5-2014

Export Control Reform Where Are We Now?

Mark J. Sundahl
Cleveland State University, m.sundahl@csuohio.edu

Jon P. Yormick
jon@yormicklaw.com

Original Citation

Mark J. Sundahl & Jon P. Yormick, Export Control Reform Where Are We Now?, 6 Bar Journal of the Cleveland Metropolitan Bar Association 14 (2014).

Export Control Reform

Where Are We Now?

BY JON P. YORMICK &

MARK J. SUNDAHL

The Underpinnings of Export Control Reform

Five years have passed since the Obama Administration launched the Export Control Reform Initiative (ECR) in 2009. This initiative was undertaken to remedy the complexity, ambiguity, and occasional absurdity of the existing regulations governing the export of military and dual-use items (i.e., items that have a civilian as well as a military application). While significant progress has been made in reforming this critical area of law, the project is not yet complete.

The primary thrust of the ECR effort is to move less sensitive items and technologies from the United States Munitions List (USML) to the Commerce Control List (CCL). Items on the USML are subject to the strict controls of the International Traffic in Arms Regulations (ITAR) which, with few exceptions, require a license from the U.S. Department of State's Directorate of Defense Trade Control (DDTC) prior to the export of the listed items (known as "defense articles"). Those items and technologies that are transferred to the CCL will be subject to the less strict controls of the Export Administration Regulations (EAR) which regulate the export of dual-use commodities and technologies.

The other goal of the ECR is to transform the USML into a "positive" list, i.e., a list that describes the controlled defense articles and technologies with specificity in order to enable companies to more easily determine when their products are subject to the ITAR. Unlike the CCL (which is a positive list), the descriptions of items on the USML have been notoriously broad. As a result, a manufacturer's product may fall within the scope of the ITAR even if the item has no inherent military application. For example, prior to the ECR, all parts and components that were "designed" or "modified" for incorporation into a controlled item were subject to ITAR control. This was true even if the part taken by itself had no inherent military application, such as a screw that had been painted "army green" for use in a tank. This overly broad language of the USML has required a multitude of lower-tier manufacturers to be regulated under the ITAR with its annual registration requirement (even if the manufacturer does not export or only had a single transaction involving a defense article or technology), licensing mandates, and threats of severe penalties — civil, criminal, and debarment.

The proposed revisions to the ITAR (and those already in effect) fix this problem to a large extent by describing with specificity those items that are subject to the ITAR. Blanket categories, such as "spacecraft," have been replaced by lists of technology with clear specifications that attempt to include only those items that are of true military value, and which therefore deserve the strict controls of the ITAR. Perhaps most importantly, the number of parts and components that are controlled has been significantly reduced and now generally exclude those parts that have no inherent military or intelligence applications. This has been achieved by subjecting to the ITAR only those parts and components that have been "specially designed" for use in a defense article. The new definition of "specially designed" excludes any fasteners (nuts, bolts, screws, etc.), as well as any part that has performance specifications equivalent to an item regulated under the lower tier of export controls of the EAR. It also sets up a "catch and release" structure so that articles and technologies that are initial caught under the new "specially designed" may nonetheless be "released" from the jurisdiction of the ITAR if the item is not specifically listed on the USML.

At the outset of the discussion of the ECR, there was hope for the eventual unification of the two regimes. If this is accomplished, we will have a single list of controlled items, rather than the existing bifurcated system based on the USML and the CCL, and this single list of items would be subject to a single set of regulations administered by one agency. At this point, a unitary "one-stop shop" approach to export controls is not likely to evolve within the near future. This goal may be realized in the next wave of reforms, but the current project will be restricted to the transfer of items from the USML to the CCL and the transformation of the USML to a positive list.

ECR Progress to Date

Last April, in these pages of the CMBJ, we wrote that the initial steps of the ECR had occurred in early March. At that time, we explained that the Administration had issued its first "38(f) notice" to Congress regarding USML Category VIII (Aircraft and Associated Equipment) and the newly established Category XIX (Gas Turbine Engines and Associated Equipment) and that the first transfer of items from the USML to the CCL would likely occur in October 2013. Despite a federal government shutdown last October, ECR forged ahead with the first transfers effective on October 15, 2013.

Since then, the Department of Commerce and the Department of State have been and continue to be engaged in transferring appropriate items on the USML to the CCL pursuant to the "38(f) process" as provided under Section 38(f) of the Arms Export Control Act which requires the President to periodically review the USML "to determine what items, if any, no longer warrant export controls under" the ITAR. Items moved to the CCL are now and will continue to be grouped under the new "600 Series" category that will also contain certain significant military items that are already on the CCL.

So how far along are we in this process? The process has moved forward methodically through the review and revision of each category of the USML. The amendments to the following categories have already gone into effect: Category VI (Surface Vessels of War and Special Naval Equipment), Category VII (Ground Vehicles), Category VIII (Aircraft and Related Articles), Category XIII (Materials and Miscellaneous Articles), Category XVII (Classified Articles, Technical Data and Defense Services Not Otherwise Enumerated), Category XX (Submersible Vessels and Related Articles), and Category XXI (Articles, Technical Data and Defense Services Not Otherwise Enumerated).

Amendments with respect to other categories go into effect in a few short months on July 1: Category IV (Launch Vehicles, Guided Missiles, Ballistic Missiles, Rockets, Torpedoes, Bombs, and Mines), Category V (Explosives and Energetic Materials, Propellant, Incendiary Agents, and Their Constituents), Category IX (Military Training Equipment), Category X (Personal Protective Equipment), and Category XVI (Nuclear Weapon, Design, and Testing Related Articles).

We are still awaiting the publication of final rules with respect to two categories of the USML

for which proposed rules have been published: Category XI (Military Electronics) and Category XV (Spacecraft Systems and Associated Equipment). The proposed changes to Category XV have been particularly momentous — and generated the greatest volume of public comments. On May 24, 2013, the DDTC issued proposed rules that will transfer (for the most part) all but the most sensitive space technology to the CCL, thus restoring the appropriate level of control to civil space systems that existed prior to an unauthorized disclosure of controlled technology resulting from a 1996 failed launch of a U.S. satellite from China. Those items that would remain on the USML include satellites and spacecraft with significant military value, such as the ability to detect nuclear detonation, track missiles, destroy other satellites, or strike targets on Earth. However, some aspects of the proposed rule remain controversial, such as the retention on the USML of any hosted payload that is funded by the U.S. Department of Defense (regardless of the payload's capabilities), as well as any "man-rated" spacecraft, even if such spacecraft (such as Virgin Galactic's SpaceShipTwo) has no military application. Despite these controversies, a final rule for Category XV will likely be published in May of this year.

As we also stated last year, companies that manufacture or export defense articles that are currently subject to the ITAR, but will be transferred to the CCL later this year will face a lighter regulatory compliance burden. Generally, although a license will still be required for items transferred to the CCL's new "600 Series" category (unless the item is being exported to Canada), a number of license exceptions may permit export without a license. Of particular significance is License Exception Strategic Trade Authorization (STA). Under specific circumstances and upon meeting certain EAR requirements, this license exception is available when products or technologies are exported to a NATO country and to those located in other allied countries, such as Australia, Japan, New Zealand, and South Korea. If a license is required, the online licensing process under the Department of Commerce regulations are less complicated.

ECR is here. Companies that have not yet reviewed the jurisdiction (USML v. CCL) under which their products and technologies are governed under ECR cannot afford to wait any longer to determine how ECR affects their export compliance processes and procedures, and their customer relations.

Mark Sundahl is Chair of the CMBA International Law Section and serves Of Counsel to the Law Offices of Jon P. Yormick Co. LPA, where he practices in the area of export controls and Space Law. He is also an Associate Professor and the Associate Dean for Administration at Cleveland-Marshall College of Law. He has been a CMBA member since 2007. He can be reached at (216) 687-2300 or mark.sundahl@law.csuohio.edu.

Jon Yormick is the Immediate Past Chair of the CMBA International Law Section. He practices out of offices in Cleveland and Buffalo, regularly advising and representing clients on matters of compliance, investigations, self-disclosures, and penalties involving export controls, economic sanctions, and U.S. Customs laws. He has been a CMBA member since 2007. He can be reached at (216) 269-5138 or jon@yormicklaw.com.

Welcome *New Members*

Matthew Paul Baca

Jialin Bai

T. Merritt Bumpass, Jr.
Frantz Ward LLP

Frank A. Camardo, Jr.

Michael W. Czack

Mary Ingles Edquist
McDonald Hopkins LLC

Adam Michael Ekonomon
The J.M. Smucker Company

Peter Omar Farah
The J.M. Smucker Company

Tami Zupkow Hannon
Mazanec, Raskin & Ryder Co., L.P.A.

Pierre John Harb

Tiffany Henderson

Rania A. Kabli

Edward G. Kagels
Murman & Associates

Edward J. Kelley, III

Alanna B. Klein

Jeanette L. Knudsen
The J.M. Smucker Company

David G. Lambert
Cuyahoga County Prosecutor's Office

Sergey V. Litvak

Bing Lu

Christina Marino
United States District Court

Jennifer A. McGee

Dawn Mead
Weltman, Weinberg & Reis Co., LPA

Matthew **Moldovanyi**

Rachel Lynn Parks

Patricia W. Pribisko

Donna J. Ramsey-Caputo
Ramsey Caputo & Ramsey

Deborah L. Riley

Michelle Marie Schuld
The J.M. Smucker Company

Michael P. Shaughnessy

Michael Patrick Sheridan
Dollar Bank

David A. Shively
Eighth District Court of Appeals

Kelly J. Skeat
Benesch, Friedlander, Coplan & Aronoff LLP

Donald **G.** Slezak

Kara Soppeisa
Weltman, Weinberg & Reis Co., LPA

Jason Suslak
The J.M. Smucker Company

Bryan Kenneth Szalewski

Theodore C. Theofrastous
The Law Offices of T.C. Theofrastous, Ltd.

Maria Tosheva-Nikolova
Forest City Enterprises, Inc.

Ana M. Tyler

Christopher Ryan Uhle

Kathleen Christine Valdez

Ashley Collier Wakefield
Wade Weber, CPA

Wade Weber

Jennifer L. Whitney
The J.M. Smucker Company

Timothy Daniel Wolff

Jacob H. Zoghlin