PROPOSED ITAR AMENDMENTS TO CHANGE THE DEFINITION OF DEFENSE SERVICE

The Department of State issued a proposed rule on April 13, 2011 that would substantially amend and narrow the definition of “defense service” in the International Traffic in Arms Regulations (“ITAR”). Under the ITAR, U.S. persons require licensing to furnish assistance to foreign persons in an expansive list of activities relating to defense articles, and this requirement has long posed compliance challenges due to its broad and ambiguous scope. The proposed amendment includes potentially important reductions in the scope of controls on (1) assistance to foreign parties that only involves public domain data, (2) assistance with the operation or use of a defense article, (3) assistance to foreign persons in basic-level maintenance of defense articles, and (4) the employment of U.S. citizens by foreign defense companies.

The State Department’s Directorate of Defense Trade Controls (“DDTC”), which administers the ITAR, is accepting comments on the proposed rule until June 13, 2011. This proposed amendment is part of DDTC’s efforts to implement the Administration’s export control reform initiative, and follows on several other recent proposed amendments that would ease licensing requirements for certain defense-related replacement parts/components and defense articles incorporated into commercial items, as discussed in our E-Alert of April 12, 2011.

In promulgating the proposed rule, the State Department noted that the current definition of “defense service” is “overly broad.” It also observed that the breadth of ITAR controls on assistance that U.S. persons render to non-U.S. persons in the defense trade area has hindered the ability of the United States to support its allies and has resulted in licensing inefficiencies and unintended controls over activities that bear little or no relationship to defense trade control objectives.

ANALYSIS OF SPECIFIC PROPOSED CHANGES TO THE “DEFENSE SERVICE” DEFINITION

Currently, ITAR Section 120.9 defines “defense service” in three parts. The proposed rule, if adopted, would change each of these parts significantly. Further, the amendment would add a fourth component to the definition of defense service, in a new Section 120.9(a)(4).

Furnishing of Assistance to Foreign Persons

ITAR Section 120.9(a)(1) currently defines “defense service” to include “the furnishing of assistance (including training) to foreign persons, whether in the United States or abroad in the design, development, engineering, manufacture, production, assembly, testing, repair, maintenance, modification, operation, demilitarization, destruction, processing or use of defense articles.” Three major changes are proposed to this core part of the definition.

First, the proposed revision would narrow the scope of “furnishing of assistance” to exclude from this particular control the provision of services by a U.S. person to a foreign person that is based solely on the use of public domain data, such as information that is generally accessible to the public.
through published materials (books, newspapers, and the like), libraries, patents, open conferences, and fundamental research at U.S. colleges and universities. Presently, furnishing covered assistance to a foreign person solely using such public domain materials would give rise to ITAR controls that would require a license or licensing agreement approved by DDTC, unless a license exemption applied.

While this change is likely to be welcomed by defense companies, it is more limited than DDTC had originally planned. An earlier DDTC draft of the proposed amendment would have controlled only assistance that involved “technical data.” When the Defense Trade Advisory Group suggested that DDTC should clarify that it was controlling assistance that involved “U.S. origin technical data,” DDTC not only rejected this suggestion, but eliminated the reference to “technical data” entirely. As a result, as DDTC explains, the regulation would continue to apply to assistance that involves any type of proprietary data. Thus, the provision would presumably continue to control U.S. persons providing assistance to foreign persons as specified in the regulation, even if the assistance does not involve export-controlled data or even any U.S.-origin data. For example, if a U.S. person assists a foreign person in manufacturing a foreign defense article more quickly or more cheaply using proprietary manufacturing process techniques (e.g., a “just-in-time” system), this assistance could still potentially qualify as a defense service. Further, “public domain” data has a limited definition under the ITAR; for example, it does not include all information on the Internet, such as technical data posted without U.S. government approval.

The other two changes to this part of the definition seem to afford more relief to exporters. First, the proposal would remove from the litany of activities that could constitute defense services the rendering of assistance to foreign persons in the “operation” or “use” of a defense article. While little discussed in the proposed rule, these changes are underscored in a new ITAR Section 120.9(b), which specifies that “training in the basic operation (functional level) or basic maintenance . . . of a defense article” is not considered to be a defense service. The removal of these controls could constitute a loosening of licensing requirements for companies that are offering services that involve the use or operation of defense articles.

Second, for those that are involved in the maintenance of defense articles, the definition would limit defense services to the rendering of assistance to foreign persons in “intermediate or depot level repair or maintenance,” as opposed to just “repair” or “maintenance.” Intermediate-level maintenance is defined to include work on removed components, parts, or equipment by maintenance shops. Depot-level maintenance is maintenance performed either on- or off-equipment at a major repair facility. By contrast, basic-level maintenance, which would not be included in the defense service definition, is defined to include maintenance performed directly on the defense article or support equipment by the end-user. These definitions are quite broad, however, and may not provide the needed clarity. For example, the definition of organizational-level (or basic) maintenance includes the replacement of minor parts, while intermediate-level maintenance includes replacement of damaged or unserviceable parts, components, or assemblies. Exporters may find it difficult to distinguish between basic and intermediate-level maintenance, for example, where a minor part may be damaged or unserviceable, although the focus in the definitions on what types of entities may provide different types of maintenance appears potentially helpful in this regard.

It is noteworthy also that the proposed rule does not amend the definition of “technical data” in the ITAR. The transfer of technical data, which includes (among other things) information “required” for the “operation” or “maintenance” of defense articles, to a foreign person would continue to be an export requiring authorization under the ITAR. Thus, those who are providing technical data on the operation or maintenance of defense articles to foreign persons still would be engaging in ITAR-
controlled exports, even if they are not otherwise “furnishing . . . assistance” to foreign persons in these activities.

**Integrating Items into Defense Articles**

The proposed rule, if adopted, also would add a new prong to the “defense service” definition related to the integration of military or commercial items into defense articles. The existing second part of the definition (“[t]he furnishing to foreign persons of any technical data controlled under this subchapter . . ., whether in the United States or abroad”) would be eliminated. (However, as discussed above, the transfer of technical data to foreign persons remains an export of a defense article that is subject to the controls of the ITAR.) Replacing the second part of the defense service definition would be an entirely new provision that includes among defense services: “The furnishing of assistance to foreign persons, whether in the United States or abroad, for the integration of any item controlled on the U.S. Munitions List (USML) . . . or the Commerce Control List . . . into an end item . . . or component . . . that is controlled as a defense article on the USML, regardless of origin.” Such integration activities could be controlled as a defense service even if no technical data are provided and even if any data provided are publicly available.

While “integration” is not defined, DDTC explained in the preamble to the notice of proposed rulemaking that “integration” involves “the systems engineering design process of uniting two or more things in order to form, coordinate, or blend into a functioning or unified whole, including introduction of software to enable proper operation of the device,” and could include determining where or how to install something that is not simply “plug and play.” DDTC distinguished “integration” from the less-extensive “installation,” which it considers to involve putting a component into a pre-determined place that does not require changes or modifications to the item into which the component is being installed. Despite DDTC’s statement that the difference should be clear, the distinction will be highly fact-specific and may not always be easily drawn.

Moreover, it is unclear whether the second prong of the proposed defense service definition is intended to exclude the furnishing of assistance to foreign persons in the integration into defense articles of non-sensitive EAR99 items, while controlling as a defense service the integration into defense articles of more sensitive commercial items controlled on the EAR’s Commerce Control List (“CCL”). Such a distinction would be especially puzzling in light of the fact that the proposed rule provides that it is not a defense service for a U.S. person to assist a foreign person in the testing, repair or maintenance of an item subject to the EAR that has been incorporated or installed into a defense article. (Items subject to the EAR include both items on the CCL and EAR99 items.) This point hopefully will be addressed and clarified or confirmed in the final version of the regulatory amendments.

**Training Foreign Units and Conducting Combat Operations/Intelligence Services**

The State Department also proposed significant revisions to the third component of the definition of “defense service,” and added a new fourth part to the definition. Under the proposal, training foreign units or forces, as well as “providing advice to” them, would be considered a defense service if the training/advice related to the employment of a defense article. Such activities would result in a defense service even if no technical data are transferred and even if any data transferred are publicly available.

In addition, the proposed rule would add a fourth component to the definition of defense service that would control “[c]onducting direct combat operations for or providing intelligence services to a foreign person directly related to a defense article.”
DEFENSE SERVICES EXCLUSIONS

The revised Section 120.9 also would include specific examples of activities that are not considered to be defense services, several of which were discussed above. These include mere employment of a U.S. citizen by a foreign person. DDTC noted that some companies abroad had been reluctant to hire U.S. persons because they feared that by doing so, the U.S. person might be found to be rendering a defense service, even if the U.S. person was not transferring any technical data to the foreign employer. The proposed revisions make clear that such an employment arrangement of an individual U.S. citizen by a foreign company would not raise ITAR issues on its own. Interestingly, however, DDTC omitted from this defense services exclusion U.S. lawful permanent residents employed by foreign companies, apparently because it was trying to focus on natural persons and sought to avoid the defined ITAR term “U.S. persons,” which includes both natural persons (U.S. citizens and lawful permanent residents) and U.S. companies. The anomalous result seems to be that mere employment of a U.S. permanent resident by a foreign company could still be a defense service, even though employment of a U.S. citizen would not. One would expect this anomaly to be called to DDTC’s attention in comments and potentially addressed when the final amendment to the definition is issued.

Also excluded from the scope of defense services are:

- Training in the basic operation or basic maintenance of a defense article;
- Testing, repair, or maintenance of an EAR item that has been incorporated or installed into a defense article;
- Providing training, advice, or services to or for a foreign person using only public domain data in law enforcement, physical security or personal protective training; and
- Providing assistance or training in medical, logistical (other than maintenance), or other administrative support services to a foreign person.

SUMMARY

It appears that many of these changes will be welcomed by exporters seeking greater clarity in what had previously been a broad area of control under the ITAR. Moreover, the revisions, if adopted, may result in a reduction in the licensing burden for certain activities, such as assisting foreign persons in the use, operation, and basic maintenance of defense articles. However, by continuing to apply the defense services regulation to a broad range of activities relying on proprietary information, DDTC has proposed an approach that is significantly more restrictive than originally briefed in 2010 to the exporting community, and exporters likely will continue to face challenges arising from this broad and ambiguous rule.

We are well-positioned to assist clients in understanding the impact that the proposed rule would have, if adopted, on their operations, or in assisting clients or groups of clients in preparing comments in response to the proposed rule.
If you have any questions concerning the material discussed in this client alert, please contact the following members of our international trade controls group:

Peter Flanagan 202.662.5163 pflanagan@cov.com
Corinne Goldstein 202.662.5534 cgoldstein@cov.com
Peter Lichtenbaum 202.662.5557 plichtenbaum@cov.com
Kimberly Strosnider 202.662.5816 kstrosnider@cov.com
David Addis 202.662.5182 daddis@cov.com
Peter Trooboff 202.662.5512 ptrooboff@cov.com
Caroline Walsh 202.662.5008 cwalsh@cov.com

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