

Defense Trade Advisory Group



Trade Compliance Process

Plenary Session

October 29, 2015



Agenda

- Working Group Members
- Task Description
- Identifying “Administrative” Violations
 - Methodology
 - Consequences
- Additional Task Issues
 - DTCC & OEE – Enforcement approaches
 - Lessons from other disclosure programs
- Recommendations



Working Group Members

- Dava Casoni
- Monica Chavez
- Giovanna Cinelli
- *Mike Cormaney
- Greg Creeser
- B.J. Demery
- Larry Dodson
- Matthew Goldstein
- *Cindy Keefer
- Spence Leslie
- Christine McGinn
- Joy Robins
- Joe Veiga

**Team Leaders*



Task #1 – Trade Compliance Process

Review the current Voluntary Disclosure (VD) process and provide recommendations for how to ensure that foreign policy and national security interests are given greater focus in the preparation, review, and adjudication process. Specifically,

- a) analyze how to address “administrative” VDs, including how to distinguish “administrative” VDs from other VDs and whether a “binning” or triage process would be beneficial both to DDTC and industry;
- b) review the Department of State’s approach to regulatory enforcement versus the Department of Commerce’s approach and analyze how or if the approaches could be synchronized and/or modified;
- c) consider whether VD policies or procedures from other regulatory agencies may have elements that could be of benefit for State; and
- d) review how the trade compliance process may need to change if/when State and Commerce’s trade regulatory bodies merge in the future.



Working Group Approach

- Gather relevant information from:
 - Working Group/DTAG members
 - Companies (all sizes)
 - Law firms & consultants
 - Non-profits & universities
- Research:
 - Other USG agency disclosure programs
 - Other USG regulations addressing national security issues
 - Effectiveness of VD programs
- Develop recommendations



Underlying Considerations

- Disclosures are *voluntary* – *Except 126.1*
- Post ECR...
 - USML items more sensitive/likely to implicate national security concerns
 - Increase in “multi-agency” disclosures
 - Presumed increase in USG coordination of investigations



Identifying “Administrative” VDs

- Terminology
- Requirements for methodology to identify “administrative” VDs:
 - Objective
 - Straightforward
 - Flexible
 - Address differing opinions on Industry ability to assess national security impact of violations



Options Considered

1. Borrow standard from National Industrial Security Program (NISP)
2. Designate specific ITAR provisions that are “administrative”
3. Classify by severity/risk – “Risk Matrix”
4. Review of aggravating/mitigating factors to identify less serious violations
5. Combination

Option #1 – Analogizing to the NISP Standard



- An “administrative” violation = One that does **not** involve either:
 - Loss, compromise or suspected loss or compromise of a Defense Article (includes Technical Data); or
 - Performance of a Defense Service
- Considerations:
 - Objective standard
 - Actual release = Most likely national security impact
 - Standard is a known concept



Option #2 – Classifying by ITAR Section

- Designate specific ITAR provisions as “administrative”
 - Look for industry reporting requirements that assist DDTC in managing its process
 - Define violations of those provisions as “administrative” violations
- Considerations:
 - Straightforward and objective
 - Industry may not have all necessary information
 - Limited flexibility – for both DDTC and industry
 - Circumstances when violation of process-related provisions can implicate national security
 - Circumstances where “substantive” violations can cause no harm or potential harm to national security



Option #3 – Risk Matrix

- Graphical method of identifying, assessing and assigning a level of risk to potential violations to identify “administrative” VDs

Concerns:

- Subjective determinations – Highly dependent on facts/circumstances
- Potential incongruity regarding magnitude determinations
- Relevant information may not be known to industry

		Level of Magnitude: Impact on National Security/Foreign Policy			
		Level 1	Level 2	Level 3	Level 4
Rate of Occurrence: Probability	CERTAIN	Annual Report	Semi-Annual Report	Semi-Annual Report	Monthly
	LIKELY	Annual Report	Monthly	Monthly	Immediately
	POSSIBLE	Semi-Annual Report	Monthly	Immediately	Immediately
	UNLIKELY	Semi-Annual Report	Monthly	Immediately	Immediately
	RARE	Monthly	Immediately	Immediately	Immediately



Option #4 Aggravating/Mitigating Factors

AGGRAVATING	FACTOR	MITIGATING
<ul style="list-style-type: none"> 126.1 issues or “ineligible” parties Implicates reason for control 	Destination & Parties	<ul style="list-style-type: none"> “Friendly” countries Unrelated to reason for control
<ul style="list-style-type: none"> None (or RWAs/denials) 	Precedent Approval(s)	<ul style="list-style-type: none"> Multiple – for same country/end user
<ul style="list-style-type: none"> Repetitive violations of same type Systemic issues Intentional/willful action 	Nature of Violation(s)	<ul style="list-style-type: none"> Isolated incident No willful/intentional conduct Small quantity/value of exports
<ul style="list-style-type: none"> Continuing conduct Failure to identify in timely manner 	Corrective Actions	<ul style="list-style-type: none"> Effective actions implemented Item/technology retrieved
<ul style="list-style-type: none"> Attempt to hide/conceal violations 	Cooperation	<ul style="list-style-type: none"> VD/alternative process Respond fully in a timely manner
<ul style="list-style-type: none"> Lack of support Ineffective resources allocated 	Management Support	<ul style="list-style-type: none"> Full support Adequate personnel & resources available
<ul style="list-style-type: none"> Sensitive (<i>e.g.</i>, MTCR, SME) Manufacturing “know how” 	Items/ Technology Involved	<ul style="list-style-type: none"> Less sensitive (<i>e.g.</i>, parts/components) No knowledge transfer (<i>e.g.</i>, “build to print”)



Proposed Methodology

CATEGORY	DESCRIPTION	PRESUMED CONSEQUENCES
1	Involves: 1. 126.1 country/national; <u>and</u> 2. One of the following: (a) Loss or compromise; (b) Defense Service; <u>or</u> (c) Proposal/presentation – 126.1(e)	<ul style="list-style-type: none">• “Immediate” disclosure mandatory• Presumption not rebuttable by mitigating factors
2	Involves: 1. Countries/nationals other than 126.1; <u>and</u> 2. Loss or compromise or performance of Defense Service	<u>IF</u> decision made to disclose: <ul style="list-style-type: none">• Existing 127.12 process• Presumption rebuttable by aggravating/mitigating factors
3	<u>No</u> loss or compromise or Defense Service	<u>IF</u> decision made to disclose: <ul style="list-style-type: none">• Options for alternatives to 127.12• Presumption rebuttable by aggravating/mitigating factors• <u>Note</u>: Proposals/presentations involving 126.1 countries with no loss/compromise still Category 1



Category 1 Violations

- Involves:
 1. 126.1 country/national; and
 2. One of the following:
 - a) Loss or compromise of Defense Articles (including Technical Data)
 - b) Performance of Defense Service; or
 - c) Proposal or presentation to sell, export, re-export, etc.
- Consequences – *No change*
 - Most serious
 - Disclosure required (No flexibility)
 - DTCC can use “triage” process to identify/focus on cases of actual concern



Category 2 Violations

- Involve:
 1. Countries/nationals other than 126.1; and
 2. Either:
 - a) Loss or compromise of Defense Articles (including Technical Data); or
 - b) Performance of a Defense Service
- Presumed Consequences:
 - Disclosure *voluntary* per 127.12 process
 - Presumption is rebuttable
 - Mitigating factors can change to Category 3



Category 3 Violations

- Violations that do ***not*** involve any loss or compromise of Defense Articles (including Technical Data) or performance of a Defense Service
- Presumed consequences:
 - Unlikely to have national security implications
 - ***Option for alternative(s) to 127.12***
 - Allow DDTC to meet its requirements without overly burdening industry
 - Precedent: Web guidance on temp. import violations
 - Presumption is rebuttable based on aggravating/mitigating circumstances



Alternative Processes for Category 3

- Precedent: Alternative to VD for certain Temporary Import Violations - <http://pmddtc.state.gov/licensing/documents/WebNoticeTemporaryImportViolations.pdf>
- Extend same concept to create options for other Category 3 violations
 - Periodic reports or “binning” of Category 3 violations
 - Report issue in application
 - Notification of corrective action
 - DTCC issue guidance that Category 3 violations do not affect ability to continue with program
 - Remove requirement from ITAR, if no significant USG purpose
- DTCC has ability to rescind a company’s ability to use alternative processes

Standard 127.12 process *always* remains an option



Excerpt from Violations Spreadsheet

ITAR Section	Violation Category	Option(s) for Alternative Process (Category 3)
Part 122 - REGISTRATION OF MANUFACTURERS AND EXPORTERS		
§122.1 - Requirement to register if engaged in the U.S. in the business of manufacturing, exporting or temporarily importing defense articles or furnishing defense services	3	Submit registration and notify DDTC that you should have registered at an early date. Include root cause and corrective action(s)
§122.4(a) - Five-day notification requirement for specified changes in information contained in registration statement	3	Submit notice with explanation of why notice was not timely, root cause and corrective action(s)
§122.4(b) - 60-day advance notification requirement for intended sale or transfer to a foreign person of ownership or control of the registrant	3	Submit notice with explanation of why notice was not timely, root cause and corrective action(s)
§122.4(c) - Notification requirement when registrant merges with another company or acquires, or is acquired by, another company	3	Submit notice with explanation of why notice was not timely, root cause and corrective action(s)
§122.5 - Five-year recordkeeping requirement for registrants	3	Submit a notice that recordkeeping issues identified and describe corrective action(s)
Part 123 - LICENSES FOR THE EXPORT AND TEMPORARY IMPORT OF DEFENSE ARTICLES		
§123.1(a) - License requirement for export or temporary import of defense articles	2	
§123.3(a) - License (DSP-61) requirement for temporary import and subsequent export of unclassified defense articles	3 <i>(for import & return)</i>	Apply for DSP-5 to return and provide explanation in application, along with root cause and corrective action(s)
	2 <i>(for trans-shipment)</i>	
§123.4 - Exemptions for temporary import (and subsequent export) of unclassified U.S.-origin defense articles	3	Alternative process already in place <i>(Temporary Import Violations)</i>



Excerpt from Violations Spreadsheet

ITAR Section	Violation Category	Option(s) for Alternative Process (Category 3)
§124.4(a) - Applicant must file a copy of the concluded TAA or MLA with DDTC not later than 30 days after Agreement enters into force	3	Upload executed agreement to D-Trade with cover letter that explains reason for missed deadline, root cause & corrective action(s)



Excerpt from Violations Spreadsheet

ITAR Section	Violation Category	Option(s) for Alternative Process (Category 3)
§123.3(a) - License (DSP-61) requirement for temporary import and subsequent export of unclassified defense articles	3 (for import & return)	Apply for DSP-5 to return and provide explanation in application, along with root cause and corrective action(s)
	2 (for trans-shipment)	



Other Process Improvements

- Public change in expectations
 - Single most effective method to reduce administrative VDs
 - Recognize industry ability to exercise discretion
- Electronic submission/tracking system – Later
- Case officer assignment process
 - Try to assign VDs from same company or USML Category to same case officer(s)
 - Develop background to better assess cases
 - Facilitate better understanding of expectations and requirements on both sides
- Increase interagency coordination for “transition” VDs
 - Assign “lead agency” for multi-agency matters
 - One VD for underlying conduct, with copies to other agencies



Differing Enforcement Approaches

- Industry perception on enforcement
- Positive elements to synchronize:

DTCC	OEE
Process to address less sensitive violations administratively	Extended timeframe for VD investigation/report (180 days)
Greater emphasis on corrective measures, less on assessing penalties/publicity	



Lessons from Other Programs

- Various positive elements that may warrant consideration by DDTC
- Four main categories:
 - Electronic Submission Process* (CBP, EPA, HHS, Treasury)
 - Administrative “Binning” Process* (CBP, Census)
 - Clear benefits offered to those who disclose (CBP, Census, IRS, NRC, OFAC)
 - Published Guidance (CBP, Census, FAA, NRC, TSA)

**Offered for some types of disclosures*



Electronic Submission - CFIUS

- Simple document upload system
 - No electronic form
 - Email address for submission of documents in .pdf format
 - Email response with case number & name of compliance specialist
 - Use existing EFS system?
- Benefits:
 - Expedite initial phases - including corrective license applications
 - Facilitate tracking and status updates
 - Decrease labor intensive process of logging, copying, etc.
 - Electronic records help prevent “lost” submissions



DTAG Summary & Recommendations

- Methodology for identifying “administrative” violations
 - Based on “loss or compromise” standard; *and*
 - Analysis of aggravating/mitigating factors
- Alternatives to 127.12 process for Category 3 violations
- Additional process changes
 - Modify public statements regarding VD expectations
 - Case officer assignment
 - Electronic submission process



Thank you



Back-up Slides



Lessons from Other Programs

US Government Agency	Positive Elements
Bureau of Industry and Security (BIS)	<ul style="list-style-type: none"> • CCL Part 764.1 provides detailed information association with violations • Supplement No. 1 to Part 766 ; describes how BIS responds to violations and how it typically exercised its discretion regarding whether to pursue an administrative enforcement • Violations are to be disclosed “as soon as possible” • The initial notification date is the date received by the Office of Export Enforcement • Option to disclose a violation orally, with a confirmation in writing as soon as possible • Final Due 180 days of the initial notification; long lead time • Oral presentations can be requested • BIS Warning and “Closure No Action” Letters at times may come with an offer by BIS to conduct outreach training • Anti-boycott Issues/Concerns; industry is allowed to call and request advice
Census Bureau <ul style="list-style-type: none"> • Disclosure of violations of the FTR. 	<ul style="list-style-type: none"> • Guidance outlined in Foreign Trade Regulations, 15 CFR Part 30.74 • Provides sample guidance on website • Allows you to combine multiple transactions in one disclosure • Recommends review/disclosure back five years
Customs and Border Protection (CBP) <ul style="list-style-type: none"> • Disclosure of Import Violations of 19 USC 1592 	<ul style="list-style-type: none"> • Recognized prior disclosure process with published guidance • Mitigation of civil penalties • Other published mechanisms for reporting and correcting administrative errors, although they do not provide mitigation of civil penalties. <ul style="list-style-type: none"> • Post Entry Amendment (PEA) process – correction of entry mistakes prior to liquidation. <ul style="list-style-type: none"> • “Binning” and quarterly reporting of errors with a Customs duty impact <\$20 (owed or refund) • Protest process – allows for recovery of overpayment of Customs duties up to 90 days after liquidation. • Voluntary Tender – allows for payment of Customs duties owed.



Lessons from Other Programs

US Government Agency	Positive Elements
Customs and Border Protection (CBP) <ul style="list-style-type: none">• Disclosure of a violation of the Foreign Trade Regulations (FTR) (Export)	<ul style="list-style-type: none">• Drafted guidelines with a review of DHS and DOC• Separates mitigation schemes (each one with a separate criteria)<ol style="list-style-type: none">I. The failure to file the export information in AESII. The late filing of the export information in AESIII. The failure to file all the necessary information in AES, the filing of incorrect information in AES, or failure to comply with some other requirement of the FTRIV. The failure of the exporting carrier to provide certain documents or certain information to CBP• Offers special handling of certain circumstances• Penalties can be applied to all parties involved not just the one disclosing• Penalties are assessed per each AES transaction rather than per violation• The decision whether or not to impose penalties heavily weighs on “informed compliance” (i.e. first time offenses, alternative to educate and inform industry, company outreach, etc.)
Environmental Protection Agency (EPA)	<ul style="list-style-type: none">• Electronic Submittal Available• Provides annual results of enforcement accomplishments; including those not penalized however showing a significant compliance program put in place
Internal Revenue Service	<ul style="list-style-type: none">• Mitigating factor used by IRS in determining whether criminal prosecution will be recommended.
Office of Foreign Assets Control (OFAC)	<ul style="list-style-type: none">• Offers penalty mitigation of 50% of base penalty, when self-disclosed.



Lessons from Other Programs

US Government Agency	Positive Elements
Federal Aviation Administration (FAA)	<ul style="list-style-type: none">• Issues Guidance on the five types of actions related to FAA enforcement<ol style="list-style-type: none">I. Administrative Action<ul style="list-style-type: none">• FAA considers a violation minor if the action was not deliberate, was not significantly unsafe, and did not evidence a lack of competency or qualification . Warning Letter or Letter of Correction is issuedII. Re-examination Action<ul style="list-style-type: none">• Can reexamine an airman at any time if the FAA has reasonable groundsIII. Certification Action<ul style="list-style-type: none">• Seeks to suspend or revoke a pilots license when a violation indicates a lack of technical proficiency or qualificationIV. Civil Penalty<ul style="list-style-type: none">• Used as an option onlyV. Criminal Action<ul style="list-style-type: none">• Applied to acts such as aircraft privacy, forgery of certificates, carry weapons aboard aircraft, etc.
Nuclear Regulatory Commission (NRC)	<ul style="list-style-type: none">• Strong emphasis on self-identification of violations, through self disclosure.• Will consider providing “credit” for corrective actions and self-identification of violations.• Fairly comprehensive guidance published in the NRC Enforcement Policy –<ul style="list-style-type: none">• Identifies Severity Levels (I to IV) (highest to lowest)• Provides good information about disposition of violations.
Transportation Security Administration (TSA)	<ul style="list-style-type: none">• Published Voluntary Disclosure Program Policy• Applies to aircraft operators (except individuals), indirect air carriers, foreign air carriers, airports and flight training providers.<ul style="list-style-type: none">• They stress that the Voluntary Disclosure Program does not cover individuals.• Will issue a letter of correction in lieu of civil penalty. Case considered closed upon issuance.



Lessons from Other Programs

	OFAC	IRS	Census/FTR	NRC
Required by law or voluntary?	Voluntary	Voluntary	Voluntary	Voluntary
Benefits of Disclosing	Penalty Mitigation – 50% of base penalty	Mitigating factor used by IRS in determining whether criminal prosecution will be recommended	Mitigating factor used by Census in determining what administrative sanctions, if any, will be sought.	If problem requiring corrective action was self-identified and corrective action is promptly taken, no civil penalty.
Timing of Disclosure	Prior to or at the same time USG discovers the apparent violation or another substantially similar	Prior to the IRS initiating a civil exampation, regardless of whether I relates to undisclosed foreign accounts or undisclosed foreign entities, the taxpayer will not be eligible to come in under the IRS's Voluntary Disclosure Practice	Prior to Census or any other USG agency learning the same or substantially similar information from another source, and the commencement of an investigation or inquiry in connection with that information.	Prior to discovery by USG



U.S. Customs and Border Protection (“CBP”)

Prior Disclosures, Post Entry Amendments, and Protests

	Prior Disclosure (PD)	Post Entry Amendment (PEA)	Protest	Voluntary Tender
Required by law or voluntary?	Voluntary	Voluntary	Voluntary	Voluntary
When must it be filed?	Prior to CBP discovery	Prior to Liquidation	After Liquidation	Prior to CBP discovery
Offers relief from penalties?	Yes	No	No	No
What is it used for?	Reporting a violation of 19 U.S.C. 1592	Correction of an entry mistake	Refund of Customs Duties	Payment of Customs Duties
How is it filed?	Letter, to local CBP office	Letter, to local CBP office or via ACE	CF19 form, to local CBP office	
Offers special handling of certain circumstances?	No	Yes: Administrative corrections may be “batched” in quarterly reports, when the Customs duty impact is <\$20 per entry (owed or refund)	Yes: you may request further review by someone other than the local port.	No