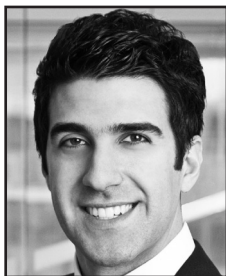




ITAR Reform: A Work in Progress

By Dara Panahy and Bijan Ganji



In 2010, after more than a decade of heightened scrutiny of exports and reexports of satellites, component systems, and related ground equipment and technology, the U.S. government began to reevaluate its export control regulations. The goal of this reevaluation was to establish a regulatory

environment that would continue to protect national security interests without doing unnecessary economic harm to the U.S. space industry. After conducting a thorough interagency review of existing export control regimes, in May 2013, the U.S. Departments of State and Commerce issued proposed rules that would revise the applicable regulations to more effectively and efficiently protect U.S. national security and remove the burden of unnecessary restrictions on the development and activity of the U.S. space industrial base. Should the proposed rules become final and effective, they would transform the export control regulatory landscape for manufacturers and exporters of satellites, component systems, and related ground equipment and technology.

More Than a Decade under the ITAR

On February 15, 1996, a Chinese-made launch vehicle carrying a U.S.-manufactured satellite failed during launch, crashing into a town near Xichang, China. Immediately following the crash, China Great Wall Industry Corporation, the launch services provider, commenced an investigation of the launch failure and invited Space Systems/Loral, LLC (SS/L), the satellite's manufacturer, to participate. SS/L initially cooperated with and participated in the investigation but stopped all investigation activity upon receiving a cease-and-desist letter from the U.S. government. Although SS/L had obtained two export licenses from the U.S. government authorizing the launch of its satellite in China, the U.S. government's view was that SS/L was not

authorized under any of its licenses to participate in the investigation of the launch failure. Because no U.S. government monitors had been involved in the launch failure investigation, the Department of Defense and the Central Intelligence Agency launched their own investigations to address concerns that SS/L, through its cooperation with and participation in the launch failure investigation, may have provided unauthorized defense services to China. The matter was later referred to the Department of Justice, which ultimately levied a \$14 million fine on SS/L as part of a consent decree.¹

In response to these developments, the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999 (the 1999 NDAA)² effectively removed the president's authority to determine the jurisdictional status of satellites and related items under U.S. export control regulations. Specifically, the 1999 NDAA issued the sweeping direction that all space-related items, including satellites, be controlled as "defense articles." Defense articles and defense services are subject to the jurisdiction of the International Traffic in Arms Regulations (ITAR),³ administered by the Directorate of Defense Trade Controls (DDTC), U.S. Department of State, and are identified on the ITAR's U.S. Munitions List (USML).⁴ Items not subject to the jurisdiction of the ITAR or to the exclusive jurisdiction of one of the few other U.S. export control regimes are subject to the jurisdiction of the Export Administration Regulations (EAR),⁵ administered by the Bureau of Industry and Security (BIS), U.S. Department of Commerce. The EAR include the Commerce Control List (CCL) in Supplement No. 1 to part 774.

While both the ITAR and the EAR impose restrictions and require licenses for exports and reexports of the items and services subject to their respective jurisdiction, the ITAR represents a significantly more stringent and burdensome export control regime than does the EAR. Licensing under the ITAR generally involves the filing of more applications (e.g., exporters are required to reapply even if they have an existing license for the same item and customer), a processing period sometimes involving six months or more, and the satisfaction of more onerous requirements, such as detailed disclosure regarding the transaction underlying the specific export application, in addition to submission of related commercial contracts. Moreover, the ITAR prohibits exports to countries that are subject to U.S. government

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embargoes,⁶ allows for very few license exceptions, and requires licenses issued pursuant to the ITAR to include provisos as to the detail and extent of technical information that can be shared or exchanged with non-U.S. persons, irrespective of their nationality or domicile. In contrast, under the EAR, licensing involves fewer requirements, greater flexibility, and a number of exemptions for exports to certain destinations and for certain purposes.

Signaling and Processing Change

Operating in the regulatory environment created by the 1999 NDAA proved damaging for the U.S. space industrial base. The onerous requirements of the ITAR not only drove up the costs and burdens of compliance with U.S. export control regulations, but also drove down the level and frequency of business conducted with international customers and partners. Under the ITAR, any foreign-made item that incorporates an ITAR-controlled item becomes subject to the ITAR. The burdens imposed by this rule motivated a European manufacturer, Thales Alenia Space, to develop and bring to market an “ITAR-free” satellite—essentially a satellite devoid of any U.S.-source content—in order to relieve its customers of the burdens of compliance, and risks of noncompliance, with U.S. export control regulations. Meanwhile, U.S. government investment in the space sector, ever more critical to the industry as a result of these developments, began to shrink, further reducing the number of business opportunities available to the U.S. space industrial base such that U.S. government investment could no longer be relied upon to offset lost business abroad.

In addition, during the years following passage of the 1999 NDAA, the space industry endured a period of unprecedented globalization. Hardware and services that traditionally had been difficult to procure in the global market gradually became readily available from manufacturers and service providers throughout the world. Such globalization only further diminished the competitive standing of U.S. manufacturers vis-à-vis their foreign competitors. More importantly, however, these economic forces undermined the purpose and effectiveness of U.S. export control regulations, particularly the ITAR, to safeguard U.S. national security. As satellites, their components, and related technology were no longer only, or even primarily, available from the U.S. market, heightened export controls became a significant burden to U.S. competitiveness instead of an effective barrier to the proliferation of sensitive space technology.

The twin forces of globalization of the space market and contraction of the U.S. space industrial base, together with increasing pressure from space industry leaders, eventually compelled lawmakers to undertake a reevaluation of the regulatory environment created by the 1999 NDAA. Accordingly, the National Defense

Authorization Act for 2010 (the 2010 NDAA)⁷ directed both the secretary of defense and the secretary of state to assess the risks associated with removing satellites and related items from the USML. As required by Section 1248 of the 2010 NDAA, in March 2012, the Departments of Defense and State jointly filed with Congress their “Final Report” (the 1248 Report).⁸

The 1248 Report identified certain types of satellites and related items that should not be designated as “defense articles” and controlled under the ITAR. The rationale for this proposed change was that such satellites and related items no longer contain technologies that are unique to the United States and, thus, no longer can be deemed critical to U.S. national security. Based on these findings, the Departments of Defense and State concluded that it would be more appropriate for such satellites and related items to be subject to the export control jurisdiction of the EAR and recommended, “[f]or the sake of national and economic security . . . that authority to determine the appropriate export control status of satellites and space-related items be returned to the President.”

After reviewing the 1248 Report, Congress passed the National Defense Authorization Act for Fiscal Year 2013 (the 2013 NDAA),⁹ which effectively returned to the president the authority to determine which export control regulations should govern exports and reexports of satellites and related items. Specifically, Section 1261 of the 2013 NDAA eliminated the requirement that all satellites and related items be subject to the export control jurisdiction of the ITAR.

President Obama signed the 2013 NDAA on January 2, 2013. Shortly thereafter, with the president’s new, or renewed, authority, the Department of Defense commenced a review of the items covered by USML Category XV for purposes of identifying those items that either are (1) inherently military or otherwise warrant control on the USML or (2) common to non-military space applications but carry capabilities that provide a critical military or intelligence advantage to the United States and are exclusively or primarily available from the United States. The Department of Defense recommended that items falling under either or both of these categories remain on the USML and that all other items become subject to the export control jurisdiction of the EAR. Based on the Department of Defense’s review and recommendation, in May 2013, both the Department of Commerce and the Department of State issued proposed rules to revise the applicable export control regulations.

The Proposed Rules

Department of State Proposed Rules Regarding the ITAR

The Department of State proposed revisions to USML Category XV to limit its scope to only certain types of spacecraft, namely spacecraft that (1) are

designed to detect or mitigate the effects of a nuclear detonation; (2) track ground, airborne, missile, or space objects using imaging, infrared, radar, or laser systems; (3) conduct signals or measurement and signatures intelligence; (4) provide space-based logistics, assembly, or servicing of spacecraft; (5) are anti-satellite or anti-spacecraft; (6) have space-to-ground weapons systems; (7) have certain electro-optical remote sensing capabilities or characteristics; (8) have certain radar remote sensing capabilities or characteristics; (9) provide positioning, navigation, and timing (but not if only a differential correction broadcast for purposes of positioning, navigation, or timing); (10) are specially designed to be used in a constellation or formation and, when operated together, form a virtual satellite with the characteristics of any ITAR-controlled spacecraft; (11) are man-rated suborbital, orbital, lunar, interplanetary, or habitat; or (12) are classified, contain classified software or hardware, are manufactured using classified production data, or are being developed using classified information.¹⁰

Pursuant to the proposed revised USML Category XV, all spacecraft not specifically enumerated in USML Category XV would become subject to the EAR.

The proposed revised USML Category XV would also cover ground control systems and training simulators specially designed for telemetry, tracking, and control of ITAR-controlled spacecraft, global positioning system receiving equipment designed, modified, or configured for military use or with certain specific characteristics and certain highly sensitive spacecraft parts, components, accessories, and systems. All other ground control systems and training simulators, global positioning system receiving equipment, and spacecraft parts, components, accessories, and systems not specifically enumerated in USML Category XV would become subject to the EAR.¹¹

Even though the proposed revised USML Category XV does not guarantee that a satellite or related item in normal commercial use will not be subject to the ITAR (e.g., in cases where a satellite or related item provides the United States with a critical military or intelligence advantage), the Department of State has emphasized that it is not the intention of the U.S. government to subject satellites and related items to the ITAR. To protect against such inadvertent consequences, the Department of State has specifically requested that the public provide comments to the proposed revised USML Category XV to identify examples of satellites and related items that would be controlled by the ITAR under the revised USML Category XV and are now in normal commercial use.¹²

Department of Commerce Proposed Rules Regarding the EAR

The Department of Commerce has also proposed revisions to the CCL to provide for export control

regulations for satellites and related items that no longer merit control on the USML and are not otherwise within the scope of existing provisions of the CCL. Specifically, such satellites and related items would be identified in new Export Control Classification Numbers (ECCNs), namely ECCNs 9A515, 9B515, 9D515, and 9E515, together known as the “500 Series” ECCNs. Satellites and related items covered by the 500 Series ECCNs are essentially commercial items with no military or intelligence applications, such as commercial communications satellites.¹³

Proposed ECCN 9A515 would control (1) spacecraft, including satellites and manned or unmanned space vehicles, whether developmental, experimental, research, or scientific, not covered by USML Category XV; (2) ground control systems and training simulators specially designed for telemetry, tracking, and control of such spacecraft; (3) certain radiation hardened microelectronic circuits; and (4) parts, components, accessories, and attachments that are space qualified but not controlled on the USML or elsewhere in an ECCN.¹⁴

Proposed ECCN 9B515 would control (1) test, inspection, and production equipment specially designed for the production or development of commodities covered by ECCN 9A515 or USML Category XV; (2) equipment, cells, and stands specially designed for testing, analysis, and fault isolation of commodities covered by ECCN 9A515, ECCN 9A004, or USML Category XV; and (3) certain environmental test chambers and components specially designed for them.¹⁵

Proposed ECCN 9D515 would control software specially designed for the development, production, operation, installation, maintenance, repair, overhaul, or refurbishing of commodities covered by ECCN 9A515 or 9B515. Proposed ECCN 9E515 would control technology required for the development, production, operation, installation, maintenance, overhaul, repair, or refurbishing of items controlled by ECCN 9A515, 9B515, or 9D515.¹⁶

Currently, items manufactured outside the United States that incorporate items subject to the export control jurisdiction of the EAR are subject to the EAR if the total percentage of their EAR-controlled content, measured in terms of the proportion of the value of such U.S.-source content to the total value of the relevant foreign-made item, exceeds a certain *de minimis* threshold. The CCL’s *de minimis* rule normally allows reexport without a U.S. license if the foreign-made item contains equal to or less than 25 percent by value of controlled U.S.-source content.¹⁷ Under the proposed rule, the *de minimis* threshold for 500 Series items would be 0 percent in cases where the foreign-made item is destined for a country subject to a U.S. arms embargo¹⁸ and 25 percent in all other cases. Therefore, foreign-made items that incorporate any U.S.-source 500 Series content would only be subject to the export control jurisdiction of the EAR if intended for export to

countries subject to a U.S. arms embargo or if containing greater than 25 percent U.S.-source content.

In addition, the Department of Commerce proposes that foreign-produced direct products of U.S.-source 500 Series technology that constitute 500 Series items be subject to the EAR in cases where such items are destined for countries subject to a U.S. arms embargo or countries that are of concern for national security, chemical and biological weapons capability, missile technology, or terrorism reasons. The Department of Commerce presumably included this limitation to address a recommendation in the 1248 Report that the United States maintain strict controls on transfers of space-related items, including even noncritical space-related items, to end-users that are likely to use such items for purposes that are adverse to U.S. national security interests.¹⁹

Effects on Industry

The proposed rules of the Departments of State and Commerce reform the existing export control regimes in order to stimulate greater business for the U.S. space industrial base while protecting U.S. national security interests.

Under the proposed rules, exporters and reexporters of 500 Series items will need to apply for fewer licenses because their transactions will be eligible for EAR license exceptions that permit exports to U.S. government agencies (License Exception GOV), exports valued at less than \$1,500 (License Exception LVS (limited value shipments)), exports of items intended to be used for servicing purposes or as replacement parts (License Exception RPL), temporary exports (License Exception TMP), and exports to NATO member countries or other export control regime partner countries (License Exception STA (Strategic Trade Authorization)).²⁰ Under the regulatory environment created by the 1999 NDA, hardly any license exceptions are available to exporters because, with few exceptions, the ITAR provides for license exceptions only for certain exports to Canada.

The Departments of State and Commerce have formulated the proposed rules so that License Exception STA will be available for most 500 Series items. While License Exception STA imposes its own burdens (including requirements that the exporter provide certain information about the item being exported and obtain from the applicable consignee a statement acknowledging and committing the consignee to comply with the EAR and other U.S. laws), such burdens are significantly less onerous and more streamlined than the corresponding requirements under the ITAR. Under License Exception STA, a consignee statement does not need to have an expiration date and does not need to be submitted in advance for approval. Moreover, a single consignee statement may apply to an unlimited number of items. As a result, exporters with regular customers can prepare and use repeatedly a

single consignee statement for each transaction they conduct with a particular customer.

The applicable 25 percent de minimis threshold under the EAR will also result in a net reduction of export license applications for 500 Series items. So long as such items constitute less than 25 percent of any foreign-made item and such foreign-made item is not intended for a country subject to a U.S. arms embargo, such foreign-made item will not be subject to the export control jurisdiction of the EAR. Unlike items subject to the EAR, items subject to the ITAR remain subject to the ITAR when they are incorporated abroad into a foreign-made item, no matter the percentage of U.S.-source ITAR-controlled content in the foreign-made item. This distinction between the ITAR and the EAR is particularly significant because of its impact on foreign manufacturers. With respect to ITAR-controlled items, foreign manufacturers have an incentive to avoid incorporating any amount of U.S.-source content in their products, whereas with respect to EAR-controlled items, foreign manufacturers are only impacted if they incorporate U.S.-source content in an amount that exceeds 25 percent of the value of their product. As any percentage of U.S.-source content below 25 percent will not implicate the application of the EAR, foreign manufacturers are more likely to incorporate EAR-controlled items than ITAR-controlled items in their products. Consequently, the proposed rules are expected to stimulate greater business for the U.S. space industry from foreign manufacturers.

Even in cases where a license will be required under the EAR, the process of obtaining such a license will be more favorable to exporters because the licensing procedure for items on the CCL is simpler, faster, and less costly than the licensing procedure for items on the USML. Under the USML licensing procedure, an applicant must include with its application an executed contract or purchase order for the relevant items to be exported. As there is no such requirement under the CCL licensing procedure, exporters will benefit from knowing whether the U.S. government will authorize their transaction before engaging a consignee in further negotiation or documentation, which can be complex, expensive, and commercially prejudicial. Furthermore, under the USML licensing procedure, the same exporter is required to apply repeatedly for licenses for each export, even when the export is intended for a familiar and trustworthy customer in a country that is either a close ally of the United States or an export control regime partner. Conversely, under the CCL licensing procedure, an applicant may apply for a license authorizing all of its exports to a particular consignee for the validity period of the license (usually four years), reducing the total number of licenses for which the applicant must apply. In addition, the USML licensing procedure requires applicants to pay registration fees, starting at \$2,250 per year. The CCL licensing procedure, however,

does not involve any registration or processing fees.

The proposed rules are likely to have the greatest impact on exporters of space-related parts, components, and accessories, which are generally made by small or mid-sized commercial entities, as opposed to complete spacecraft, which are the province of large manufacturers or systems integrators. While the proposed rules will not eliminate control of such items, they will likely reduce administrative costs and delays associated with exports of such items by, for example, making available a greater number of license exceptions. To the extent they consistently deal in certain items or with certain consignees, exporters of space-related parts, components, and accessories will experience a significant reduction in the number and frequency of export license applications they are required to file and, therefore, will experience less delays in conducting their business. Due to the EAR de minimis threshold, which reduces the disincentive for foreign manufacturers to incorporate U.S.-source content in their products, the proposed rules are also likely to increase demand from foreign customers for U.S.-source space-related parts, components, and accessories, which can be incorporated in a foreign-made product without exceeding the 25 percent limit.

The licensing of exports or reexports of satellites and related items transferred from the USML to the CCL will involve a case-by-case review by the Department of Commerce to determine whether the underlying transaction is in conflict with the national security or foreign policy interests of the United States.²¹ The Department of Commerce has made clear that applications for licenses involving export or reexport to a country that is subject to a U.S. arms embargo will be decided in a manner that is consistent with U.S. arms embargo policies.²² Additionally, as required by Section 1261 of the 2013 NDAA, all applications for licenses involving an export or reexport to the People's Republic of China, North Korea, or any country that is designated by the United States as a state sponsor of terrorism will be denied.²³

Conclusion

By effecting a change in the jurisdictional status of certain satellites, component systems, and related ground equipment and technology from the ITAR to the EAR, the proposed rules will eliminate certain license requirements, make available a greater number of license exceptions, simplify license application procedures, and reduce or eliminate associated fees. Members of the U.S. space industrial base, however, will not benefit from the proposed new regulatory environment until the relevant changes are in effect. After submitting formal notification of the proposed rules to Congress, and assuming Congress does not raise any objections, the Departments of State and Commerce will publish their final rules, following

which there will be a 180-day transition period before the rules take effect. As a result, the "launch" of the new regulatory environment, and its anticipated benefits for U.S. exporters, is expected to take place sometime in the spring of 2014.

Endnotes

1. H. SELECT COMM. ON U.S. NATIONAL SECURITY AND MILITARY/COMMERCIAL CONCERNS WITH THE PEOPLE'S REPUBLIC OF CHINA, FINAL REPORT (Comm. Print 1999).
2. Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub. L. No. 105-261, 112 Stat. 1920.
3. 22 C.F.R. §§ 120.1–130.17.
4. *Id.* § 121.1.
5. 15 C.F.R. §§ 730.1–774.2.
6. The following countries are subject to a U.S. arms embargo: Afghanistan, Belarus, Burma, China, Cote d'Ivoire, Cuba, Cyprus, Democratic Republic of Congo, Eritrea, Fiji, Haiti, Iran, Iraq, Lebanon, Liberia, Libya, North Korea, Somalia, Sri Lanka, Sudan, Syria, Venezuela, Vietnam, and Zimbabwe. 22 C.F.R. § 126.1.
7. National Defense Authorization Act for 2010, Pub. L. No. 111-84, 123 Stat. 2190.
8. DEP'TS OF DEFENSE & STATE, REPORT TO CONGRESS, SECTION 1248 OF THE NATIONAL DEFENSE AUTHORIZATION ACT FOR FISCAL YEAR 2010 (PUB. L. NO. 111-84), RISK ASSESSMENT OF UNITED STATES SPACE EXPORT CONTROL POLICY (2011) [hereinafter SECTION 1248 REPORT], http://www.defense.gov/home/features/2011/0111_nsss/docs/1248_Report_Space_Export_Control.pdf.
9. National Defense Authorization Act for Fiscal Year 2013, Pub. L. No. 112-239, 126 Stat. 1632.
10. Amendment to the International Traffic in Arms Regulations: Revision of U.S. Munitions List Category XV and Definition of "Defensive Service," 78 Fed. Reg. 31,444, 31,449–50 (May 24, 2013) (to be codified at 22 C.F.R. pt. 121).
11. *Id.* at 31,451–52.
12. *Id.* at 31,444–45.
13. Export Administration Regulations (EAR): Control of Spacecraft Systems and Related Items the President Determines No Longer Warrant Control Under the United States Munitions List (USML), 78 Fed. Reg. 31,431, 31,433 (May 24, 2013).
14. *Id.*
15. *Id.*
16. *Id.* at 31,434.
17. See SECTION 1248 REPORT, *supra* note 8, at 7.
18. 22 C.F.R. § 126.1.
19. See SECTION 1248 REPORT, *supra* note 8, at 4–6.
20. Export Administration Regulations (EAR): Control of Spacecraft Systems and Related Items the President Determines No Longer Warrant Control Under the United States Munitions List (USML), 78 Fed. Reg. 31,431, 31,435 (May 24, 2013).
21. *Id.* at 31,434.
22. *Id.*
23. *Id.*