

DTAG Policy & Regulatory Working Group
(November 15, 2016 Plenary Session)

DTAG Working Group Members:

- Candace Goforth, Goforth Trade Advisors, working group co-chair
- Greg Hill, DRS Technologies, working group co-chair
- Bryce Bittner, Textron
- Nathaniel Bolin, Skadden, Arps, Slate, Meagher & Flom, LLP
- Steve Casazza, General Atomics
- Dava Casoni, University of Southern California
- Sandra Cross, Huntington Ingalls Industries
- Tom Donovan, Northrop Grumman
- Jeremy Huffman, Huffman Riley PLLC
- Rob Lawson, General Electric
- Christine McGinn, InterGlobal Trade Consulting
- Angela Merck, Globaleyes
- Mary Menz, Harris Corporation
- Mike Miller, University of Central Florida
- Ari Novis, Pratt & Whitney
- Dale Rill, Honeywell
- Gretta Rowold, University of Oklahoma
- Brandt Pasco, In-Q-Tel, Inc.
- Bill Schneider, International Planning Services, Inc.

Purpose/Task

The Policy & Regulatory Working Group was tasked to:

1. Review past DTAG reports on issues previously examined and identify those issues/reports that remain relevant, warrant further DTAG review/update, and should be considered by DDTC for implementation.
2. Identify and recommend to DDTC new issues for DTAG to review.
3. Organize all (past and new) issues into a list of priorities for DTAG action and DDTC consideration.

Discussion

The working group started its tasking with a discussion of the prior year issues and the current state of business operations within the ITAR regulatory framework. To address the first tasking the working group reviewed DTAG history from 2003 through 2016. There were a total of 114 issues/action items identified by those prior efforts. Many of them were either repeat issues (ex. brokering and defense services), adopted/resolved issues (ex. PPE exemption), or overcome by events (re. resolved via ECR). There were eight regulatory and nine policy issues that remain unresolved. The working group consensus was that all of them remain very relevant today. They are listed below:

1. Clarification regarding dual-nationals, §126.4 shipments by/for/to USG agencies, signatures on agreements, transshipments, publish redacted AOs, cloud computing/cyber, and using the DTAG in a role more similar to the Commerce Department Technical Advisory Committees (TACs).
2. Regulatory Definition revisions: Dual-Nationals, Brokering, Defense Service, Public Domain, Technical Data, fundamental research, cloud computing/cyber.
3. Regulatory exemption revisions/additions: §126.4 & shipments by/for/to USG agencies, Return for Repair of non-US items, University employee expansion, exemption for FFRDCs and UARCs for work directed by USG, exemption for spare parts/components for previously exported articles.

To address the second task, the group took open inputs on any and all possible new issues. The group then spent time developing a methodology to evaluate those issues for consideration (third task). From this, we identified nine new policy and six new regulatory issues for consideration. These issues are listed below in no specific order.

Proposed Policy Issues:

- Recommend DDTC provide guidance on current licensing policies and procedures not currently included on their website to enhance consistency in communications to industry such as supporting cooperative programs, country policy guidance and XX.
- DDTC would help exporters if they expanded their FAQs. For example, BIS has a very specific and detailed FAQ section that is most helpful to exporters, and it would be helpful if DDTC used a similar tool.
- More transparency and collaboration between USG regulatory agencies and industry during the development of export policies and implementing regulatory language related to new technologies and capabilities. Specifically, capabilities developed by industry that are not part of a US DoD “program of record” which creates a lack of technical ownership within DoD resulting in DTSA being the sole technical decider (i.e. software defined radios).
- Revisit previous DTAG recommendations related to cloud computing and receive clarity from DDTC based on the current technology environment.
- Extra-regulatory conditions imposed by export agencies.
- Establish a process by which the DTAG can provide input, and review and comment on proposed and final rules in a DTAG confidential setting.
- The DTAG could be very useful in helping DDTC get ahead of technology developments that will challenge regulatory assumptions. For example, the rapid introduction of the technologies of autonomy, man-machine integration, machine learning, artificial intelligence, etc. will soon be reflected in interest in allied and friendly governments will be interested in adapting these technologies to defense applications.

Proposed Regulatory Issues:

- a. Definitions
 - Dual-Nationals, Brokering, Defense Service, Public Domain, Technical Data, fundamental research, cloud computing/cyber
- b. The USML
 - DoD funding based controls in the USML. Guidance to contracting officers and appropriate contract clauses need to be put in place to routinize DoD components' ability to decide, for example, that USML Category XI(a)(7) electronic equipment is not subject to the ITAR because it is for both civil and military applications
 - USML Category XI(b). Controlling anything specially designed for an "intelligence purpose" if it does anything useful with the electromagnetic spectrum is terribly overbroad. Currently, XI(b) is open for amendment, and language is needed that more tightly describes what is subject to necessary to control.
- c. Exemptions
 - §123.4(a)(1) – U.S.-Origin Defense Articles – Why is §123.4(a)(1) limited to "U.S.-origin defense articles." Would it be possible to expand it to cover all defense articles regardless of origin? If not, can DDTC clarify the rules of origin that apply to this exemption.
 - §126.6 FMS Exemption – Since industry rarely, if ever, gets a copy of the LOA, how can companies ensure that the defense articles/tech data are "specifically identified in an executed LOA," to satisfy §126.6(b)(2).
 - §126.6 FMS Exemption – Why does §126.6(b)(5)(i) limit delivery to the "the relevant foreign diplomatic mission of the purchasing country or its authorized freight forwarder?" The ITAR allow U.S. exporters to ship under virtually all other license exemptions. Would it be possible to allow us to ship directly under the FMS exemption also? Industry often receives contracts from PMAs in furtherance of FMS cases where we are required to ship. This automatically precludes us from using the FMS exemption.
 - §126.5(b) – *Permanent and temporary export of defense articles to Canada* – expand exemption to include section regarding Foreign Person Employees.
 - By/For USG Exemption - Rewrite & expand §126.4(a) & (c) to allow for all exports at written direction of USG to be exempt from licensing requirements. This will be regardless of permanent, temporary, Title 10 or FAA status. USG published draft language last year that did this; the DTAG would like to see it actually implemented.
 - Add a new exemption permitting governments to retransfer/re-export to parties on contract to that government for repair, maintenance, servicing of US-origin defense articles, the defense retransfer for servicing exemption.

d. Other

- Provide support on transition/re-transition plans for items moving back to the USML.
- UAV Export Policy impacts to US Industry, and industry recommended changes & improvements.
- There will soon be unmanned systems that are electronically tethered to manned aircraft, and some of the UAVs will be operating in autonomous swarms. There is a need for the regulatory apparatus to get ahead of this problem or we will face the problem the DTAG effort identified a couple of years ago; the global UAV market is roaring ahead with US exploitation of the market hobbled by an outdated regulation

The third task was to prioritize the past and present issues into a consolidated list. We developed a methodology for evaluating items that would enable the group to roughly determine their priority. The group developed a two-phased approach for this effort, each phase consisting of a set of questions. The first phase is designed to frame the scope of the issue itself, the second phase is designed to frame the scope of the effort to resolve it.

Phase 1: Framing the Scope of the Issue

What is the scope of the issue to the defense industry? Is it one segment of industry or does it encompass the entire community?

What is the current negative impact? Is it to one part of the international chain or is it broader, capturing both domestic and international? Does it only capture sales or does it capture other activities such as procurement and/or manufacturing?

Is the issue presently being addressed adequately by the USG?

Phase 2: Framing the Scope of Resolving it

Are other agencies involved in the resolution or is it just the DDTC?

Does the resolution require legislative changes?

Does the resolution require Congressional notification?

How does the resolution help both the defense industry and the USG?

In our review of the complete list of issues, we sorted them into three bins, “policy,” “regulatory,” and “other.” This enabled the group to better frame and then assess the validity of the issue. From this we ran issues through the question process to determine their validity and their relative priority in attempting to address them. It was of little surprise that there was an extremely tight grouping of several issues at the top of the list.

Scoring extremely high were the definitions of Defense Service, Fundamental Research, and Public Domain, needed policy interpretations of USML Category XI, and the ability for the DTAG to function more in an advisory role regarding pre-release consultation of regulatory changes. This last point is especially important with regard to the scope of regulatory control as more commercial technologies are adapted for the military to ensure the growth and robustness of the US industrial base is not inadvertently stunted.

Following closely behind these were new exemptions and changes to existing exemptions to keep pace with both industry, U.S. government, and allied government practices, the remaining definitions, and both regulatory changes and policy guidance regarding FMS sales of both ITAR and EAR regulated commodities and better delineation of sales containing encompassing both

FMS and DCS procurement routes. The working group will continue to evaluate the list, both the content and the priority going forward.

The final discussion point for the group was to start work on evaluating a regulatory and two policy areas: better utilizing the DTAG, the definition of a Defense Service, and the interpretation of certain sections of USML Category XI.

As previously presented by DTAG, there is incredible value in utilizing the knowledge base and expertise of the DTAG membership. The working group identified several previous instances – defense services, proposed replacement exemption, brokering, Defense Trade Cooperation Treaties – where the DTAG provided pre-publication input without any conflict of interest or statutory issue. While the working group appreciates the taskings and efforts from DDTC, the working group believes the support provided by the DTAG can be expanded and asks DDTC to explore all available mechanisms to permit DTAG's review and input on draft regulations prior to publication.

Those drafting regulations know the intent of the control language; those reading the regulations do not have that advantage. The DTAG membership consists of professionals that either make or are responsible for thousands of regulation interpretation decisions a day for scenarios not always envisioned by the drafters. A DTAG review of draft regulations can serve as a 'pressure test' of regulation language to ensure that it meets the intent of DDTC across the broad range of industry experience, products, and nomenclature.

The working group discussed that the DTAG is valuable beyond the review of regulatory issues but also as an industrial base advisor. The DTAG membership is on the front-line of technology advances and changes which may not be readily evident to DDTC. For example, as civil technology advances (e.g. AI, autonomous machines) and military adopts more of it, the DTAG could advise on approaches to minimize negative impacts to the broader U.S. industrial base.

The DTAG has also presented the possibility of an Interagency Trade Advisory Group (I-TAG) and this working group found there was a continued interest. With the implementation of Export Control Reform, defense trade activities are now controlled by both the ITAR and the EAR. Therefore, any issue related to the ITAR may have a companion issue within the EAR. The working group discussed the need for a venue to address overlapping issues to ensure consistent and collaborative review by the USG. An example of an overlapping issue would be revisions to the control lists. The TACs have access to proposed EAR rule making prior to publication which directly impacts the companion proposed ITAR rule making. However, the DTAG is not afforded the same opportunity. The working group felt an integrated environment for the USG to hear from all effected parties – at the same time and as a single voice – would be beneficial.

The definition of defense service was the number one issue for the working group. The application and interpretation of this definition impacts virtually all companies and commodities within the working group. The biggest concern expressed by the working group related to the implementation of export control reform and how to apply the definition. Without a formally revised definition, there remains confusion on servicing items subject to the EAR that are part of a larger defense article. This confusion is compounded by AOs issued by DDTC that state servicing items subject to the EAR is not a defense service but public presentations state that it is still a defense service.

The working group believes that the latter interpretation is inconsistent with the intent of export

control reform. The transition of hardware and data to lesser controls is negated by the higher control on the services. The only result being multiple authorizations from DDTC and BIS which minimizes the effectiveness of export control reform. The working group also discussed the complication of managing these authorizations and explaining the need to non-US customers and supply chain.

The last proposed revision to the definition of defense service also sparked discussion on the possible expansion of the definition beyond statutory authority and intent. Specifically, the working group discussed the inclusion of US persons employed abroad. The working group identified numerous scenarios where a US person can and should be excluded from this provision. The working group also discussed the inclusion of foreign person employees of US persons in the definition which many believe is not warranted as these individuals should already be authorized and are not separate from the activities of the US person employer.

Additionally, the proposed “proof of knowledge” requirement enhances US and non-US vulnerability as this is extremely difficult to prove. Most importantly the working group discussed the fact there are other US statutes and laws that should be used to enforce DDTC’s concern instead of the ITAR.

The working group focused on the defense services definition but also noted similar issues arise as we do not yet have other proposed final definitions to review. If, for example, fundamental research is pulled out of the definition of public domain, but defense service is defined to exclude the provision of services via public domain info, arguably conducting fundamental research could be considered performance of a defense service. This goes against the premise that fundamental research is excluded from control under the ITAR. The working group concluded that we could not delve deeply into this review until we see the remaining proposed definitions.

Certain regulatory text and related interpretations related to USML Category XI were discussed by the working group. These issues included USML Category XI(b), XI(c)(1-3), and the concept of system versus software.

The control text of USML Category XI(b) presented several issues for the members of the working group. The first issue discussed was the temporary nature of the current control text. USML Category XI(b) is currently in the middle of the third temporary modification which remains in effect until 8/30/2017. The temporary modifications have added software into the control text without any further guidance. Per the 12/16/15 FRN, DDTC is concerned over the potential exclusion of certain intelligence analytics software and promised a proposed rule to resolve this issue. The working group believes this is an excellent opportunity for DTAG to provide review and input of the proposed rule prior to publication.

The working group believes that software is not the only concern with the current language in USML Category XI(b). Another issue discussed was that unlike the other sections of USML Category XI subparagraph (b) was not revised into a positive control and lacks technical parameters for guidance. As currently written, the control text appears to capture certain items such as two-way communications systems (e.g. wireless networks, software definable radios/phones) or imaging systems (e.g., cameras), which are either enumerated elsewhere on the USML or are subject to the EAR. Additionally, there was significant discussion over the meaning of “intelligence purposes” and whether this was an end-use/end-user control that is inconsistent with

policy for control list revisions.

Another area of USML Category XI discussed by the working group involved the handling of USML Category XI(c)(1-3). There were three specific areas discussed by the working group – what does the language control, how to conduct the Order of Review for a higher-level assembly and licensing policy for items controlled in these entries – which are all inter-related.

What may seem like a simple question – what does the language control – has been complicated by conflicting guidance received by industry including several members of the working group. The language provides for control of a specific item – an ASIC, a PCB, a MCM – as a separate item. The language does not impose a control on the item when incorporated or integrated into a higher-level assembly. This leads to the other areas of discussion – how to conduct an Order of Review for a higher-level assembly and how to license the controlled item when incorporated or integrated.

The current FAQs published by DDTC addresses the Order of Review for classifying the specific item controlled – an ASIC, a PCB, a MCM – but not how to handle the Order of Review for the higher-level assembly or the licensing policy for these items. Industry continues to receive RWAs stating a 600-series item is subject to the ITAR due to the incorporation of a USML Category XI(c)(1-3) item or that the USG believes that the incorporated items are subject to the ITAR due to end-platform despite industry demonstrating the controls of 3A611.f-h or .y.14-16. The working group all agreed that the handling of USML Category XI(c)(1-3) items must be clarified and formalized.

The working group also discussed whether the proposed ITAR §126.19 related to the incorporation of defense articles into items subject to the EAR (76 FR 13928, dated 3/15/11) would assist in resolving the concerns about USML Category XI(c)(1-3).

The last topic discussed by the working group – system versus software – is largely an issue for USML Category XI classifications but can impact other categories. Most systems controlled in USML Category XI are reliant upon software to function or perform the specified control criteria. Often the only differentiation between a commercial or military capability is the software version. But what if the software is not installed yet? What happens to the classification of the hardware? This concern is further complicated when dual-use computers/equipment can become a C4 System with the simple upload of specific software.

This led to several questions for which the working group requests DDTC provide clarification:

1. Do the USML Category XI(a) and (c) entries control both hardware and software as a system?
2. If the hardware does not have any software installed where is the hardware captured?
3. Should the hardware be considered SME even if it cannot perform the stated technical parameters/capabilities since the software is not installed?
4. Does the USG believe there is a difference?

Overall the working group found that industry policy and regulatory priorities have remained consistent – updating of key definitions and clarification of guidance. The new policy and regulatory items focused on amending the new lists, revising/adding exemptions and FAQs to accommodate global changes. To assist in achieving these goals, the working group looked at exercising DTAG's role as both a defense industry and a broader industrial base advisor.