

COALITION FOR SECURITY AND COMPETITIVENESS

RECOMMENDATIONS FOR MODERNIZING EXPORT CONTROLS ON MUNITIONS LIST ITEMS

EXECUTIVE SUMMARY

March 6, 2007

The United States currently faces unprecedented threats to its security both at home and abroad. In confronting these threats, we must be able to exploit the full advantage we derive from our economic strength and technological prowess. To that end, the U.S. export control system must be modernized so that it is better able to respond quickly and effectively to evolving security threats, and promote our nation's continued economic and technological leadership. The Coalition for Security and Competitiveness, representing multiple industry and trade associations, is committed to working with the Executive Branch and Congress in a cooperative spirit to accomplish these important goals.

To modernize the system and make it more efficient, predictable and transparent, the Coalition has developed the following eleven recommendations on export controls for munitions list items.

- State strategic policy principles for defense and technology trade and cooperation
- Appoint a senior director at the NSC responsible for defense trade, export policy and technology cooperation
- Create a presidential advisory body on defense trade and security cooperation
- Re-program funds for the Directorate of Defense Trade Controls (DDTC) to add a sufficient number of officers for agreements, licenses and commodity jurisdiction evaluations
- Ensure accurate interpretation and consistent use of International Traffic in Arms Regulations (ITAR) that govern the commodity jurisdiction process
- Keep items, particularly FAA-certified equipment, on the Commerce Control List (CCL) until after a final commodity jurisdiction determination is made
- Implement more efficient, effective, and transparent licensing procedures and technology disclosure review processes
- Establish a quarterly interagency appeals process (at the political appointee level) for decisions on critical jurisdiction and licensing applications
- Provide industry "intent to deny" and "intent to Return Without Action" feedback before such decisions are finalized
- Accelerate implementation of a more robust electronic system for processing and tracking license applications, including licenses that require congressional notification
- Require license and agreement processing to follow reasonable and predictable metrics

A more detailed description of the Coalition's concerns and proposals for action is provided in the attached recommendations. Additional recommendations for modernizing export controls on dual-use items, as well as other information on the Coalition, can be found on www.securityandcompetitiveness.org.

RECOMMENDATIONS FOR MODERNIZING EXPORT CONTROLS ON MUNITIONS LIST ITEMS

PROPOSAL: State strategic policy principles for defense and technology trade and cooperation

U.S. national security is more dependent than ever on our technological leadership and ability to bring our technological advantage to bear on the security challenges facing the nation today. A statement by the president advocating the importance of defense and technology trade and the overarching principles that guide policy development and implementation across the federal government would help advance our national and economic security interests. These principles and policies should be incorporated into and support the National Security Strategy and should aim, inter alia, to:

- Prevent proliferation of, and access to, our most sensitive and militarily critical technologies by current and potential adversaries.
- Support U.S. foreign policy objectives.
- Support U.S. technological leadership and competitiveness essential to our nation's security.
- Promote defense cooperation, foreign sales, and interoperability with U.S. partners and allies.
- Preserve a cutting-edge industrial base, including a highly skilled workforce, able to leverage the security and economic benefits of foreign technological innovation and free trade.

PROPOSAL: Appoint a senior director at the NSC responsible for defense trade, export policy and technology cooperation

A senior director for these issues at the National Security Council is needed to further develop, coordinate and unify U.S. export control and defense trade policies and practices so they are fully implemented and made more predictable, transparent and efficient. This person would monitor the export control, defense trade and technology release system to ensure it is advancing the president's principles and priorities. He or she should also clarify, coordinate and promulgate administration priorities and policy adjustments that guide technology and data transfer decisions across the interagency system to promote consistency with the president's policies, aid transparency, and help officials manage the process from a common set of instructions. Industry would also welcome a senior and central point of contact for these issues.

PROPOSAL: Create a presidential advisory body on defense trade and security cooperation

An advisory body of this nature could serve as a common forum for senior leaders from Congress, industry and the administration to discuss ways of improving our country's defense trade, export controls and technology cooperation with our allies and coalition

partners. Such a new presidential advisory body could open lines of communications at the highest levels of the private and public sectors.

PROPOSAL: Re-program funds for the Directorate of Defense Trade Controls (DDTC) to add a sufficient number of officers for agreements, licenses and commodity jurisdiction evaluations

Industry urges the addition of at least 10 new officers to DDTC with a focus on adding capability to process agreements, licenses, and commodity jurisdiction requests in the timelines proposed. Providing these resources would cost less than \$5 million and would greatly enhance efficiency by providing more staff to process licenses, especially those critical to enhancing our capabilities for joint warfighting and interoperability. Going forward, industry would also be supportive of additional funding for post-shipment verification of exports and for resource needs in other agencies in the export control system. DDTC should also continue to receive its full complement of 10 congressionally mandated military officers. These officers should have relevant career backgrounds, undergo thorough pre-training, and have an assignment at DDTC qualify as service in a joint DoD billet.

PROPOSAL: Ensure accurate interpretation and consistent use of International Traffic in Arms Regulations (ITAR) that govern the commodity jurisdiction process

Reducing the regulatory caseload is a top priority for industry. The export control system will be improved by reducing the total number of transactions subject to the stringent controls under the International Traffic in Arms Regulations (ITAR). Reducing the overall caseload to make the process for the remainder more efficient will allow the government to commit more time and resources to transactions that raise particular concerns.

Many items controlled by the ITAR are the performance equivalent of commercial items and do not have significant military or intelligence applicability. The presence of these ITAR-controlled items in a larger system subjects the entire system to stringent U.S. Munitions List (USML) controls. The export control system would be made more efficient by ensuring it does not control (or overly control) such no risk/low risk items as if they were munitions list items, particularly if there is compelling evidence of predominant commercial application. To reduce the regulatory burden on both the government and industry, the government must institute a process for periodic, comprehensive review of the USML, and update or revise regulatory guidance and criteria to ensure that only items appropriately classified as USML items are subject to AECA/ITAR controls.

Existing export control regulations governing commodity jurisdiction have the flexibility to allow such determinations of risk but are not being interpreted or implemented in a consistent and predictable fashion. In addition, the Commerce Department's expertise in analyzing commercial applications of technology is not always given appropriate consideration. These factors create large caseloads that overwhelm the system, result in

delays and strain already scarce resources that should be used to scrutinize licenses of real concern and expedite those licenses that promote U.S. security and economic interests. Industry requests enhanced oversight of the interagency commodity jurisdiction process to ensure it is correctly and consistently following existing regulations, as well as clarifying guidelines on how to use the regulations and interagency input properly in evaluating technology for export. Annex 1 contains recommendations to achieve these ends.

PROPOSAL: *Keep items, particularly FAA-certified equipment, on the Commerce Control List (CCL) until after a final commodity jurisdiction determination is made*

Items on the USML have more stringent levels of control than items on the CCL. Under current practice, companies are advised to treat a CCL item as a USML item and subject it to strict military controls and licensing requirements when a commodity jurisdiction (CJ) determination (USML vs. CCL) is requested and a decision is pending. During this process, because of how USML items are controlled, the commodity using this item becomes immediately subject to strict military controls. If the commodity is embedded in another, larger, commercial end item, the ability to export that commercial end item is at risk. This practice is very disruptive to U.S. commercial relationships. It is particularly critical to allow (without penalty) treatment of FAA-certified equipment on commercial aircraft as CCL items until after a formal, final CJ judgment is made.

PROPOSAL: *Implement more efficient, effective, and transparent licensing procedures and technology disclosure review processes*

In addition to reducing the regulatory caseload, industry supports the implementation of more efficient approaches to licensing that could make the export control system more efficient and transparent without compromising government oversight or U.S. security interests. Moving beyond a “transaction-based” system to one that does licensing differently or implements new types of licenses would achieve that goal. Annex 2 contains a number of proposals that would streamline licensing for both major programs and routine export activity. These include: development of more effective, less onerous program licenses that would help reduce the overall number of licenses being processed; the development of certified (domestic and foreign) company licensing systems that reduce paperwork requirements for those companies with effective compliance programs; the modification/elimination of licenses for routine transfers (e.g. bulk, multi-year exports) and administrative matters; and the establishment of more transparent and disciplined processes for initial technology disclosure decisions.

PROPOSAL: *Establish a quarterly interagency appeals process (at the political appointee level) for decisions on critical jurisdiction and licensing applications*

Industry requests an appeals process to either the new aforementioned National Security Council senior director (proposal 2) and/or a panel consisting of the assistant secretaries of State, Defense, and Commerce for the most critical of jurisdiction and/or licensing policy decisions that could set precedent, clarify policy or regulation, and lead to greater

efficiency. At a minimum, such a system would give exporters a forum to provide feedback and better understand the current system.

PROPOSAL: Provide industry “intent to deny” and “intent to Return Without Action” feedback before such decisions are finalized

There are many occasions when licensing decisions to deny or “Return Without Action” (RWA) could be appropriately adjusted if the company has the ability to provide additional information to clarify a particular question/concern with their application. The ability to provide this information and avoid re-submitting an application is now dependent on the willingness of the official in question to communicate questions/concerns to companies. Industry welcomes the ability to have this exchange of additional information become common practice facilitated through a more robust, real-time electronic licensing/tracking system that lists the originating agency of pending denial / “RWA” recommendations. Such a system is already in place at the Commerce Department. A similar system for pending provisos and commodity jurisdiction determinations would also be useful. At minimum, industry would welcome a system that would allow for occasional review (“quality control”) of decisions to deny/“RWA” cases to ensure such decisions are consistent with policy/regulatory intent.

PROPOSAL: Accelerate implementation of a more robust electronic system for processing and tracking license applications, including licenses that require congressional notification

To improve efficiency and enforcement, a paperless/all-electronic licensing system should be accelerated and expanded with greater functionality. The system should track across the entire interagency process automatically not only the current status of license applications but also their transit times and next steps against mandatory timelines. Industry is especially interested in tracking licenses that require congressional notification from when they are first submitted to the government to when they are sent to Congress for review.

PROPOSAL: Require license and agreement processing to follow reasonable and predictable metrics

The current export control system is not delivering decisions on technology release in the time sensitive fashion critical to U.S. interests. As both an individual proposal and a yardstick to measure progress, we believe a more efficient export control system should process decisions on individual “unstaffed” (i.e. State Department review only) licenses or decide to send individual licenses for inter-agency “staffing” within 5 calendar days. More complex agreements that may or may not require inter-agency review should be either processed as unstaffed or staffed out within 10 calendar days. If licenses or agreements are staffed, the inter-agency review should be completed within a total of 30 days. Understanding that licenses and agreements for NATO+3 allies may involve more sophisticated technology transfer requests, the fact that they are close allies should be given due consideration and their staffed license and agreement applications fast-tracked

and completed within 20 total days. A final licensing decision by the State Department after the completion of an interagency review should be issued within five days. These standards should apply to over 95 percent of all licenses and 85 percent of all agreement applications, and those that do not should be raised to the assistant secretary of State or Defense (as appropriate) for adjudication.

Annex 1: ITAR Clarifications Regarding Commodity Jurisdiction

Interpretation of the existing commodity jurisdiction regulations can vary considerably across the government. This is due in no small part to the fact that controlling regulations and their criteria for judgment are administered by one department but are interpreted and implemented by scores of offices in other departments. As a result, these regulations are difficult for Industry to use as a reliable guide to how an item should be classified. That said, many of these problems can be addressed through constant referral, a complete reading, and a dutiful implementation of current regulations. Further improvements can be made through a complementary process that adopts established “best practices” learned from other parts of the interagency system.

Recommended Actions

- Reaffirm ITAR Sections 120.3 and 120.4, not the “designed or modified for” clauses in the U.S. Munitions List, as the primary policy guidance for industry and the entire interagency commodity jurisdiction (CJ) determination process. In other words, allow industry and the interagency process to use sections 120.3 and 120.4 (and all their relevant decision-making criteria) for initially determining commodity jurisdiction of an item.

Current practice, which relies on the standard catch-all “designed or modified for” clauses in the USML categories, compels industry and the interagency process to often initially classify commercial technology as USML items because of *any* kind of design or modification affecting form or fit but not function.

Sections 120.3 and 120.4 are the basis for determining whether or not to initially classify items as USML/ITAR controlled. However, because this approach is not properly/consistently followed, these sections have been relegated to the secondary role of justifying the removal of ITAR controls on such items.

- Ensure final determinations are consistent with 120.3/120.4 regulatory language.
- Designate the Commerce Department as the lead agency for analyzing predominant “civil application” of an item, taking into consideration how the performance equivalent of an item is controlled for export and used in other countries.
- Restore the practice of publishing CJ determinations (with appropriate sensitivity to protection of proprietary information) for use by industry as guidance.
- Give the Commerce and Defense Departments full transparency into the State Department commodity jurisdiction process.

Annex 2: New Licenses and Licensing Procedures to Enhance Efficiency

Recommendations of Alternative Licensing Procedures for Systemic Efficiency Improvements

- **Simplify and expand the eligibility for programmatic licensing.**
 - Activity – Industry has tried to take advantage of program licenses that grant pre-approval for a slate of transactions between U.S. and foreign customers/partners to support major weapons programs.
 - Current practice – Eligibility for these program licenses are restricted to major weapons programs. Also, the paperwork required to prove compliance with the terms of a program license is more onerous than if a company had obtained individual licenses for each transaction undertaken under the program license. Finally, applying for a program license requires companies to lock in a significant amount of information on what and how they will be operating without much flexibility to address changes in required export transactions.
 - Problem for industry – Program licenses are less useful than continuing to apply for licenses for individual transactions.
 - Recommendation - Program licenses should be more flexible and expanded to include more than major program activities (e.g. transactions between U.S. companies and their foreign subsidiaries/parents, focused research and development projects on critical technologies such as anti-IED and missiles) and the paperwork requirements to demonstrate compliance with the terms of a program license for a given set of transactions should be made much less onerous than the cumulative requirement for all license applications otherwise necessary for the same set of transactions.

- **Institute a certified (domestic and foreign) company licensing program.**
 - Activity – Leading exporters (and their foreign customers/partners) invest millions of dollars to ensure they have “best practice” programs to comply with U.S. export control regulations.
 - Current practice – These (domestic and foreign) companies with “best practice” export compliance programs are treated the same as any other company in terms of their risk profile and the processing of their license applications.
 - Problem for industry – With limited resources and an ever-growing number of license applications, an export control system that treats all parties to an application alike will become increasingly overwhelmed and unable to process license applications in an efficient manner.
 - Recommendation – The administration should consider developing the certification, audit, and corresponding benefit systems of the C-TPAT program

for exporters (and their foreign customers/partners), which will also allow more government focus on transactions with higher risk profiles.

Recommendations for increasing transparency of license processing/review for industry

- **Require the State Department’s Directorate of Defense Trade Controls to organize forums with relevant industry and agency representatives to discuss changes to license processing guidelines.**
 - Activity – Industry uses the ITAR regulations to ensure their export activities are in compliance and their license applications are properly prepared for review.
 - Current practice - There are a number of guidelines issued by the Directorate of Defense Trade Controls (DDTC) through their website that carry the full force of regulations, and in many cases create new policy on important matters (e.g., “dual nationals,” sub-licensing, content within purchase orders) in the absence of standard regulatory review and implementation.
 - Problem for Industry - The result for industry (and licensing officers) can be an unpredictable and inconsistent set of rules that can make compliance and correct preparation of license applications difficult.
 - Recommendation - Industry requests an opportunity to participate in a review and comment process (along with other relevant government agencies) on these guidelines prior to their formal release. This process should largely mirror the process of submitting draft regulations for review and comment before revision and adoption. In some cases, industry may recommend transforming guidelines into formal regulations to justify requesting compliance-related information from their foreign partners.

- **Develop more transparent and disciplined processes for initial technology disclosure decisions.**
 - Activity – In most cases during government to government consultations on new military programs, several Defense Department technology disclosure/transfer committees review the specific country’s request for release of specific technologies.
 - Current practice – These committees, which include the National Disclosure Policy Committee, the Executive Committee for Low Observables/Counter-Low Observables and the Committee for National Security Systems, decide if they are going to conduct a review, when they are going to start the review and when they are going to complete the review. This process is usually non-transparent and unpredictable for industry.
 - Problem for industry – Industry and our foreign allies must wait for decisions on what technologies can be released and in what timeframe before moving to

the license application process. This process hurts our ability to enhance interoperability, build partnerships, and conduct business because the process is opaque and unpredictable.

- Recommendation – The administration should develop a more transparent process to ensure all the required Defense Department reviews of the proposed release/disclosure of technology are completed in a timely and predictable manner.
- **Establish industry ombudsmen responsibilities at State, Commerce and Defense Departments.**
 - Activity – Industry often requires clarifications on export control regulations, and seeks appropriate opportunities to voice concerns and make recommendations about improving the current export control system.
 - Current practice – Opportunities to engage in such dialogue are limited to occasional advisory committee meetings or infrequent one-on-one meetings with key officials.
 - Problem for industry – Such communications with each agency are not routine or at a senior level to ensure responsiveness on matters of the greatest concern. There is also difficulty in ensuring follow-up on these matters given the numerous other responsibilities that government officials have.
 - Recommendation - An industry ombudsman (or senior staff member assigned this responsibility) who reports to the appropriate under secretary at each of these departments could monitor and improve license processing metrics, help enforce internal agency processing timelines, and find ways to increase transparency for industry regarding the status of license applications. Ombudsmen at these departments could also work with each other and industry (including the small business community) to communicate and clarify export control policies and processes, and provide feedback on how to improve industry license applications.
- **Institute a more consistent and transparent processing of requests from foreign customers/partners to transfer U.S. technology to third-parties**
 - Activity – For a variety of legitimate reasons, foreign customers/partners who have acquired by license U.S. technology controlled by the ITAR will seek permission to transfer this technology to a third-party.
 - Current practice – Once these applications are submitted for review, their status and the need for any further information relating to the request are often opaque to the foreign customer/partner.
 - Problem for industry – The U.S. Original Equipment Manufacturer (OEM) is brought in as an intermediary to assist both sides of this discussion. The foreign customer/partner requires assistance tracking the status of these requests, which requires investigation by the OEM. The officers reviewing

the transfer request will also ask questions about the transfer that must then be conveyed for response to the foreign customer/partner.

- Recommendation – Industry would favor an electronic system that would allow foreign customers/partners to track the status of their requests to transfer ITAR-controlled technology to third parties. Such a system should also allow U.S. officials to send routine inquiries directly to the foreign partner/customer. At minimum, industry would appreciate more transparency to help find these requests in the system to help their foreign customers/partners and the officials processing the request.

Recommendations for expediting license processing/review

- **Develop a routing/triage system to process routine license applications separately**
 - Activity – Industry often engages in routine activities in furtherance of legitimate export activity.
 - Current practice – The required licenses and amendments to previously approved agreements governing these routine activities are being lumped together with more complex cases and processed in a first-in/first-out manner.
 - Problem for Industry – Industry, and our foreign customers/partners, are frustrated by the delay caused by waiting for simple license applications to be processed.
 - Recommendation – DDTC should develop a routing system for immediate review and approval by new, dedicated licensing sub-teams of the most routine business activities requiring license applications and amendments to agreements.

- **Clarify and expand the utility of existing license exemptions in the ITAR**
 - Activity – Industry wants to make more frequent use of the almost 60 exemptions to license requirements that are currently available in the ITAR.
 - Current Practice - Interpretations of these exemptions and related compliance requirements vary among licensing officers.
 - Problem for Industry – Industry is reluctant to use these exemptions because the conditions under which they can be utilized are not interpreted consistently and/or the paperwork required to assure compliance with the terms of the exemption is more onerous than obtaining a license.
 - Recommendation – Clarify the conditions under which exemptions can be utilized, and make the paperwork required to use them less onerous than that required of corresponding license applications.

- **Change licensing requirements for administrative and other actions that could be reviewed and approved on an expedited basis:**
 - Company name changes for freight forwarders/foreign customers/partners
 - Activity – Freight forwarders and foreign customers/partners who appear(ed) on license applications will sometimes change/modify their corporate name.
 - Current practice - All licenses previously approved or being processed citing the old name must be individually corrected and re-submitted for review and approval.
 - Problem for industry – Industry is forced to produce additional paperwork that clogs up the license application processing system and delays routine business activity without a demonstrable benefit to U.S. national security.
 - Recommendation – Develop a system to allow licenses/applications citing the old corporate name to remain active/remain in process after one-time review of the corporate name change by DDTC, and/or develop a system that automatically makes the update throughout the system.
 - Shipment of unmodified foreign-origin items back to foreign manufacturers for repair/replacement/upgrade
 - Activity – U.S. companies often purchase and import many foreign made military items for use in other/larger systems. These items are controlled by the ITAR once they enter the United States. Sometimes these items need to be repaired, replaced, or upgraded—a task that often can only be done by the original foreign manufacturer.
 - Current practice: A license is required to ship back unmodified foreign technology to its original foreign manufacturer to get it repaired, replaced, or upgraded. Sometimes these license applications are delayed by interagency staffing instead of handled as unstaffed/State Department-only review.
 - Problem for industry – Industry is forced to produce needless paperwork that clogs up the license application processing system and delays routine business activity without a demonstrable benefit to U.S. national security.
 - Recommendation – A license should not be required to return an unmodified item to its foreign manufacturer. Industry would favor a new exemption from license requirements for this activity, especially since DDTC can track these items through the Shipper’s Export Declaration and the records companies are required to keep for such exemptions.

- Executing the terms of previously reviewed and approved agreements for export
 - Activity – Industry will submit an agreement for approval that often outlines activity that may require multiple export-related transactions.
 - Current practice: Industry is free to conduct only a one-time transaction under the authority of an approved agreement (according to licensing practice vs. regulations). If executing the agreement requires multiple transactions, industry must get licenses for each individual export in service of that approved agreement.
 - Problem for industry - Too often these individual licenses relating to an approved agreement are subject to much longer interagency staffing/review instead of unstaffed/State Department-only review. Also, the implementation of agreements has resulted in an increase, rather than a decrease, in the number of individual authorizations.
 - Recommendation – To reduce the licensing burden on both the State Department and industry, industry requests the flexibility to execute an approved umbrella agreement that permits multiple export transactions without further license or notification requirements. Industry suggests other mechanisms to capture decrement of exports from approved amounts in previously approved agreements.

- Amendments to non-Significant Military Equipment (SME) approved agreements
 - Activity – Industry sometimes needs to change an approved agreement (e.g. add to the quantity of items, add value to defense services, extend the duration of an agreement) for transactions involving non-Significant Military Equipment.
 - Current practice: Such amendments are almost always staffed and treated as completely new requests rather than modifications to previously approved export activities.
 - Problem for industry - Industry, and our foreign customers/partners, are frustrated by the need to re-submit applications and the delay caused by waiting for amendments to be processed.
 - Recommendation - Appropriate risk-management principles should be applied to process most of these amendments as administrative changes on an unstaffed/State Department only basis or at minimum as notifications subject to requests for further review as needed by the Defense Department.
