

# CRS Report for Congress

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## Defense Trade Security Initiative: Background and Status

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### Summary

In response to complaints voiced by the U.S. defense industry and foreign customers about the unwieldiness of the defense export licensing review process, the Department of State, with the Department of Defense, developed a set of seventeen reform proposals. Referred to as the Defense Trade Security Initiative (DTSI), it was announced by the Secretary of State during May of 2000. This report gives the background on the DTSI and discusses associated congressional actions that are reflected in the Security Assistance Act of 2000. It also gives the current status of each of the proposals. It will be updated as necessary.

### Background

The licensed commercial sale of defense articles and services to foreign governments and international organizations is supervised by the Department of State in accordance with the International Traffic in Arms Regulations (ITAR, 22 C.F.R. Parts 120-130). The process by which required export licenses are granted originated in the mid-1950s and developed over the ensuing several decades. Complaints about the license review process rose in frequency and severity during the late 1990s. U.S. companies, particularly those in the aerospace sector, asserted that delays in the licensing process had handicapped their efforts to compete effectively with foreign firms.<sup>1</sup>

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<sup>1</sup> According to data collected by the Satellite Industry Association, representing U.S. space and communications companies, the U.S. share of the world satellite market dropped from a 10-year average of 75% to 45% during 2000, the first complete year after licensing responsibility was  
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In mid-1998, the Department of Defense began studying ways to streamline licensing. A joint State/Defense working group undertook a more comprehensive revision of the process late in the following year. On May 24, 2000, at a NATO ministerial meeting in Florence, Italy, the Secretary of State announced a set of seventeen measures, known collectively as the Defense Trade Security Initiative (DTSI), that was intended to not only improve the international competitiveness of U.S. companies, but also to promote international business arrangements, improve the interoperability of U.S. forces with allies in coalition warfare, and reduce the technological gap between U.S. and other NATO militaries.

The DTSI can be broken into four general categories: reduction of the number of export licenses needed to conduct business; encouragement of better utilization of existing licenses; streamlining of the license-granting process; and modernization of the list of goods requiring licenses for export. (A table listing each of the seventeen proposals and the status of their implementation is provided at the end this report.)

Most of the proposals are uncontroversial. One proposal would single out for expedited review those license requests NATO allies submit as part of the Defense Capabilities Initiative (a program begun in 1998 to close the technology gap between U.S. and other-NATO forces). Another promises to streamline the licensing process for commercial communications satellite components. A third would create a single comprehensive export authorization permitting the exchange of broad-ranging technical data between U.S. and foreign companies needed to forge a variety of business arrangements, such as joint ventures and product teams. The enhancement of computer connectivity to enable electronic transmission between the State and Defense Departments of the voluminous data required to justify license requests is also proposed. This process is currently transacted in paper format.

**Congressional Concerns and Action.** When the provisions of the DTSI were made known to the committees in Congress, Members expressed general satisfaction with its intent and with the manner in which the licensing process would be revised. However, one proposal was singled out for special concern because of its potential implications for technology security and diversion of shipments. This proposal was entitled “Extension of International Traffic in Arms Regulations (ITAR) Exemption to Qualified Countries.”<sup>2</sup> Under this proposal, the Administration offered to create broad exemptions under which unclassified defense items (equipment and intellectual materials) could be exported license-

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<sup>1</sup> (...continued)

transferred from the Department of Commerce to the Department of State. German firm DaimlerChrysler Aerospace announced last year that it would begin seeking non-U.S. satellite component suppliers because of the lengthy time required for State Department licenses. See Bruce A. Smith, “In Orbit.” *Aviation Week and Space Technology* 154/20, May 14, 2001, and Vago Muradian, “State Dept. to Implement Export Control Reforms Over Coming Weeks.” *Defense Daily International*, June 2, 2000.

<sup>2</sup> Proposal 10 in the table at the end of this report. The ITAR is the set of regulations that governs the export of military-specific goods and services from the United States to foreign customers. It designates the officials within the United States government responsible for administering the export licensing process, details the process itself, and lists the specific types of goods and services that the regulations cover (22 C.F.R. Parts 120-130).

free to selected companies in some foreign countries. In order to qualify for the exemption, a foreign government would have to execute with the United States a bilateral agreement ensuring that both states share congruent and reciprocal policies in export controls, industrial security, intelligence, law enforcement, and market access.

The President is authorized to administer defense export controls through regulations issued under authority delegated in the Arms Export Control Act (AECA). Recently, the Administration has used this authority to allow license-free trade in defense articles and services with Canada – the so-called “Canada exemption.” Congress encouraged this exchange in light of the unique relationship enjoyed by the two countries in defense, law enforcement, general commercial trade, intertwined industrial bases, and geographical contiguity.

In late June of 2000, the Secretary of Defense communicated to the chairman of the Senate Foreign Relations Committee his intention to negotiate a Canada-like exemption with the governments of the United Kingdom and Australia.<sup>3</sup> At the same time, he assured the Committee that such agreements would be made legally binding on the recipient states in order to safeguard shipments from diversion en route or illegal re-export to third-country destinations.

While this stipulation to render U.S.-style export controls and technology security measures legally binding went beyond the language incorporated in the original DTSI, Members expressed concern that it did not go far enough in its safeguards, given the potential breadth of license-free trade likely to ensue under an agreement modeled on the Canada exemption. This concern centered on possible third-party sales to undesirable buyers or diversion of defense shipments to unintended destinations.

**Enactment of the Security Assistance Act of 2000.** Because of these policy concerns, Congress passed the Security Assistance Act of 2000 (P.L. 106-280, enacted October 6, 2000). One section of this legislation provides that no exemption from U.S. licensing requirements can be granted unless and until a foreign government binds itself to impose the full range of United States export controls and laws, regulations, and policies befitting the level of sensitivity of the exported items.

This Act expressly requires that, before an exemption can be granted, the U.S. Government must conclude a legally binding bilateral agreement which contains, among other provisions, specific stipulations regarding the ability to verify the identity of the end user, the specific use to which the item will be applied, the control of subsequent re-export of the item, and the establishment of a list of controlled defense articles to include all those covered by the exemption. The Act directs the President to certify that the agreement meets these requirements and that the foreign country has, in fact, promulgated the

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<sup>3</sup> The original list of potential ITAR-exempted states included NATO members, Australia, and Japan. Late in 2000, State Department negotiations with both the U.K. and Australia appeared to have bogged down, and DOD began preliminary discussions with the Netherlands as a potential alternative country interested in the ITAR exemption. However, in July of 2001 the ITAR was amended instead to extend the exemption to Sweden. See Amy Svitak, “U.S. Turns to Smaller Nations as ITAR Exemption Talks Stall,” *Defense News*, December 18, 2000, p. 10, and ITAR 22 CFR Parts 124, 125, 126, July 10, 2001.

necessary policies and regulations and enacted changes to its domestic law to bring them into compliance with U.S. practices before the exemption can be implemented.

Congressional oversight is ensured by the Act's requirement that the President continue to notify Congress of the details of specific defense exports made, regardless of the existence of any license exemption for the recipient. Through enactment of the Security Assistance Act of 2000, Congress has given the President and the defense industry a clear set of boundaries within which to craft licensing relief. In the report of the conference committee on this bill, the Managers expressed approval of the overall thrust of the DTISI, noting that it incorporated several recommendations made previously by the House and Senate committees of jurisdiction.

## **Current Status of the DTISI**

Fifteen months after the adoption of DTISI, most of the proposals have been put into effect. The State Department has published a list of NATO-specific projects to receive expedited license review. The State and Defense Departments have reviewed five of nineteen active USML categories. ITAR changes designed to encourage the creation of international defense business arrangements have been published in the Federal Register. Work has begun to increase State and Defense Department export data connectivity. In the conference report accompanying the Security Assistance Act of 2000, Managers stated their expectation that the President will continue to keep the Congress abreast of progress in bilateral negotiations with candidate countries, including discussions on whether the resulting agreements should be treaties subject to Senate approval. Such negotiations are ongoing with the United Kingdom and Australia. In July 2001, the Commerce and State Departments resolved jurisdictional disputes for sixteen categories of space-qualified items controlled under the Commerce Control List (CCL).<sup>4</sup> This is expected to expedite the licensing review process of commercial satellites and their components.

Despite these advances, defense industries have expressed concern that the State Department has not fully implemented the initiatives and that more changes are warranted. A growing concern has been a decline in U.S. market share of defense items. Some industry analysts believe that an expeditious realization of these initiatives would increase U.S. market share for defense items and help maintain technological superiority. According to the Aerospace Industries Association, reforms have not yet made a significant impact on expediting licensing or streamlining the process. They argue that the State Department needs to establish clear guidelines, regulations, and administrative procedures before defense industries can take advantage of these new licensing measures.

The table at the end of this report lists each of the DTISI proposals along with its current status. This report will be updated as required to keep current the information presented.

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<sup>4</sup> Two of the sixteen space qualified items were removed from the list altogether, six will be included on the USML, four will be included on the CCL, and four will be shared by both Commerce and State. See Amy Svitak, "U.S. State, Commerce Reconcile Export Control Dispute," *Defense News*, August 10, 2001.

### Defense Trade Security Initiative

Initiative	Summary	Issue	Status	Congressional Role
1. Major Program License	Single 8-year license covers entire project where U.S. firm is prime contractor, includes commercial development of defense articles.	Cut number of licenses	Change effective Sept. 1, 2000	None, regulatory change
2. Major Project License	Single licence for major commercial sale to NATO, Australia, Japan, and Sweden <sup>d</sup> expedites processing of associated exports	Expedite licensing	Change effective Sept. 1, 2000	None, regulatory change
3. Global Project License	Single license for exports associated with government-to-government-agreed cooperative project	Reduce number of licenses	Change effective Sept. 1, 2000	None, regulatory change
4. Technical Data Exports for Acquisitions, Teaming Arrangements, Mergers, Joint Ventures, and Similar Arrangements	Single authorization to exchange technical data between qualified firms in the U.S., NATO countries, Japan, Australia, and Sweden <sup>d</sup> for assessing depth and transparency for business ventures	Encourage and speed international business ventures	Change effective Sept. 1, 2000	None, regulatory change
5. Enhance the Use of Multiple Destination Licenses	Increase use of existing license category for U.S. firms to market specific products to specified end-users for specified end-uses	Establish <i>de facto</i> sales territory	Ongoing	None
6. Enhance the Use of Overseas Warehousing Agreements	Increase use of agreements, permitting quantity export of items (e.g., spare parts) for further shipment to pre-approved end-users for specified end-uses	Establishes regional suppliers for U.S. products	Ongoing	None
7. Expedited License Review for NATO	Expedite review of export licenses for DCI <sup>a</sup> projects or programs	Increase U.S. competitiveness for NATO customers	Projects list effective Oct. 30, 2000	None, procedural change
8. Special Embassy Licensing Program	Expedite license reviews submitted by NATO countries, Japan, Australia, and Sweden <sup>d</sup> through their Washington embassies	Speed sales to selected end-user countries	Change effective May, 2000	None, procedural change
9. Interagency Export Licensing Electronic Control Process	Enhance connectivity and compatibility of license-related databases maintained by Departments of State and Defense	Reduce paper, speed license reviews	USXPORTS opened Jan 16, 2001 <sup>b</sup>	None, interagency implementation
10. Extension of ITAR Exemption to Qualified Countries	Canada-like exemptions extended to countries with export and security controls congruent with those of U.S. after internationally enforceable bilateral commitments are executed <sup>c</sup>	Exemption from some ITAR licensing requirements	Negotiation under way with U.K. and Australia	Set baseline (Security Assistance Act of 2000)

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Initiative	Summary	Issue	Status	Congressional Role
11. Defense Services Exemptions for Maintenance and Maintenance Training	New ITAR exemption for maintenance services and training for existing arrangements in NATO countries, Japan, Australia, and Sweden <sup>d</sup>	Reduce number of required licenses for extending services	Change effective Sept. 1, 2000	None, regulatory change
12. Exemptions for Department of Defense Bid Proposals	Removes licensing for some technical data and services supporting DOD bid proposals	Enhance bidding competitiveness	Change effective Sept. 1, 2000	None, regulatory change
13. More Effective Use of Existing ITAR Exemptions by DOD	DOD clarifies improvements in its use of existing exemptions	Ensure advantages of current exemptions are used	Ongoing	None
14. Streamlined Licensing for COMSAT Components/Technical Data	Streamline licensing for commercial communications satellite parts, components, and technical data	Minimize licensing for bidding on and insuring satellite components	ITAR change effective July 1, 2000	H.R. 1707 was introduced on May 3, 2001 to return export licensing authority for commercial communications satellites to the Commerce Department
15. ITAR Exemption for Foreign Military Sales Defense Services	Permit license-free export of technical data and defense services for duration of executed Letter of Offer and Acceptance (LOA) and contract with U.S. company	Eliminate licenses for specific category of services	Change effective Sept. 1, 2000	None, regulatory change
16. Advance Retransfer Consent for Items Sold or Granted by the U.S. Government	Permit retransfer of some items between NATO countries, Japan, Australia, and Sweden <sup>d</sup> if first sold by U.S. Government	Eliminates licenses for some item transfers between U.S. allies	Change effective May 26, 2000	None, regulatory change
17. Review/Revise the U.S. Munitions List	Examine one quarter of USML each year to comport with Military Critical Technologies List	Conform restricted product lists with one another	One quarter of the USML was reviewed	None, interagency initiative

<sup>a</sup> The Defense Capabilities Initiative (DCI) is a NATO program to reducing the technological gap between the equipment fielded by U.S. military forces and those of the other allies. It was initiated in the aftermath of the NATO air campaign over Kosovo during mid-1999.

<sup>b</sup> The U.S. Export Systems Interagency Program Management Office (USXPORTS IPMO) is a major DoD acquisition program to create an interoperable electronic export license review system among the Departments of Commerce, State, Defense, and other agencies. The concept originated during the summer of 1998, thereby predating the DTSI. It is funded through DoD.

<sup>c</sup> The "Canadian exemption" permits unlicensed export of unclassified equipment or technical data for end-use in Canada by Canadian citizens or return to the United States, or temporary import of Canadian-origin items for end-use in the United States or return to Canada for a Canadian citizen.

<sup>d</sup> Amended to add Sweden on June 14, 2001.

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