
Department of State Defense Trade Controls Overviews

Report Released By The Directorate of Defense Trade Controls

[The following article was recently released by the Directorate of Defense Trade Controls (DDTC), U.S. Department of State (DoS). This and several other documents of interest to the international community are available at the following web site: <http://www.pmdtcc.state.gov>.]

This document is intended to provide an overview of the Department of State's defense trade controls. These controls are contained in the *Arms Export Control Act* (AECA) and the *International Traffic in Arms Regulations* (ITAR), both of which are authoritative on this matter. (Additional information regarding the Act and the Regulations are available on the following web site: http://www.pmdtcc.state.gov/docs/defense_trade_overview_2006.pdf.) This document is not intended to serve as a basis for any registration or licensing decisions on the part of the public or the Directorate of Defense Trade Controls. If any discrepancy between this document and either the AECA or the ITAR, the Act and the Regulations will prevail.

Defense Trade Controls Overview

The Department of State has been responsible for regulating defense trade since 1935, with the objective of ensuring that U.S. defense trade supports the national security and foreign policy interests of the United States. We seek to deny our adversaries access to U.S. defense technology while ensuring that defense cooperation with friends, allies, and coalition partners contributes to their ability to defend themselves and fight effectively alongside U.S. military forces in joint operations. We also scrutinize potential defense exports for their effect on regional stability. Depending on the context, exports of small arms or helicopter spare parts can contribute to instability as easily as attack aircraft or missiles.

Today this function is vested in the Bureau of Political Military Affairs' Directorate of Defense Trade Controls (DDTC), headed by a Deputy Assistant Secretary and Managing Director and consisting of the following offices:

- Offices of Defense Trade Controls Policy (DTCP)
- Defense Trade Controls Licensing (DTCL)
- Defense Trade Controls Compliance (DTCC)
- Defense Trade Controls Management (DTCM)

The AECA and *Foreign Assistance Act* (FAA) of 1961 are the basic legal authorities, implemented by the ITAR.

DDTC regulates the temporary import and the permanent and temporary export of defense articles and defense services, to include brokering, involving items on the *U.S. Munitions List* (USML), Part 121 of the ITAR). The USML generally covers items specially designed or modified for military applications, and its twenty categories extend from firearms to the Joint Strike Fighter (JSF). The scope of items on the USML is similar to the control lists of most other significant arms exporting countries, although the USML contains some items that other countries do not generally control as defense articles. For example, commercial communications satellites, their parts, components and technology, are controlled under Category XV of the USML.

The ITAR covers not only hardware but also technical data and defense services, but excludes basic research and information that is in the public domain. Under the ITAR, an “export” includes not only physically taking a defense article out of the United States but also disclosing (including oral or visual disclosure) or transferring technical data to a foreign person, whether in the U.S. or abroad. It also includes performing a defense service on behalf of, or for the benefit of, a foreign person, whether in the U.S. or abroad.

Registration

Any U.S. person involved in the manufacture, export, or brokering of U.S. defense articles or services is required to register with DDTC and pay a fee of \$1,750 per year. Any U.S. person or any foreign person subject to the jurisdiction of the U.S. who engages in brokering activities with respect to U.S. or foreign defense articles or services must also register. A U.S. person is a U.S. lawful resident, “protected person,” or a U.S. incorporated business or entity. Registration is necessary before a U.S. person may apply for a license or other approval or use a regulatory exemption from a license requirement. However, even manufacturers that do not export are required to register and pay the fee, as has been the case since 1935. In fact, less than half of the 5,000+ entities currently registered are likely to apply for a license in any given year. However, registration provides important information on the identity and location of defense companies and enforces on their management a large degree of responsibility for compliance with export controls laws. Moreover, even companies that do not export to other countries in the traditional sense have responsibilities under the ITAR, including the obligation not to transfer controlled technical data to a non-U.S. person within the U.S. without the written authorization of the DoS.

Registration is also important to determining that a U.S. person is eligible to export, as certain parties are prohibited from participating in defense trade. For example, persons indicted of violating the AECA or certain other U.S. laws are ineligible to export, and persons convicted of such violations are formally debarred. Registration (as well as all license applications) requires the applicant to certify that the corporate officers are eligible under the regulations to participate in defense trade.

The ITAR also requires a license for any brokering activity by U.S. persons anywhere in the world or foreign persons subject to U.S. jurisdiction involved in the brokering of U.S. or foreign defense articles or services. Brokers (U.S. and foreign parties who are subject to the jurisdiction of the United States) must separately register and pay the fee. Under the ITAR, a “broker” is anyone who acts as an agent for others in negotiating or arranging contracts, purchases, sales or transfers of defense articles or services in return for a fee, commission or other consideration.

Licensing

A registered party may apply for an export authorization a “license” or “agreement” from the Office of Defense Trade Controls Licensing (DTCL). With few exceptions defined in the ITAR, all transfers of U.S. defense articles or services to foreign persons require case-by-case review and authorization by DTCL. A “foreign person” is anyone who is not a “U.S. person,” as described above, and includes inter alia foreign companies and governments, international organizations, and foreign diplomatic missions in the United States. In fiscal year (FY) 2006, the office took final action on 66,000 cases, with case volume increasing at about 8 percent per year.

Export licensing requirements are based on the nature of the article or service and not its end use. For example, a defense article, e.g., a radar component designed for military purposes, being exported to a civilian end user such as a foreign equivalent of the Federal Aviation Administration is subject to the same licensing requirements as if it were going to a foreign military. The issues in the review

process might be different, but the licensing requirement remains. This approach is based on the idea that the technology itself requires control, no matter what the end use.

Each license application for permanent hardware export must be accompanied by a purchase document (e.g., a signed contract) and identify the items to be exported, as well as all parties to the transaction – not just the end-user but also brokers, shippers, freight forwarders, distributors, etc. About a third of license applications are referred to other DoS bureaus, as well as the Department of Defense’s (DoD) Defense Technology Security Administration (DTSA) or other agencies for review.

All export approvals require the prior written consent of the DoS before the recipient may retransfer the item to another end-user (including to another country) or change its end-use from that originally authorized. This prior consent requirement applies even if the ITAR–controlled article or technology is incorporated in a foreign item. For items that are designated on the USML as “significant military equipment” (SME) because of their “substantial military utility or capability,” as well as for all classified defense articles, a specific non-transfer and end-use certificate (DSP-83) is required. This form must be executed by the exporter, the foreign end-user and any foreign consignees before the export will be authorized under a license or an agreement. It stipulates that the parties will not re-export, resell or otherwise dispose of the SME outside the country without the prior written approval of the Department of State. In cases where a DSP-83 is not required, the agreement, invoice or bill of lading must contain specific language ensuring that the foreign parties to the transaction are aware of and accept the requirement for prior written approval for any retransfer or change in end use.

These requirements apply to U.S. defense exports to all countries, including our North Atlantic Treaty Organization (NATO) allies, Japan and Australia. Although most export applications are for hardware, the most important and complex cases are for defense services, which include:

- Furnishing assistance (including training) to a foreign person, whether in the U.S. or abroad, in the design, development, engineering, manufacture, production, assembly, testing, repair, maintenance, modification, operation, demilitarization, destruction, processing or use of defense articles.
- Furnishing any technical data controlled under the ITAR to a foreign person, whether in the United States or abroad.
- Military training of foreign units or forces, including formal or informal instruction of foreign persons in the United States or abroad.

The export of defense services is authorized under a Technical Assistance Agreement (TAA) or Manufacturing License Agreement (MLA). In fiscal year 2006, more than 7,000 agreement applications were received, and their number, value and complexity are growing. In fact, the value of defense services provided in accordance with such agreements is roughly equal to or greater than the value of hardware exports. Almost all agreements are referred to DTSA for national security and technical review. The vast majority are only approved subject to specific conditions on technology release.

Defense service and technical assistance agreement are terms of art that are utilized in Section 38 of the AECA, and the ITAR extends beyond the normal meaning of the words “service” and “assistance.” For example, if a U.S. defense company provides controlled technical data to its foreign supplier so the latter can manufacture a component to certain specifications, the U.S. company is performing a “defense service” for which it will require a “technical assistance agreement” despite the fact that it would seem that it is the foreign company that is providing a “service” or “assistance” to the U.S. company.

Even if there is a government-to-government agreement applicable to the defense service, e.g., a Memorandum of Understanding (MoU) for JSF cooperation, a TAA is still required to cover the activities of the U.S. company. Furthermore, it is necessary for all parties to sign the TAA or MLA, even if the same parties have signed a MoU. This is to ensure that each party, U.S. or foreign, involved in activities covered by the agreement understands and accepts its responsibilities, including the requirement for prior written consent from the DoS for any retransfer or change in end use.

As with government-to-government transfers, licensed commercial defense exports are subject to advance notification to Congress if they exceed a certain value. For NATO, Japan, Australia and New Zealand, the thresholds are \$25 million for major defense equipment (MDE) and \$100 million for all other defense articles and services, and the notification period is fifteen days. For all other countries, the thresholds are \$14 million for MDE and \$50 million for all other exports, and the notification period is 30 days. Small arms exports (USML Category I) over \$1 million must also be notified to Congress, as well as all overseas manufacturing agreements for SME, regardless of value. The AECA allows both houses of Congress to enact a joint resolution prohibiting the export within the 15/30 day notification period.

The median review time for cases handled internally in DTCL (two thirds of total cases) is eighteen calendar days. Review time for the remaining third that are staffed to DoD and other offices in the State Department is about fifty-five calendar days. Denials amount to only about 1 percent of applications, largely due to the fact that Part 126.1 of the ITAR publicly identifies proscribed locations (e.g., Iran, China), so exporters don't bother seeking approvals for such countries. Also, when exporters have questions on whether a prospective transaction might be denied, they often request a non-binding advisory opinion before submitting a license application. In addition to actual denials, however, about 15 percent of applications are returned without action (RWA, essentially a denial without prejudice), usually because some required documentation is missing or because DTCL does not have confidence in some specific aspect of the transaction. Another 30 percent of cases are approved subject to specific conditions or provisos.

Outreach and Automation

In fiscal year 2006, 78 DDTC speakers participated in fifty-eight events around the U.S. and in foreign countries, including Australia and India. DDTC's Response Team handled roughly 25,000 phone inquiries and 8,500 e-mails from the public, which somewhat diminished the demands on the time of licensing and compliance officers. In addition, our IT help line answered about 6,500 requests for information and technical support regarding our expanding paperless Defense Trade Application System (DTAS), of which the D-Trade electronic licensing system is a major part.

DTAS, and in particular two of its components, D-Trade and Trade Registration, Enforcement (T-RECS), and Compliance System) play an essential role for DDTC. Today half of all cases are submitted through D-Trade, which is a fully-electronic system. They are generally completed in half the time it takes for legacy cases, which were either hardcopy or partially electronic. The quality control dimension of D-Trade (improperly documented applications will be automatically rejected by the system) economizes licensing officers' time, as they spend less time correcting applicants' errors. Case tracking and information management is significantly improved. Electronic registration combined with direct deposit of registration fees through PAY.gov is also a major process improvement.

On October 12, 2006, DDTC stopped accepting applications through the legacy (partially electronic) system for three license types (which together account for more than 70 percent of all licenses and agreement applications). DDTC has recently received OMB authority to use three additional D-Trade forms (for the amendment of the other three licensing forms), and we expect to make their use mandatory by February 1, 2007. We expect to make the use of D-Trade available

for all unclassified authorizations, including agreements, during 2007. Our goal is to make D-Trade so attractive that exporters will use fully electronic licensing as a business choice. The impact on timeliness, effectiveness, and efficiency will be huge.

Compliance

Nothing that happens with registration or licensing matters much if the parties to an export do not comply with the applicable law and regulations, as well as the terms of the authorization. The DTCC has a vigorous program to ensure all parties to an export have reason to respect the export process and its regulation. The office works in close cooperation with Customs and Border Protection (CBP) and Immigration and Customs Enforcement (ICE), which are parts of the Department of Homeland Security (DHS). An officer from ICE is detailed to the staff of DTCC, as is an agent of the Federal Bureau of Investigation (FBI). DTCC works closely with the FBI and the Department of Justice's U.S. Attorneys Offices around the country on criminal prosecutions.

DTCC activities support the licensing process and enforce the law and regulations through criminal and civil enforcement actions. The licensing review process involves a risk assessment of proposed exports and relies to a large part on an evaluation of the reliability of the parties to the transaction. DTCC supports this review by providing intelligence and law enforcement information to licensing officers through the use of a watch list and through the conduct of overseas end-use checks conducted under the Blue Lantern Program.

DTCC maintains a watch list of more than 130,000 foreign and domestic companies and individuals identified from various open and classified sources. All parties on license applications and agreement applications are checked against this watch list. If the name of a party is on the watch list, the licensing officer evaluates the information on the listed party, and the license may be denied. DTCC also coordinates the Blue Lantern end-use monitoring program, a system of overseas pre-license and post-shipment checks usually conducted by U.S. embassy personnel at posts around the world. These end-use checks seek to verify the bona fides of foreign parties or confirm that the conditions of approved license authorizations are being respected (e.g., that the shipper actually delivered the defense article to the intended end-user, or that the foreign recipient has not retransferred the item without U.S. consent). In fiscal year 2006, there were 613 Blue Lantern checks (surpassing the previous record number of 563 in fiscal year 2005), and unfavorable information was identified in over 90 cases.

The Blue Lantern program is an important factor in developing and maintaining our confidence in the recipients of U.S. defense exports. Parties that cooperate with Blue Lantern checks soon establish a track record of reliability, with the result that they are less likely to be the target of such checks in the future. On the other hand, parties that refuse to cooperate or cannot account for previously authorized defense exports raise significant doubts about their reliability, which will constrain future licensing decisions and may result in a company being put on the watch list of suspect parties.

DTCC is also responsible for supporting criminal investigations of violations of the AECA and for initiating administrative enforcement actions under its own authorities. The AECA provides for criminal penalties of up to ten years in prison and \$1 million in fines for each violation. Criminal investigations and prosecutions are the responsibility of the Departments of Homeland Security and Justice. DTCC assists DHS and the Justice Department in their cases, including verifying documents and providing expert testimony in criminal cases. In fiscal year 2006, support for law enforcement agencies that initiated criminal actions pursuant to the AECA and the ITAR resulted in 119 arrests, 92 indictments, and 60 convictions. (Usually, these cases involved efforts to export defense articles or technology to China or Iran.)

In addition to criminal penalties, DTCC can initiate administrative actions for violations of the AECA and the ITAR that do not rise to the level of a criminal case. The AECA provides for civil penalties of up to \$500,000 per violation and debarment from future exports. Over the last few years, the DoS has imposed the largest administrative fines in history for violations of the AECA and ITAR, which includes the following:

- Boeing Company (\$15 million)
- EDO Corporation (\$ 2.5 million)
- General Motors/General Dynamics (\$20 million)
- Goodrich/L3 (\$7 million)
- Hughes Electronics (\$32 million)
- ITT (\$8 million)
- L3 Communications Corporation (\$1.5 million)
- Lockheed-Martin (\$3 million)
- Loral (\$20 million)
- Raytheon (\$25 million)

In fiscal year 2006, civil penalties amounted to \$22 million. The combination of a vigorous civil enforcement program with a dedicated criminal enforcement effort helps support the integrity of the law and regulations and provides a powerful incentive for full compliance by the defense industry.

In addition to supporting criminal and administrative cases for AECA violations, DTCC has several programs to promote and improve industry compliance with the law and regulations. DTCC administers a voluntary disclosure program that encourages industry to self-assess and report violations to the Department. In 2006, DTCC visited twenty-three companies, helping to identify compliance issues or specific problem areas.

Policy

Controlling defense trade is not just a regulatory function but an important element of U.S. foreign policy. The DTCP plays an important role in cross-cutting issues involving defense trade, including sanctions policy. In particular, in recent years DTCP has made significant contributions to space-related export control issues, the opening of a new U.S. defense cooperation relationship with India, and U.S. efforts to persuade the European Union to not lift its arms embargo on China. The office also plays a major coordinating role when the United States imposes an arms embargo on another country (as with Venezuela in August 2006) or removes an existing embargo.

Section 38(f) of the *Arms Export Control Act* requires the following:

The President shall periodically review the items on the USML to determine what items, if any, no longer warrant export controls under this section.

Since 2000, DTCP has organized an interagency review of the USML. In addition, the office is responsible for “commodity jurisdiction” determinations, i.e., decisions whether specific products are appropriately controlled under the ITAR or Commerce’s Export Administration Regulations. In fiscal year 2006, 340 commodity jurisdiction cases were completed.

The Directorate of Defense Trade Controls web site: www.pmdtdc.state.gov has a reference library, including links to the ITAR and USML, lists of debarred parties and embargoed countries, and other useful information.