

EXPORT COMPLIANCE UPDATE

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ITAR QUIZ

Q A U.S. defense company has a contract with the U.S. Army to provide maintenance training on certain military radars. As part of the contract, the exporter is required to provide training to U.S. troops stationed at an Army base in Kuwait. Test equipment will be loaned to the Army base and 50 copies of the maintenance training materials will be shipped to Kuwait to facilitate the training. What are the U.S. exporter's options for shipment of the equipment and training to Kuwait?

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DOD CONTRACTS AND THE U.S. EXPORT REGULATIONS

A July 12, 2005 Federal Register Notice from the Department of Defense (DoD) proposes to add export compliance requirements to the Defense Federal Acquisition Regulation (DFARS). The intent of the proposed changes is to prevent the unauthorized disclosure of export-controlled information, services, software, hardware and technology obtained, provided or developed under DoD contracts.

This proposed rule will impact companies who bid on solicitations and contracts for research and development or for services or supplies that may involve the use or generation of export-controlled information or technology. The new rule will require DoD contractors to: 1) Comply with all applicable laws and regulations regarding export-controlled information and technology; 2) Maintain an effective export compliance program, which includes developing a process to establish adequate controls over physical, visual, and electronic access to export-controlled information and technology by foreign firms and foreign individuals including foreign person employees; 3) Conduct initial and periodic training on export compliance controls; and 4) Perform periodic export compliance assessments.

The proposed rule specifically states that contractors are to prevent any unauthorized access to export-controlled information or technology by a foreign national or a foreign person anywhere in the world, including the United States, as this is considered to be an export to the home country of the foreign national or foreign person. Contractors are expected to specifically identify information and technology that is subject to export controls and to control it in accordance with U.S. export regulations. This new requirement appears to be driven by a recommendation in the 2004 DoD Inspector General (IG) Report D-2004-061 "Export Controls" dated March 25, 2004.



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COMPLIANCE FOCUS: DUAL USE OR DEFENSE ARTICLE?

U.S. exporters are subject to the requirements of one of two sets of export regulations – either the International Traffic in Arms Regulations (ITAR), which covers the export of defense articles, or the Export Administration Regulations (EAR) which covers the export of commercial or dual-use commodities. In order to comply with the export regulations, exporters need to know which regulations apply to their products.

The ITAR identifies that a product that is specifically designed, modified, configured or adapted for a military application is considered to be a defense article and therefore subject to the ITAR. Commodities that are designed for commercial applications are subject to the authority of the EAR. Commercial products that are used by or sold to military end users are not considered to be defense articles, unless they are specifically modified or adapted for that military application. Commercial products that are altered in any way for a military application also become subject to the ITAR.

Exporters who are not certain as to which set of export regulations applies to their products should request a Commodity Jurisdiction (CJ) ruling in accordance with the procedures addressed in ITAR § 120.4 from the Department of State. If a product is determined to be a defense article, then the ITAR will apply to that product. If the product is determined to be a commercial product and subject to the EAR, then a further request may be submitted to Department of Commerce Bureau of Industry and Security (BIS) to determine the correct Export Control Classification Number (ECCN) for the product. Companies should not bypass the jurisdiction determination process by directly requesting a commodity classification from the Department of Commerce. The Department of Commerce can only advise of the applicable ECCN if the commodity is controlled by the EAR. BIS does not have the legal authority to determine the correct export jurisdiction; this can only be determined by the State Department CJ process.

This newsletter is provided as a service to our clients and is not intended to replace the ITAR or EAR as a reference source. If you have questions concerning the correct interpretation of the regulations please call us at (703) 847-5801.

EXPEDITED LICENSE REVIEW FOR U.K. AND AUSTRALIA

In the November 2004 edition of this newsletter, we reported that the State Department was making progress on setting up a special review process for licenses for the United Kingdom and Australia. On July 12, 2005, in a Federal Register Notice, the U.S. State Department revised the International Traffic in Arms Regulations (ITAR) to specify that licenses for many U.S. origin defense items and services for export to Australia and the United Kingdom will be handled under a new expedited review process.

The Federal Register Notice identified that the ITAR is amended to include new section 126.15, which states that "any application submitted for authorization of the export of defense articles or services to Australia or the United Kingdom will be expeditiously processed by the Department of State, in consultation with the Department of Defense." The notice further stated that applications "will not be referred to any other Federal department or agency, except when the defense articles or defense services are classified or exceptional circumstances apply."

Exporters are advised that the expedited processing applies to applications that involve Australia and/or the United Kingdom only. Applications including other countries will not be processed in the expedited manner. Please note that there is no time frame specified for these expedited reviews.

FOREIGN BROKERS AND ITAR LICENSES

Section 129 of the International Traffic in Arms Regulations (ITAR) identifies that any person who receives a fee or other compensation for arranging or negotiating sales of defense articles is considered to be a broker and must be registered with the Office of Defense Trade Controls Licensing (ODTCL). Recently, the ODTCL has begun to Return Without Action (RWA) any license that includes a foreign sales representative that ODTCL considers to be an unregistered foreign broker. Based on these actions, it is clear that the definition of the term "broker" is not agreed upon between the ODTCL and the exporting community. Unofficially, the ODTCL appears to consider a broker to be ANY foreign party that enters into an agreement with a U.S. manufacturer for the marketing of any defense articles.

U.S. exporters should review the responsibilities of their foreign sales agent to determine if ODTCL registration is required.

ITAR ANSWER

The U.S. company has several options:

- A** • Provide the test equipment and the manuals to the U.S. Army for shipment to Kuwait under a Government Bill of Lading (GBL) or via other U.S. military channels authorized by ITAR § 126.4 (a);
- Obtain a temporary export license (DSP-73) to send the test equipment to Kuwait and a permanent export license (DSP-5) for the training information; or
- Obtain specific written approval by the Army export control office, i.e. USASAC to use ITAR § 126.4 (c) exemption.

DUAL-USE ITEMS TO CHINA

Companies who export certain types of commercial technologies to the People's Republic of China (PRC) may soon face additional licensing requirements for those exports. With the support of the Department of Defense and the House International Relations Committee (HIRC), the Bush Administration is seeking to add to the list of commercial products requiring specific approval from the Department of Commerce prior to exports to China. Products that may be used for a military application, such as aircraft parts, computer chips and machine tools will be affected by the changes that are expected to be implemented by the end of 2005.

REGULATORY UPDATES

The President

Aug. 5, 2005 – 70 Fed. Reg. 45273: President Bush continued for another year the national emergency regarding export control regulations. This action was required to authorize the continued application of the Export Administration Regulations (EAR) under the International Emergency Economic Powers Act (IEEPA) following the expiration of the Export Administration Act.

Department of Commerce

July 15, 2005 – 70 Fed. Reg. 41093 and correction July 26, 2005 – 70 Fed. Reg. 43041: BIS amended the following Export Control Classification Numbers (ECCNs) to implement the changes agreed at the December 2004 plenary meeting of the Wassenaar Arrangement: 1C008, 2B001, 2B005, 2B006, 2B201, 3A001, 3A001, 3A002, 3B001, 3B002, 3B991, 3B992,

4D001, 4E001, 5A001, 6A001, 6A002, 6A003, 6A006, 6A993, 6A996, 6E001, 6E002, 6E003, 6E991, 6E993, 7A002, 7A007, 8A002, and 9A001. BIS also amended the EAR to impose or expand unilateral U.S. controls affecting ECCNs 6A001, 6A002, 6A003, and 7A002 and added Slovenia to the list of Wassenaar member countries.

July 21, 2005 – 70 Fed. Reg. 41952: BIS amended ECCN 0C005 and added ECCN 1C298 to reflect the transfer of jurisdiction over exports of nuclear grade graphite intended for uses other than in a nuclear reactor from the Nuclear Regulatory Commission to the Commerce Department. An export license for such graphite will be required only for destinations of concern for nuclear proliferation reasons. A corresponding notice was published by the Nuclear Regulatory Commission (July 21, 2005 – 70 Fed. Reg. 41937).

Aug. 5, 2005 – 70 Fed. Reg. 45276: BIS amended the EAR to implement the understandings reached at the April 2005 Plenary Meeting of the Australia Group (AG). The amendments reflect the addition of Ukraine as a member of the AG and make clarifying changes in ECCNs 1C353, 2B350, and 9A120.

Department of Defense

July 12, 2005 – 70 Fed. Reg. 39976: The Defense Department proposed an amendment to the Defense Federal Acquisition Regulation Supplement (DFARS) addressing export control concerns raised by defense contracts. See article on page 1.

Department of State

July 7, 2005 – 70 Fed. Reg. 39362: DDTC notified Congress of the following proposed commercial arms export licenses: a commercial communications satellite for launch from Russia and Kazakhstan; military vehicles to the Iraqi Ministry of Defense (MoD); vertical launch anti-submarine rocket components for end use in Japan; spare parts for the SH-2G(A) helicopter to Australia; technical services to New Zealand to upgrade the RNZAF P-3K Orion Maritime Patrol Aircraft System; technical services to Australia to manufacture the RAN SEA 4000 Air Warfare Destroyer for end-use in

REGULATORY UPDATES

Australia; technical services to Japan for cooperative development with the US of the SM-3 Block II missile for the AEGIS ballistic missile defense system; and technical services to Japan to manufacture AN/APG063(V)1 radar system retrofit kits.

July 12, 2005 – 70 Fed. Reg. 39919: DDTC amended ITAR Sec. 126 to clarify exclusions from the Canadian exemption in Sec. 126.5(b) and to add new Sec. 126.15 prescribing expeditious processing of license applications for exports of defense articles and services to Australia and the United Kingdom. See article on page 2.

Fines & Penalties

July 5, 2005: BJ Services Co. USA of Tomball, Texas, agreed to pay \$142,450 to settle BIS charges involving 13 unlicensed exports to China, Colombia, and Russia of chemicals classified under ECCN 1C350 and related false statements on shipping documents, and to submit an audit of its Internal Compliance Program to BIS. BJ had voluntarily disclosed the violations.

July 6, 2005: Abbas Tavakolian of Tehran, Iran was sentenced in Baltimore, MD federal court to 57 months in prison following his guilty plea to charges of attempting to buy \$380,000 worth of parts and weapons components for F-4 and F-14 fighter jets for shipment to Iran. Tavakolian was arrested in a U.S. territory in the South Pacific after trying to make the purchases from a dummy business run by undercover customs agents in Maryland.

July 7, 2005: Gould Pumps of Seneca Falls, NY, agreed to pay \$123,500 to settle charges involving 13 unauthorized exports of industrial pumps classified under ECCN 2B350.i to consignees in Taiwan, India, Egypt, Saudi Arabia, and the PRC. Gould voluntarily disclosed the violations.

July 27, 2005: Encore Medical, as successor to Chattanooga Group, Inc. (CGI) of Hixson, TN, agreed to pay \$101,000 to settle charges by BIS relating to three unlicensed exports by CGI of EAR 99

physical therapy equipment to Iran. The shipments, worth a total of \$7,402, were routed through Australia to conceal their actual destination.

Aug. 5, 2005: Asher Karni of Cape Town, South Africa, was sentenced to 36 months in prison in Washington, DC federal court for violations arising out of the illegal exports of oscilloscopes and triggered spark gaps usable as detonators for nuclear weapons to Pakistan. Karni's substantial assistance to the US government earned him the relatively light sentence. See related article in May 2005 Update.

Sanctions & Denial Orders

Department of Commerce

July 7 and Aug. 5, 2005: The Bureau of Industry and Security (BIS) added, modified, or deleted 66 entries on the Denied Persons List (DPL).

July 27, 2005: BIS extended the temporary denial order (TDO) against Wen Enterprises, Ning Wen, Hailin Lin, and Beijing Rich Linscience Electronics Company by 180 days and added Ruo Ling Wang to the TDO as a related party.

Aug. 5, 2005: 70 Fed. Reg. 45366: BIS renewed for a further 180 days a TDO against Pakland PME Corporation and Humayun Khan, both of Islamabad, Pakistan.

Department of State

Aug. 9, 2005 – 70 Fed. Reg. 46258: DDTC imposed statutory debarment on the following persons who had been convicted of violating or conspiring to violate the Arms Export Control Act or certain other statutes: Mexpar International, Inc. (a/k/a Pasadena Aerospace and Aviation Logistics and Supply); Ahmad (a/k/a Alex) Nahardani; and Gabriela de Brea (a/k/a Gabriela Grea and Gabriela Lopez-Sosa).

Department of Treasury

July 14, 19, and 21 and Aug. 1 and 3, 2005: The Office of Foreign Assets Control (OFAC) made numerous changes to the Specially Designated Nationals (SDN) list.