under Chinese law.” ZTE also said it will pursue recovery from (certain) former employees of bonus payments for 2016 that the company had informed the U.S. Government would be reduced, but, contrary to those statements, were paid in full. Finally, ZTE reiterated what it described as the company’s serious commitment to export control compliance and summarized its plan to continue its internal investigation of the matter.

ZTE’s Pattern of Deception, False Statements, and Repeated Violations of U.S. Law

In issuing the March 13, 2018 notice letter to ZTE, and in considering ZTE’s response, I have taken into account the course of ZTE’s dealings with the U.S. Government during BIS’s multi-year investigation, which demonstrate a pattern of deception, false statements, and repeated violations. I note the multiple false and misleading statements made to the U.S. Government during its investigation of ZTE’s violations of the Regulations, and the behavior and actions of ZTE since then. ZTE’s July 20, 2017 letter is brimming with false statements in violation of § 764.2(g) of the Regulations, and is the latest in a pattern of the company making untruthful statements to the U.S. Government and only admitting to its culpability when compelled by circumstances to do so. That pattern can be seen in the November 30, 2016 letter, which falsely documented steps the company said it was taking and had taken, as well as in the 96 admitted evasion violations described in the PCL, which detailed the company’s efforts to destroy evidence of its continued export control violations.

In agreeing to the Settlement Agreement and the imposition of the March 23, 2017 Order, ZTE admitted committing 380 violations of the Regulations as those

violations were alleged in BIS's PCL. The PCL detailed an extensive conspiracy, including as laid out in a 2011 company memorandum drafted by ZTE Corporation's Legal Department and ratified by its then-CEO, to evade U.S. export control laws and facilitate unlicensed exports to Iran. During the conspiracy, ZTE leadership and staff employed multiple strategies in an attempt to conceal or obscure the true nature and extent of the company's role in the transactions and thereby facilitate its evasion of U.S. export controls, of which ZTE had detailed knowledge. As a result of the conspiracy, ZTE was able to obtain hundreds of millions of dollars in contracts with and sales from Iranian entities to ship routers, microprocessors, and servers controlled under the Regulations for national security, encryption, regional security, and/or anti-terrorism reasons to Iran.

ZTE Cover-Up Activity

Of the 380 alleged and admitted violations, ZTE committed 96 evasion violations relating to its actions to obstruct and delay the U.S. Government's investigation.³ These violations included making knowingly false and misleading representations and statements to BIS special agents and other federal law enforcement agents and agency official during a series of meetings between August 26, 2014, and at least January 8, 2016, including that the company had previously stopped shipments to Iran as of March 2012, and that it was no longer violating U.S. export control laws. In doing so, ZTE acted through outside counsel, who were unaware that the representations and statements that ZTE had given to counsel for communication to the U.S. Government were false and

³ These 96 admitted violations are discussed in fuller detail in the Proposed Charging Letter attached to and incorporated by reference in the Settlement Agreement. In the Settlement Agreement, ZTE admitted each of the allegations and violations contained in the Proposed Charging Letter.

misleading. ZTE failed to correct those representations and statements, which were continuing in effect, until beginning to do so (via outside counsel) on April 6, 2016.

ZTE also engaged in an elaborate scheme to prevent disclosure to the U.S. Government, and, in fact, to affirmatively mislead the Government, by deleting and concealing documents and information from the outside counsel and forensic accounting firm that ZTE had retained with regard to the investigation. Between January and March 2016, ZTE went so far as to form and operate a “Contract Data Induction Team” made up of ZTE employees tasked with destroying, removing, and sanitizing all materials concerning transactions or other activities relating to ZTE’s Iran business that post-dated March 2012. ZTE required each of the team members to sign a non-disclosure agreement covering the ZTE transactions and activities the team was directed to hide from the U.S. Government, subject to a penalty of 1 million RMB (or approximately \$150,000) payable to ZTE if it determined that a disclosure occurred.

Determination to Activate the Suspended Denial Order

It was with this backdrop in mind, as more fully alleged in the PCL, that the Settlement Agreement and the March 23, 2017 Order mandate that ZTE truthfully disclose, upon request, all factual information (not subject to certain privileges, which are inapplicable here), and that led BIS to make its February 2, 2018 request for information relating to the employee disciplinary actions stated in the November 30, 2016 and July 20, 2017 letters.

BIS has determined that the company’s admission, in response to inquiries from BIS, that it made false statements to the U.S. Government during the probationary period under the Settlement Agreement and March 23, 2017 Order indicate that ZTE still cannot

be relied upon to make truthful statements, even in the course of dealings with U.S. law enforcement agencies, and even with the prospect of the imposition of a \$300 million penalty and/or a seven-year denial order. The provision of false statements to the U.S. Government, despite repeated protestations from the company that it has engaged in a sustained effort to turn the page on past misdeeds, is indicative of a company incapable of being, or unwilling to be, a reliable and trustworthy recipient of U.S.-origin goods, software, and technology. BIS is left to conclude that if the \$892 million monetary penalty paid pursuant to the March 23, 2017 Order, criminal plea agreement, and settlement agreement with the Department of the Treasury did not induce ZTE to ensure it was engaging with the U.S. Government truthfully, an additional monetary penalty of up to roughly a third that amount (\$300 million) is unlikely to lead to the company's reform.

The false statements ZTE made in the July 20, 2017 letter violate Section 764.2(g) of the Regulations and the terms of the Settlement Agreement and the March 23, 2017 Order, and thus violate the conditions of ZTE's probation under the Agreement and the Order. The false statements in the November 30, 2016 letter, made during the investigation, are pertinent and material in at least two ways.⁴ First, they are evidence that ZTE's false statements to the U.S. Government did not cease in April 2016, as are the additional false statements ZTE made in its July 20, 2017 letter. Second, under Section 764.2(g) of the Regulations, all representations, statements, and certifications to BIS or any other relevant agency made, inter alia, in the course of an investigation or

⁴ They are also possibly material in another way, as the pertinent 2016 bonus payments may not have been made until after the Settlement Agreement had been executed or after it had been approved via the March 23, 2017 Order. The November 30, 2016 letter indicated that 2016 bonus figures would be "announced in March 2017."

other action subject to the Regulations are deemed to be continuing in effect.

Notification must be provided to BIS and any other relevant agency, in writing, of any change of any material fact or stated intention previously represented, stated, or certified. Such written notification is to be provided “immediately upon receipt of any information that would lead a reasonably prudent person to know that a change of material fact or intention has occurred or may occur in the future.” 15 C.F.R. § 764.2(g)(2) (2014-2017).⁵ Thus, with regard to the probationary conditions at issue here, ZTE failed to comply even partially with this continuing duty to correct by written notification, from the date of the March 23, 2017 Order until March 8, 2018.⁶

I note that in its response to BIS’s notice of proposed activation of suspended sanctions and in making its case for leniency, ZTE acknowledged that it had submitted false statements, but argued that it would have been irrational for ZTE to knowingly or intentionally mislead the U.S. Government in light of the seriousness of the suspended sanctions. The heart of its argument is the question, posed by the company in rhetorical fashion, asking “why would ZTEC risk paying another \$300 million suspended fine and placement on the denied parties list, which would effectively destroy the Company, to avoid sending out employee letters of reprimand and deducting portions of employee bonuses?” ZTE argued that BIS should not act until the company completed an internal investigation so that ZTE could answer such questions.

⁵ Under the Regulations, “[k]nowledge of a circumstance (the term may be a variant, such as ‘know,’ ‘reason to know,’ or ‘reason to believe’) includes not only positive knowledge that the circumstance exists or is substantially certain to occur, but also an awareness of a high probability of its existence or future occurrence. Such awareness is inferred from evidence of the conscious disregard of facts known to a person and is also inferred from a person’s willful avoidance of facts.” See 15 C.F.R. § 772.1 (parenthetical in original).

⁶ As discussed *supra* and in the March 13, 2018 notice letter, ZTE did provide some notice by telephone on March 6, 2018.

ZTE has posed such questions not because additional investigation could render its false statements true, but in the hope of postponing action by the U.S. Government and ultimately avoiding or minimizing the consequences of its additional violations. Similarly, additional time to continue its investigation is unnecessary and irrelevant to the issue of whether the company violated the provision against giving false statements to BIS under Section 764.2(g) of the Regulations, and in violation of the Settlement Agreement and March 23, 2017 Order. The reasons that ZTE violated the EAR are red herrings to BIS's concern that the company has repeatedly made false statements to the U.S. Government—as the company has now repeatedly admitted. As recently as March 21, 2018, in a certification to the U.S. Government signed by ZTE Corporation's Senior Vice President, Chief Legal Officer and Acting Chief Compliance Officer, ZTE admitted that it “had not executed in full certain employee disciplinary measures that it had previously described in a letter to the U.S. government dated November 30, 2016, and there are inaccuracies in certain statements in the letter dated July 20, 2017.” Giving ZTE additional time to complete its internal investigation will not erase the company's most recent—in a series—of false statements to the U.S. Government.

Furthermore, ZTE's suggestion that it could or would not have made such a poor or irrational cost-benefit calculation, or otherwise assumed the risks involved, simply ignores the fact that throughout the U.S. Government's investigation ZTE has acted in ways that BIS would consider illogical and unwise. ZTE committed repeated violations of the Regulations and U.S. export control laws *while knowing and accepting* the most significant of liability risks, both before and after it knew it was under investigation. ZTE then raised the risks and stakes even further *while under investigation* by repeatedly lying to BIS and other U.S. law enforcement agencies and engaging in a cover-up scheme to destroy, remove, or sanitize evidence. The bottom line is that the proffered

irrationality of the unlawful conduct does not excuse or minimize it; nor does the conduct stand alone, being part of an unacceptable pattern of false and misleading statements and related actions, as discussed above. Moreover, until BIS asked for all of the underlying documentation of the steps that ZTE said it had already taken, some of the most culpable employees faced no consequences—ZTE paid their bonuses and paid them in full and the employees went without reprimand. This is the message ZTE sent from the top.

Based on the totality of circumstances here, I have determined within my discretion that it is appropriate to activate the suspended denial order in full and to suspend the export privileges of ZTE for a period of seven years, until March 13, 2025.⁷

IT IS THEREFORE ORDERED:

FIRST, from the date of this Order until March 13, 2025, ZTE Corporation, with a last known address of ZTE Plaza, Keji Road South, Hi-Tech Industrial Park, Nanshan District, Shenzhen, China, and ZTE Kangxun, with a last known address of 2/3 Floor, Suite A, Zte Communication Mansion, Keji (S) Road, Hi-New Shenzhen, 518057 China, and when acting for or on their behalf, their successors, assigns, directors, officers, employees, representatives, or agents (hereinafter each a "Denied Person"), may not, directly or indirectly, participate in any way in any transaction involving any commodity, software or technology (hereinafter collectively referred to as "item") exported or to be exported from the United States that is subject to the Regulations, or in any other activity subject to the Regulations, including, but not limited to:

- A. Applying for, obtaining, or using any license, license exception, or export control document;

⁷ This date is seven years from the date of BIS's March 13, 2018 Notice of Proposed Activation of Suspended Sanctions and Opportunity to Respond in this matter.

- B. Carrying on negotiations concerning, or ordering, buying, receiving, using, selling, delivering, storing, disposing of, forwarding, transporting, financing, or otherwise servicing in any way, any transaction involving any item exported or to be exported from the United States that is subject to the Regulations, or engaging in any other activity subject to the Regulations; or
- C. Benefitting in any way from any transaction involving any item exported or to be exported from the United States that is subject to the Regulations, or from any other activity subject to the Regulations.

SECOND, no person may, directly or indirectly, do any of the following:

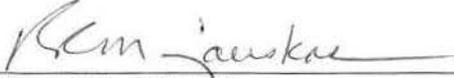
- A. Export or reexport to or on behalf of a Denied Person any item subject to the Regulations;
- B. Take any action that facilitates the acquisition or attempted acquisition by a Denied Person of the ownership, possession, or control of any item subject to the Regulations that has been or will be exported from the United States, including financing or other support activities related to a transaction whereby a Denied Person acquires or attempts to acquire such ownership, possession or control;
- C. Take any action to acquire from or to facilitate the acquisition or attempted acquisition from a Denied Person of any item subject to the Regulations that has been exported from the United States;

- D. Obtain from a Denied Person in the United States any item subject to the Regulations with knowledge or reason to know that the item will be, or is intended to be, exported from the United States; or
- E. Engage in any transaction to service any item subject to the Regulations that has been or will be exported from the United States and which is owned, possessed or controlled by a Denied Person, or service any item, of whatever origin, that is owned, possessed or controlled by a Denied Person if such service involves the use of any item subject to the Regulations that has been or will be exported from the United States. For purposes of this paragraph, servicing means installation, maintenance, repair, modification or testing.

THIRD, after notice and opportunity for comment as provided in Section 766.23 of the Regulations, any person, firm, corporation, or business organization related to a Denied Person by affiliation, ownership, control, or position of responsibility in the conduct of trade or related services may also be made subject to the provisions of this Order.

FOURTH, that this Order shall be served on ZTE, and shall be published in the *Federal Register*.

This Order is effective immediately.


Richard R. Majauskas
Acting Assistant Secretary of Commerce
for Export Enforcement

Issued this 15th day of April 2018.