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International Traffic in Arms Regulations Government and Corporate Perspectives

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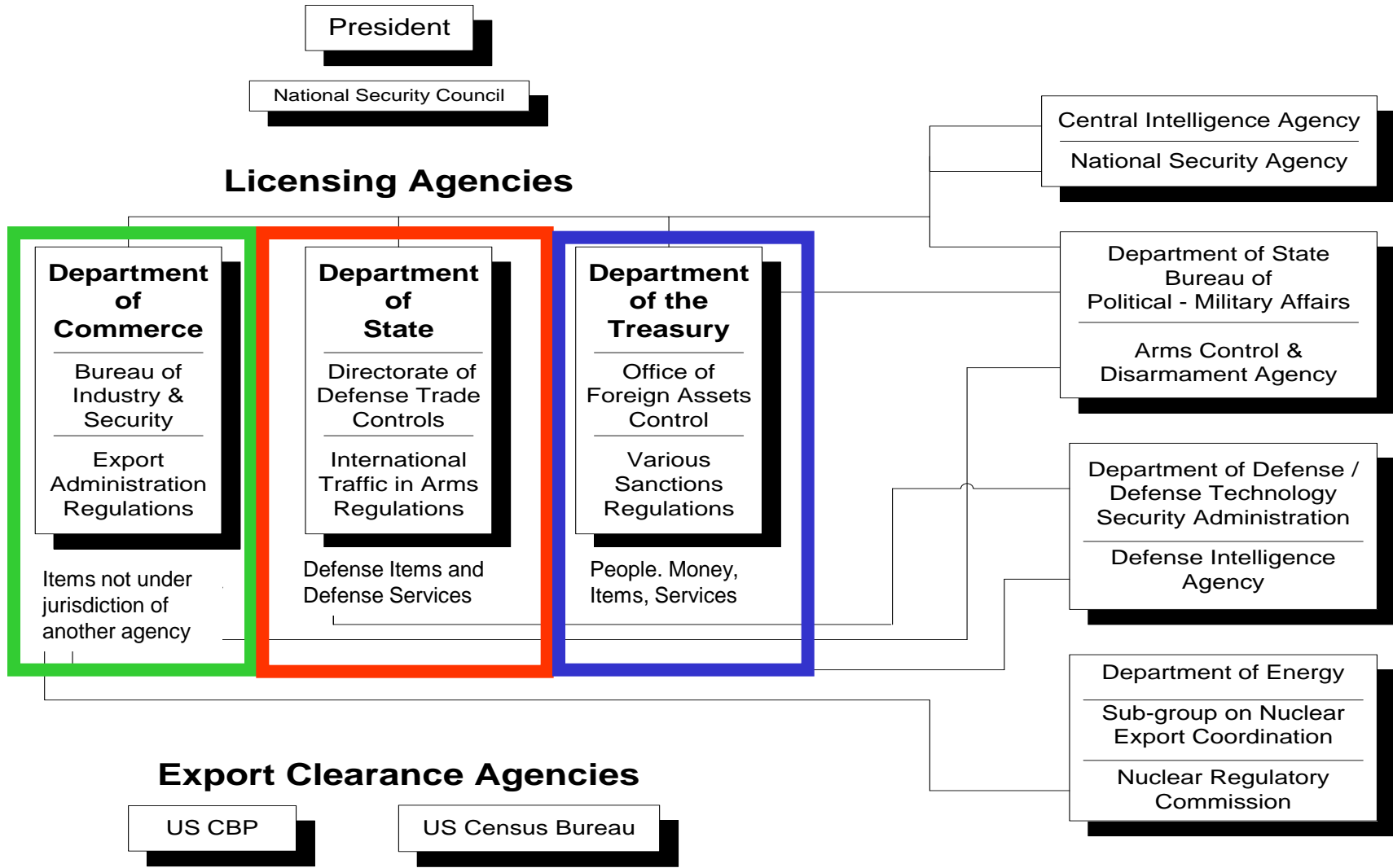
Introduction

- I do not work for the USG, it will just sound like that explaining the rules in plain English
- You can manage your business effectively under the ITAR
- You have heard the basics, and now we will dig deeper into how to manage your complex supply chain while achieving compliance, profits, satisfied customers and employees proud of your companies.
- You can do this. You can plan your affairs with DDTTC, properly set the expectations of you non-U.S. customers, meet the requirements under the ITAR, give DDTTC there due, and prove to your customers that you are a compliant company that can be proud to do business with.

Who is in the group by show of hands?

- Sales or marketing
- Engineering
- Compliance
- U.S.
- Non-U.S.
- Holding Classified Facilities
- More than five years of experience with the International Traffic in Arms Regulations (ITAR)
- More than two years
- More than one
- Clueless or in the wrong seminar

U.S. Export Control System – Regulations and Agencies



The ITAR Licensing Life Cycle

From Go to Market to Contract Completion

- Creation of the distribution system
- Trade shows
- Engineering discussions generally
- Requests for Proposals
- Presentations and proposals
- Demonstrations and test firing
- Meetings hosted and/or required by DOD
- Defense services
- Permanent export of defense articles under DSP-5s
- Returns for repairs or calibration

Engineering discussions--pitfalls under the ITAR:

- Engineering discussions present the biggest challenge for compliance officers.
- DOD program officers do not understand the ITAR.
- Foreign firms set RFP response deadlines too short to permit a U.S. exporter to obtain a TAA or authority to make a presentation or proposal for SME (all firearms and guns).
- Marketing and sales think they can get away with oral discussions re engineering, but that is not permitted.
- Foreign competitors to foreign potential buyers may already have a license before you, a U.S. firm, even realize you need one.

Lessons in dealing with DOD program officers:

- If they ask you to make technical presentations or demonstrations to foreign persons, simply do not.
- Learn to decline diplomatically and blame the State Department and your compliance lawyers:
 - Colonel, we are ready and able to provide that information to your guests from [fill in the name of the country] once we have an ITAR license in hand. We do not want a violation of the ITAR to taint the program and individuals working on the program we all support. If we had been informed of this request a few weeks ago, we could have gotten permission from the Directorate of Defense Trade Controls (DDTC). We can accomplish our goals and yet give DDTC their due.

Lessons in dealing with DOD program officers (cont):

- Program officers do not speak for the Directorate of Defense Trade Controls, not even colonels and generals. If they doubt that, give them the contact information for DDTC.
- If they persist rudely, give them the phone number at the DDTC response team, and let them have their spat with DDTC.
- There are a few DOD license exceptions under the ITAR but only 3 people in the entire Pentagon can approve them; and your project officer is not one of them even if he has stars on his shoulders.

Lessons for non-U.S. companies in the RFP process:

- Recognize your U.S. bidder needs time to get authority to provide some of the information required by your Request For Proposal.
- Set response times sufficient for the U.S. bidder to obtain authority from DDTC (the times have come down dramatically over the last year, but preparation time and the current review time add up to many weeks--it used to be many months).

Lessons for U.S. suppliers in the RFP process:

- The response to the RFP must either:
 1. Not contain any controlled technical data (ITAR or EAR), AND
For SME must not be a detailed presentation or proposal ,
or
 2. Obtain a DSP-5 Technical Data Marketing License or TAA that authorizes release of the controlled technical data , and, if SME, permission to present a detailed presentation or proposal sufficient for the potential buyer to determine to accept whether to enter into a TAA.

Lessons for U.S. suppliers in the RFP process (cont.):

- Obtain a DSP-5 Technical Data Marketing License early for all potential customers and countries. Regularly update the list of potential customers, countries, and marketing messages.
- Publish on your website your marketing messages, capabilities, and offerings after review with compliance counsel and review of government limitations on disclosure. See public domain discussion below and DO NOT provide a defense service with public domain information or EAR-controlled information without first obtaining a Technical Assistance Agreement.

When can we have engineering discussions:

- When authorized in a DSP-5 TDML.
- When authorized in a Technical Assistance agreement.
- When the discussion is no more than specific information published about your capabilities and offerings.
- When all the information is in the public domain both in individual messages and when taken as a whole & you do not provide a defense service.
- A DSP-5 may authorize a one-way export; not discussion.
- I know engineers are trained and paid to solve problems.
- But DDTC's goal is to prevent solutions for bad guys, untrustworthy parties, and parties without constraints on retransfer. Your unauthorized engineering discussions do not meet one or more of those goals.

Trade show, demonstrations, and firing tests:

- Obtain DSP-73 for temporary export:
- Follow the guidelines for fire arms and ammunitions.
- If the trade show and item are previously licensed, then use license exemption for a second or third show if such is defined in the license. It is not a blanket trade show license exception.
- Do not combine a marketing license request and a trade show request. Some times you can combine marketing and test firing and some times you cannot.
- Technical data disclosed at trade shows is often in the public domain. However, see discussion below re public domain, defense services, and presentations and proposals.

DDTC Guidance:

- Guidelines for the “Permanent Export, Temporary Export, and Temporary Import of Fire Arms and Ammunition, U.S. Munitions List Categories I and III”
 - Discussion of the sample checklist at pages 12 to 15.
 - Record this title so you may look it up on the Internet for updates. The recent changes to improve the DDTC website eliminated the search function, and this document and others are now difficult or impossible to find.

Defense Services defined:

- TAA is required for Defense Service, including:
 - Service provided with publicly available technical data or EAR-technical data,
 - Military training, and/or
 - Transfer of ITAR-controlled technical data.
- Do not turn a response to an RFP into:
 - An unauthorized engineering discussion,
 - An unauthorized sales presentation or proposal, or
 - A defense service.

Public domain treatment & the defense services pitfalls:

- Public domain treatment is available for information released at a trade show, presentation, or in any other context EXCEPT PROVIDING A DEFENSE SERVICE.
- Do not publish technical data or software without checking contracts with DOD. Note that for DOD related TD, release into the public domain often requires approval from the Office of Security Review (formerly known as of Office of Freedom of Information) and Security Review or from the Cognizant Security Agency.
- DDTC argues that some information is not “in a public library” and is not published just because it is on the Internet. DDTC says that if you sit at a terminal in a public library and go on the Internet, the technical data is not “in” the library.

The Export Administration Regulations:

- This is a seminar about coping with the ITAR. However, there are licensing requirements under the Commerce Control List for:
 - Defined gun making machinery (see ECCN 2B018) if the items are not subject to the ITAR, and
 - Certain shotguns with a barrel length of 18 inches or greater (see ECCN 0A984)

Commodity Jurisdiction

- Category II(g) for equipment and tooling to make gun is subject to the ITAR.
- It conflicts with ECCN 2B018 of the CCL.
- The ITAR prevails over the CCL.
- Never rely upon a commodity classification performed by BIS to determine agency jurisdiction. Only the State Department can determine the scope of its jurisdiction.

The see-through rule:

- If you sell parts, be prepared to answer the commodity jurisdiction certifications to your commercial customers of parts.
- Some items designed for military applications under the design intent standard have commercial applications. They remain subject to the ITAR even when incorporated into commercial items.

The Munitions Parts Incorporated into Munitions items

- What do these two items have in common?



- This little \$1,500 part (QRS-11)

Quartz Rate Sensor



- *What is the consequence?* Commercial items may be considered munitions and subject to stringent export controls (for example exports to China were prohibited under the ITAR—at least until a jurisdictional change in the regulations just for certain QRS-- applications)

Jurisdiction Determination Analysis

Some of the Things to Consider

Was it originally designed for commercial market applications has it been modified in any way for a military use?

Is the part number unique to the customer or application?

Was it originally developed for a military/defense application?

Was the underlying technology for it originally developed for a military/defense application?

If it (think: exact same part number!) has predominant civil applications, was it MODIFIED in any way from a military version of the product?

Does it contain any parts, components, or assemblies that were specifically designed, developed, configured, adapted or modified for an Aerospace or Military Application?

Was it originally developed for a governmental application?

What was the intended market at time of initial design?

Does it (think: exact same part number!) have predominant civil (commercial) applications?

Was it designed or tested to a military/defense customer's specifications?

Has any of the funding for development or manufacturing of it come from governmental entities?



Value:

- The ITAR calls for the arms length value the exporter will receive in payment from the direct buyer abroad.
- The same standard applies for the Export Declaration to the Bureau of the Census via your filing with Customs and Border Protection for each export.
- Recognize the need for a signature from the ultimate non-U.S. government on the DSP-83 will result in the in-country contractor's markup becoming known.
- Discussion of the issues surrounding procurement by the Japanese MOD.
- Do not give your compliance people the amount paid by the end user. Give the price paid to you by your immediate buyer.

Coatings--manufacturing versus defense service or overlap:

- Example of a grey area requiring some guidance.
- Typically, DDTTC views coating in the U.S. of non-U.S. munitions parts (aircraft parts, satellite parts, and gun parts) to be a defense service.
- The ITAR require a TAA for any defense service for a foreign person.
- However, at least for aircraft parts, DDTTC usually will accept a DSP-5, and that requires less paper work and less review time.
- What of gun parts?

Returns and repairs:

- Temporary returns to the United States of items subject to the ITAR require:
- Specific entry descriptions on the foreign firm's commercial invoice to inform the U.S. import authorities of the reliance upon an ITAR license exception for such a temporary import and special information from the importer of record upon import into the United States.
- Export declaration claiming the right to use an ITAR license exception for return of the repair or recalibrated item.
- Compliance with the limitations of the license exception.

U.S. manufacturers who do not export:

- You have to register with DDTC as a manufacturer under the ITAR even if you do not export.

What if I just export to Canada?

- You have heard of a Canadian exemption, but there is no Canadian exemption (among the many) that is a blanket exemption.
- You have to register under the ITAR to use any exemption.
- Canada is NOT the 51st State even though it is a close ally.
- Watch for the controlled goods program of Canada in addition to the DFAIT licensing requirements.

Non-U.S. Firms & Other Rules:

- I am a non-U.S. firm, what else do I need to consider before investing in a U.S. maker of firearms, guns, or ammunition?
- There are three national security agencies you must consider.
 - Directorate of Defense Trade Controls (DDTC)
 - Committee on Foreign Investment in the United States (CFIUS)
 - Defense Security Service (DSS)

Non-U.S. Firms & Other Rules (cont.):

- A U.S. registrant must report to DDTC 60 days in advance of the transfer of control to any non-U.S. company.
- You will need to organize a U.S. subsidiary and register with DDTC and provide this information to the target.
- The Committee on Foreign Investment in the United States (CFIUS) reviews investment in the U.S. with national security implications.
- An investment in a U.S. registrant always requires a CFIUS review. The reviews are not really voluntary because DDTC forces them.
- The list of information required is extensive and the questioning or vetting phase is intense.

Non-U.S. Firms & Other Rules (cont.):

- You need to account for the CFIUS review in your acquisition agreements, the price of the acquisition, and the time necessary for review before you may close. Insist your deal counsel consult with national security counsel before signing any agreement or letter of intent.
- The Defense Security Service regulates classified facilities and classified contracts. It also regulates Foreign Ownership Control and Influence (FOCI) to avoid diversion of classified information to foreign persons and foreign corporations, including foreign owners.
- Mitigation agreements (a) usually put the majority of the board in the hands of persons approved by DSS, responsible to DOD, and with no prior involvement with the owners, and (b) prevents foreign management.

So-called brokering and your supply chain:

- Foreign persons, including your wholly own-foreign subsidiaries, are required to register and seek certain approvals from DDTTC for arranging sales and asset-based lending for U.S.-origin items subject to the ITAR.
- U.S. persons, in the U.S. or abroad, including your foreign unincorporated branches of a U.S. corporation, are required to register and seek certain approvals from DDTTC for arranging sales and asset-based lending for U.S. and foreign-origin items described on the USML but not subject to the ITAR because there are no U.S.-origin ITAR-controlled parts.
- DDTTC is likely modifying the rule; however, it is not likely to reduce requirements in my judgment.

The enforcement environment:

- Increased criminal actions against both large and small companies.
- Hundreds of voluntary disclosures to DDTC per year:
 - Almost completely eliminates criminal risks assuming a complete and accurate disclosure.
- While DDTC imposes substantial administrative fines in a handful of cases each year, it often directs self-audits (shared with DDTC) and requires responses and compliance steps that may be costly.
- Until this year, the high water mark for a criminal fine was \$100 million dollars and a multimillion dollar administrative fine against ITT. Their monitorship end in April of 2010.
 - The statement of facts by the U.S. attorney is riveting reading for business people. It is required reading.

The enforcement environment (cont.):

- In 2010, the Department of Justice settled with BAE Systems UK for \$400 million for failure to report fees and commission required under the ITAR. The allegations were largely of bribes paid to government officials in other countries to obtain contracts to reexport defense articles and defense services subject to the ITAR.
- Department of Justice uses stings and fronts in export control matters, and those stings and fronts are similar to the Shot Show stings for allegations of the Foreign Corrupt Practices Act.

The enforcement environment (cont.):

- Department of Justice arrests foreign persons for export control violation while in the U.S. on travel and is willing to seek extradition for export control violations.
- It is more likely than not to succeed in such efforts when the home country requires a license for the same items to the same ultimate country of destination.
- Department of Justice recently lost an extradition case in France regarding an Iranian for reexports to Iran because the export from France was not prohibited by its laws:
 - U.S. will seek extradition, and
 - For guns and armaments, there will usually be a local law violation that supports extradition.
- China is the greatest concern under the ITAR and licenses are prohibited and denied.

General lessons and observations:

- Your business has a complex supply.
- The project life cycle requires DDTC approvals in many separate parts of that supply chain and often does not permit requests for a combination of authorities.
- The DSP-5 Technical Data Marketing License is a useful tool for marketing and detailed SME presentations and proposals.
- DDTC may soon eliminate the requirement for prior approval of such presentations and proposals; however, you will still need DDTC authority for the controlled technical data you wish to release in presentations and proposals.
- The enforcement environment is becoming more active, especially on the criminal side.

General lessons and observations (cont.):

- You need compliance advisors in-house and/or outside. Keep them informed early and often. They can help you with your plans and help you properly set customer expectations but only if you communicate with them.
- The ITAR is a benefit. It enables you to trade with the blessing of the United States Government.
- You can do this. You can plan your affairs with DDTC, properly set the expectations of your non-U.S. customers, meet the requirements under the ITAR, and give DDTC there due.
- More importantly, your customers want to deal with responsible, compliant companies; and you can demonstrate that you fill the bill.



Thank You.

May I Take Your Questions?

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