



U.S. State Department Export Compliance Hot Topics – Changes & Trends

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State Department Trends

- **Increase in enforcement activity**
 - New “Export Czar” - Steven Pelak, DOJ National Export Control Coordinator
- **Jurisdiction – broader discretion exercised... DDTC asserts jurisdiction often**
- **Political concern with ITAR-free development by companies competing for major DOD contracts**
 - European Space Agency proposing 400 million Euro budget for technology to “free Europe of dependence on ITAR” items

ITAR Enforcement

Increase in Enforcement Activity in FY 2007

- 759 voluntary disclosures (up 60%)
- Big fines
 - ITT - \$100 million criminal penalty
 - Northrop Grumman fine of \$15 million
- 516 directed disclosures
- 50% increase in criminal investigations
- 50% increase in criminal indictments
- Record number of Blue Lantern checks
- ICE arrests = 164
- ICE indictments = 121
- ICE convictions = 91

ITAR Enforcement

Future Trends

- Defense Services
 - Head of enforcement indicates DDTC takes a broad approach, and
 - DDTC knows companies have difficulties appreciating that defense services license requirements are broad
 - Example: use of public domain technology and principles to perform fault analysis, collate pieces of information, and apply them to a military application
 - A TAA is required for almost all discussions related to defense articles



ITAR Updates

ITAR Amendment Regarding Aircraft Parts (8/14/2008)

- Elements for non-hot section aircraft parts:
 - standard equipment on civil aircraft per FAA certificate
 - integral part of a civil aircraft
- Apparent goal of DDTC is to eliminate the need to look historically to the original design intent and perform a forensic jurisdiction; however, the amendment leaves in place 120.3 discretion

ITAR Updates

Dual and Third Country Nationals

- Amendment to 22 C.F.R 124. 12 and 124.16
- Allow access to defense articles and services for dual and third country nationals of NATO countries through revised procedures for defense services agreements.
- NATO countries the members of the European Union, Australia, Japan, New Zealand and Switzerland.



ITAR Updates

DDTC Registration Fees

- New regulations effective Sept. 25, 2008
- DDTC mission = 75% “self-funded”
- Fees based on usage (includes license application volume – DSP-5s, 73s, 61s, 85s, 119s, 53s, agreements and amendments – excludes RWAs, disclosures, CJs)
- Base fee = \$2,250 per year
- DDTC to send notification of fee due 60 days prior to expiration
- Appeal process to request alternate payment schedule

ITAR Updates

Voluntary Disclosure

- **60 day deadline after initial notification to submit a full disclosure of suspected violations.**
- **Directed disclosures – Not regulatory requirement but there appears to be a current trend towards increasing directed disclosure requests from DDTC.**

ITAR Updates

Voluntary Disclosure (Cont.)

- **DDTC trend is to request a “directed audit” of the company’s last 5 years of ITAR exports**
 - **must be done by “independent” auditor (i.e., firm or consultant that hasn’t previously provided services to the company)**
 - **auditor must be approved by DDTC**
 - **audit plan requires DDTC prior approval**
 - **comprehensive – typically must include all business units**
 - **company must make export documentation available to DDTC**

ITAR (Related) Update

Mandatory use of AES

- New regulations effective July 2, 2008
- Enforcement begins September 30, 2008
- “SED” becomes “EEI” (Electronic Export Information)
- Criminal penalties for knowingly failing to file EEI or knowingly submitting false export information
- Civil penalties increased for filing errors or late filings
- New regulatory scheme transforms a routine administrative statistical filing into a new area of export enforcement

ITAR Updates (Pending)

Security Assistance and Arms Export Control Reform Act

- Performance goals for DDTC license application/Agreement processing (60 day target)
- Minimum DDTC Licensing staffing requirements
- ICE officially authorized to investigate ITAR violations
- DDTC flexibility on user fees, self-financing
- 5-year review of ITAR and USML
- Special licenses for spare/replacement parts to NATO & NATO-ally countries
- Report on Satellite Export Controls w/in 180 days
- STATUS: 5/15 Approved by House, 5/18 sent to Senate Foreign Relations Committee

ITAR Update - Guidelines

New DDTC License Documentation Guidelines

- **Published on DDTC website April 28, 2008**
- **Purchase documents (P.O., Contract, Letter of Intent) MUST be from foreign buyer, not US subsidiary, and MUST be addressed to US registrant selling the defense articles & submitting the license application**
- **Purchase documents MUST have issue date within 1 year from date of license application submission (if not, need a letter of explanation, handled case-by-case)**
- **Exchange rate – applicant must convert to US \$**
- **Purchase documents MUST state ultimate end-user and end-use & be consistent w/license application**
- **Application RWA'ed if not compliant with these guidelines**

ITAR Update - Guidelines

Foreign National Employees

- Guidelines published on DDTC website 9/08
- DSP-5s required for employees
 - full time regular employee
 - directly paid, insured, hired/fired or promoted
 - resident in U.S. or abroad
- Current authorizations (e.g., TAA) are still valid, must change to DSP-5 at renewal
- Be specific in scope



ITAR Update - Guidelines

Defense Service Agreement Rebaseline

- DDTC effort to review existing agreements (TAAs/MLAs) to determine if compliant with current policies
- Factors:
 - age of agreement (> 10 years old)
 - numerous amendments (> 10 amendments or proviso reconsiderations, regardless of age)
- Licenses issued pursuant to agreements are part of rebaseline
- Agreement rebaseline submission treated as a new submission, current agreement still valid while submission pending

DDTC News

DDTC Website Announcements

- Updated D-Trade Frequently Asked Questions (FAQs)
- Final Rule issued regarding DDTC registration fees
- Company Visit Program FAQs
- Licensing of Foreign Persons FAQs
- DDTC In-house training now available
- Final Rule amending USML Category VIII (civilian aircraft parts/components)
- D-Trade 2 updates
- Reminder - ITAR registration period is 1 year
- See: <http://pmddtc.state.gov/index.html>

DDTC News

Company Visit Program

- **WHAT IS IT?**

Visits by DDTC Compliance officials to registered companies – a “learning tool”

- **WHAT IS IT NOT?**

An audit or inspection

- **PURPOSE?**

- (1) learn how companies have established an ITAR compliance program
- (2) understand how those programs are implemented/function
- (3) gather information to determine if DDTC is properly exercising its regulatory responsibility in licensing and compliance
- (4) gather information to revise regulations and practices

DDTC News

Company Visit Program (Cont.)

- **HOW ARE COMPANIES SELECTED?**

By volume of licenses, nature of business, type of technology, geographic location, follow-up to a disclosure, monitoring of a consent agreement

- **HOW IS IT CONDUCTED?**

- (1) notification letter sent 6-8 weeks prior, includes materials required to be provided (e.g., compliance manual, policies & procedures, organizational chart, overview of ITAR program and facility)
- (2) agenda for 1 or 2 day visit, 2-4 DDTC staff
- (3) post-visit briefing at conclusion of on-site visit
- (4) formal letter w/issues raised in briefing and lists areas of improvement

DDTC News

Company Visit Program (Cont.)

- **RESULTS (published by DDTC):**
 - 60+ companies visited since 10/05
 - Overall results are positive
 - Win/Win?



DDTC News

Electronic Licensing Update

- **D-Trade**

- Required for most license applications (DSP-5, DSP-61, DSP-73)
- Requires a digital certificate – plan ahead!

- **D-Trade2**

- Will support new amendment forms (DSP-6, DSP-62, DSP-74), GCs, Opinions, CJs, Registration, notifications
- Currently in User Acceptance Testing – no date published for roll-out

ITAR Enforcement Trends

Critical U.S. Military Technologies

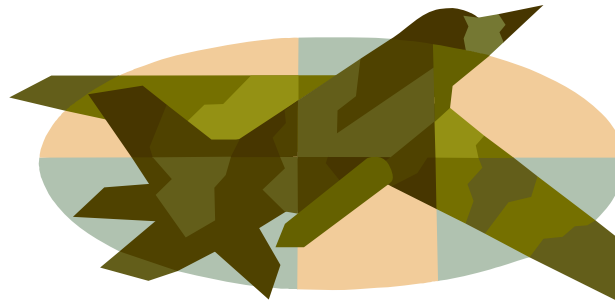
- DDTC discretion to exercise jurisdiction - need to know what items are focus for control
 - Night vision technology (to see the enemy before it sees you)
 - Underwater sea technology (seismic or audio sensing to see the enemy before it sees you)
 - Other technology designed to see the enemy before it sees the U.S. military (imaging and other technologies useful for target acquisition, stealth technologies and techniques to avoid detection, detection countermeasures)



ITAR Enforcement Trends

Critical U.S. Military Technologies (Cont.)

- Aircraft technology (composite materials and means to make missiles and aircraft stronger, lighter and/or faster)
- Hot section technical data for gas turbine engines (having aircraft ready to fight at a high level of performance at every moment)
- Communications secure from the enemy (encryption, command and control)



ITAR Enforcement Trends

Critical U.S. Military Technologies (Cont.)

Per Export Prosecutions

- **Carbon-fiber material** with rocket & spacecraft applications to China (10/08 grand jury indictment)
- **Electronics & IED Components** to Iran (9/08 indictment)
- **Rifle scopes** to Russia (9/08 grand jury indictment)
- **Technical Data on Unmanned Aerial Vehicles** to China (conviction 9/08)
- **Infrared Assault Rifle Scopes** to Indonesia (sentencing 7/08)

ITAR Enforcement Trends

Key National Security Issues:

- China
 - concern of potential war over Taiwan
 - fundamental difference in U.S. and E.U. view of Chinese threat or lack thereof
- Iran
 - development of nuclear weapon
 - full U.S. embargo
 - concern regarding diversion to Iran
- North Korea
 - development of further nuclear weapons
 - willingness to proliferate nuclear and missile capabilities

ITAR Compliance

Mergers and Acquisitions:

- ITAR notifications
- CFIUS (Committee on Foreign Investment in the United States) legislative updates
- Business reasons to perform pre-acquisition export compliance due diligence and assessments
- Test case: Titan



ITAR Compliance

Mergers and Acquisitions (Cont.):

- ITAR notifications
 - complex procedural steps required in advance of closing
 - foreign acquiring firms must give DDTC 60 days advance notice and other notifications before and after the closing – even if only an investment by a foreign party in a U.S. registrant
 - DDTC also expects certain notifications and steps by a U.S. acquiring firm
 - Remember that the acquiring firm must be registered with the DDTC to acquire ITAR regulated activities

ITAR Compliance

Mergers and Acquisitions (Cont.):

- CFIUS Requirements
 - voluntary filing - pre-acquisition approval of a foreign acquisition
 - recent developments indicate greater emphasis on export compliance during the review
 - CFIUS review agencies requesting evidence of export control and embargo compliance (including reexport controls – ITAR, EAR and OFAC)
 - certifications of compliance to DDTC and BIS
 - Commerce requests to submit classification requests

ITAR Compliance

Mergers and Acquisitions (Cont.):

- Importance of Pre-acquisition Due Diligence
 - Buyers – avoid buying a violation and paying too much for the target company
 - Buyers take on successor liability in both stock and asset acquisitions
 - Sellers – get the best price and avoid costly delays and failed negotiations and closings



ITAR Compliance

Goal: be a trusted exporter

- Each submission to the U.S. Government presents:
 - An opportunity to illustrate your expertise, care and commitment to compliance, OR
 - A means to reduce the trustworthiness of your company in the eyes of the U.S. Government
- Indifference to the regulations will damage your company's reputation and reduce the likelihood of favorable licensing decisions
- Think like a licensing officer / investigator

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