

UIC John Marshall Journal of Information Technology & Privacy Law

Volume 7
Issue 3 *Computer/Law Journal - Summer 1987*

Article 1

Summer 1987

Exporting High Technology From the United States Under the Revised Distribution License Procedures, 7 Computer L.J. 289 (1987)

G. Gregory Letterman

Follow this and additional works at: <https://repository.law.uic.edu/jitpl>



Part of the [Computer Law Commons](#), [Internet Law Commons](#), [Privacy Law Commons](#), and the [Science and Technology Law Commons](#)

Recommended Citation

G. Gregory Letterman, Exporting High Technology From the United States Under the Revised Distribution License Procedures, 7 Computer L.J. 289 (1987)

<https://repository.law.uic.edu/jitpl/vol7/iss3/1>

This Article is brought to you for free and open access by UIC Law Open Access Repository. It has been accepted for inclusion in UIC John Marshall Journal of Information Technology & Privacy Law by an authorized administrator of UIC Law Open Access Repository. For more information, please contact repository@jmls.edu.

EXPORTING HIGH TECHNOLOGY FROM THE UNITED STATES UNDER THE REVISED DISTRIBUTION LICENSE PROCEDURES

by G. GREGORY LETTERMAN*

TABLE OF CONTENTS

I. POLICY REASONS FOR RECENT DISTRIBUTION LICENSE PROCEDURE REVISIONS	289
II. STATUTORY AND REGULATORY FRAMEWORK FOR UNITED STATES EXPORT CONTROLS	291
III. THE DISTRIBUTION LICENSE	293
IV. DISTRIBUTION LICENSE CONSIGNEES	296
V. COMMODITIES EXPORTABLE UNDER A DISTRIBUTION LICENSE	297
VI. COUNTRY EXPORT/REEXPORT DESTINATIONS UNDER A DISTRIBUTION LICENSE	301
VII. DISTRIBUTION LICENSE ADMINISTRATION	304
VIII. INTERNAL CONTROLS	307
IX. A DISTRIBUTION LICENSEHOLDER'S INTERNAL CONTROL PROGRAM	310
X. DISTRIBUTION LICENSE CONSIGNEES' INTERNAL CONTROL PROGRAMS	320
XI. RECENT ACTIONS, EXPECTED DEVELOPMENTS, AND CONCLUSIONS	324

I. POLICY REASONS FOR RECENT DISTRIBUTION LICENSE PROCEDURE REVISIONS

The United States is one of the world's developers and suppliers of high technology products with both military and commercial uses. The

© G. Gregory Letterman, 1986.

* Mr. Letterman is of counsel to the law firm of Cox & Smith Incorporated in San Antonio, Texas, and is Chairman of the Subcommittee on Export Controls, International Trade Committee, International Law and Practice Section of the ABA.

transfer of this technology to hostile foreign powers would have adverse strategic consequences for the United States and would pose a threat to national security. Recently publicized cases demonstrate the frequency and ease with which unfriendly countries have improperly acquired such technology from the United States.¹ United States export control legislation attempts to minimize the threat to United States national security while permitting United States businesses to operate in reasonably free and open international commerce. Additionally, export control legislation may be imposed for foreign policy reasons or because the exported items are in short supply in the United States.

The United States, Belgium, Canada, Denmark, France, West Germany, Greece, Holland, Italy, Japan, Luxembourg, Norway, Portugal, Spain, Turkey and the United Kingdom have jointly created the Coordinating Committee for Multilateral Export Controls ("CoCom"), an informal, non-treaty organization founded to coordinate the national programs of controlling member states' high technology exports to hostile countries.² In 1984, CoCom significantly revised its export control policies and procedures to update the International Control List of multilaterally controlled materials to reflect advancing technology. This update released a number of established technologies and products from multilateral export restrictions, but made others subject to multilateral controls which had previously been subject only to unilateral United States controls. CoCom, however, lacks authority to enforce its policies. Its policies are implemented through the national legislation or regulations of its member states.

The United States, particularly under the Reagan Administration, imposes stricter export controls than do other CoCom members. This is evidenced by new statutes, regulations and enforcement practices. The United States exerts unilateral export controls over many commodities and destinations which are not subject to CoCom review.³ The United States also has attempted to extend enforcement of its high technology export control policies beyond its borders. Foreign nations, including the United States' closest allies, strongly resent and protest these efforts by the United States to extra-territorialize its laws and policies.⁴

Within the Administration, the Department of Defense (DOD) is a strong advocate for strict export controls while the Department of Commerce (DOC) is more sensitive to the commercial needs of the export-

1. See 3 Int'l Trade Rep. (BNA) No. 32 at 1006 (Aug. 6, 1986); No. 29 at 919 (July 16, 1986); No. 28 at 906 (July 9, 1986); No. 27 at 880 (July 2, 1986); No. 24 at 789 (June 11, 1986); No. 22 at 727 (May 28, 1986); No. 21 at 701 (May 21, 1986).

2. 50 U.S.C. app. § 2404(i) (Supp. III 1985).

3. 15 C.F.R. § 370.11(c) (1986).

4. High Tech for the Russians, THE ECONOMIST, February 15, 1986, at 63.

ing industry. The debate over how to balance controlling and promoting exports is unresolved between the DOD and the DOC.

II. STATUTORY AND REGULATORY FRAMEWORK FOR UNITED STATES EXPORT CONTROLS

The Export Administration Amendments Act of 1985 ("Act Amendments"),⁵ enacted on July 12, 1985, amends the Export Administration Act of 1979 ("Act"),⁶ which had expired in 1984 and was preserved in force only by Executive Order. The Act is the principal statute establishing controls over most United States exports. The Act Amendments codified Distribution Licenses (DLs), which were earlier administrative creations.⁷

The DOC is responsible for approving and issuing export licenses, including DLs, except for export items exclusively controlled by other agencies.⁸ CoCom or other United States government agencies may also review export applications.

The DOC has recently revised the Export Administration Regulations⁹ ("regulations"), which implement the Act, to conform United States regulations with CoCom directives and to follow Administration instructions on strengthening export controls. The DOC's first proposed revisions in January 1984¹⁰ were made in an effort to soften industry opposition and to establish the DOC as a strict export control advocate, similar to the DOD. These first proposed revisions frightened the high technology exporting industry, but amended DL regulations were issued in May 1985. The high technology exporting community accepted the amended revisions with little criticism or complaint because the industry was relieved at being spared from the calamity threatened by the earlier version of the revised regulations. Many other regulation revisions affecting, *inter alia*, exports under a DL have been issued from the end of 1984 to the present.¹¹

5. Export Administration Amendments Act of 1985, Pub. L. No. 99-64, 99 Stat. 120 (codified as amended at 50 U.S.C. §§ 2401-2420).

6. 50 U.S.C. app. §§ 2401-2420 (Supp. III 1985).

7. *Id.* § 2403(a)(2)(A).

8. 15 C.F.R. § 370.10 (1986). This regulation lists exports which are not controlled by the Department of Commerce.

9. Export Administration Regulations, 15 C.F.R. §§ 368-99 (1986).

10. Amendments to Distribution License Procedure, 49 Fed. Reg. 2,264 (1984).

11. Approximately seventy revisions of the Export Administration Regulations have been made from late 1984 to date. Among those most directly applicable to Distribution License procedures are: Change in Reporting Frequency From Monthly to Quarterly Under the Distribution License Procedure, 50 Fed. Reg. 14,373 (1985) (to be codified at 15 C.F.R. 373.3); Revision of Distribution License Procedure, 50 Fed. Reg. 21,562 (1985) (to be codified at 15 C.F.R. §§ 373.1, 373.3, and 373, Supps. 1, 4, 5 and 6); Export Administration Regulations; Editorial Amendments, 50 Fed. Reg. 23,111 (1985) (to be codified at 15 C.F.R.

A General License (GL) approving exports must be established or a Validated License (VL) issued before any commodity or Technical Data¹² may be exported from the United States.¹³ Most exports to Canada for use in Canada, exports to the United States Armed Forces abroad, and exports of commodities controlled by other agencies are exempted from this requirement.¹⁴ Any export authorization may be revoked, suspended, or otherwise limited.¹⁵ Under the Act, a party may ask the DOC to determine the applicability of the regulations to specific export transactions or to classify a commodity under the Commodity Control List (CCL).¹⁶

"Exports", for the purposes of export control, include certain sales or transfers within the United States. These include transfers to embassies or affiliates of controlled countries or to persons known to be intending to remove commodities from the United States without proper authorization.¹⁷

The DOC may grant DLs to an exporter so that the exporter may avoid the requirement of obtaining a large number of Individual Validated Licenses (IVLs) for periodic, multiple shipments to a number of

§ 373, Supp. 3); Revision of Distribution License Procedure, 50 Fed. Reg. 23,666 (1985) (to be codified at 15 C.F.R. § 373.3); Export Controls on the Republic of South Africa, 50 Fed. Reg. 47,363 (1985) (to be codified at 15 C.F.R. §§ 371.2, 373.1, 379.4, 385.4, 385, Supps. 1 and 2, 386.6, and 399.1); Revision of Processing Times for Applications for Export Licenses, 50 Fed. Reg. 48,745 (1985) (to be codified at 15 C.F.R. §§ 370.1, 370.13, 370.14, 372.4, 372.11, and 386.3); Addition of "Foreign Availability Procedures and Criteria" to the Export Administration Regulations, 50 Fed. Reg. 52,912 (1985) (to be codified at 15 C.F.R. § 391.1, 391.2, 391.3, 391.4, 391.5, and 391.6); Revision of Enforcement and Administrative Proceedings Provisions of the Export Administration Regulations, 50 Fed. Reg. 53,130 (1985) (to be codified at 15 C.F.R. §§ 370.15, 372.1, 387.1, 387.2, 387.3, 387.4, 387.5, 387.6, 387.7, 387.8, 387.9, 387.10, 387.11, 387.12, 387.13, 387.14, 388.1, 388.2, 388.3, 388.4, 388.5, 388.6, 388.7, 388.8, 388.9, 388.10, 388.11, 388.12, 388.13, 388.14, 388.15, 388.16, 388.17, 388.18, 388.19, 388.20, 388.21, 388.22, 388.23, and 388, Supps. 1 and 2); Exports to India; Export and Reexport of National Security Controlled Commodities, 51 Fed. Reg. 10,365 (1986) (to be codified at 15 C.F.R. §§ 374 and 375); Export Administration Regulations; Editorial Clarifications and Corrections, 51 Fed. Reg. 12,838 (1986) (to be codified at 15 C.F.R. § 370-73, 375-77, 379, 386, and 399); Export Controls on the Republic of South Africa, 51 Fed. Reg. 18,773 (1986) (to be codified at 15 C.F.R. §§ 370.2 and 373.1); Exports to Countries Listed in Supplement No. 8 to Part 373, 51 Fed. Reg. 22,503 (1986) (to be codified at 15 C.F.R. §§ 373.3, 373 Supps. 1, 4 and 8, and 399.1); Establishment of Import Certificate Delivery Verification Procedure for Spain, 51 Fed. Reg. 22,504 (1986) (to be codified at 15 C.F.R. §§ 375.1, 375.3, and 375 Supp. 1); and Clarifications of Special Licenses Not Available for Certain Commodities, 51 Fed. Reg. 23,528 (1986) (to be codified at 15 C.F.R. §§ 377, Supp. 1, and 399.1).

12. 15 C.F.R. § 379.1(a).

13. *See id.* § 370.3(a).

14. *Id.* § 370.3(a)(1)-(3).

15. *Id.* § 370.3(b).

16. 50 U.S.C. app. § 2409(l); *see also* 15 C.F.R. § 399.1 (Supp. 1) which contains the Commodity Control List.

17. 50 U.S.C. app. § 2404(a)(1); *see also id.* § 2415(5)(B), (C).

foreign consignees of designated goods which are not quantifiable at the time of application.¹⁸

Some exports may be licensed under GLs, IVLs, other Multiple Licenses or some combination of these. These other export licenses may be used in lieu of a DL for all an exporter's transactions or may be used for some transactions jointly with a DL which is used for others. A commodity exported under a DL may be subject to reexport, notice or other restrictions that would not apply to the commodity if it was exported under other types of licenses.

III. THE DISTRIBUTION LICENSE

The DL permits a DL license holder (DLH) to export unlimited quantities of certain commodities, but not Technical Data, from the United States under an international marketing program without additional DOC authorization. The DLH may only export to pre-approved DL consignees (DLCs) in the DLCs' designated territories. Software, as contrasted with the media upon which it is recorded, is Technical Data. Most manufacturers of high technology find the DL an essential tool in implementing an effective world-wide marketing program. Approximately eighty percent of United States high technology exports are made under DLs.¹⁹

Although the Act encourages the use of multiple licenses,²⁰ the revised regulations apply more stringent standards for obtaining and retaining a DL. The revised regulations state that receipt of a DL is a privilege and not a right. The regulations make explicit that a failure of the DLH or a DLC to comply with export control regulations, particularly the creation and implementation of Internal Control Programs (ICPs),²¹ could result in the revocation, restriction or suspension, in part or in whole, of the DL.²²

An exporter may usually request and obtain a DL if the exporter: (a) is able to adhere to DL requirements, (b) has more than three qualifying foreign consignees, (c) has an acceptable ICP, and (d) has a reasonable expectation that the DL, in its first year, will replace at least twenty-five IVLs.²³ The DOC will consider requests for relief from provisions of the regulations under unusual circumstances. The DOC will give special consideration to small exporters, but will not waive the re-

18. 50 U.S.C. app. § 2403(a)(2)(A); see also 15 C.F.R. § 373.3.

19. *CoCom Computer Regulations Criticized for Their 'Ambiguities, Contradictions'*, 2 Int'l Trade Rep. (BNA) No. 20 at 678 (May 15, 1986).

20. 50 U.S.C. app. § 2404(e)(1), (4), (5).

21. See *infra* text accompanying notes 157-61.

22. 15 C.F.R. § 373.1(f).

23. *Id.* § 373.3(c).

quirements of an adequate ICP and reliable DLCs.²⁴

Persons not subject to United States jurisdiction, who may apply through qualifying agents, and persons specially designated by DOC are not eligible to apply for, receive or use a DL.²⁵

The DOC publishes a Table of Denial Orders (TDOs). This table lists persons or organizations considered unsuitable recipients of controlled United States goods or users of United States export privileges because the DOC anticipates that the person or organization will violate United States export regulations. Other persons or organizations may also be determined to be inappropriate DLHs or DLCs and their names may be published in the Federal Register.²⁶

The DOD has reportedly received presidential authorization to review all DL applications. The Department of Energy reviews any DL application for exporting a commodity on the CCL Nuclear Referral List or for exporting to a nuclear end-use or end-user, regardless of the commodity.²⁷ The Department of State may review any DL application for controlled commodities for foreign policy purposes.²⁸ The Department of Treasury's Office of Foreign Assets Control reviews DL applications to export commodities to certain embargoed countries, such as Nicaragua or Libya.²⁹ The Department of Treasury applies different standards than the regulations and approval of a DL application for embargoed countries is improbable.

A DL is valid for two years from the last day of the month in which it is issued.³⁰ The DL may be extended for two additional years and is subsequently renewable for four-year periods.³¹

Within ten days of assigning a DL application a Case Identification Number, the DOC's Multiple Licensing Branch will acknowledge receipt of the application and furnish the applicant with the single letter and six-digit Case Identification Number for reference purposes.³²

Within forty-five days of assigning a DL application with a case identification number, or thirty days for amendment requests, the DOC will advise the applicant of any correctable problems, deficiencies or

24. *Id.* § 373.3(o).

25. *Id.* § 372.3(b)(1)(ii).

26. 50 U.S.C. app. § 2404(1)(1)(A); 2410(c)(2)(A), (c)(3), (d), (h); 2412(d). *See also* 15 C.F.R. §§ 370.15, 371.2(f), 372.1(h), 373.2(f), 373.7(h)(3), 387.1(b), 387.12, 388.3, 388.16(c), 388.19, 388 (Supp. 1 and 2), 390.2.

27. 15 C.F.R. § 378 (Supp. 1).

28. 50 U.S.C. app. § 2405(a)(5).

29. *See also* 31 C.F.R. §§ 500-5.

30. 15 C.F.R. § 373.3(f)(3)(ii).

31. *Id.* §§ 373.3(f)(3)(ii), (1)(3)(i).

32. *Id.* § 373.3(f)(2)(i).

needed clarifications before final processing.³³

Generally, the DOC will process DL applications that do not require any supplemental information within ninety days.³⁴ The DOC will usually process amendments to DLs within sixty days.³⁵ Applicants may be required by the DOC to undergo a pre-license audit of their ICPs and past transactions.³⁶

When a DL application is approved in whole or in part, the DOC will issue a Form ITA-628, Export License, which bears a four-digit DL number prefixed by the letter "V".³⁷ Approved DLs, or approved amendments adding a DLC, will be accompanied by two Forms ITA-6052P for each approved DLC. One Form ITA-6052P will be retained by the DLH, and the other will be sent to the appropriate DLC.³⁸ The Form ITA-6052P which is sent by the DHL to the DLC will be accompanied by a transmittal letter which must comply with several requirements.³⁹

A DL application returned without action will be accompanied by all supporting documents submitted and a Form ITA-651, "Advice on Application Returned Without Action." This Form states the reason for return of the DL application and explains the deficiencies or required additional information. Resubmission must be made within 120 days.⁴⁰ Applicants must insure that all application documents are accurately completed in accordance with the DOC's requirements. The Form ITA-651 is an easy solution for bureaucrats that cannot meet processing time limits. This solution has been frequently exercised.

The DOC, to the extent compatible with national security and foreign policy, notifies the applicant when questions or negative recommendations are received from reviewing agencies. The applicant has thirty days to respond in writing or fifteen days to submit a written request to respond in person to the questions or recommendations.⁴¹

If the DOC decides to deny the application, the applicant will receive detailed notification within five days of the decision and the applicant has thirty days to respond in writing before the application is finally denied.⁴²

Rejected DL applications are returned with a Form ITA-687, "Noti-

33. *Id.* §§ 373.3(f)(2)(ii), (1)(2).

34. *Id.* § 373.3(f)(2)(iii).

35. *Id.* § 373.3(l)(2)(ii).

36. *Id.* §§ 373.3(f)(1), (n).

37. *Id.* § 373.3(f)(3).

38. *Id.* § 373.3(g)(1).

39. *Id.* § 373.3(g)(3).

40. *Id.* § 373.3(f)(4).

41. 50 U.S.C. app. § 2409(f)(2); *see also* 15 C.F.R. § 370.13(i).

42. 50 U.S.C. app. §§ 2405(a)(4), 2409(f)(3); *see also* 15 C.F.R. § 370.13(j).

fication of Rejection of Export License Application", or with a letter specifying the reason for rejection.⁴³ Export license denials may be appealed within forty-five days of the denial.⁴⁴ If a DLC is rejected, the DLH is advised of the reason for rejection by a rider to the returned Form ITA-687.⁴⁵

IV. DISTRIBUTION LICENSE CONSIGNEES

Consignee and end-use restrictions are intended to assure that exported items will not be diverted to hostile countries or to restricted destinations without authorization.

The DOC must approve DLCs. To determine the acceptability of a DLC, the DOC considers, among other things: (a) whether the DLC has had an ongoing business relationship with the applicant for at least one year, (b) whether the DLC was an approved DLC under another DL, (c) whether the DLC has a satisfactory record as a consignee under IVLs, and (d) whether the DLC is controlled-in-fact by the applicant or another approved DLC.⁴⁶ The DOC has stated that the earlier one-year relationship may be waived.⁴⁷ The DOC may require evidence of the DLC's firm intention to continue to place orders with the applicant.⁴⁸ Applicants for renewed DLs must demonstrate ongoing economic activity with each renewed DLC.⁴⁹

DLCs must be characterized as either "resellers" or "end-users".⁵⁰ Resellers are parties which receive commodities from the United States to sell to other parties. The category includes: (a) parties which resell United States commodities in the basic form received, (b) parties which modify or add value to the United States commodity, which continues to be primarily of United States origin, before reselling or reexporting it, (c) parties which attach a United States commodity in the same or essentially the same form as received to foreign equipment, and (d) parties which supply United States commodities as support equipment for foreign products.⁵¹ By contrast, end-users are parties which use commodities from the United States permanently or incorporate them as integral parts, components or materials in the production of primarily foreign commodities.⁵²

43. 15 C.F.R. § 373.3(f)(5).

44. *Id.* §§ 370.13(j)(2), 389.

45. *Id.* § 373.3(g)(2).

46. *Id.* § 373.3(c)(4)(ii).

47. Revision of Distribution License Procedure, 50 Fed. Reg. 21,563 (1985).

48. 15 C.F.R. § 373.3(c)(5).

49. *Id.* § 373.3(k)(3)(iii).

50. *Id.* § 373.3(c)(3).

51. *Id.* § 373.3(c)(3)(i).

52. *Id.* § 373.3(c)(3)(ii).

The DLH may, upon DOC approval, add or delete DLCs from the DL. Added DLCs must satisfy DOC requirements. The DLH must advise the DOC if a DLC is deleted for noncompliance with the DL or the regulations.⁵³

No seller may make any sale, export or transaction to a person or organization which the seller/exporter knows or has reason to know intends to make an unauthorized diversion, reexportation or exportation.⁵⁴

A new addition to the regulations lists items eligible for DL shipment only to specifically pre-approved end-users.⁵⁵ Some listed items are limited for export to pre-approved end-users only when sent to other than certain countries.⁵⁶

Export Control Commodity Numbers (ECCNs) in the CCL sometimes limit exports of the listed commodity to special consignees or destinations. For example, exports to DLCs in South Africa and South West Africa (Namibia) are specially monitored to assure that exported commodities do not come into the possession of any branch or agency of the police, military forces, or enforcers of apartheid.⁵⁷ Written certifications by DLCs located in South Africa or Namibia or DLC end-users exporting manufactured products containing United States components are required.⁵⁸

If a DLC is controlled by, or is affiliated with, embassies of countries in certain Country Groups (CGs)⁵⁹, it may not receive commodities under a DL.⁶⁰ Sales or transfers of DL shipped equipment to these customers is improper even if they are located in the United States, Canada, or another friendly country. In addition, aircraft parts and accessories may not be provided under a DL to service aircraft controlled by Iran⁶¹ or Libya.⁶²

V. COMMODITIES EXPORTABLE UNDER A DISTRIBUTION LICENSE

Commodities listed for export on DL applications must be listed by CCL entry and paragraph number and must identify portions which are

53. *Id.* § 373.3(1)(4).

54. *Id.* § 374.1(b).

55. *Id.* § 373 (Supp. 4).

56. *Id.* § 373.3(b)(2).

57. *Id.* §§ 373.1(a), 373.3(d)(3)(ii)(E)(3), 385.4(a), 385 (Supps. 1 and 2), 386.6(a)(2).

58. *Id.* § 373.1(a)(i),(ii); *see also id.* §§ 373.3 (d)(3)(ii)(E)(3), 385.4(a)(9).

59. *Id.* § 370 (Supp. 1).

60. *Id.* § 373.3(b)(1)(vi).

61. *Id.* § 390.6.

62. *Id.* § 390.7.

ineligible for certain DL shipments.⁶³ When the applicant expects to ship a broad range of goods within a CCL entry, listing to entry level only is permitted without reference to paragraph numbers. If spare or replacement parts will not exceed twenty percent of the total export value under the DL, they need not be listed by CCL entry.⁶⁴

The CCL⁶⁵ covers all commodities controlled by the DOC. The CCL does not, however, include those items exclusively controlled for export by other agencies. Instructions on how to use the CCL are provided in the regulations⁶⁶. The DOC provides interpretations of the categorization of some commodities within an ECCN.⁶⁷

The regulations divide CCL commodities into ten general Groups. The ten Groups, numbered from 0 to 9, are: (1) Metal-Working Machinery; (1) Chemical and Petroleum Equipment; (2) Electrical and Power-Generating Equipment; (3) General Industrial Equipment; (4) Transportation Equipment; (5) Electronics and Precision Equipment; (6) Metals, Minerals, and their Manufactures; (7) Chemicals, Metalloids, Petroleum Products, and Related Materials; (8) Rubber and Rubber Products; and (9) Miscellaneous.⁶⁸

A four-digit ECCN and a code letter references each CCL entry. The first digit indicates the strategic level of control. The second digit identifies the Group to which the commodity belongs. The remaining two digits identify related commodities.⁶⁹ Within each Group, entries are numbered consecutively by the final two digits. Code letters indicate the documentation requirements and the level of imposed control. Code letters are "A", "B", "C", "D", "E", "F", "G", "H", "I" and "M".⁷⁰ Code letter A commodities are controlled multilaterally to all destinations. Code letter B commodities are controlled unilaterally to all destinations. Code letter C through I commodities are controlled to a diminishing number of CGs and countries. Code letter M commodities are governed by other CCL entries.

Each ECCN states the reason or reasons for its control, such as national security. Each ECCN describes special licenses that may be used to export the commodity.

A particular DL may exclude some commodities. Additionally, the DL may place special conditions on exporting such commodities to specified destinations.

63. *See id.* § 373 (Supp. 5 (g)) for instructions on listing items on Form ITA-622P.

64. *Id.* § 373.3(d)(3)(i).

65. *Id.* § 399.1 (Supp. 1).

66. *Id.* § 399.1(f).

67. *Id.* § 399.2 (Supp. 1).

68. *Id.* § 399.1 (Supp. 1).

69. *Id.* § 399.1(b).

70. *Id.* § 399.1(f)(2).

The DL must not be used for exports of commodities for sensitive nuclear uses.⁷¹ Certain commodities are unexportable under a DL⁷² except where authorized by surreptitious intercept equipment,⁷³ Short Supplies,⁷⁴ or certain aircraft parts and accessories.⁷⁵

A list of those items ineligible for DL shipment is found in the Regulations.⁷⁶ The list refers to complete machines only, not to parts of listed machines, and uses a Floating Point Processing Data Rate in its descriptions.⁷⁷

Later revisions clarified the categorization of certain digitally controlled test equipment.⁷⁸ Also, certain DL export-excluded electronic computers have higher cut-off performance levels for shipment to certain destinations.⁷⁹

The DOC added a special provision to the regulations for ECCN 1355A semiconductor manufacturing equipment. DL exports are allowed only if the exporter manufactures semiconductors or semiconductor manufacturing equipment, the customer is pre-approved by the DOC and manufactures semiconductors, and the exporter describes adequate means to assure that the shipped items will reach the designated customer and will not later be transferred without prior United States approval.⁸⁰

The commodities covered by the section of the regulations on "Special Commodity Policies and Provisions" include chemicals;⁸¹ machinery, equipment and parts;⁸² aircraft and equipment;⁸³ ship and plane stores, supplies and equipment;⁸⁴ electronic computers and related equipment;⁸⁵ machine tools and/or numerical controls;⁸⁶ parts, components and materials in foreign made products;⁸⁷ communication inter-

71. *Id.* § 378.3; *but see id.* 373.3(a)(2).

72. *Id.* § 373.3(b)(1)(ii).

73. *Id.* § 376.13(a).

74. *Id.* § 377 (Supps. 2-4).

75. *Id.* § 373.3(b)(1)(v).

76. *Id.* § 373 (Supp. 1).

77. 15 C.F.R. § 399.1 (Supp. 1, Group 5, Advisory Note 16 to ECCN 1565A). The Floating Point Processing Data Rate expresses the relative performance speeds of computers. This is a measure developed solely for export licensing. It is not used commercially.

78. *Id.* § 373 (Supp. 1, 4).

79. *Id.* § 373 (Supp. 1, note 8).

80. 15 C.F.R. § 373 (Supp. 1, n.5).

81. *Id.* § 376.6.

82. *Id.* § 376.7.

83. *Id.* § 376.8.

84. *Id.* § 376.9.

85. *Id.* § 376.10.

86. *Id.* § 376.11.

87. *Id.* § 376.12.

cepting devices;⁸⁸ crime control and detection commodities;⁸⁹ donations of goods to meet basic human needs;⁹⁰ regional stability commodities,⁹¹ and robots, robot controllers, end effectors, related vision systems, or related software.⁹²

The commodities covered by the section of the regulations on "Special Nuclear Controls" are controlled for nuclear non-proliferation purposes.⁹³ Commodities that could be used for significant nuclear explosive purposes if used other than as intended are called collectively the "Nuclear Referral List". Items exported for nuclear end-uses or to nuclear end-users are controlled for reasons of national security and are subject to more stringent procedures.⁹⁴ These procedures augment rather than replace other export procedures.⁹⁵

Since the end of 1984, every CCL Group has been frequently and significantly changed. Among the most important changes are those of the CCL Group covering Electronics and Precision Instruments. Often, the ECCNs for the Group are long and complex. Main entries may be qualified by up to four levels of exceptions. The exceptions sometimes are of greater practical consequence than the main entry.

ECCN 1565A,⁹⁶ which covers electronic computers and similar or related equipment, was greatly modified and ECCN 1567A,⁹⁷ which covers communication switching equipment, was created. Generally, export controls were eliminated over established, low technology computers such as most eight-bit computers and basic peripherals such as impact printers. Export controls have been reduced for other similar items.

Paragraph (h) of the "List of Electronic Computers and Related Equipment Controlled by ECCN 1565A" is a significant revision for many commercial computer manufacturers. It covers "other" digital computers and related equipment. This provision explicitly covers digital computer products that are embedded in, incorporated in, or associated with other equipment or systems. "Embedded" digital computers and related equipment are microprocessors which cannot feasibly be removed from the parent equipment or systems nor be used for other purposes. "Incorporated" digital computers and related equipment are

88. *Id.* § 376.13.

89. *Id.* § 376.14.

90. *Id.* § 376.15.

91. *Id.* § 376.16.

92. *Id.* § 376.17.

93. *Id.* § 378.8.

94. *Id.* § 378 (Supp. 1).

95. *Id.* § 378.8.

96. *Id.* § 399.1 (Supp. 1, Group 5).

97. *Id.*

microprocessors which may feasibly be removed from the parent equipment or systems or be used for other purposes, but which are essential to the operation of the parent equipment or systems. "Associated" digital computers and related equipment are similar to "incorporated" digital computers and related equipment, except that the microprocessors in "associated" equipment are not essential to the operation of the parent equipment or systems.⁹⁸

An exporter may request that a commodity generally or on a specific export license be excluded from United States export controls due to "foreign availability."⁹⁹ Foreign availability means that an equivalent commodity not subject to United States controls is available in required quantities to controlled countries such as to make futile United States controls over the export of the commodity. This export control exclusion was long provided for by statute but has only recently been implemented through regulations and DOC staffing. Recent experience casts doubt on whether exclusions from export controls based on foreign availability will be readily granted.

VI. COUNTRY EXPORT/REEXPORT DESTINATIONS UNDER A DISTRIBUTION LICENSE

Foreign countries are assigned for export control purposes, to seven CGs, designated by the symbols "Q," "S," "T," "V," "W," "Y," and "Z".¹⁰⁰ Canada is not in a CG and is treated separately. The remaining countries of the Western Hemisphere, except Cuba, are categorized in CG T. Communist countries, except for some selected for favorable or embargoed treatment, are in CGs Q, W and Y. CG V covers almost all other non-communist countries, plus nonhostile communist states such as the People's Republic of China. CGs S and Z are groups of embargoed countries.¹⁰¹ The DL is valid only for exports to CGs T and V with the exclusion of Afghanistan, Iran and the Peoples Republic of China.¹⁰²

A DLC is authorized to receive commodities, or to reexport commodities received, under the DL only in or to the DLC's approved sales or reexport territory. The countries designated on the DLC's validated Form ITA-6052P or validated Form ITA-699P comprise a DLC's territory.¹⁰³ Resellers must certify that at least six sales of controlled com-

98. *Id.* § 399.1 (Supp. 1, Group 5, Advisory Note 16 to ECCN 1565A).

99. *See generally* 50 U.S.C. app. §§ 2403(c), 2404(d),(f), 2405(h), (i),(j),(k); *see also* 15 C.F.R. § 391.

100. 15 C.F.R. § 370 (Supp. 1).

101. *Id.* § 399.1(c).

102. *Id.* § 373.3(a)(1)(ii).

103. *See also id.* § 373.3(j).

modities were made in each country of their authorized reexport territories in one year preceding the application. This requirement does not apply to certain countries.¹⁰⁴ DLCs which fail to meet this requirement may still be approved for reexport territories by justifying specific levels of projected economic activity in the target countries.

DLCs may make temporary exports for exhibition or demonstration purposes to countries specifically authorized on their Forms ITA-6052P provided that additional certification is furnished.¹⁰⁵ DLCs may make permissive reexports under GLs *GLV*, for items of limited value, and *GTE*, for temporary reexport for demonstrations or exhibits.¹⁰⁶ Upon compliance with written assurance requirements, approved DLCs may also make temporary exports for exhibition or demonstration to certain countries outside their reexport territories.¹⁰⁷ DLCs may also seek authorization to make other specific reexports.¹⁰⁸ DLCs may reexport to any other DLC on the DL. However, certain commodities received under a DL may only be reexported to specifically approved consignee end-users.¹⁰⁹

An "end-user" DLC may reexport manufactured products incorporating United States commodities received under a DL to any DOC-approved destination listed in its Form ITA-6052P. An end-user usually will be authorized to reexport parts to service manufactured products that incorporate those parts if the volume of parts is reasonable and the end-user agrees to maintain records and to permit the DOC to audit those reexports.¹¹⁰

The DLC must notify its customers of United States restrictions on reexports through invoices sent to them. This notice is not required for shipments to retail customers, customers in certain countries unless there is a special condition on a license,¹¹¹ other approved DLCs, or governments.¹¹²

A "drop shipment" occurs when a DLC directs the DLH to ship directly to the DLC's customers within its territory. This is allowed by the regulations.¹¹³ Also, an approved DLC may request another DLC to

104. *Id.* § 373.3(d)(3)(iii)(D).

105. *Id.* § 373.3(d)(3)(ii)(C).

106. *Id.* §§ 373.3(j)(5), 374.2. This is available only to the United States registrant.

107. *Id.* § 373.3(j)(2)(iii).

108. *Id.* § 373.3(j)(4).

109. *Id.* § 373.3(j)(3).

110. *Id.* § 373.3(j)(1); *but see* Proposed Rulemaking, Revision of Controls on Foreign Products Incorporating U.S. Origin Parts, Components and Materials, 51 Fed. Reg. 24,533 (1986) (to be codified at 15 C.F.R. §§ 376.12 and 385.1).

111. 15 C.F.R. § 373 (Supps. 2, 8).

112. *Id.* § 373.3(j)(3)(iii).

113. *Id.* § 373.3(k).

ship directly to its customers.¹¹⁴ Payments for drop shipments may be made directly from the customer to the drop shipper. Both the drop shipper and the requesting DLC must retain copies of the applicable invoices.

Some items on the Nuclear Referral List are controlled to all CGs, and in some cases to Canada, but some items are controlled only to certain countries.¹¹⁵

The "Special Country Policies and Provisions" section provides for special treatment of some exports to the People's Democratic Republic of Yemen and Syria,¹¹⁶ Iran and Iraq,¹¹⁷ other CG T and V countries,¹¹⁸ and Canada.¹¹⁹

The regulations contain two lists of "Computer Consignee Destinations".¹²⁰ List A covers NATO countries, except Spain and Canada, and includes Australia, Japan and New Zealand. List B mainly contains countries which are signatories to the Nuclear Non-proliferation Treaty or a regional equivalent agreement. Some exports to countries in Lists A or B are subject to lesser controls.¹²¹ The regulations also list countries which have mutually agreed with the United States to assert controls acceptable to the United States over exports from their own countries.¹²² Lesser export controls are applied to countries on this list. Only Switzerland is now on this list. The Special Commodity Policies and Provisions section of the regulations may have CG or country export restrictions which apply to some commodities.¹²³

Shipments and reexports of commodities to India, Spain, Switzerland, (including Liechtenstein), and Yugoslavia must be accompanied by special International Import Certificates which provide for certified verifications of delivery. These certificates are issued by the government of the recipient country and confirm that the exported item was received in its territory and will not be reexported without the exercise of receiving country controls.¹²⁴ Other countries may require similar documents when certain commodities are exported to them.¹²⁵

114. This procedure may not be used for items listed in 15 C.F.R. § 373 (Supp. 4) unless authorization is specially provided.

115. *Id.* § 378.2(a).

116. *Id.* § 385.4(d).

117. *Id.* § 385.4(e).

118. *Id.* § 385.4(g).

119. *Id.* § 385.6.

120. *Id.* § 373 (Supps. 2, 3).

121. *Id.* §§ 399.1 (Supp. 1, group 5, ECCN 1565A, First Note), 378.2(a).

122. *Id.* § 373 (Supp. 8).

123. *Id.* § 376.

124. *Id.* §§ 373.3(h), (j)(1)(ii), 375.4, 375.5, 375.6, 375.7, 375.8, 375.9.

125. *See generally id.* § 375.3; *see also id.* §§ 375.3(b), 375 (Supp.1).

VII. DISTRIBUTION LICENSE ADMINISTRATION

The regulations provide instructions regarding the completion of DL export license applications.¹²⁶ The regulations require a prospective DL applicant to consult with the Multiple Licensing Branch of the DOC before making an application.¹²⁷ A DL application includes: (a) Form ITA-622P, Application for Export License;¹²⁸ (b) Forms ITA-6052P, Statement by Foreign Consignee in Support of Special License Application¹²⁹ and (c) a Comprehensive Narrative Statement (CNS).¹³⁰ The Statement by Foreign Consignee is not required for a DLC that is a foreign government or one of its branches except in the case of an institution of higher learning. The following applicable certifications should accompany the Statement by the Foreign Consignee: (a) existence of a DLC ICP; (b) notice restricting reexport; (c) temporary exports; (d) description of the scope of each DLC's activities under the DL; and (e) other required certificates including those concerning a DLC's promise to keep records and make them available to the DOC (Swiss DLCs, under Swiss law, may only agree to forward records on the request of the DLH or DOC, which DOC has determined to be an acceptable certification), a DLC's promise to comply with the regulations, and South Africa controls compliance where appropriate.¹³¹

A CNS describes an applicant's proposed utilization of the DL and includes the following five points.

(1) The CNS should include an overview of the proposed license, including the nature of applicant's business, the source of the commodities to be exported, the estimated annual DL export volumes, the primary activities of the various classes of proposed DLCs, and the anticipated volume of regular transactions between DLCs. The applicant should specify if the DL is to be used solely for distribution. The applicant should describe proposed manufacturing, assembly, testing, servicing and other activities. A detailed description of products to be exported may be made, which will sometimes speed the DL application processing. The applicant should indicate whether it or an affiliated entity currently has any other special multiple export licenses and, if so, the applicant should provide the applicable numbers and expiration dates.¹³²

126. See generally *id.* §§ 373.3(d), 373 (Supps. 5, 6), 375.

127. *Id.* § 373.3(d)(1).

128. *Id.* § 373.3(d)(2)(i). For additional completion instructions see *id.* §§ 372.4, 373.3(d)(3)(i), 373 (Supp. 5).

129. *Id.* § 373.3(d)(2)(ii). For additional completion instructions see *id.* §§ 373.3(d)(3)(ii), 373 (Supp. 6).

130. *Id.* § 373.3(d)(2)(iii).

131. *Id.* § 373.3(d)(3)(ii).

132. *Id.* § 373.3(d)(3)(iii).

(2) The CNS should also include a description of the DLC's activity and applicant/DLC relationships. The applicant should provide the volume of sales or other transactions with each DLC for the twelve months or calendar year preceding application. The applicant should also indicate its relationship with, and the proposed reexport territory for, each proposed DLC.¹³³

(3) The CNS should also include the applicant's certification that an ICP exists or is about to be implemented. This certification must specify any unimplemented elements established in the regulations and explain why the applicant believes they do not apply.¹³⁴

(4) The CNS should further include a justification, either by the applicant or by a proposed DLC, for the inclusion of each country in a reexport territory.¹³⁵

(5) Finally, the CNS should include the applicant's justification of the need for a DL and an explanation of why IVLs are unsuitable. This requirement only applies to applicants with three or fewer proposed DLCs.¹³⁶

The DLH may periodically file DL amendment requests to extend the DL's term, to add or delete DLCs, or for other reasons. Amendment requests should be filed on Form ITA-685P, Request For and Notice of Amendment Action.¹³⁷ Sometimes certifications or Form ITA-6052P must accompany requests. An extension by amendment may be granted.¹³⁸ A DLH unable to submit a timely renewal application may request a temporary extension by filing a Form ITA-685P. A DLH must submit an extension request at least ninety days before the scheduled expiration date.¹³⁹ Upon extension approval, DHLs must notify each of their DLCs of the new expiration date. Other required or permitted amendments are described in the regulations.¹⁴⁰

General instructions regarding export clearance and more specific DL export clearance guidance are found in the regulations.¹⁴¹

The regulations specify reporting requirements and records that must be maintained, including their retention periods, for the DL.¹⁴² All records must be made available for inspection by the DOC or repre-

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

137. *See generally id.* § 372.11; *see also id.* § 373(1)(3).

138. *Id.* § 373.3(1)(3).

139. *Id.* § 373.3(1)(3)(v).

140. *Id.* § 373.3(1)(4).

141. *See generally id.* § 386, 373.3(i).

142. *Id.* §§ 373.3(m), 387.13. *But see* § 386.3(r).

sentatives of the United States government.¹⁴³ Foreign laws may prohibit the inspection by United States government officials of the records in the country in which they are located. In such cases, a DLC must submit alternative arrangements acceptable to the DOC with its Form ITA-6052P¹⁴⁴. The regulations describe pre-license, post-license, and mini audits.¹⁴⁵

Violations of the Act are dealt with in the Act and the regulations.¹⁴⁶ Failure to report a violation under certain circumstances constitutes a violation.¹⁴⁷ The Act Amendments and the revised regulations add two violations. First, an attempt or conspiracy to violate or willfully evade compliance with the Act or the regulations and, second, the possession of goods or technology with the intention to violate export restrictions or with knowledge or reason to believe that the goods will be illegally exported are violations.¹⁴⁸

Violations of the Act or the regulations may result in criminal penalties administered by the United States Attorney General or civil penalties or fines administered by the DOC.¹⁴⁹ The Act Amendments and the revised regulations impose a new penalty. Property (or any interest in or proceeds derived from it) involved in an executed or attempted illegal export may be forfeited.¹⁵⁰ Demands for civil penalties and administrative sanctions are conducted in public hearings before an administrative law judge. The administrative law judge is authorized to issue recommendations to the Assistant Secretary of the DOC for Trade Administration. This Assistant Secretary determines and exercises the final decision.¹⁵¹

The Act Amendments gave statutory legitimacy to the TDO, but they limit its use to the prevention of "imminent violations".¹⁵² Some reports indicate that the DOC is experiencing increased difficulty in obtaining TDOs under the new Act provisions. TDOs may be issued initially on an *ex parte* basis, but may be appealed and may not be extended, or reextended, beyond a sixty-day effective period without a formal hearing.¹⁵³

The DOC enforcement agents have police powers, but now their

143. *Id.* § 373.3(m)(3).

144. *Id.*

145. *Id.* § 373.3(n), 387.13(f).

146. *See generally* 50 U.S.C. app. § 2410; *see also* 15 C.F.R. § 387.

147. 15 C.F.R. §§ 387.1(a)(1)(ii)(B), 387.4(a).

148. *Id.* § 387.1(a)(1)(ii)(A), (C).

149. *Id.* § 387(a)(1).

150. 50 U.S.C. app. 2410 (g), *see also* 15 C.F.R. 387.1(b)(4).

151. *See generally id.* 15 C.F.R. § 388.

152. 50 U.S.C. app. § 2412(d)(1); *See also* 15 C.F.R. § 388 (Supp. 3).

153. 50 U.S.C. app. § 2412(d)(1); *See also* 15 C.F.R. § 388.19.

territory is confined to the United States, exclusive of points of entry and exit, except for overseas audits.¹⁵⁴ The United States Customs Service has export control enforcement authority abroad and at points of entry and exit in the United States.¹⁵⁵

VIII. INTERNAL CONTROLS

The new emphasis on DLHs and DLCs establishing and implementing ICPs is a significant change to United States export control practices. In the past, DLHs and DLCs had to agree to abide by a number of compliance and "self-enforcing" requirements. The new regulations¹⁵⁶ augment and clarify this "self-enforcement" duty.

DLHs and DLCs know more about their product-lines and day-to-day exporting and distributing activities than any bureaucrat. Self-enforcement couples the DLH's and DLC's economic self-interest in the DL with self-administered control measures. These factors offer some hope that the current export controls will be more efficient and effective than earlier bureaucratically exercised measures. Costs to administer ICPs will be significant for both DLHs and DLCs and may be unbearably large for smaller DLHs and DLCs.

Each DLH, DLC and applicant is required to have an ICP, which is subject to DOC audits. The ICP is designed to ensure compliance with the regulations and the terms of the DL. The specifics of an ICP may vary, depending on circumstances. Factors that may influence the form and detail of any ICP include the twelve following items:¹⁵⁷

(1) The nature of the DLH, such as whether it is a manufacturer, a trading company, a purchasing agent, an original equipment manufacturer, or a systems integrator;

(2) Whether the reseller DLCs are independent distributors, subsidiaries of the DLH, sales agents, systems integrators, original equipment manufacturers or some combination of these;

(3) Whether the end-user DLCs are government entities, manufacturers, original equipment manufacturers, banks, other purchasers of capital equipment, or some combination of these;

(4) Whether the products shipped under the DL to the DLCs are for the DLCs' exclusive use, resold to retail customers, resold to manufacturers or original equipment manufacturers for their use, incorporated into new products manufactured for resale, used as support

154. 50 U.S.C. app. § 2411(a)(3)(A).

155. *Id.* § 2411(a)(2)(A).

156. 15 C.F.R. § 373.3(e), (g).

157. See UNITED STATES DEPARTMENT OF COMMERCE, Export Management Internal Control Guidelines for U.S. Exporters and Foreign Consignees, at 4 (September 1985) [hereinafter Guidelines].

equipment for foreign equipment which is resold, used for servicing other equipment, warehoused for further distribution, some combination of these or used in some other manner;

(5) Whether DLCs are located in certain countries;¹⁵⁸ in other CG T or V countries, excluding Afghanistan, Iran and the People's Republic of China; or in some combination of these;

(6) Whether the products exported under the DL are software, production materials, parts or components, or end-use items for retail consumption or use by the DLC;

(7) Whether the products exported under the DL are from the DLH's own manufacturing facilities (and whether from one or more locations), or whether they are purchased from manufacturers, or from distributors;

(8) Whether the products exported under the DL are authorized for export/reexport to all destinations, authorized for export/reexport subject to certain restrictions,¹⁵⁹ restricted for export/reexport only to pre-approved end-users, potentially usable in nuclear applications, potentially usable for the surreptitious interception of wire transmissions, or aircraft parts and accessories restricted for export/reexport to certain destinations;

(9) Whether the DLCs may only dispose of the products shipped under the DL in their individual approved sales territories; reexport the products only to other approved DLCs or to certain countries;¹⁶⁰ reexport to certain countries¹⁶¹ may reexport the products to South Africa and/or Namibia; reexport the products to India, Switzerland or Yugoslavia; or engage in some combination of these reexport activities;

(10) Whether the DLH and DLCs have a contractual relationship, a corporate relationship where one is controlled-in-fact by the other, some other relationship, or some combination of these;

(11) Whether the product is exported from a United States manufacturing site or sites, from an off-shore manufacturing site or sites or from both and whether the products are shipped directly to end-users, to DLCs, or to both; and

(12) Whether orders are received at one United States location, several United States locations, at a regional international sales offices, a single overseas headquarters, or some combination of these, and whether records are maintained at one or several locations.

The form of a DLH's export control function depends upon the size

158. See specifically, those countries listed in 15 C.F.R. § 373 (Supp. 2, 3).

159. See 15 C.F.R. § 373 (Supp. 1).

160. See those countries listed in 15 C.F.R. § 373 (Supp. 2).

161. See those countries listed in 15 C.F.R. § 373 (Supp. 3) and those countries *not* listed in either 15 C.F.R. § 373 (Supp. 2) or § 373 (Supp. 3).

of the DLH, its organizational structure, the nature of its distribution network, and the type and variety of products it distributes. Centralized export control functions may be appropriate for larger DLHs. These larger DLHs must have trained export control personnel in each location where orders are accepted or where commodities are shipped who will oversee daily operations and verify that all shipments are licensed properly and have complete export documentation. Smaller DLHs may delegate export control functions to an export related department. The export control function should never be assigned to or report to a DLH's marketing or sales departments. The DLH's export control unit should be responsible for all aspects of export policy, procedures, training, and compliance and control, not just those under the DL. The export control unit should be placed at an appropriate level within the organizational structure. It must be headed by a person with sufficient authority to make final decisions and to lend credence to the DLH's commitment to export compliance.

Audits should be regular and should conform to an established auditing procedure suited to the DLH's organization and export practices. Audits may be performed by persons inside of or independent from the DLH. All audit reports should be submitted to, and be evaluated, by all key personnel in the DLH's export control function.

Even if outside consultants develop the ICP, the DLH must participate actively in its preparation. The ICP must be incorporated into written manuals and be oriented toward the specific products, country and customer markets, and procedures of the DLH. The manuals must specify which persons or positions are responsible for precise export control procedures.

Each DLH and DLC must have standard policies and procedures to review new DLCs and customers and to develop profiles on them before approving new sales orders or adding them to the DL. A customer or DLC profile assists a DLH or a DLC in evaluating the nature of a DLC's or customer's business, in evaluating the legitimacy of the DLC or customer, and in evaluating the risk of diversion in selling to the new DLC or customer. Information relevant to a DLC or customer profile may include: names of all DLC or customer principals or owners; end-user information such as their names, names of their principals and nature of the end-users' businesses; the intended use of the commodity; the legal organizational structure of the DLC or customer; the financial solvency of the DLC or customer; and references supplied by the DLC or customer of other United States suppliers or local customers.

DLCs should be active customers with a close and established relationship with the DLH and should not be added to a DL for "one-time" or infrequent orders. Also, DLHs and DLCs should review existing DLC or customer profiles periodically to confirm the continued accu-

racy of the data; that principals or owners of DLCs or customers do not appear on TDOs; that changes in ownership, control or financial stability of DLCs or customers have been properly evaluated; that customer and field service information has been checked to verify the location of equipment and its current end-use; and that the previous twelve months' business activity with the DLC or customer has been analyzed. Irregularities or unexplained anomalies discovered during these reviews should be reported to upper management, which should advise the DOC of unresolved questions.

DLH and DLC contracts should contain specific clauses on export compliance, including compliance with United States export regulations, submission to audits or reviews by the DLH and/or the DOC, abstention from doing business with parties deemed by the DOC and notified to the DLC as being unsuitable, and the right of the DLH to refuse performance under the contract in the event of the DLC's non-compliance with export control requirements or restrictions. Such contracts and clauses are not required when the DLH and DLC are organizations controlled-in-fact by one another.

The DOC published a detailed booklet dated September 1985, entitled, "Export Management Internal Control Guidelines For U.S. Exporters And Foreign Consignees" ("Guidelines"), through its Multiple Licensing Branch. The DOC states that this publication is to assist DL participants and is not a "model program." Common sense, however, dictates that a regulated industry should probably take the "suggestions" of its regulating agency as setting the minimum acceptable ICP standards unless particular requirements clearly do not apply. Special circumstances may require DLHs or DLCs to have different or more thorough ICPs than provided in the Guidelines. If any element of an ICP is not implemented, the DLH must advise the DOC through the DLH's CNS. The DLH must state why the element does not apply.

IX. A DISTRIBUTION LICENSEHOLDER'S INTERNAL CONTROL PROGRAM

Unless an element clearly does not apply because of a DLH's special circumstances, a DLH's ICP must include at least the following thirteen elements.

(1) The ICP must include a clear statement of the DLH's policy which must be communicated to all levels of the DLH involved in export sales, traffic and related functions, which emphasizes the importance of compliance with the DL and the regulations.¹⁶²

The statement must be issued by the highest management levels af-

162. *Id.* § 373.3(e)(1)(i).

ter consultation with and upon the advice of the DLH's export administrator. The statement should emphasize the enforcement actions the DOC may take in the event of noncompliance. The policy statement should be disseminated to all levels of the DLH and be reinforced through programs of continuing education. The policy statement should be promulgated at new employee orientation, distributed through in-house publications, and given a prominent position in training and procedure manuals. The training and procedure manuals should be distributed within the DLH sections that deal with exports, domestic and international sales and marketing, customer service, contracts, finance and accounting, legal affairs, field services, export administration, order entry, shipping, traffic and engineering. The DLH should consider distributing these training and procedure manuals to all DLCs as well. The corporate policy statement should include detailed instructions that no sales will be made contrary to United States export regulations, that any questions regarding the propriety of a transaction should be referred to the export administrator (whose name, title and phone number should be given), and that all violations or possible violations of United States export regulations that come to the attention of an employee should be reported immediately to the named export administrator.

(2) The ICP must include the identification of positions in the DLH and the DLCs responsible for DL compliance. Also, updated lists of persons occupying those positions should be distributed.¹⁶³

Information regarding the individual in the DLH organization responsible for compliance with the requirements of the DL should be communicated throughout the DLH organization. Overall responsibility for compliance should be at the highest level possible in the DLH. The position and person selected as the DLH's export administrator must be granted sufficient authority to exercise final approval over all DLH export transactions. DLCs should be encouraged to direct questions or problems to the export administrator. The position should continue to function despite personnel changes. The person and position responsible for compliance must not be in the DLH's sales or marketing operations. If possible, the export control function should be centralized and have direct contacts and reporting relationships with related departments. If order processing is not centralized, frequent audits and reviews are essential. In a large company where each division is responsible for its own DL, each division may maintain records separately under general corporate control.

The export control organization of the DLH must have the authority and responsibility to submit export license applications, develop the

163. *Id.* § 373.3(e)(1)(ii).

ICP and related DL procedures, coordinate the export related activities of the DLH and monitor the export control activities of the DLCs. An organizational chart that includes names, titles, and telephone numbers and describes various levels of export compliance responsibility should be developed and distributed throughout the DLH organization and to all DLCs. This chart should also be included in training manuals. Detailed policies, procedures and job descriptions of the export control organization should be formalized to ensure clarity in the identification of responsibilities and smooth transition during personnel changes.

(3) The ICP must include a system for timely distribution to DLCs (with verification of receipt) of TDOs, the list (where appropriate) of South African entities enforcing apartheid, and other regulatory materials necessary to ensure compliance.¹⁶⁴

The export administrator should be responsible for ensuring that all regulation updates or revisions, TDOs, Forms ITA 6052P, required transmittal letters, changes in DLH's operations or products, and other appropriate documents are forwarded to DLCs on a timely basis. Both the DLH and the DLC should record the transmission of these documents to reflect the documents sent, dates mailed, and recipients. Receipt verification may be by telex, form response letter, or a registered mail record of delivery. The DLH must keep proof of verification on file. The DLC must keep copies of verifications and the transmitted data on file.

(4) The ICP must include a methodology for screening orders from and shipments to customers covering servicing, sales of commodities, software sales, and training against TDOs.¹⁶⁵

The export administrator must specify the points at which screening occurs and the exact documentation procedures to be followed. All departments dealing with DLCs must ensure that each transaction is screened. If the DLH does not know the ultimate end-user's name, the DLH must assure that the DLC screens the ultimate end-user against the TDO. For certain high value systems or sensitive technology, a DLH should consider requesting the name of the ultimate end-user with each order. Screening may occur when contact is made with the prospective customer, when the order is accepted by the DLC and/or the DLH, when the order is received by the DLH, and/or when the order is shipped. Rescreening of back orders more than thirty days old or those orders submitted prior to TDO updates is essential. Fully-trained employees who understand the importance of the screening procedure must screen every order before shipment is made. The screening procedures will include: comparing current world-wide TDOs against receiv-

164. *Id.* § 373.3(e)(1)(iii).

165. *Id.* § 373.3(e)(1)(iv).

ing entities, known ultimate end-users, and the principals of receiving entities or known end-users at each location where sales, service and training orders are received; recording the screening verification signed by an employee for each order; screening the backlog of aging orders; regularly reviewing screening procedures to ensure that they are being followed; and notifying the DLH's management and the DOC of all names on TDOs found during the screening process.

(5) The ICP must include a system for ensuring compliance with product and country restrictions, including controls over reexports by DLCs and over direct shipments to DLCs' customers.¹⁶⁶

The system should assure that only commodities authorized under the DL are shipped or transferred and then only to authorized destinations and end-users. A procedure to check product technology must be incorporated into the order entry system. The DLH's order administrator must perform and document the procedure. The system must ensure that shipments do not contravene the restrictions on commodities found in the DL or the regulations.¹⁶⁷ To assure that products exported individually or collectively under the DL do not exceed, or upgrade previously exported equipment above, permitted levels for export or reexport destinations, a product technology matrix identifying the types of commodities eligible for specific destinations under the DL procedure must be a part of a DLH's formal procedure manual.¹⁶⁸ Larger DLHs may elect to use automated order entry system procedures. An order entry system should include hold functions for shipments requiring IVLs. A manual back up system is desirable if the DLH deals with sensitive or potentially targeted commodities and Technical Data. An appropriate management level must perform the order entry system technology review. This review will incorporate records of signed employee compliance verification; assure that only commodities authorized on the DL are shipped under the DL; assure that shipped product technology levels do not exceed those permitted for export or reexport destinations; and assure that items not permitted to be shipped under the DL, whether generally or to specific destinations, end-users or end-uses, are identified and shipped under other export licenses. The DLH must be satisfied that each DLC understands DL reexport restrictions and implements adequate screening procedures to assure compliance with those restrictions. Drop shipments by the DLH at the DLC's request must be screened to ensure compliance with the DL restrictions on commodities, end-users, end-uses or reexport territory destinations.

(6) The ICP must include an internal audit system or compliance

166. *Id.* § 373.3(e)(1)(v).

167. *See id.* § 373.3(b).

168. *See Guidelines, supra* note 157 at Attachment A.

review program for the applicant or DLH, which extends to all DLCs.¹⁶⁹

The DLH should make a special review of foreign subsidiaries, such as overseas headquarters, which are decision-making centers. The DLH must audit independent DLCs unless the DOC specifically approves other arrangements. Sometimes, audits of DLCs are most effective when performed in conjunction with scheduled on-site training. Auditing includes the daily supervision of export-related staff, particularly when manual review systems are employed. Audits should include both spot-checks and regularly scheduled audits. The person who assesses export compliance quality control should not be involved in daily export functions. The compliance review staff should be independent of, and should not directly report to, persons with line export management responsibilities. Supervision and audits of DLCs should assure that DLCs have developed and implemented complying ICPs. DLCs approved on two or more DLs may need to develop different controls for each DL because specifics, such as reexport authorization and product restrictions, may vary between DLs. Such DLCs should provide their DLHs with information on their various ICPs and audit programs to avoid multiple audits, compliance review requests, TDO distributions, and education programs. The details of an ICP and the rigor with which it is implemented must be commensurate with the technology levels of the products shipped under the DL and the DLH's type of business. Audits must verify compliance with recordkeeping requirements; including maintaining on file a copy of the current regulations; the current validated Form ITA-628P; the correct and timely submissions of amendments advising the DOC of substantive changes; updated TDOs; current validated Forms ITA-6052P; and Indian Import Licenses, Spanish entrance verification certificates, Swiss Blue Import certificates, and Yugoslav End-use certificates (including applicable supplemental end-use statements and quarterly reports). The audit should also review other required documents, such as transmittal letters and acknowledgments; records of all export transactions (including shipping documents, purchase orders, invoices, contracts and other pertinent records such as proper destination control statements on invoices and air waybills); current product matrices at appropriate sites; documented TDO, nuclear and product technology screening checks; written procedures for processing orders, IVLs, reexports, and drop shipments; required certifications that an ICP is in place, an internal control manual; records of training programs; a chart of the organization naming persons and defining positions assigned export control functions (including written updated records of names of persons in DLCs responsible for the

169. *Id.* § 373.3(e)(1)(vi).

administration and implementation of the ICP if different than the person signing in Item 9 of Form ITA-6052P); records of the location of, and ability to locate, sensitive equipment at end-user sites; customer and product lists; records of DLC training; records of all ICP communications to DLCs; and written procedures for correcting deficiencies discovered during audits.

Internal auditing techniques should include flow-charting the order processing system, interviewing export-related personnel, inspecting all required export-related documents, analyzing sample transactions, reviewing the ICP and procedures manual, checking for all sign-offs for TDO and nuclear screening, obtaining product and customer breakouts to identify the focus of the audit, reviewing customer and product lists against TDOs and suitability for shipments under a DL, and implementing a system for correcting discrepancies or violations discovered and or reported to management.

(7) The ICP must include a system for assuring compliance with the limits on delivery of commodities to nuclear end-uses and end-users.¹⁷⁰

The export administrator must establish a procedure to comply, and to document compliance with, nuclear restrictions. If the DLH does not know the names of end-users and cannot, consequently, screen for nuclear end-uses, the export administrator must provide adequate training and guidance to DLCs. The DLH should ensure that checks are performed and documented thoroughly by the DLC. The efforts of certain countries to obtain equipment secretly for nuclear end-uses may require special DLC training in determining customers' end-uses. The DOC and the DOE have prepared sample nuclear end-use checklists to assist compliance.¹⁷¹

(8) The ICP must include a continuing program to inform and educate the appropriate DLH, applicant and DLC personnel in the applicable regulations, limits and restrictions of the DL procedure.¹⁷²

The DLH's export administrator must develop formats and schedules for training programs. Persons from the DLH's training department or other qualified personnel will teach the training programs. Training will be provided to all personnel in export related departments and will be specially formulated for each audience. It may be necessary to develop different training programs for different groups of trainees. Each appropriate employee will receive training at various times including during orientation training, refresher courses, and peri-

170. *Id.* § 373.3(e)(1)(vii).

171. See Guidelines, *supra* note 157, at Attachments B, C.

172. 15 C.F.R. § 373.3(e)(1)(viii).

odic training necessitated by changes in the regulations or the DLH's policies or procedures.

The orientation training program must review the written procedures manual. This manual should include a description of the DLH's export control organization structure, requirements of the regulations, the DLH's procedures, and a description of DLH's products to be exported (with product restrictions stated in terms of series and model numbers of products exceeding permissible parameters, not just in terms of technical measures). The orientation program must also instruct the employees on sections of the regulations, not just those dealing with the DL.

Orientation training may be conducted by persons or organizations outside the DLH. The frequency of orientation training depends upon the personnel turnover of the DLH. Refresher courses and update sessions should be held frequently to keep pertinent employees apprised of changes and to reinforce earlier training. Refresher courses should include an overview of the purposes and scope of export controls, a review of license types and requirements, and a description of destination and commodity restrictions. The refresher course should also review the required order processing checks such as TDO, nuclear end-use and commodity technology review checks and sign-offs. Procedures concerning reexports and drop shipments, new customer review procedures, and new employee training should also be covered by the refresher course. A DLH's written procedures and the regulations should be available to relevant employees for consultation and reference. Employees should also know who to contact for answers to their questions. To ensure continuity of qualified export control personnel and to avoid interruption during personnel changes, these courses should be given with sufficient frequency and thoroughness.

(9) The ICP must include a program for DLHs to screen and identify relevant customers with a high diversion risk profile which are scheduled to receive drop shipments.¹⁷³ At a minimum, the program should screen:

- (a) Small or little-known customers for which financial information and identification of principals is not available from normal sources;
- (b) Customers unwilling to use normal installation and maintenance services;
- (c) Customers reluctant to provide end-user/end-use information;
- (d) Customers that request atypical payment terms or currencies;

173. *Id.* § 373.3(e)(1)(ix).

(e) Customers that request order amounts, packaging or routing at variance with normal industry practice;

(f) Customers that request commodity performance or design characteristics inappropriate for their businesses or stated end-uses;

(g) Customers that use only Post Office Box addresses or use facilities inappropriate for the commodities shipped;

(h) Customers that order parts known to be inappropriate or for which the customer appears to have no legitimate need; and

(i) Customers known, or suspected of having, unauthorized dealings with parties and or destinations in sensitive CGs or countries.¹⁷⁴

The DLH must establish diversion risk screening procedures for all drop shipments and provide these procedures to DLCs to ensure adequate control. The content of the screening procedures depends upon the nature and technology level of the commodity and its destination. The level of screening scrutiny should be in direct proportion to the technology level of the products shipped. If any unresolved uncertainty results from the diversion risk screening, the DLH should contact the DOC for further information. DLCs should not ship to identified high-risk customers before advising, and receiving approval from, their DLH. DLHs unable to authenticate identified high-risk customers should submit a written request to the DOC for information on the customer. For high technology level products, a supervisor should document the sign-off for diversion risk screening compliance. In addition to screening the recipient and order for risk of diversion, the DLH should check to confirm compliance with all the requirements of the regulations¹⁷⁵ for drop shipments.

(10) The ICP must include a program to satisfy the regulation's recordkeeping requirements.¹⁷⁶

The export administrator shall consult with other persons in the DLH export related departments to establish clear procedures on where, how and by whom records are to be kept. Instructions on the maintenance of records, including procedures to be followed and information to be maintained, should be thoroughly understood by and disseminated to the DLH's export related departments. Once established, the departments are responsible for compliance, accuracy and completeness. All records must be readily available for inspection. The DLH should consider establishing a centralized recordkeeping system for export control purposes. Minimally, the DLH's recordkeeping must permit the ready matching of invoices and Shipper's Export Declarations.

DLCs should be advised clearly of the recordkeeping require-

174. *Id.* § 373.3(e)(1)(ix)(I).

175. *Id.* § 373.3(k).

176. *Id.* § 373.3(e)(1)(x); *see also id.* § 373.3(m).

ments.¹⁷⁷ The records DLCs must maintain depend upon the nature of their businesses and whether they are classified as resellers or end-users.

The records to be maintained include: (a) a current copy of the regulations; (b) a current VL and CNS; (c) copies of transmittal letters and receipt verifications sent with validated Forms ITA-6052P, TDOs accompanied by the required explanation, and nuclear end-use restrictions; (d) copies of Indian Import Licenses; (e) copies of Spanish Entrance Verification Certificates; (f) copies of Swiss Blue Import Certificates; (g) copies of Yugoslav End-Use Certificates with supplemental end-use statements; (h) reports on partial shipments for Indian, Spanish, Swiss and Yugoslav orders; and (i) internal control documents. Documentation and filing procedures should permit the timely retrieval of the purchase order, invoice, bill of lading, air waybill, Shipper's Export Declaration, letters of special authorization, telexes and any other relevant correspondence relating to a transaction. Correct destination control statements must appear on each invoice. Correct license numbers must be referenced appropriately on all documents. The drop shipment provisions must be followed where and as appropriate.

(11) The ICP must include an order processing system affixing responsibility for all required internal control reviews.¹⁷⁸

The DLH's export administrator should determine, establish, implement and assure compliance with the mode and frequency of review procedures. All order processing checks should be recorded and should be verifiable during an audit. These include screening against TDOs, screening for nuclear end-uses, checking product technologies, processing reexports and approving drop shipments. A supervisor should document and sign off on all special transactions. Special transactions may include drop shipments, upgrades which approach or exceed product restrictions, reexport transactions, shipment of commodities authorized to certain countries under the DL,¹⁷⁹ shipments of commodities restricted to pre-approved customers,¹⁸⁰ and shipments requiring an IVL. Whether the order processing system is manual or automated, it should have hold functions which ensure adherence to sign-off procedures and prevent the preparation of commercial invoices and shipping documents prior to review and sign-off. Each individual must be held accountable for those orders he or she processes.

(12) The ICP must include a system to monitor intransit ship-

177. *Id.* § 373.3(m).

178. *Id.* § 373.3(e)(1)(xi).

179. *See id.* § 373 (Supp. 2).

180. *See id.* § 373 (Supp. 4).

ments and shipments to bonded warehouses and Free Trade Zones.¹⁸¹

Commodities not originally manifested to the country of unloading are intransit.¹⁸² Intransit shipments must show an intermediate consignee in a destination other than the country of ultimate destination, except in the case of CGs Q, S, W, Y and Z, on the Shipper's Export Declaration. Goods unloaded from a vessel or aircraft in CGs Y or Z, or transshipped through Y or Z while enroute to Canada or to CGs Q, S, T, V or W, require a VL specifically authorizing such transshipment. A VL is not required, however, if the commodities are transshipped through East Germany to West Berlin or are items not having ECCN code letters A, B or M and are exportable to CG Y or Z countries under a GL.¹⁸³ Commodities intransit through Canada from the United States enroute to other destinations are subject to other regulations.¹⁸⁴ Furthermore, goods shipped with optional ports of unloading are subject to other regulations.¹⁸⁵ The United States exporter remains responsible for the shipment until it is received by the DLC. A drop shipment export is not considered an intransit shipment.

A United States exporter of commodities from a Foreign Trade Zone continues to be responsible for the commodity until it is accepted by a DLC. A DLC is in turn responsible for commodities it accepts in a Foreign Trade Zone. It is essential that the CNS and/or Form 6052P clearly indicate whether the commodities shipped under a DL will be off-loaded at a Foreign Trade Zone. This is particularly important if the commodities have substantial "value-added" in the Foreign Trade Zone or if they lose their original identity with respect to form and are no longer considered to be of United States origin. This enables the DOC to make a correct determination concerning the nature of the DLC's business. The regulations require specific documentation of goods exported from Foreign Trade Zones.¹⁸⁶ Commodities originating in Canada or sold by the United States Government as foreign excess property and exported from a Foreign Trade Zone may require VLs under certain conditions.¹⁸⁷ If a DLH places commodities in a bonded warehouse for its own stocking purposes, only the DLH may withdraw the commodities from bond. A DLC that places commodities in a bonded warehouse is responsible for them and may dispose of the commodities only in accordance with its validated Form ITA-6052P.

Appropriate records must be maintained for all intransit shipments

181. *Id.* § 373.3(e)(1)(xii).

182. *See* Guidelines, *supra* note 157, at 31.

183. *See id.* §§ 370.9, 371.2(c)(2), 372.8(b).

184. *Id.* § 386.1(d).

185. *Id.* § 386.3(k). *See also* §§ 376.9(c)(4), 386.5(a)(3)-(5).

186. *Id.* § 386.3(p)(2).

187. *Id.* § 370.6(c), (d).

and shipments to a Foreign Trade Zone or bonded warehouse. Agents or employees of the responsible party must monitor goods in Foreign Trade Zones. The DLH's export control personnel must screen intermediate consignees and their principals against TDOs, (generally a bonded warehouse is an approved consignee subject to certain restrictions on its Form ITA-6052P and must maintain records) must ensure Shipper's Export Declarations are properly prepared, must ensure proper documentation is on file with DOC, must know that commodities shipped into bond by a DLC in Switzerland are subject to Swiss Blue Import Certificate requirements, and must know that commodities exported under a DL may not be shipped through or via countries other than CGs T or V without the prior written approval of DOC. The ICP should particularly guard against the unauthorized disposition of more sensitive commodities, because many foreign governments assume no responsibility for intransit or bond shipments through, to, or from their countries.

(13) The ICP must include a system to notify the DOC promptly if the DLH has knowledge that a DLC is not complying with the DL's terms.¹⁸⁸

The DLH's export administrator must ensure that relevant employees of all of the DLH's departments that deal directly with DLCs are clearly instructed to report any violations or indications of noncompliance by DLCs to the DLH export control organization. The export administrator must timely report any such violations or suspicious transactions to the DOC. The DLH should periodically review its business relationship with each of its DLCs and confirm the continued accuracy of its information on the principals, ownership and financial solvency of each of its DLCs. If the DLH terminates a relationship with a DLC, the DLH should timely notify the DOC. If the DLC's noncompliance with the regulations caused the termination, written notice of noncompliance must be sent to the DOC's Office of Export Enforcement.¹⁸⁹

X. DISTRIBUTION LICENSE CONSIGNEES' INTERNAL CONTROL PROGRAMS

Each approved DLC must certify that it has an ICP. The DLC's ICP is subject to DOC audits. The elements of the Guidelines' DLC ICP are common to it and the Guidelines' DLH ICP. These elements will be defined by many of the DOC comments in the analogous elements of the previous DLH ICP section. These will not be repeated in this section. DLHs should identify applicable comments and explain

188. *Id.* § 373.3(e)(1)(xiii).

189. *Id.* § 373.3(1)(4)(ii).

them to their DLCs. The ICPs of the DLH and its DLCs should complement each other. The DOC must assess the effectiveness of ICPs by considering how ICPs of a DLH and its DLCs are mutually reinforcing. The DLH should establish a comprehensive program for all its DLCs. If the DLH is unable to review the ICP of a particular DLC, the DLH must make other arrangements acceptable to the DOC. Every DLC does not require an ICP that includes each element in the Guidelines. DLCs that are agencies of foreign governments and classified as end-users are not required to develop and implement an ICP. Whether a DLC is classified as an "end-user" or a "reseller" greatly affects the DL internal control obligations imposed on the DLC. Because DLCs unrelated to and independent of the DLH are less influenced by the DLH than controlled-in-fact DLCs, DLHs should screen such DLCs' reexport territories and shipped product technology levels more carefully and should ensure the effectiveness of such independent DLCs' ICPs.

A DLC's ICP will include at least the following ten elements, unless certain elements clearly do not apply under a DLC's special circumstances.

(1) The ICP should include a statement of DLC policy, communicated from the DLC management to DLC employees, directing compliance with the regulations as they apply to DLs.¹⁹⁰

Similar to the ICP element for DLHs, this is particularly important for foreign DLCs where employees may neither support nor take seriously the aims of United States export controls.

(2) The ICP should include the maintenance of a current list of DLC employees charged with export compliance responsibilities.¹⁹¹

This element is essentially the same as the analogous element for a DLH ICP.

(3) The ICP should include a system to screen hardware, software, training and servicing transactions against updated TDOs provided by the DLH.¹⁹²

Screening must extend to all aspects of DLC activity, including hardware and software sales, training offered to customers, and servicing. Screening of the principals of customers is essential, particularly for significant orders or major accounts. TDO updates should be screened against existing orders and customer bases as well as against backlog orders, new orders and new customers. Screening should occur when the order is taken, when the order is received at order entry, and before the product is released. Many foreign DLCs maintain separate

190. *Id.* § 373.3(e)(2)(i).

191. *Id.* § 373.3(e)(2)(ii).

192. *Id.* § 373.3(e)(2)(iii).

customer bases for their various sales functions. Where possible, consolidated customer bases should be used for screening.

(4) The ICP should include a system to assure compliance with the product and country reexport restrictions on the Form ITA-6052P and compliance with the restrictions on the export of products incorporating commodities received under the DL.¹⁹³

For DLCs classified as resellers, reexports are permitted only to destinations authorized in its Form ITA-6052P. Shipment invoices by the DLC to many customers outside certain destinations must comply with the notice requirement.¹⁹⁴ Reseller DLCs with a wide range of commodities and a variety of authorized reexport destinations are advised to use automated screening techniques. Manual product and country matrices are probably satisfactory for DLCs with low volumes or limited product lines. The DLC's ICP manual should incorporate such matrices and should be made available to all employees having export compliance responsibilities. For DLCs approved on two or more DLs, the DLC must take special care to match varying product and country restrictions on the different DLs with the appropriate shipment. This element does not apply to DLCs which sell only within their home country sales territory and do not reexport. Nonetheless, a system to advise their customers who are known reexporters of applicable reexport restrictions may be desirable.

DLCs classified as end-users must list for DOC the countries to which they propose to export commodities. Certain technology level country restrictions¹⁹⁵ do not apply to these export transactions. The DLC's screening only needs to confirm that the recipient country is authorized on the DLC's Form ITA-6052P.

Reexport transaction files must display the names or initials of persons performing the product technology and country screening functions. Before a DLC makes a drop shipment to customers of other DLCs in other countries, the shipping DLC must confirm that the customer is within the sales or reexport territory of the requesting DLC, the commodity is authorized for shipment to the requesting DLC, the commodity is authorized for shipment to the requesting destination or customer, and the commodity does not exceed country technology parameters.

(5) The ICP should include a system for complying with nuclear restrictions under DL procedure.¹⁹⁶

The DLC that resells commodities received under a DL must deter-

193. *Id.* § 373.3(e)(2)(iv).

194. *Id.* § 373.3(j)(3)(iii).

195. *See* restrictions in 15 C.F.R. §§ 373.3(b)(2), 373 (Supp. 4).

196. *Id.* § 373.3(e)(2)(v).

mine whether its customer's proposed end-use involves restricted nuclear end-uses. Attachment C to the Guidelines provides a sample nuclear screening guideline and questionnaire. DLCs need to know their customers' businesses, since the customers' names may not reflect their nuclear activities. DLCs dealing in commodities known to have direct nuclear applications and/or in transactions outside certain countries¹⁹⁷ must make nuclear screening a priority. DLCs' questions concerning whether a particular customer is engaged in sensitive nuclear activities should be addressed in writing, directly or through its DLH, to the DOC's Multiple Licensing Branch.

(6) The ICP should include an internal audit program to verify DLC compliance with its ICP.¹⁹⁸

All DLCs must develop effective internal audit programs and are subject to audits by their DLH. The nature of the DLC and its activities under a DL will determine the content, frequency and scope of the DLC audit activities. Persons in or outside the DLC not associated with departments or persons responsible for establishing or administering the ICP should perform the audit. An ICP audit requires a thorough knowledge of the DL procedures and the regulations. Except for very small DLCs, audits should follow a formal audit sequence and procedure. For large or high diversion risk DLCs, annual audits may be required. For other DLCs, audits every two years will probably be sufficient. Audits are intended to identify and rectify potential ICP weaknesses. The DOC treats violations discovered at a DLC with an inadequate audit program appropriately in determining administrative actions to be taken against the DLC.

(7) The ICP should include an education program for DLC employees that process transactions for products received under DLs.¹⁹⁹

A continuing education program in DL procedures and the regulations for employees is more important in the case of foreign DLCs. The DLC export control coordinator will generally conduct the education program.

(8) The ICP should include a process for screening customers against the diversion risk profile described earlier.²⁰⁰

If definite negative screening risk profiles are discovered, a hold should immediately be placed on a transaction until uncertainties are resolved. If discovered negative risk profiles are not conclusive, a decision to hold is subjective and will usually be predicated on the triggering of more than one such negative risk profile factors. A DLC's

197. See countries listed in 15 C.F.R. § 373 (Supps. 2, 3).

198. *Id.* § 373.3(e)(2)(vi).

199. *Id.* § 373.3(e)(2)(vii).

200. *Id.* § 373.3(e)(2) (viii).

screening can most effectively be performed by thoroughly knowing its customers. If a DLC doubts the legitimacy of a transaction, the DLC should contact the DLH export administrator or the DOC directly. Questions to DOC should include the circumstances which generated the questions.

(9) The ICP should include the required recordkeeping and reporting system.²⁰¹

Reseller DLCs must retain certain records described in the regulations.²⁰² End-user DLCs do not have to keep records of components incorporated into a foreign end-product but such DLCs that sell components for servicing under DOC authorization must maintain records. If a DLC acts as both a reseller and an end-user, the DLC should maintain the appropriate records for each role. Records of transactions involving countries other than the DLC's home country must be maintained in accordance with the reexport provisions.

(10) The ICP should include an order processing system that documents the employee clearance of transactions in accordance with the applicable internal control elements above.²⁰³

Transaction files should contain written, named employee sign-offs for each required check. Someone other than the action employee should regularly confirm performance of this procedure.

XI. RECENT ACTIONS, EXPECTED DEVELOPMENTS, AND CONCLUSIONS

More changes in the regulations are expected from the DOC in coming months. These may include a much-needed change of the regulations' methodology of reference to a decimal system.

Under a Bill submitted to the United States House of Representatives in late 1986 by Rep. Don Bonker of Washington, major elements of which were incorporated into H.R. 4800 and passed by the House, shipments to the People's Republic of China would be permitted under a DL, reexports of multilaterally controlled United States items from CoCom countries would not be subject to prior United States authorization, reexports of United States parts and components would be subject only to *de minimis* restrictions, "Foreign Availability" would be defined more broadly, and the number of controlled commodities would be halved within three years. This Bill was not passed by the Congress, but it reflects the Congress' concern regarding the impact of export controls on the volume of United States export trade. Similar provisions may be included in a trade bill expected to be enacted by Congress in

201. *Id.* § 373.3(e)(2)(ix); see also *id.* § 373.3(h),(m).

202. *Id.* § 373.3(m)(2).

203. *Id.* § 373.3(e)(2)(x).

1987. The National Academy of Sciences recently issued an analysis of the effectiveness and costs of United States export controls, which was generally damning of current United States export control laws and practices, ascribed a huge cost to the U.S. economy of the misapplication or maladministration of these controls, and will provide a great impetus for easing export controls in the next Congress.²⁰⁴

The new export regulations for DLs have significantly changed the manner in which an exporter may seek and use a DL. In particular, the new ICP requirement for DLHs and DLCs places a heavy financial and administrative burden on exporters and consignees to formulate and implement these ICPs. It remains to be seen how effective the ICP method of controlling exports will be and how costly the implementation of ICPs will be for DLHs and DLCs. DOC's exercise of denial rights for new and renewed DLs has not been as severe as had once been expected and DL issuance and renewal practices have not dramatically changed under the new regulations.

204. NAT'L ACADEMY OF SCI., *Balancing the National Interest, U.S. National Security Export Controls and Global Economic Competition* (1987).

