I. **INTRODUCTION**

2008 has been an active year in the export controls and sanctions field. The President issued a directive on the reform of export controls, spawning regulatory proposals and revisions. Sanctions programs have been modified and, in the case of North Korea, eliminated. There has been an increasing trend both in the export controls and sanctions area toward more targeted restrictions focused on named individuals and entities. Enforcement of export controls and sanctions regulations remained active in 2008. This article summarizes the most significant changes to dual-use export controls, arms export controls, and economic sanctions.

II. **DUAL-USE EXPORT CONTROLS**

A. **Presidential Directive On Dual-Use Export Control Reform**

On January 22, 2008, the President announced directives\(^1\) to reform dual-use export control policies for protecting the national security of the United States, while also facilitating U.S. economic and technological leadership.

The directives stated that the dual-use export control system should increasingly focus on foreign end-users of U.S. high technology products, so as to facilitate trade with trustworthy foreign customers while denying sensitive technologies to weapons proliferators, terrorists, and

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others acting contrary to U.S. national security and foreign policy interests. The Directive sought to advance these policies by implementing a Validated End User (“VEU”) program for reliable foreign companies and expanding the U.S. Department of Commerce Bureau of Industry and Security’s (“BIS”) Entity List.

The Directive also required a regular process for systematic review of the Commerce Control List (“CCL”), reducing controls on intra-company transfers, revising controls on encryption products, and reviewing reexport controls. The Directive also requires BIS to publish advisory opinions on BIS’ website, as well as lists of foreign parties warranting higher scrutiny.

Many of these initiatives have been implemented this year through amendments to the Export Administration Regulations (“EAR”), 15 C.F.R. parts 730-774, and are discussed below.

B. Deemed Export Advisory Committee Recommendations

1. Deemed Export Advisory Committee Report

On December 20, 2007, a federal advisory committee, the Deemed Export Advisory Committee (“DEAC”), submitted a report to the Secretary of Commerce providing recommendations to modernize and reform dual-use deemed export and reexport controls, such as to make the CCL less encompassing, streamline deemed export rules, promote awareness of deemed export controls to academic institutions and relevant industries, and reconsider the criteria utilized for assessing threats posed by foreign nationals. Of significance, the DEAC recommended that the existing rule for determining the nationality of a non-U.S. person for “Deemed Export purposes,” based on the person’s most recent or current citizenship or

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permanent residency, should be reconsidered as “superficial.” Instead, the DEAC proffered a more holistic approach to the deemed export analysis, whereby an overall assessment of the probable loyalty of a foreign individual of interest should be conducted, including consideration of the length of time, character, and nature of past and present foreign ties. As part of its “implementing construct,” the DEAC recommended that such information should be submitted to the U.S. Government for review and approval or disapproval, implying that U.S. exporters should not make these “loyalty” determinations on their own. If such a review indicates a “tie” to a sanctioned or terrorist supporting country, or if any other “significant” loyalty concerns exist, a deemed export or reexport license application could be denied. The DEAC also recommended that this consideration should include other factors, such as the nature of the items, software, or information proposed for transfer.

2. Public Comments Regarding BIS’ Deemed Export Policy

On May 19, 2008, BIS published a notice of inquiry to elicit public comments regarding two specific recommendations made by the DEAC with respect to BIS’ deemed export licensing policy. First, BIS asked whether the scope of technologies on the CCL subject to deemed export requirements should be narrowed, and if so, which technologies should remain subject to deemed export licensing requirements. The DEAC recommended that BIS narrow the CCL to focus on technologies having the greatest national security implications, and to eliminate those having

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3 See id. at 19.

4 Id. at 21.

5 See id. at 24-30.

little concern. This recommendation contributed to the creation of the Emerging Technology and Research Advisory Committee (ETRAC), discussed below in section II.I.

Second, BIS sought comments on whether more comprehensive criteria should be used to analyze country affiliation for foreign nationals regarding deemed exports, as proposed by the DEAC. BIS posted comments received by the public on its website. As of November 30, 2008, BIS has not published a preliminary or final rule making any revisions to existing deemed export licensing policy.

C. Mandatory Use of Electronic Filing via SNAP-R

On August 21, 2008, BIS amended the EAR to require that, effective October 20, 2008, export and reexport license applications, classification requests, encryption review requests, License Exception AGR notifications, and related documents be submitted via the Simplified Network Application Process (SNAP-R) system. This requirement does not apply to applications for Special Comprehensive Licenses, advisory opinion requests, or in certain other situations where BIS authorizes paper submissions. As implemented, the rule amended Parts 748.1, 748.3, and 748.6 of the EAR – as well as other provisions related to the paper forms.

D. Revisions to the Encryption Rules

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8 See Mandatory Electronic Filing of Export and Reexport License Applications, Classification Requests, Encryption Review Requests, and License Exception AGR Notifications, 73 Fed. Reg. 49,323 (Aug. 21, 2008) (to be codified at 15 C.F.R. pts. 740, et al.) (Previously, Part 748 of the EAR set forth procedures for submitting to BIS the various documents required from parties wishing to engage in certain transactions or seeking advice on the proper classification of items subject to the EAR. Parties could submit license applications, encryption review requests, and any required notifications to BIS either via the SNAP–R system, the Electronic License Application Information Network (ELAIN), or the paper BIS Multipurpose Application Form BIS 748-P.).
In an interim final rule published on October 3, 2008, BIS revised the encryption-specific rules in the EAR to provide a modest liberalization of the restrictions that apply to encryption hardware, software, and technology. The amendment removes the need to notify BIS of hardware, software, and technology classified under Export Control Classification Numbers (“ECCNs”) 5A992, 5D992, and 5E992 before such items could be exported or reexported “no license required” or “NLR”. The following are some of the noteworthy changes.

**Exclusions:** BIS has adopted two additional “exclusions” from the review and reporting requirements for certain “ancillary cryptography” commodities and software and certain “personal area network” items, which are defined in part 772. Additionally, license exception Encryption Commodities and Software (“ENC”) now excludes wireless personal area network items with certain specifications from the review and reporting requirement.

**Strong Encryption Items:** Section 740.17(b) of the EAR defines strong encryption items that require prior review by BIS. The provision explains when a 30-day waiting period is required prior to exports and reexports; adds favored countries for export purposes; and retains distinctions for non-favored countries, government end-users, and non-government end-users. BIS also has raised the threshold of items exempt from the 30-day waiting period to include encryption items with symmetric algorithms having key lengths up to 80 bits. Finally, the provision expressly authorizes temporary ENC treatment for items pending mass market review.

**Restrictions:** The rule expands the list of ENC Restricted (government end-users in non-favored countries) network infrastructure software and commodities to include “digital packet telephony/media (voice/video/data) over internet protocol.”

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Foreign Produced Products: BIS revised license exception ENC to establish more clearly that foreign products developed with or incorporating U.S.-origin encryption source code, components, or toolkits are eligible for the review and reporting exclusion only if the U.S.-origin encryption items they contain have previously been reviewed and authorized by BIS and the cryptographic functionality of those components has not been changed.

Reporting: The reporting requirements for license exception ENC are now split into two sections – one dealing with the semiannual reporting requirement of exports made under ENC and another for reporting key length increases. The rule also lays out what information shall be included in the reports for exports to distributors, individual consumers, and foreign manufacturers.

E. COUNTRY-RELATED ISSUES AND THE EAR

1. Preventing Diversion to Iran

On September 24, 2008, BIS issued guidance concerning actions that exporters can take to prevent the illicit diversion of items to Iran’s nuclear weapons or ballistic missile programs.\(^{10}\) The guidance is part of an effort to counter Iran’s pursuit of technology that could enable it to develop weapons of mass destruction ("WMD") and the means to deliver them. It followed enforcement and administrative actions already taken by BIS and other agencies against 75 entities involved in a global procurement network which sought to illegally acquire U.S.-origin dual-use and military components for the Iranian Government.\(^{11}\)

2. Expansion of Authorization for Temporary Exports/Reexports to Sudan

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BIS issued a final rule\textsuperscript{12} on February 28, 2008, amending the EAR to expand authorization for temporary exports and reexports to Sudan under EAR License Exception TMP ("Temporary Imports, Exports, and Reexports"), 15 C.F.R. part 740.9. Under the new regulation for TMP, reexports are now authorized. Additionally, exports and reexports of exempted items can continue to accompany persons on travel (either hand carried or as checked baggage) or they can be sent to Sudan by an "eligible user" and via a method reasonably calculated to assure delivery to a permissible end-user. TMP also now authorizes export or reexport of software to be used solely for servicing or in-kind replacement of software legally exported or reexported. The software must remain loaded on exempted equipment while in Sudan. The list of items authorized to be exported to Sudan pursuant to TMP has now been expanded to include items controlled under certain ECCNs.

The revised exception retains the restrictions previously applied to the type of permissible end-users, the permissible end uses, and the requirement to return the temporary items to the United States within one (1) year or obtain permanent re-transfer, re-export, or disposal authorizations for the items in Sudan.

\textbf{F. Amendments to the De Minimis Regulations}

BIS published an interim final rule\textsuperscript{13} revising the EAR with regard to the application of the \textit{de minimis} rule to foreign-produced products containing U.S.-origin software and technology. This amendment reflects a significant change from the prior rules used to determine

\textsuperscript{12}See Expanded Authorization for Temporary Exports and Reexports of Tools of Trade to Sudan, 73 Fed. Reg. 10,668-70 (Feb. 28, 2008) (to be codified at 15 C.F.R. pt. 740). Previously, TMP only allowed for the personally accompanied temporary export (and not the reexport) of a limited scope of commodities used only for humanitarian assistance (and not specific related support activities) in Sudan.

when U.S. re-export jurisdiction applies to items made abroad containing U.S.-controlled content.

Most notably, the regulation makes changes to the following areas:

**Bundling**: Section 734.4 is amended to exclude, in certain cases, foreign-made commodities “bundled” with *de minimis* amounts of U.S.-origin software from the jurisdiction of the EAR. U.S.-origin software will remain subject to the EAR when exported or re-exported separately from (i.e., not incorporated or bundled with) a foreign made commodity, and exports or re-exports of software for additional users and upgrades are considered separate transactions for export control purposes. The “bundling” concept applies to “software that is configured for a specific commodity, but is not necessarily physically integrated into the commodity.” Only certain U.S.-origin software falls within the scope of bundling for foreign made commodities; the rule applies exclusively to software controlled for Anti Terrorism (“AT”) reasons or which is classified as “EAR99.” Therefore, software that is controlled for other reasons, such as ECCN 5D002 encryption software, or software that might be associated with specific products and controlled for reasons other than anti-terrorism controls, will not be considered bundled with foreign-produced items and shall remain subject to the EAR.

**Revised De Minimis Calculations**: Supplement No. 2 to part 734 of the EAR, which includes guidelines for calculating *de minimis* values as defined by § 734.4, has been amended in various respects. The amendment clarifies the previous rule on “controlled” content, noting that U.S.-origin content need only be included in the *de minimis* calculation if it is controlled for re-export to the end destination, and stipulating that part 744 controls should *not* be considered in making this assessment. Special rules on encryption in § 734.4(b) are retained. The guidance
also now clarifies that costs should be determined by the local market costs in the country of export, and that cost depreciation for components is not permitted.

**Definition of “Incorporated”:** Supplement No. 2 to part 734 is amended to make clear that U.S.-origin controlled content is considered “incorporated” for *de minimis* purposes if the item is: (1) “essential to the functioning of the foreign equipment”; (2) “customarily included in sales of the foreign equipment”; and (3) “reexported with the foreign produced item.” BIS has removed the “rack mounted” and “cable connected” concepts previously utilized to determine the extent to which U.S.-origin content is incorporated into foreign produced items.

**One Time Report:** Based on prior reporting history, BIS has removed the requirement for a one-time reporting requirement for foreign-made software that incorporated controlled U.S.-origin software. However, BIS is maintaining the one-time report requirement for foreign-made technology that incorporates controlled U.S.-origin technology.

**G. Rule for Amendments to Entity List**

On August 21, 2008, BIS published a final rule\(^{14}\) amending the EAR, 15 C.F.R. parts 730, 744, and 756, concerning export and reexport requirements for persons and entities designated on the Entity List (Supplement No. 4 to part 744). A newly-established, inter-agency End-User Review Committee (“Committee”) will have the discretion to add a party to, remove a party from, or modify a party’s designation on the Entity List.

Under the new rule, an entity may be added to the Entity List where there is reasonable cause to believe that a foreign entity has been involved in, or poses a risk of being involved in,

\(^{14}\) See Authorization To Impose License Requirements for Exports or Reexports to Entities Acting Contrary to the National Security or Foreign Policy Interests of the United States, 73 Fed. Reg. 49,311 (Aug. 21, 2008) (to be codified at 15 C.F.R. pts. 730, et al.).
activities that are contrary to the national security or foreign policy interests of the United States, or is acting on behalf of such an entity.

Section 744.11(b) provides “illustrative” examples of the type of conduct the Committee may view as grounds for designating parties on the Entity List, including: (1) supporting persons engaged in acts of terror; (2) enhancing the military capability of, or supporting terrorism sponsored by, foreign governments designated by the State Department as providing support for acts of terror; (3) transferring, developing, servicing, repairing, or producing conventional weapons, or enabling such action by supplying parts, components, technology, or financing for weapons, contrary to U.S. national security and foreign policy interests; (4) preventing the accomplishment of an end use check conducted by or on behalf of BIS or the Directorate of Defense Trade Controls; or (5) engaging in conduct that poses a risk of violating the EAR when such conduct raises sufficient concern that prior review of exports or reexports involving the party, and the possible imposition of license conditions or license denial, enhances BIS ability to prevent violations of the EAR.

Finally, the rule amended § 744.16 and adds new Supplement No. 5 to part 744, allowing a party listed on the Entity List to request that its designation be removed or modified, and providing procedures for making such requests, which will be considered by the newly-established Committee.

On September 22, 2008, BIS amended the EAR by adding 108 additional persons to the Entity List who were determined by the U.S. Government to be acting contrary to the national security or foreign policy interests of the United States.\(^{15}\)

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H. Proposed Rule on License Exception for Intra-Company Transfers

On October 3, 2008, BIS published a proposed rule\(^{16}\) amending the EAR to add a new license exception entitled Intra-Company Transfer (“ICT”). ICT would allow for license-free exports and reexports to and among affiliated entities, as long as certain requirements are met. The exception would not be available automatically. Instead, a parent company must first submit an internal control plan, among other information, which BIS would review to determine whether the company merits use of the exception. Even then, ICT would be restricted to pre-approved subsidiaries and ECCNs. There would also be reporting, audit, and recordkeeping requirements for companies that make use of this license exception. Further details on the proposed rule for ICT are provided below:

**Eligible Entities:** Only a parent company would be authorized to apply for use of ICT, although it does not have to be an ultimate parent company. The parent company must be incorporated in or have its principal place of business in the United States or one of 37 other countries listed in Supplement 4 to Part 740 of the EAR. Eligible users and recipients under this license exception include wholly-owned or controlled in fact subsidiaries or branches of the parent company.

**Restrictions:** ICT may not be used to export, reexport, or transfer items to any countries (or nationals thereof) in Country Group E or North Korea. Items exported, reexported, or transferred under ICT may be subsequently exported, reexported, or transferred in accordance with the EAR, but not under license exception APR (Additional Permissive Reexports). The license exception also does not apply to items controlled for Encryption Items (EI) or Significant

Items (SI) reasons, nor can it be used to transfer technology to foreign national employees without valid work authorization or those on any U.S. Government end-user list of concern.

**Reporting Requirements:** Approved companies must submit an annual report to BIS, including the following information: (1) data on foreign national employees that received technology or source code under license exception ICT during that year; (2) data on foreign national employees that terminated their employment during that year; and (3) a certification that all approved eligible users and recipients are in compliance with the applicable terms and conditions, including the results of the self-evaluations.

**Audits:** BIS will conduct biennial audits of approved companies, eligible users, and eligible recipients.

### I. Establishment of Emerging Technology & Research Committee

On May 23, 2008, BIS announced the creation of a new Emerging Technology and Research (“ETRAC”) Advisory Committee and invited public and private sector experts to apply for membership.\(^{17}\) The ETRAC has a mandate to identify emerging technologies and research and development activities that may be of interest from a dual-use perspective, prioritize new and existing controls related to deemed exports to determine which are of greatest consequence to national security, and examine how research is performed to understand the impact that the EAR have on academia, federal laboratories, and industry.

### J. Expansion of Eligible Items under License Exceptions TMP and BAG

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On December 12, 2007, BIS issued a final rule amending the EAR to expand and clarify eligibility under two widely-used EAR license exceptions, License Exception TMP (“Temporary Imports, Exports, and Reexports”) (§ 740.9) and License Exception BAG (“Baggage”) (§ 740.14). The revisions allow for the export or reexport of technology and technical information subject to the EAR by U.S. persons to U.S. persons or their employees traveling or temporarily assigned abroad, subject to certain important limitations. Previously, TMP and BAG were focused only on hardware and software and did not authorize technology exports and reexports.

The eligible items now are expanded to include technology, either in the form of actual shipments, transmissions, or other “releases.” The other categories of exports/reexports authorized under TMP and BAG apart from “tools of trade” continue to be limited to hardware and software. The “tools of trade” provisions in TMP and BAG are subject to a number of limitations as described in further detail by the rule.

K. FOREIGN AVAILABILITY ASSESSMENT PROCESS

On September 2, 2008, BIS announced a 90-day study to assess the foreign availability of uncooled thermal imaging cameras in the People’s Republic of China (“PRC”). The study was initiated in response to a petition filed by the Sensors and Instrumentation Technical Advisory Committee (“SITAC”) asserting that uncooled thermal imaging cameras are widely available in China and render U.S. export controls ineffective in achieving their purpose. If foreign

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18 See Revisions to License Exceptions TMP and BAG: Expansion of Eligible Items, 72 Fed. Reg. 70,509 (Dec. 12, 2007) (to be codified at 15 C.F.R. pts. 740 and 772). These revisions to the EAR are effective immediately. There is no formal comment period for the regulation, but BIS has invited public comments on a continuing basis.

availability exists, the Department may remove the license requirement, unless the President determines that this would be detrimental to national security.

L. **BIS Study on High Precision Machine Tools**

On May 19, 2008, BIS initiated a systematic study of the U.S. 5-axis simultaneous control machine industry. BIS intends to assess the health and competitiveness in the industry, and the impact of export control practices and foreign availability on the industry. Further, BIS will examine the capability of U.S. and foreign members of this industry to meet U.S. national security needs. A report is expected in late 2008.

M. **Enforcement Actions / Penalty Enhancements for 2008**

In Fiscal Year 2008, BIS’s Office of Export Enforcement ("OEE") continued to focus on violations relating to proliferation of weapons of mass destruction and missile delivery systems, terrorism, and diversions of dual-use goods to military end uses. BIS reports that during Fiscal Year 2008 (October 1, 2007 through September 30, 2008) it closed [] administrative enforcement cases resulting in the imposition of $[(blank)] million in administrative penalties.[] [Note trends] from FY 2007 when 75 cases resulted in fines of over $6 million. In FY 2008, BIS reports that OEE investigations resulted in [] convictions and $[(blank)] in criminal fines,[citation] compared with 16 convictions and $25.3 million in fines in 2007. [Note – Awaiting updated FY 2008 figures from BIS.]

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22 Id.
In Fiscal Year 2008, nine (9) enforcement cases were closed where the recently-increased maximum civil penalty amount, $250,000, was available pursuant to enhancements under IEEPA. Of those cases, two involved criminal charges, and none of the parties involved voluntarily disclosed the violations. Each case resulted in a settlement. The average penalty paid per case was $95,982 in non-criminal cases and $266,595 in criminal cases.

In addition to penalizing U.S. persons and entities, BIS also focused its enforcement efforts on foreign entities. For example, on July 17, 2008, a French company, Cryostar SAS, was sentenced to a criminal fine of $500,000 and two years probation for its role in a conspiracy to sell cryogenic pumps to Iran. Cryostar, together with two other French companies, had developed a plan to conceal the sale of the pumps to an Iranian customer.

III. Arms Export Controls

A. Treaties With UK and Australia

The United States moved toward implementation of two defense trade cooperation treaties signed in 2007, one with the United Kingdom and the other with Australia. If ratified, the treaties will permit license-free exporting of certain ITAR-controlled items and services in specified programs to members of an "Approved Community" of governments and companies in each country. Transfers outside the Approved Community would remain subject to State Department licensing. UK Government employees and employees of eligible UK entities may have access to these defense articles (which would include, for example, exports or deemed

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exports of controlled technical data) if they meet certain criteria including UK security accreditation and need-to-know. The U.S. Approved Community would include companies registered with the U.S. Department of State’s Directorate of Defense Trade Controls (“DDTC”) under ITAR Part 122, unless debarred. The UK Government will not require licenses to export these defense articles to members of the U.S. Community, and may permit such exports under blanket or open authorizations. The Australia treaty text is generally similar to the UK treaty.

For both treaties, specific procedures and parameters are described in bilateral implementing arrangements finalized in 2008. The State Department developed draft regulations for the UK Treaty and posted these on the DDTC website for comment in 2008. In September 2008, the Chairman and Ranking Member of the Senate Foreign Relations Committee, the Committee of jurisdiction, wrote to Secretary of State Rice stating that the Committee continues to support the objectives of the two treaties but would not be able to approve the two treaties during the current Congressional session. The UK Government has ratified the UK treaty. In Australia, the Parliamentary Joint Standing Committee on Treaties has made its recommendations and legislation necessary to give effect to the Treaty is expected to be submitted to the Federal Parliament early in 2009 for passage.

B. U.S. Munitions List and International Traffic in Arms Regulations

The ITAR was amended once in late December 2007 and eight times in 2008.

1. Dual and Third Country Nationals

On December 19, 2007, 22 C.F.R. §§ 124.12 (a) (1) and 124.16 were amended²⁵ to allow access to defense articles and services for dual and third country nationals of certain countries through revisions in procedures for technical assistance agreements and manufacturing licensing.

agreements. This regulatory change was intended to reduce the burden on exporters of defense articles and on foreign parties to the agreements by reducing the number of individual Non Disclosure Agreements (NDA's) which must be executed and maintained on file.

2. Sri Lanka

On March 24, 2008, 22 C.F.R. part 126 was amended\(^\text{26}\) to make it policy to deny licenses and other approvals to export or otherwise transfer defense articles and defense services to Sri Lanka except, on a case-by-case basis, for technical data or equipment made available for the limited purposes of maritime and air surveillance and communications.

3. NATO Organizations

On March 26, 2008, 22 C.F.R. § 123.9(e) was amended\(^\text{27}\) to clarify U. S. policy to allow for reexports or retransfers of U.S.-origin components incorporated into a foreign defense article to the North Atlantic Treaty Organization (“NATO”), and its agencies, as well as to NATO member governments.

4. U.S. Munitions List Correction

On May 19, 2008, 22 C.F.R. part 121.1(b) was corrected\(^\text{28}\) by adding an asterisk to indicate that the paragraph refers to Significant Military Equipment.\(^\text{29}\)

5. Registration Renewals


\(^{29}\)“Significant military equipment means articles for which special export controls are warranted because of their capacity for substantial military utility or capability.” 22 C.F.R. § 120.7(a) (2008).
On July 8, 2008, 22 C.F.R. § 122.3 was amended\textsuperscript{30} to limit the registration period to one year, and requiring registrants to submit renewal packages within 60 days before their current expiration date.

6. U.S. Munitions List Civil Aircraft Components

On August 14, 2008, 22 C.F.R. § 121.1, Category VIII (b), (h), and the Note, were amended\textsuperscript{31} to clarify how the criteria of Section 17(c) of the Export Administration Act of 1979 are implemented in accordance with the Arms Export Control Act. This rule reinstated the Section 17(c) reference in the ITAR to assist exporters in understanding the scope and application of the Section 17(c) criteria to parts and components for civil aircraft. It also clarified that any part or component that (a) is standard equipment; (b) is covered by a civil aircraft type certificate (including amended type certificates and supplemental type certificates) issued by the Federal Aviation Administration for civil, non-military aircraft (this expressly excludes military aircraft certified as restricted and any type certification of Military Commercial Derivative Aircraft, defined by FAA Order 8110.101 effective date September 7, 2007 as “civil aircraft procured or acquired by the military”); and (c) is an integral part of such civil aircraft, is subject to the jurisdiction of the Export Administrative Regulations (“EAR”). Where such part or component is not Significant Military Equipment (“SME”), no Commodity Jurisdiction (CJ) determination is required to determine whether the item meets these criteria for exclusion under the United States Munitions List (“USML”), unless doubt exists as to whether these criteria have been met. However, where the part or component is SME, a CJ determination is always required.


except where a SME part or component was integral to civil aircraft prior to the effective date of
this rule.

Additionally, this proposed rule added language in a new Note after Category VIII(h) to
provide guidelines concerning the parts or components meeting these criteria. The change to
Category VIII*(b) also identifies and designates certain sensitive military items, heretofore
controlled under Category VIII(h), as SME.

7. U.S. Munitions List Toxicological Agents

On September 9, 2008, 22 C.F.R. § 121.1(c), was amended to add Note 5 to Category
XIV--Toxicological Agents, to clarify that certain anti-tumor drugs are not within the definition
of "chemical agents," but the definition retained the know-how for production of nitrogen
mustards or their salts on the U.S. Munitions List.

8. Rwanda

On September 25, 2008, 22 C.F.R. § 126.1(c) was amended to remove Rwanda from
the list of prohibited countries as a result of United Nations Security Council Resolution 1823,
which terminated remaining arms sanctions against Rwanda.

9. Increased Registration Fees

On September 25, 2008, 22 C.F.R. parts 122 and 129 were amended to increase
registration fees charged to persons required to register with the Directorate of Defense Trade

\[\text{Amendment to the International Traffic in Arms Regulations: U.S. Munitions List Interpretation,}

\[\text{Amendment to the International Traffic in Arms Regulations: Rwanda, 73 \text{ Fed. Reg. 55,441 (Sept. 25,}
2008) (to be codified at 22 C.F.R. pt. 126).}\]

\[\text{Amendment to the International Traffic in Arms Regulations: Registration Fee Change, 73 \text{ Fed. Reg.}
55,439 (Sept. 25, 2008) (to be codified at 22 C.F.R. pts. 122 and 129).}\]
Controls under Section 38 of the Arms Export Control Act (22 U.S.C. § 2778), change the registration renewal period, and make other minor administrative changes.

C. MAJOR ENFORCEMENT ACTIONS

1. Major Civil Settlements

a. Northrop Grumman

On March 14, 2008, Northrop Grumman Corporation of Los Angeles, California, agreed\(^\text{35}\) to pay civil penalties of $15 million and take additional corrective actions to settle 110 ITAR violations that it and its predecessor in interest, Litton Industries, Inc. (which Northrop acquired in April 2001), were alleged to have committed between 1994 and 2003 in connection with unauthorized exports of modified versions of its commercial LTN-72 and LTN-92 Inertial Navigation Systems (INS), related software source code, and related defense services.

b. Boeing

On June 9, 2008, the Boeing Company of Chicago, Illinois, agreed\(^\text{36}\) to pay civil penalties of $3 million and take additional corrective actions to settle 40 alleged ITAR violations in connection with the administration of Manufacturing License Agreements (“MLA”s) and Technical Assistance Agreements (“TAA”s).

c. Lockheed Martin

On July 24, 2008, Lockheed Martin Corporation of Arlington, Virginia, agreed\(^\text{37}\) to pay civil penalties of $4 million and take additional corrective actions to settle eight alleged ITAR


violations in connection with unauthorized export of classified and unclassified technical data to United Arab Emirates; export of classified technical data related to Hellfire missiles to foreign persons; export of classified technical data relating to the Joint Air-To-Surface Standoff Missile to a major non-NATO ally; failure to notify DDTC of proposals for the sale of significant military equipment; and failure to obtain a Non-transfer & Use Certificate for export of classified technical data.

2. Major Criminal Convictions

a. Roth

On September 3, 2008, a jury in the Eastern District of Tennessee convicted former University of Tennessee Professor J. Reece Roth of 15 counts of violating the AECA by exporting controlled technical data, and one count of conspiring with Atmospheric Glow Technologies, Inc. (“AGT”) to unlawfully export controlled technical data. The controlled technical data in this case related to plasma actuators for unmanned aerial vehicles or drones that was were developed under a U.S. Air Force research and development contract. Roth provided this technical data to Chinese and Iranian foreign nationals who were students at the University of Tennessee. Roth also carried documents containing controlled military data with him on a trip to China and he caused other controlled military data to be emailed to an individual in China. Sentencing in this case is scheduled for January 7, 2009. AGT pleaded guilty on August 20, 2008 to charges of illegally exporting U.S. military data about drones to a Chinese citizen in violation of the Arms Export Control ActAECA.38

b. Meng

On June 18, 2008, a judge in the Northern District of California sentenced a Canadian citizen, Xiaodong Sheldon Meng, to two years in prison, 3 years of supervised released, and a $10,000 fine. On August 1, 2007 Meng had pleaded guilty to committing economic espionage and to violating the AECA. Meng had misappropriated a trade secret involving night vision software for pilots from his former employer, Quantum 3D, Inc., and he had done so with the intent to benefit China’s Navy Research Center in Beijing. He had also illegally exported military source code pertaining to a program for training military fighter pilots. This case is the first to result in a conviction for exporting military source code under the AECA. In addition, Meng is the first defendant to be sentenced under the Economic Espionage Act.39


c. Mak

On March 24, 2008, a judge in the Central District of California sentenced Chi Mak, a U.S. citizen, to 24 years and five months in prison, and a $50,000 fine for conspiracy to obtain and send ITAR-controlled technical data relating to U.S. naval warship technology to China. Mak, who was formerly an engineer with a U.S. navy contractor, was convicted of conspiracy to violate the AECA, attempting to violate the AECA, acting as an unregistered agent for a foreign government, and making false statements to federal investigators. Mak’s co-conspirators in China had requested U.S. naval research on nuclear submarines, among other information. The four co-defendants in this case, who included his brother and wife, also pleaded guilty and have been sentenced to terms of imprisonment.40

d. Euro Optics, Ltd.

On March 17, 2008, Euro Optics, Ltd. pleaded guilty to illegally exporting advanced combat gun sights to Sweden and Canada. On July 24, the judge in the Middle District of Pennsylvania sentenced Euro Optics to a $10,000 corporate fine, a $800 special assessment, and five years of corporate probation.41

IV. Economic Sanctions

During 2008, the Office of Foreign Assets Control of the United States Department of the Treasury (“OFAC”) continued its trend of recent years by continuing to emphasize targeted programs against specific individuals, activities and companies in lieu of adopting new, broad-based economic sanctions programs.42

A. BELARUS

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42 Of the first 78 public releases published on the OFAC website in 2008, 44 related primarily to OFAC’s list of Specially Designated Nationals. See http://www.treas.gov/offices/enforcement/ofac/actions/index.shtml.
On September 4, 2008, OFAC issued a new general license\textsuperscript{43} that authorized transactions between U.S. persons and two of the three entities that had been only recently designated under the Belarus sanctions program on May 15, 2008.\textsuperscript{44} However, all property and interests in property of these two entities, Lakokraska OAO or Polotsk Steklovolokno OAO, that were previously blocked pursuant to Executive Order 13405 remained blocked.\textsuperscript{45}

B. BURMA

On May 6, 2008, and May 9, 2008, OFAC issued two new general license exceptions to the Burmese Sanctions Regulations.\textsuperscript{46} The first of these licenses authorized the exportation or reexportation of certain financial services to Burma in support of the not-for-profit humanitarian or religious activities in Burma of U.S. or third-country non-governmental organizations.\textsuperscript{47} Subsequently, OFAC authorized U.S. financial institutions to process certain transfers of funds, of any amount, for non-commercial, personal remittances to or from Burma, or for or on behalf of an individual ordinarily resident in Burma, in excess of the previous limit of $300 per Burmese household for any consecutive three-month period.

\textsuperscript{43} OFAC, General License No. 1 (Sept. 4, 2008), \textit{available at} http://www.treas.gov/offices/enforcement/ofac/programs/belarus/gls/belarus_gl_1.pdf.

\textsuperscript{44} OFAC, Recent OFAC Actions (May 15, 2008), \textit{available at} http://www.treas.gov/offices/enforcement/ofac/actions/20080515.shtml.

\textsuperscript{45} Exec. Order No. 13,405, 71 Fed. Reg. 35,485 (June 16, 2006) (implementing new economic sanctions against certain members of the Government of Belarus and other persons believed to have undermined Belarus’ democratic processes or institutions, primarily during the country’s March 2006 elections, as well as to have committed human rights abuses and to have engaged in public corruption).


\textsuperscript{47} OFAC, General License No. 14 (May 6, 2008), \textit{available at} http://www.treas.gov/offices/enforcement/ofac/programs/burma/gls/burmagl14.pdf. Also, on May 9, 2008, and then again on July 11, 2008, OFAC issued amendments to General License 14 to authorize, for a period of 120 days each, funding to any organization or individual engaged in not-for-profit humanitarian or religious activities in Burma through January 4, 2009. The previously issued General License No. 14 only authorized the transfer of funds in support of not-for-profit humanitarian or religious activities in Burma only if they involved U.S. or third-country non-governmental organizations. Upon the expiration of these extension periods, the terms of the original General License No. 14 remain in effect.
C. **CUBA**

In 2008, OFAC updated its list of authorized providers of air, travel and remittance forwarding services\(^{48}\) and made several automation improvements to expedite the processing of Cuban travel licenses and requests for the release of blocked funds.\(^{49}\) In addition, on July 29, 2008, OFAC issued a notice clarifying that the transfer of a claim against the Government of Cuba, even if certified by the Foreign Claims Settlement Commission, generally requires OFAC authorization.\(^{50}\)

D. **IRAN**

Effective November 10, 2008, OFAC amended the Iranian Transactions Regulations to revoke its previous authorization allowing U.S. depository institutions to process “U-turn” transfers; which are transactions that are initiated offshore as dollar-denominated transactions by order of a foreign bank’s customer, become transfers from a correspondent account held by a domestic bank for the foreign bank to a correspondent account held by a domestic bank for second foreign bank, and ultimately are returned offshore as transfers to a dollar-denominated account of the second foreign bank’s customer.\(^{51}\) However, the amendment did not revoke certain “U-turn” transactions that are authorized by a specific or general license or are exempt or not otherwise prohibited by the Iranian Transaction Regulations.


\(^{50}\) See Cuban Assets Control Regulations, 31 C.F.R. § 515.201 (2008).

E. NORTH KOREA

On June 26, 2008, the President signed a proclamation\(^{52}\) stating that the exercise of authorities under the Trading With the Enemy Act\(^ {53}\) with respect to North Korea was no longer in the national interest of the United States. As a result of this action, the Foreign Assets Control Regulations and the Transaction Control Regulations no longer apply to North Korea.\(^ {54}\) However, contemporaneously with the release of the proclamation, the President also issued an executive order\(^ {55}\) continuing certain restrictions with respect to North Korea that otherwise would have been lifted pursuant to the proclamation. These restrictions included the continued blocking of property and interests that were blocked prior to June 16, 2000, as well as the prohibition against U.S. persons registering vessels in North Korea, obtaining authorization for a vessel to fly the North Korean flag or owning, leasing, operating, or insuring any vessel flagged by North Korea.

F. SPECIALLY DESIGNATED NATIONALS

In addition to actions discussed elsewhere, OFAC frequently updated the Specially Designated National List under a variety of programs. Of note, designations in 2008 were particularly directed toward designating global terrorists.\(^ {56}\)

\(^{52}\) Proclamation No. 8271, Termination of the Exercise of Authorities Under the Trading With the Enemy Act With Respect to North Korea, 73 Fed. Reg. 36,785 (June 26, 2008).

\(^{53}\) Trading With the Enemy Act, 50 U.S.C. app. §§ 1 et seq.


\(^{56}\) Of the first 44 public releases related primarily to OFAC’s list of Specially Designated Nationals, 14 related to Specially Designated Global Terrorists. See
G. ROUGH DIAMONDS

On May 21, 2008, OFAC issued a notice amending the Rough Diamonds Control Regulations\(^57\) to add new requirements designed to enhance the collection of statistical data on importations and exportations of rough diamonds.\(^58\) Specifically, these amendments (i) add a new note to Section 592.301 of the regulations explaining that U.S. Customs and Border Protection (“CBP”) will not release shipments of rough diamonds unless the import paperwork conforms with CBP’s formal entry for consumption requirements set forth in CBP’s regulations\(^59\) and (ii) add a new section to these regulations, which requires rough diamond importers and exporters to file an annual report with the Department of State detailing their import, export and stockpiling information.

H. TERRORISM

Under the Global Terrorism Sanctions Regulations,\(^60\) OFAC may designate additional persons “otherwise associated with” already designated persons and subject the assets of these associated persons to blocking requirements. OFAC added forty-one parties to, and removed nine parties from, its list of Specially Designated Global Terrorists over the past year\(^61\) and released a report in October 2008 on the effectiveness of its asset blocking programs in

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\(^{59}\) See Entry of Merchandise, 19 C.F.R. § 141.0a(f) (2008).


combating international terrorism.\textsuperscript{62}

I. \textbf{TRADE SANCTIONS REFORM AND EXPORT ENHANCEMENT ACT}

On November 7, 2008, OFAC updated its guidelines for submitting applications pursuant to the Trade Sanctions Reform and Export Enhancement Act of 2000 for licenses to export agricultural commodities, medicine and medical devices to Iran and Sudan.\textsuperscript{63}

J. \textbf{OTHER OFAC REGULATORY PRONOUNCEMENTS}

In addition to the other OFAC regulatory pronouncements described herein, OFAC issued guidance regarding the release of blocked funds as well as new guidance directed toward the securities industry.

1. Release of Blocked Funds

OFAC issued Guidance on the Release of Limited Amounts of Blocked Funds for Payment of Legal Fees and Costs Incurred in Challenging the Blocking of U.S. Persons in Administrative or Civil Proceedings (July 21, 2008)\textsuperscript{64} and Guidance on Entities Owned by Persons Whose Property and Interests in Property are Blocked (Feb. 14, 2008).\textsuperscript{65} The July Guidance provides for the issuance of specific licenses by OFAC, on a case-by-case basis, to authorize the release of a limited amount of blocked funds (not full compensation) for the payment of legal fees and costs incurred in seeking administrative reconsideration or judicial

\textsuperscript{62} \textit{See} OFAC, Terrorist Assets Report: Calendar Year 2007 - Sixteenth Annual Report to Congress on Assets in the United States of Terrorist Countries and International Terrorism Program Designees (Oct. 9, 2008), available at [link]. The report noted that programs targeting international terrorist organizations have resulted in the blocking of $20 million of U.S. assets and that more than $315 million in assets are blocked under sanctions imposed against the five designated state sponsors of terrorism.

\textsuperscript{63} \textit{See} [link].

\textsuperscript{64} \textit{See} [link].

\textsuperscript{65} \textit{See} [link].
review of the designation of U.S. persons or the blocking of their property/interests pursuant to Executive Orders and OFAC regulations where alternative funding sources are not available to such persons. It also sets forth a number of parameters and licensing requirements that designated or blocked parties must satisfy (e.g., evidence of U.S. person status and itemization of legal fees), and describes the monetary limitations regarding caps on legal fees and hourly rates consistent with federal legislation.

The February guidance was issued by OFAC in response to multiple inquiries received by the agency. OFAC notes that blocked property is broadly defined to include any property or interest, whether tangible or intangible, future or contingent or direct or indirect. According to the Guidance, regardless of whether the entity itself is listed, U.S. persons generally may not engage in any transactions with an entity in which a blocked person owns, directly or indirectly, a 50% or greater interest. OFAC also cautions U.S. persons to be careful in transacting business with non-blocked entities that are controlled by or have a significant ownership amount of less than 50% by a blocked person66 as they may be subject to future designation or enforcement action by OFAC.

2. OFAC Compliance for the Securities Industry

On November 6, 2008, OFAC issued guidance relating to OFAC-related due diligence procedures in the securities industry, particularly in connection with the client acceptance process and the selection of new investments or transactions.67 Of note, the guidance emphasized that securities firms should maintain adequate documentation of the results of their

66 See Section IV(A) above regarding the application of this Guidance in the context of the Belarus Sanctions.

screening processes as well as conduct adequate due diligence regarding the beneficial ownership of certain types of accounts, including, particularly, omnibus accounts. In addition, this guidance included a list of risk factors, which may warrant a heightened level of scrutiny, associated with (a) international transactions, including wire transfers, (b) foreign customers/accounts, (c) foreign broker-dealers who are not subject to OFAC regulations, (d) investments in foreign securities, (e) certain forms of investment funds and accounts creating an intermediary relationship, (f) third-party introduced business and (g) confidential accounts.

K. Enforcement Actions, Settlements and Policy Developments

In 2008, OFAC continued its practice of periodically posting important informational documents and final agency Penalty Notices and relevant case reports 68 on its website, including guidance on the application of increased penalties under the IEEPA Enhancement Act and new economic sanctions enforcement guidelines. According to OFAC’s website, 61 companies agreed to or received penalties for violations of the Burmese, Cuban, Former Liberian Regime of Charles Taylor, Iranian, Iraqi, Libyan, Sudanese, terrorism and narcotics trafficking sanctions programs between January 4, 2008 and November 7, 2008. During the same period, seven companies were penalized $100,000 or more, and 40 individuals were penalized, primarily for

68. See http://www.treas.gov/offices/enforcement/ofac/civpen/index.shtml. Notable actions involved York International Corporation (May 2, 2008), which was fined $669,507 to settle allegations that it sold equipment to Iran and Sudan by foreign nationals employed at a foreign branch and improper payments made to the Government of Iraq in connection with licensed sales of equipment to Iraq under the United Nations Oil-for-Food Program; Engineering Dynamics Inc. (May 2, 2008), which was fined $132,791.39 as part of a multi-agency settlement related to allegations that it acted in a knowing and willful manner by importing and exporting unauthorized goods and services to and from Iran to assist in the design of offshore oil and gas structures; and Minxia Non-Ferrous Metals, Inc. (July 11, 2008), which paid the largest penalty of the period, $1,198,000 to settle allegations that it acted without an OFAC license or outside the scope of its license by purchasing or otherwise dealing in Cuban metals. See also http://www.bis.doc.gov/news/2008/doj10282008_fact_sheet.pdf. The Department of Justice “Major U.S. Export Enforcement Prosecutions During the Past Two Years” Fact Sheet notes that of the 145 defendants listed, approximately 36 involved Iran, 3 involved Iraq, 2 involved Syria, 2 involved Cuba, 1 involved Libya and 1 involved the Sudan.
dealing in property in which Cuba or a Cuban national had an interest. The total amount of OFAC civil penalties for the same period totaled $3,470,709.

In addition, on June 10, 2008, OFAC published its final rule amending the civil penalty provisions affecting seventeen parts of the OFAC regulations for which IEEPA provides civil penalty authority. The amendments are technical updates to reflect the substantial increase in civil penalty authority resulting from the enactment in October 2007 of the IEEPA Enhancement Act, i.e. they modify the relevant civil penalty provisions to reflect that the current maximum civil penalty is the greater of $250,000 or twice the amount of the transactions that is the basis of the violation.

Furthermore, on September 8, 2008, OFAC issued its Economic Sanctions Enforcement Guidelines following the enactment of the IEEPA Enhancement Act. These guidelines establish the new framework by which OFAC will determine its appropriate enforcement response to apparent violations and, if a civil penalty is warranted, assess the amount of the penalty.

According to the guidelines, the two most important factors impacting OFAC’s penalty assessment are whether the case is “egregious” or “non-egregious” and whether the case involves a voluntary self-disclosure. OFAC will utilize a two-pronged approach to penalty assessment: one for “egregious” cases and another for “non-egregious” cases. The guidelines also indicate that OFAC generally intends to limit the use of the $250,000 statutory maximum as a penalty basis for what it determines to be “egregious” cases. Whether a case will be deemed “egregious”

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will be based on a case-by-case evaluation of what OFAC calls “General Factors”,\(^71\) four of which will be given substantial weight in any such determination: willful or reckless violation, awareness of the conduct, harm to sanctions program objectives, and individual characteristics of the parties involved such as commercial sophistication, size of business operations and volume of transactions. OFAC will place particular emphasis on the first two factors.

The second major element to be considered by OFAC is the submission of a voluntary self-disclosure. In egregious cases, submitting a voluntary self-disclosure will reduce the penalty to one-half of the $250,000 statutory maximum, while submitting a voluntary self-disclosure in a non-egregious case will reduce the penalty to one-half of the actual transaction value capped at $125,000 per violation. The guidelines also provide for a variety of enforcement measures short of issuing monetary penalties including the issuance of a “Findings of Violation” where a violation has occurred but a civil monetary penalty is not the most appropriate response, and a Cautionary Letter where there is insufficient evidence to conclude that a violation has occurred but OFAC is concerned that the underlying conduct is problematic for sanctions compliance.

L. COURT CASES INVOLVING OFAC PROGRAMS

In addition to significant activity at the agency, the past year also saw significant court activity. These rulings reinforced the U.S. federal government’s ability to apply its economic sanctions across international boundaries but, nevertheless, limited the ability of individual States to apply their own, even more stringent, economic sanctions upon foreign activities.

In *Faculty Senate of Florida International University v. Roberts*,\(^72\) the District Court for the Southern District of Florida held that provisions of the 2006 Florida Travel Act are

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\(^71\) The term “General Factors” replaces the use of “mitigating” and “aggravating” factors.

\(^72\) *Faculty Senate of Fla. Int’l University v. Roberts*, 574 F. Supp. 2d 1331 (S.D. Fla. 2008).
unconstitutional because they constitute an impermissible sanction on designated state sponsors of terrorism and serve as an obstacle to the objectives of the federal government. The Court held that the Travel Act’s restrictions on the use of non-state funds constitute more than an “incidental or indirect” effect on foreign affairs and therefore infringe upon the federal government’s foreign affairs power. In addition, the Court held that the Act’s restrictions on non-state funds, as well as nominal state funds necessary to administer such non-state funds, are unconstitutional because they impede the President’s authority to speak with one voice in dealing with state sponsors of terrorism.

In Lawyers’ Committee for Civil Rights of San Francisco Bay Area v. U.S. Department of the Treasury, the Court ordered the Treasury Department to disclose, under the Freedom of Information Act (“FOIA”), certain OFAC records regarding its Specially Designated Nationals List. In particular, the Court required the Treasury Department to disclose delisting petitions after determining that the documents did not fall under any of the relevant exemptions to the FOIA’s disclosure requirements.

73 The Florida Chapter 2006-54, An Act Relating to Travel to Terrorist States restricted state universities from spending state and “non-state” funds on activities related to travel to a “terrorist state,” meaning any state designated by the U.S. State Department as a state sponsor of terrorism. According to the Act, “[n]one of the state or non-state funds made available to state universities may be used to implement, organize, direct, coordinate, or administer, or to support the implementation, organization, direction, coordination, or administration of, activities related to or involving travel to a terrorist state.” In addition, “[t]ravel expenses of public officers of employees for the purpose of implementing, organizing, directing, coordinating, or administering, or supporting the implementation, organization, direction, coordination, or administration of, activities related to or involving travel to a terrorist state shall not be allowed under any circumstances.”

74 The Court found that these provisions of the Travel Act are preempted by federal law regarding state sponsors of terrorism, including the Trading with the Enemy Act, the Cuban Assets Control Regulations, the International Emergency Economic Powers Act, the Iran and Libya Sanctions Act, as well as several regulations relating to travel to Iran, North Korea, Sudan, and Syria.

75 Lawyers’ Committee for Civil Rights of San Francisco Bay Area v. United States Department of the Treasury, 534 F. Supp. 2d 1126 (N.D. Cal. 2008).

76 The Court held that the Treasury Department was not entitled to withhold the delisting petitions because it had not shown that the disclosure of the petitions “could reasonably be expected to interfere with enforcement proceedings,” or “could reasonably be expected to endanger the life or physical safety of any individual,” as
required under 5 U.S.C. §§ 552(b)(7)(A) and (F), respectively. In addition, the Court held that the Treasury Department was not entitled to relief under six other exemptions (under 5 U.S.C. §§ 552(b)(6), (7)(C), (7)(D), (3), and (4)) because the Treasury Department did not meet its burden of demonstrating the portions of the petitions to which the exemptions should be applied. Furthermore, the Court was unable to determine the portions of the petitions to which the exemptions should apply because the Treasury Department did not submit a Vaughn index, which would have identified each document withheld and the statutory exemption claimed, and would have explained how the disclosure of the particular portion of the document would damage the interest protected by the claimed exemption.