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STATE DEPARTMENT ISSUES PROPOSED RULE TO IMPLEMENT U.S.-U.K. AND U.S.-AUSTRALIA DEFENSE TRADE COOPERATION TREATIES

On November 22, 2011, the U.S. State Department issued a proposed rule (76 Fed. Reg. 72246) that would amend the International Traffic in Arms Regulations ("ITAR") to implement the U.S.-U.K. and U.S.-Australia Defense Trade Cooperation Treaties. As explained in our E-Alert of October 8, 2010, the treaties are intended to facilitate U.S. defense trade with the U.K. and Australia by eliminating the ITAR license requirements for exports or transfers of certain eligible defense articles, defense services, and technical data to "Approved Communities" of government and private sector entities and personnel in each country for certain approved end uses.

The proposed rule would implement the treaties by adding two new exemptions in sections 126.16 and 126.17 of the ITAR that provide for the permanent or temporary export without a license to members of the Australian and U.K. Approved Communities, respectively, of certain defense articles (including technical data) or defense services that meet the requirements set forth in these sections. The proposed rule also would add a supplement to ITAR Part 126 (Supplement No. 1 to Part 126) to identify defense articles and defense services that are ineligible for the new exemptions.

In addition, the proposed rule would amend the Canadian licensing exemption under ITAR § 126.5 to reference Supplement No. 1 to Part 126 instead of separately identifying a list of defense articles and defense services that are ineligible for the Canadian exemption. The proposed rule also would make various miscellaneous amendments, such as adding Israel to the list of countries eligible for the license exemption set forth under ITAR § 123.9(e), and updating the ITAR to replace references to the Shipper's Export Declaration with references to Electronic Export Information. The State Department's Directorate of Defense Trade Controls ("DDTC") will be accepting comments on the proposed rule until December 22, 2011.

APPROVED COMMUNITIES AND END-USES

Members of the United States Approved Community who would be authorized to export pursuant to the new U.K. and Australia treaty exemptions include "[d]epartments and agencies of the U.S. Government, including their personnel, with, as appropriate, a security clearance and a need-to-know, and "[n]ongovernmental U.S. persons registered with [DDTC] and eligible . . . to obtain an export license (or other forms of authorization to export) from any agency of the U.S. Government without restriction . . . ." 76 Fed. Reg. at 72252, 72257. Pursuant to the proposed new treaty exemptions, DDTC would identify on its internet web site (1) the members of the Australian and U.K. Approved Communities, (2) certain U.S., U.K., and Australian "Authorized Intermediate Consignees," and (3) the operations, programs, and projects which are approved end uses under the treaties. Other approved end uses (such as those which cannot be publicly identified) would be confirmed in written correspondence from DDTC or identified in a U.S. government contract or solicitation.

INELIGIBLE DEFENSE ARTICLES

As noted in our October 2010 E-Alert, a primary concern about the effectiveness of the new exemptions is the breadth of the lists of items the participating governments will exclude from eligibility for export pursuant to the treaties. The proposed rule provides for a long list of ineligible items in Supplement No. 1 to Part 126. The proposed supplement largely tracks the draft lists of ineligible items that were published by the State Department after the signing of the treaties and implementing arrangements in 2007 and 2008, but would exclude several new subcategories of items and services from the treaty exemptions. For example, Supplement No. 1 to Part 126 would exclude the following new items from the scope of the Australian and U.K. treaty exemptions:

- Items classified as Category XXI (Miscellaneous Items); and
- The provision of defense services related to many listed defense articles.

Apparently at the request of the U.K. Government, the supplement also would exclude the following items, among others, from the U.K. treaty exemption:

- Libraries (parametric technical databases) specially designed for military use with equipment controlled on the U.S. Munitions List ("USML");
- Defense articles and services related to ammunition and fuse setting devices for guns and armament (USML Cat. II);
- Defense articles and services specific to anti-personnel landmines (USML Cat. IV);
- Certain specified energetic materials not previously identified on the draft list of ineligible items (USML Cat. V);
- Defense articles specific to equipment specially designed or configured to be installed in a vehicle for military ground, marine, airborne, or space applications, capable of operating while in motion and maintaining temperatures below 103K (- 170 ºC) (USML Cat. VI);
- Defense articles specific to superconductive electrical equipment designed to be installed on vehicles for military ground, marine, airborne, or space applications and to operate while in motion (USML Cat.VI);
- Amphibious vehicles (USML Cat. VII(e));
- Defense articles and services specific to armored plate manufactured to comply with a military standard or specification or suitable for military use (USML Cat. XIII(c)); and
- Structural materials (including carbon/carbon and metal matrix composites, plate, forgings, castings, welding consumables and rolled and extruded shapes that have been specifically designed, developed, configured, modified, or adapted for defense articles) (USML Cat. XIII(f)).

Further limiting the potential benefit of the new exemptions, proposed sections 126.16(g)(5) and 126.17(g)(5) would mandate that ineligible defense articles incorporated into larger systems which are eligible for export under the new exemptions must be licensed separately to comply with the restrictions on the export (or transfer, reexport, or retransfer) of the embedded articles.

ADMINISTRATIVE REQUIREMENTS

As expected, the proposed rule would subject exports made pursuant to the new treaty exemptions to certain administrative requirements designed to ensure the security of the exported defense articles. The proposed rule includes detailed recordkeeping, export marking, and identification requirements which may be burdensome for exporters and pose compliance challenges particularly

in the context of shared databases where frequent exchanges of data and software occur. For example, U.S. exporters making use of the exemption would be required to meet detailed minimum recordkeeping requirements for all exports, imports, transfers, reexports, and retransfers of eligible defense articles, defense services, and technical data. *See* proposed sections 123.26, 126.16(l) and 126.17(l). These provisions would likely require companies to keep records of every phone call or email that relied on the treaty exemptions to discuss technical data.

REEXPORTS/RETRANSFERS

In accordance with the treaties' restrictive end-use provisions, reexports and retransfers of treaty articles outside an "Approved Community," or for end-uses that are not approved, will fall outside the scope of the exemptions and, with some limited exceptions, will require separate authorization from the U.S. State Department and the U.K. or Australia host government. Further, the proposed rule would prohibit the use of the reexport exemption in ITAR § 123.9(e), which permits reexports or retransfers without prior written approval from the United States of U.S.-origin defense articles incorporated into foreign defense articles that are transferred to the government of a NATO country or certain other countries, if the U.S.-origin component was previously authorized for export pursuant to Australia or U.K. treaty exemptions.

OTHER PROPOSED CHANGES

In addition to implementing the Defense Trade Cooperation Treaties, the proposed rule would make several other changes to the ITAR. First, it would revise the Canadian licensing exemption to reference the proposed supplement to ITAR Part 126, which incorporates the lists of items and defense services that currently are identified in ITAR §§ 126.5(b)-(c) as ineligible for export under the Canadian exemption.

Second, the proposed rule would implement Title III of the Security Cooperation Act of 2010 to give Israel a status in law similar to that of a NATO country or Australia, Japan, New Zealand, and South Korea with respect to Congressional certification requirements, thereby raising the dollar threshold for defense sales to Israel that trigger Congressional certification requirements prior to licensing from contracts in the amount of $14 million to $25 million (for sales of major defense equipment), and from contracts in the amount of $50,000 to $100,000 for other defense articles and services. In addition, Israel would become an eligible destination for reexports without prior written authorization from the U.S. State Department of U.S.-origin defense articles incorporated into foreign defense articles pursuant to ITAR § 123.9(e).

Third, the proposed rule replaces outdated references to "Shipper's Export Declaration" in various sections of the ITAR with the term "Electronic Export Information."

Finally, the proposed rule would amend ITAR § 123.9(a) to require that persons determine the specific destination, in addition to the specific end-user and end-use, for a defense article or defense service (through the review of readily available information, including public information or information available from other parties to the transaction) prior to submitting an application to DDTC or claiming an exemption under the ITAR.

If you have any questions concerning the implementation of the Defense Trade Cooperation Treaties, or would like to discuss the potential submission of comments to the State Department on this proposed rule, please contact the following members of our international trade controls practice group:

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