



Government Procurement & Export UPDATE

LAW OFFICES

**JOHN J. FAUSTI &
ASSOCIATES, LLC**

Part 2 of our Export Compliance Guide for Munitions List Items

Understanding and Using the Canadian and Temporary Import Exemptions

The March 2003 edition of the Fausti & Associates newsletter contained Part 1 of our Export Compliance Guide to assist you in complying with the State Department's rules governing the export and temporary import of defense articles. In this new edition of our newsletter, we are following up with Part 2, which is an issue that is dedicated to two important exemptions to the licensing requirements that are contained in the International Traffic & Arms Regulations ("ITAR"), 22 CFR 121 et. seq. These exemptions are known as the Canadian exemption and the Temporary Import exemption.

As set forth in our March 2003 newsletter, under our export control system, companies seeking to export a defense article to a foreign nation or to temporarily import a defense article into the United States are responsible for obtaining the necessary and proper licenses. Items that fall within the definition of "defense articles," as defined by the Arms Export

Control Act ("AECA"), require a license before they can be legally exported, unless an exemption applies. See discussion at pages 1-2 of our March 2003 newsletter. Two significant exemptions are the Canadian and Temporary Import exemptions. Other exemptions are available and may be applicable, depending upon the particular defense article in question and other relevant facts. This issue of our newsletter specifically discusses two of the more important exemptions: the Canadian and Temporary Import exemptions.

Please note that "back" issues of all of our newsletters, including the March 2003 Export Compliance Guide, are available on our law firm homepage at www.faustilaw.com by clicking-on the "Government Procurement & Export Update" icon. Other helpful information is available at our homepage including a description of our practice areas and biographical information for each of the attorneys in our firm.

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THE CANADIAN EXEMPTION

The Canadian exemption may be used for the export to Canada, or the temporary import into the U.S. from Canada, of **unclassified** defense articles, technical data and/or some defense services. 22 CFR 126.5. The ITAR breaks down the Canadian exemption into the following four

categories: (1) the temporary import of defense articles from Canada into the U.S.; (2) the permanent and temporary export of defense articles from the U.S. to Canada; (3) exemptions for defense services; and (4) re-exports/re-transfers occurring in Canada.

1. Temporary Import from Canada to the U.S.

Defense articles that are temporarily imported from Canada into the U.S. and returned to Canada may not require a license from the Office of Defense Trade Controls (“ODTC”). To take advantage of this category of the Canadian exemption, the defense article must originate in Canada and must be imported into the U.S. for temporary use and then returned to Canada. The item must be unclassified. See 22 CFR 126.5(a). To use this

exemption, the applicant must otherwise meet all other licensing eligibility requirements, *i.e.*, as set forth more fully below, the applicant must not be under indictment or convicted of certain export related offenses that are listed in Section 120.27 of the ITAR. In other words, if because of an indictment you are ineligible to apply for and obtain an export license, you are also prohibited from using a licensing exemption.

2. Permanent and Temporary Export from U.S. to Canada

The permanent and temporary export exemption allows for the export, without a license, of defense articles from the U.S. to Canada for end-use in Canada, providing the following six criteria are satisfied:

- a. **Defense article must be unclassified.**
- b. **End-use in Canada required.** The end-use of the defense article in question must be in Canada by “Canadian Federal or Provincial government authorities” who are “acting in an official capacity” or by a Canadian registered person or entity. A Canadian registered person is any Canadian national (including Canadian businesses incorporated in Canada), dual nationals or permanent Canadian residents who are registered under the Canadian Defense Production Act. Thus, in order to be exempted from obtaining a license for the permanent and temporary export of defense articles from the U.S. to Canada, all the Canadian parties must be authorized end-users. Further, if the receiving individual is a Canadian Federal or Provincial government authority, the person or authority must be acting in an official capacity. If the receiving individual or company is a Canadian person or business, the individual and/or business must be registered with the Canadian Government.
- c. **Non-transfer and use assurances for all “signif-**

icant military equipment” must be obtained from Canadian end-user. Significant military equipment is defined as articles for which special export controls are warranted because of their capacity for substantial military utility or capability. Significant military equipment includes items such as complete military aircraft and their engines.

- d. **Eligibility requirements must be met.** In order to be eligible for the exemption, the exporter must be a U.S. person, who is a lawful permanent U.S. resident or any corporation or business entity incorporated to do business in the U.S.. U.S. persons who are the subject of an indictment involving the criminal statutes enumerated in Section 120.27 of the ITAR are generally ineligible. These criminal statutes include export-related and other national security violations. Any licensing exemption, such as the Canadian exemption, can not be used if the U.S. exporter is ineligible to export under the ITAR.
- e. **Registration requirements must be complied with.** Any person who exports defense articles or who wishes to use the exemption must be registered with ODTC. Registration does not confer any export rights or privileges, it is however,

a precondition to issuance of a license or the use of the exemption. To register, you must complete, and submit to the State Department, a Department of State Form DSP-9 (Registration Statement) and a transmittal letter; and

- f. **Export can not transit third countries.** While in transit, the item may not pass or travel through any country other than Canada or the U.S.

When an exporter has reason to know that the end-use requirement in Canada will not be complied with, the exemption may not be used.

3. Defense Services

The third category of exemptions under 22 CFR 126.5 is an exemption for defense services performed in Canada. A license is not required for the export of defense services to Canada when six criteria are met. These criteria are set forth at 22 CFR 126.5(c). Note that the exemption for defense services is limited, as evidenced by the comprehensive requirements in 22 CFR 126.5(c) that must be satisfied in order to use this exemption. Generally, the exemption for defense services allows eligible U.S.

Additionally, there are 20 categories of defense articles that are explicitly excluded from the permanent and temporary export exemption. If the defense article falls into any of the 20 categories set forth at 22 CFR 126.5(b)(1-20), a license must be obtained before the item can be legally exported unless some other license exemption is applicable. Items in these 20 categories that can not be shipped using the exemption include, but are not limited to, classified items, missile technology, nuclear weapons, complete aircraft, and developmental aircraft, engines and components.

and registered Canadian persons to respond to and work on written requests for quotes or bid proposals from the U.S. Government or the Canadian Government, without an export license. To be eligible for the exemption, the defense services may not be related to any of the 20 categories of excluded defense articles referred to in the previous section of this newsletter. Careful attention must be paid to the type of work/services that can be performed/provided under this exemption.

4. Re-Exports/Re-Transfers

The fourth and final area that is covered under the Canadian Exemption is the area of re-exports/re-transfers. If an item was exported to Canada using the Canadian exemption, it may be re-transferred to another Canadian end-user without a license, providing the subsequent transfer would have been

allowed initially had it been made directly from the U.S. exporter using the Canadian exemption. However, State Department approval will be required prior to re-transferring an item within Canada to a non-registered Canadian entity and/or prior to exporting the item from Canada.

TEMPORARY IMPORT LICENSE EXEMPTIONS

The temporary import exemption allows for the temporary import into the U.S. (and the subsequent export from the U.S.) of unclassified U.S.-origin defense articles without a license, provided that:

- a. The item is to be serviced in the U.S., *i.e.*, tested, repaired, overhauled and one-to-one replacement of defective parts, but not modified, enhanced, upgraded, altered or improved in a way that changes the basic performance of the defense article, and the item is then returned to the country from where it came;

- b. The item is to be upgraded and incorporated into another item that ODTIC has already authorized for permanent export pursuant to a license;
- c. The item is imported for purposes of exhibition or marketing in the U.S. and returned to the country from where it came;
- d. The item has been previously rejected for permanent import by the Department of Treasury (which oversees permanent importation) and is simply being returned to the country from where it was imported; or

- e. The item is imported pursuant to the U.S. Foreign Military Sales program.

The temporary import exemption does not apply to imports from Canada. Exemptions involving Canada are governed by the previously discussed Canadian exemption at 22 CFR 126.5.

In addition, a U.S.-origin item may be temporarily imported without a license (but NOT subsequently exported) if the item will be enhanced, upgraded, modified, incorporated into another article or serviced in such a way that changes the basic performance of the defense article. In order to export such an item, a license application must be submitted to ODTC and a State Department license must be obtained.

In order to use the temporary import exemptions, the U.S. company or individual seeking to import the unclassified defense article must meet the licensing eligibility requirements and be registered with ODTC. Also, the importer must, at the time of import, file and annotate the applicable U.S. Customs documents, e.g. Form CF 3461, 7512, 7501, 7523 or 311, to read: *"This shipment is being imported in accordance with and under the authority of 22 CFR 123.4(a)(identify applicable subsection)."* Additionally, a complete list and description of the defense article(s) that is being imported, including but not limited to quantity and U.S. dollar value, must be included on the invoice and other appropriate documentation.

Furthermore, at the time of export, the ultimate consignee named on the Shipper's Export Declaration must be the same as the foreign consignee or end-user

of record named at the time of import. The ITAR provides that the following statement must be included on the exporter's invoice and bill of lading whenever a defense article on the munitions list is exported:

These commodities are authorized by the U.S. Government for export only to [country of ultimate destination] for use by [end-user]. They may not be transferred, transshipped on a non-continuous voyage, or otherwise be disposed of in any other country, either in their original form or after being incorporated into other end-items, without the prior written approval of the U.S. Department of State.

22 CFR 123.9(b). Lastly, at the time of export, the U.S. company/individual, exporting the defense article back to its original destination, must file a Shipper's Export Declaration with the District Director of Customs at the port of exit. On the SED or as an attachment, the following must be included: (1) the U.S. Customs entry document number or a copy of the U.S. Customs documentation under which the article was imported and; (2) the following statement, "22 CFR 123.4(a)(identify subsection) and 22 CFR 120.1(b) applicable."

Notwithstanding the fact that the aforementioned criteria are satisfied, the temporary import of a defense article from or on behalf of any country on the list of proscribed countries is strictly prohibited. Therefore, for example, items may not be imported from Iran or other proscribed countries using the temporary import exemption.

Other Additional Requirements Besides the License Requirement

Although a company may not need to obtain a license from the State Department before exporting or importing a defense article, because it is able to satisfy one of the exemptions discussed in our newsletter or any of the other available exemptions, there are other requirements that must be satisfied in order for the company to use an exemption. For example, to use an exemption, you must be registered with ODTC. Also, please keep in mind that whenever a licensing exemption is claimed for unclassified technical data, the ITAR requires that you make and maintain a record of each such export. 22 CFR 123.26. Another important requirement is the

Shipper's Export Declaration as discussed above. 22 CFR 123.22. In all cases when using an exemption, the exporter must certify on the Declaration that the export is exempt from the licensing requirement and you must cite the particular federal regulation under which the exporter is claiming exemption from the licensing requirement.

For more information about the export laws or how your company can implement its own export compliance program, please contact the Law Offices of Fausti & Associates at (202) 237-0505.