Defense Trade Advisory Group
Working Task #1
Export Control Reform - Unintended Consequences

Plenary Session
January 16, 2014
Working Group Members

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Task of DTAG Working Group

• Identify potential negative impacts and unintended consequences of the Export Control Reform (ECR) Initiatives on industry and provide recommendations on how to overcome/minimize such impacts.  

Dated July 25, 2013
Industry’s Support of ECR

- Industry supports the ECR initiative to overhaul the nation’s export control system and recognize that fundamental reform of the current system is necessary to enhance national security by:

1. **Focusing resources on the threats that matter most** *higher walls around fewer items*

2. **Increasing interoperability with our Allies**

3. **Strengthening the U.S. defense industrial base by reducing incentives for foreign manufacturers to design out and avoid using U.S. parts and components.**
Working Group - Key Discussion Point

• Recalibrating requirements = Rapid changes to jurisdictional controls and technology classification.

• Working Group focused on salient long and short term changes industry will encounter in response to the plethora of regulatory changes.

• Conscious decision not to get into the weeds on issues that have "already left the station."

• Major paradigm shift = Education and familiarization of the new and revised regulations.
Primary focus of proposed and final rules to date:

- Transfer of articles/items from the ITAR to EAR
- Creation of a new 600 series under the CCL
- Reconciling of key definitions and assessing whether such terms are interchangeable between the applicable regulations.

“There are known knowns; there are things we know that we know.
There are known unknowns; that is to say, there are things that we now know we don't know.
But there are also unknown unknowns – there are things we do not know we don't know.”

Donald Rumsfeld, Former U.S. Secretary of Defense
For the Prepared & Unprepared

OEMs vs. Suppliers

D-TRADE / SNAP-R

Category XV

New Version 7.1 DSP Forms

Specially Designed

Export Enforcement

New 600-Series

“Clean Up” Rules

Large vs. Small Companies

Dual Jurisdiction

Defense Services on Non-ITAR Components

Supply Chains

Product Reclassifications

Voluntary Disclosures

Product Classification

Re-transfer|Re-export

Category VIII

Transition & Grandfathering

AES Entries
Snap-Shot of Significant ECR Events

2009
- Aug: Reform Announced Press Release
- Broad Based Interagency Review

2010
- April: “4 Singles” Announced Speech
- June: Revised License Exception ENC Notice
- Aug: Pres. Obama Lays the Foundation for New Export Control System Notice
- Nov: Executive Order Est. Export Enforcement Coordination Center Notice
- Dec: Proposed “Tiers” & Control List Clarity Notice

2011
- March: Proposed ITAR Replacement Parts/Incorporation Rule Notice
- April: Proposed ITAR Clarification on Defense Services Notice
- June: Final Rule License Exception STA Notice
- July: Proposed EAR Revision: Items Moved from USML to CCL Notice
- Nov: Proposed EAR/ITAR Aircraft Revision Rule Notice
- Dec: Proposed Revision USML Cat VI, Cat XX Notice 1 and Notice 2

Creation of the “600 Series”
Snap-Shot of Significant ECR Events (Cont.)

2012
- March
  - Opening of Export Enforcement Coordination Center (E2C2) Notice

2013
- April
  - Final Revision/Proposed Rule USML Cat VIII Notice

2013
- June
  - Revised Definition of "Specially Designed" DDT & BIS

2013
- Jan
  - NDAA Includes Authorization for Satellite Exports Notice

2013
- Mar
  - Exec. Order, First Formal Notification of Reform Process Notice

2013
- Apr
  - First pair of ECR Final Rules: Revisions to USML Cat VIII, XIX, XXI, "Specially Designed" and "Transition" Rules DDT & BIS

2013
- May
  - BATF&E USML ECR Update Notice

2013
- July
  - Proposed Rule USML Cat XV, Creation of "500 Series," Definition of "Defense Service" DDT & BIS

2013
- July
  - ECR Final Rule: Revisions to USML Cat VI, VII, XIII, XX DDT & BIS

2013
- Oct
  - Proposed Rule USML Cat XI DDT & BIS

2013
- Initial Implementation of ECR Corrections DDT & BIS

2013
- Effective Date: Revisions to USML Cat VIII, XIX, XXI, "Specially Designed" and "Transition" Rules DDT & BIS
Snap-Shot of Significant ECR Events (Cont.)

2014

Jan

- Continued Implementation of ECR Corrections
  - DDTC & BIS

- Final Rule: Revisions to USML Cat IV, V, IX, X
  - DDTC and BIS

- Effective Date: Revisions to USML Cat VI, VII, XIII, XX
  - DDTC and BIS

--- As of 01/07/2014
Issuance of Federal Register Changes

Federal Register

Industry is drinking from a fire hose

U.S. Government Output

2-SETS (4) CLEAN UP RULES
21 NOTICES
47 PROPOSED RULES
18 FINAL RULES

INFORMATION OVERLOAD
Concern # 1 – Export Control Regimes Under ECR

• **ITAR** – Continues to maintain regulatory control over defense items (Those items considered critical to maintaining U.S. military strategic advantage). **No change.**

• **600.x-Series** – Is the new regulatory list that has also resulted in a new regulatory regime to control those less sensitive defense items. The “regulatory regime” has fewer restrictions than the ITAR, but greater restrictions than what is currently called out for under the EAR. **New**

• **Legacy CCL Commodities** – Continues to maintain regulatory control over dual-use commodities requiring. **No change.**
Concern # 2 - General Industry Apprehension

- Enforcement and compliance variations between the USG agencies.
- Compliance versus enforcement under ECR.
- Voluntary Self Disclosures under ECR.
- Dual & multiple agency disclosure under ECR.
- Disclosure to one agency and not the other resulting in “directed” disclosure under ECR.

Recommendation: USG compliance and enforcement entities must remain sensitive that administrative errors will occur as industry navigates through new licensing and jurisdictional changes.
Concern # 3 – Temporary Destabilization of Industries’ Compliance Posture

• Managing the continuous stream of FR changes has unintentionally destabilized industry’s ability to effectively establish consistent compliance processes.

• Industry’s concern to remain compliant and the USG’s response during this major jurisdictional shift.

• ECR changes to date has produced challenging business maneuvers for defense manufactures and suppliers to fully implement and manage the jurisdictional changes and regulatory mandates.

Recommendation: USG Regulators should remain sensitive that industry will require time beyond the implementation dates, grandfathering, etc. to mend the link in the chain.
ECR Concern # 4 – Extent of ECR Implementation Cost (Direct & Indirect)

Significant time, money, and company resources are being invested in evaluating the operating cost of transitioning items and the general implementation of ECR.

- Tied to functional disciplines (e.g., supply chain; procurement; engineering; programs; etc.) in learning and complying with the regulation (e.g., ongoing reclassification and jurisdictional changes);
- Employing and reassigning additional staff to work through the regulatory changes;
- Changes in production and information technology processes; and
- Employing consultants or other sources of expertise to help with the regulatory compliance changes.

Recommendation: USG regulators must remain sensitive to the effects of regulatory changes and industry’s global competitiveness. USG regulators must be open and agile to industry comments and simplification as industry implements changes.
Existing Technical Assistance Agreements

- Discerning the appropriate licensing pathways for post transition activity and associated services on transitioned items becomes problematic and complex during the continued management of the authorization. Ability to obtain Commerce Licenses become relevant and existing licenses (DSP-5s; 61s; 73s) in furtherance of take on varying (transitioning & grandfathering) expiration dates.

Minor Amendments to Existing Agreements

- Agreements containing transitioning and non-transitioning items would remain valid until expiration, or for two-years from the effective date of final rule. Excessive processing of paperwork with little return or value.
ECR Concern # 5 – Managing Existing Authorizations

Transitioning/Grandfathering

- Pre/Post implementation creates multiple transaction options potentially involving the same items presents confusion and for CBP Outbound Officers and potential unwanted delay, detentions, and seizures.

Foreign Military Sales Activity

- FMS activity remains under the jurisdiction of State; however, associated parts/components transitions under the jurisdiction of Commerce. Jurisdiction of transitioned items when sold, leased or loaned by the DOD under FMS is still unclear. EAR 734.3 (1) (b) (vi) – Items not subject to EAR.

Recommendation: Continuation of the publication of FAQs to address dual jurisdictional and licensing pathways.
ECR Concern # 6 – Use of License Exception Strategic Trade Authorization

• Prerequisites requirements applied to exporter and foreign end-users transacting 600-series items creates administrative duplicity and dampens effective trade between the U.S. and its most favored allies.

• Requirement for all non-U.S. parties to the transaction to have been previously approved on a DDTC or BIS license. Purpose of this requirements is to provide assurances that the non-U.S. parties are trustworthy.

• An unending onerous requirement on both U.S. and Non-U.S. parties.

Recommendation: DDTC/BIS establish and make available a public database of non US parties listed on an approved list.
Final Comments (The Gales of ECR)

Dual Licensing
End-User Certifications
Product Reclassifications
Proper Jurisdiction
Enforcement
Product Classification
Exemption/Exception
Specially Designed
Grandfathering
Categories VII, VIII, XIX, XV
AES Filings
Supply Chain Management
600-Series .x, .y

... Or they can appear as a dynamic, inter-dependent series of incremental improvements to the U.S. export regime. *Difference is preparation and planning.*
Defense Trade Advisory Group (DTAG)

Export Control Reform Impacts on Industry
Additional WG Slides
Observation – Applicability of Definitions Unclear in ITAR

Observation: The language constructs used in the ITAR and EAR are completely different. Among other differences, the application of definitions for terms used varies greatly. Where the EAR indicates when a global definition applies to a term via double-quotes and when a local definition applies to a term via single-quotes, the ITAR does not. Further, some definitions for the same term differ between the regulations.

Impact: Within the ITAR, it is unclear when a definition applies. For example, the term “aircraft” is defined in §121.3. The definition states that it applies to Category VIII. However, industry has been told that the definition applies only to the term “aircraft” used in VIII(a), and not to the term “aircraft” used in VIII(f). Without knowing when definitions apply and when they do not, the exporter is unable to self-classify with confidence. Inconsistent use and definition of terms between the regulations can also add confusion.

Recommendation: Employ the use of the EAR language constructs in the ITAR, in particular, the standards used to indicate when the definitions for various terms apply. In addition, attempt to align the language more closely by using the same terms where possible.
USG & Industry Perspectives

• The USG has been living and breathing ECR for years
  – Development of proposed rules
  – Review of industry comments for incorporation in final rules
  – Final rules, resulting in “cleanup” rules for more clarification

• Trade compliance in industry typically understaffed
  – Many within industry have difficulty finding the time to read proposed rules
  – Many within industry have difficulty finding the time to read final rules
    – particularly if the published category is not relevant, but the USG is embedding other information within the rules
  – Industry doesn’t have the “luxury” of not getting it right
Some Additional ECR Concerns

• Original Design Intent (Over Reliance on “Specially Designed”)
  – What performance levels are the regulators specifically seeking to specify?
  – Reduced the burden of the ITAR, but transferred to complexity under the EAR by creating a new section of the EAR. Subsequently, a sanity check of the EAR should be highly consider to reconcile added changes.