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## Aerospace and Defense Industries

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## Aerospace and Defense Industries

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This article reviews international law developments in the field of aerospace and defense industries in 2013.<sup>1</sup>

### I. Ready or Not: U.S. Export Control Reform is Here

#### A. BACKGROUND ON U.S. EXPORT CONTROL REFORM

The U.S. Government has called recent export control reforms “[t]he most significant changes to the U.S. export control system in decades.”<sup>2</sup> In August 2009, President Barack Obama launched the U.S. Export Control Reform (ECR) initiative to redefine how the U.S. Government regulates the export of defense and other sensitive technologies. At that time, the President instructed agencies involved in the U.S. export control system to conduct a comprehensive review of export controls they administer and enforce. In April

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\* William M. Pannier of Holland & Knight LLP and Kimberly A. Strosnider of Covington & Burling LLP were the editors of the Aerospace and Defense Industry Committee’s Year in Review of 2013. Antonia I. Tzinova and Andrew K. McAllister of Holland & Knight LLP authored Section I on “Ready or Not: U.S. Export Control Reform is Here.” Kimberly A. Strosnider and Eric Sandberg-Zakian of Covington & Burling LLP authored Section II on “Revisions to the International Traffic in Arms Regulations’ Brokering Rules.” Christina Zanette of Bryan Cave LLP authored Section III on “Directorate of Defense Trade Controls Enforcement Actions.” R. Locke Bell, a law student at George Washington University School of Law, authored Section IV on “Ending Trafficking in Persons” and Section V on “National Institute of Standards and Technology Preliminary Cybersecurity Framework.” Evelyn R. Nackman, reservist with the U.S. Air Force Legal Operations Agency/Environmental Law & Litigation Division and Counsel with the American Petroleum Institute, and Mark J. Nackman of General Dynamics Advanced Information Systems authored Section VI on “*Shell Oil Co. v. United States*: Liability for Environmental Cleanup on WW-II Era Defense Contracts, Part Deux.” The views of the authors are not attributable to their law firms, companies, or government agencies. The article covers developments during 2013.

1. For developments in 2012, see Kimberly A. Strosnider et al., *Aerospace and Defense Industries*, 47 INT’L LAW. 279 (2012). For developments in 2011, see Mark J. Nackman et al., *Aerospace and Defense Industries*, 46 INT’L LAW. 287 (2011).

2. Media Note, Office of the Spokesperson, Dep’t of State, Exp. Control Reform: First Final Rules Go Into Effect (Oct. 15, 2013), available at <http://www.state.gov/r/pa/prs/ps/2013/10/215428.htm>.

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2010, then-Secretary of Defense Robert Gates confirmed that fundamental reform of the U.S. export control system is necessary to enhance national security.<sup>3</sup>

As part of the President's ECR initiative, the U.S. Department of State Directorate of Defense Trade Controls (DDTC), in collaboration with the U.S. Department of Commerce Bureau of Industry and Security (BIS), undertook major revisions to each agency's export control regulations. These revisions are now having a sweeping impact on the U.S. aerospace and defense industry and on non-U.S. companies that trade in or use U.S. aerospace and defense items.

DDTC administers the International Traffic in Arms Regulations (ITAR).<sup>4</sup> The items subject to the control of the ITAR (i.e., defense articles) are identified on the ITAR's United States Munitions List (USML).<sup>5</sup> With few exceptions, items not subject to the export control jurisdiction of DDTC are subject to the jurisdiction of BIS under the controls of the Export Administration Regulations (EAR). The EAR includes the Commerce Control List (CCL); items not listed on the CCL are designated as EAR99 and require no license to export unless the items are being exported to an embargoed country, to a prohibited end-user, or for a prohibited end-use. Both the ITAR and the EAR impose license requirements on exports and re-exports of listed commodities and related technical data or technology.

**B. INITIAL CHANGES AND STATUS OF PENDING CHANGES**

*1. Overview of Changes*

Pursuant to the President's ECR initiative, DDTC published two final rules revising aspects of the ITAR, most notably eight USML categories, with certain items transitioning from the USML to the CCL. At the same time, BIS published revisions to the EAR to incorporate the items transitioning into the CCL. All final rules, including these two final rules, provide for a 180-day transition period between the publication date and effective date.<sup>6</sup>

DDTC and BIS have issued additional proposed rules on the rewrites of most of the other USML categories. Lastly, DDTC and BIS also plan to issue proposed rules for the remaining USML categories; however, the specific dates have been a moving target, with greatest attention to changes that will have great impact and are the least controversial.<sup>7</sup>

The major revisions to the USML are intended to make the USML a positive list that describes controlled items using objective, technical-based criteria and are intended to diminish the role of subjective criteria, such as certain "catch-all" criteria. ECR is not designed to completely decontrol currently listed items, but rather to move certain items

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3. Robert M. Gates, Sec'y of Def., Remarks to the Business Executives for National Security on the U.S. Export Control System (Apr. 20, 2010), *available at* <http://www.defense.gov/transcripts/transcript.aspx?transcriptid=4613>.

4. *Directorate of Defense Trade Controls Mission*, DEP'T OF STATE (Feb. 12, 2014), <http://www.pmdtcc.state.gov>.

5. See United States Munitions List, 22 C.F.R. § 121.1 (2014).

6. *Export Control Reform News*, EXPORT.GOV BLOG (Jan. 14, 2014), [http://export.gov/ecr/eg\\_main\\_043652.asp](http://export.gov/ecr/eg_main_043652.asp).

7. See *Export Control List Review and Creating a Single Control List*, EXPORT.GOV (Feb. 12, 2014), [http://export.gov/ecr/eg\\_main\\_027617.asp](http://export.gov/ecr/eg_main_027617.asp).

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from the stringent controls of the USML to the more flexible CCL, where exports may be made to certain countries without a license and where additional license exceptions are available. This change should ease trade with the closest allies of the United States. Items determined to no longer warrant control under the USML are mostly transitioning to the CCL under a new “600 series.” To increase interoperability with allied governments, many items transitioning to the 600 series are eligible for the strategic trade authorization (STA) license exception, which can be used under certain conditions, such as when the end-user is the government of one of thirty-six eligible allied countries.<sup>8</sup>

*2. Final Rules Published to Date*

On April 16, 2013, DDTC published its first final rule under the ECR with an effective date of October 15, 2013.<sup>9</sup> This rule includes the following changes: revisions to USML Categories VIII (aircraft) and the creation of a new Category XIX (gas turbine engines); revisions to Categories XVII and XXI to synchronize with newly adopted definitions; revisions to existing definitions and additions of new definitions; and the establishment of a transition plan to mitigate the impact of the changes with respect to commodity jurisdiction determinations, existing and new licenses, and reporting of violations.<sup>10</sup> BIS published an accompanying final rule with the same issuance and effective dates so there is no interrupted regulatory coverage for the items moving from the USML to the CCL.<sup>11</sup>

The revised Categories VIII and XIX controls rely more heavily on enumerated lists, rather than broad subjective terms. The most sensitive commodities and related technical data remain controlled under the USML. For instance, bombers, fighters, attack helicopters, certain unmanned aerial vehicles, and related sensitive systems, parts, and components (e.g., weapons systems, wing folding systems, tail hooks, and arresting gear) continue to be classified in Category VIII. On the other hand, less sensitive commodities and certain related technology (e.g., hydraulic and fuel hoses and propellers used with reciprocating engines) have transitioned to the CCL. The transition of these items to the CCL helps to remove the prior incentive for non-U.S. manufacturers of military defense articles (e.g., military aircraft) to avoid using U.S.-origin parts and components because of the ITAR controls on foreign-made defense articles containing U.S.-origin parts and components.<sup>12</sup>

With respect to revisions and additions to the definitions section, of particular significance is the definition of “specially designed,” introduced both in the ITAR and the EAR.<sup>13</sup> Although one of the goals of ECR is to create a more positive USML that is less

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8. *Export Control Reform Finally Kicks in*, STEPTOE & JOHNSON LLP (Oct. 18, 2013), <http://www.steptoelaw.com/publications-9114.html>.

9. Amendment to the International Traffic in Arms Regulation, 78 Fed. Reg. 22,740 (Apr. 16, 2013) (to be codified at 22 C.F.R. pts. 120, 121, and 123).

10. *Id.*; Amendment to the International Traffic in Arms Regulation, 78 Fed. Reg. 61,750, 61,751 (Oct. 3, 2013) (to be codified at 22 C.F.R. pts. 120, 121, 123, and 126).

11. See Revisions to the Export Administration Regulations: Initial Implementation of Export Control Reform, 78 Fed. Reg. 22,660 (Apr. 16, 2013), as amended by Revisions to the Export Administration Regulations: Initial Implementation of Export Control Reform, 78 Fed. Reg. 61,744 (Oct. 3, 2013).

12. Amendment to the International Traffic in Arms Regulation, 78 Fed. Reg. 61,750, 61,751; Revisions to the Export Administration Regulation, 78 Fed. Reg. 22,660, 61,744.

13. The term had been used on the CCL (but only defined in the context of the Missile Technology Control Regime), while it is introduced on the USML for the first time.

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focused on design intent, the term “specially designed” is used in certain sections of the revised USML categories as well as CCL 600-series entries. The analysis under the “specially designed” definition is a two-part “catch and release” structure where the first paragraph is the “catch” and the second paragraph is the “release.” For example, fasteners, washers, spacers, insulators, grommets, bushings, springs, wires, and solders are not considered “specially designed” by virtue of the “release” paragraph. Accordingly, an item is “specially designed” if it is caught in the first paragraph and not released in the second paragraph.<sup>14</sup>

The transition plans published by DDTC and BIS include details on (i) the duration of existing DDTC authorizations on transitioning items, (ii) the treatment of previously issued DDTC commodity jurisdiction determinations, and (iii) the treatment of re-exports of transitioning items. The transition plans also address the issue of filing voluntary disclosures regarding transitioning items. (The general rule is that an ITAR item remains under the jurisdiction of DDTC until the effective date of a published final rule transferring jurisdiction over that item to the CCL.) Also, to eliminate redundant licenses, the ITAR and EAR were amended to allow DDTC to issue licenses for export of items on the CCL so long as the EAR-controlled items are for end-use in or with USML defense articles exported under the same license.

On July 8, 2013, DDTC published its second final rule under ECR with an effective date of January 6, 2014.<sup>15</sup> This second final rule includes the following changes: revisions to USML Categories VI (vessels of war), VII (tanks and military vehicles), XIII (auxiliary military equipment), and XX (submersibles); revisions to existing definitions; and the addition of new definitions.<sup>16</sup> BIS published its accompanying final rule with the same issuance and effective dates.<sup>17</sup> Similar to the rewrite of Categories VIII and XIX, these revised categories enumerate the most sensitive commodities and related technical data that remain under ITAR control (e.g., warships, submarines for military use, etc.) while excluding less sensitive commodities and certain related technology (e.g., submarine rescue vehicles, magnetic compasses, and gauges and indicators) now captured by the CCL.

DDTC and BIS will continue to issue final rules in this same vein with effective dates of 180 days after publication. A current timetable of all the affected rules is available on DDTC's and BIS's websites.<sup>18</sup>

**C. COMPLIANCE CHALLENGES**

While the revisions to the ITAR and EAR are designed to simplify control and licensing of defense and dual-use items, the changes are very detailed and cause compliance chal-

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14. Nicholas Rosenberg et al., “Special” Delivery: The Export Control Reform Initiative and the Creation of a Single, Regulatory Definition of “Specially Designed,” EXPORT CONTROLS ALERT: RECENT DEVELOPMENTS IN EXPORT CONTROLS (Nixon Peabody LLP, Washington, D.C.), May 31, 2013, at 1, available at [http://www.nixonpeabody.com/files/157109\\_Export\\_Controls\\_Alert\\_31MAY2013.pdf](http://www.nixonpeabody.com/files/157109_Export_Controls_Alert_31MAY2013.pdf).

15. See Amendment to the International Traffic in Arms Regulations, 78 Fed. Reg. 40,921 (July 8, 2013) (to be codified at 22 C.F.R. pts. 120–25).

16. *Id.*

17. See Revisions to the Export Administration Regulation, 78 Fed. Reg. 40,892 (July 8, 2013) (to be codified at 17 C.F.R. pts. 740 et seq.).

18. See *Export Control Reform: Control Lists “Tracker”*, EXPORT.GOV (Sept. 2013), [http://export.gov/static/ECR%20Control%20List%20Tracker%20120313\\_Latest\\_eg\\_main\\_048264.pdf](http://export.gov/static/ECR%20Control%20List%20Tracker%20120313_Latest_eg_main_048264.pdf).

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lenges for companies in the aerospace and defense industries. Key personnel responsible for export compliance within each company should review the company's export compliance program and update as appropriate, paying particular attention to changes in jurisdiction over items between the ITAR and EAR, classification of items under the ITAR and EAR, and regulatory definitions.

A review of all export licenses is necessary to evaluate the authorization under each license and determine any changes caused by the ECR transition plan, including changes to the expiration date. (Note that existing licenses authorizing the export of transitioning items have a shorter expiration date than usual.) Importantly, compliance personnel in companies that produce, export, or otherwise trade in items that are transitioning to the EAR should be well-versed not just in the ITAR, but also in the EAR. While DDTC and BIS may provide some leeway initially, an export made under an expired license or under an incorrect license is still a violation. Companies should focus on updating their export classification matrices (ensuring existing licenses are not affected or are renewed as necessary) and providing training to address issues such as changing jurisdiction over transitioning items and licensing considerations. In order to ensure continued compliance, companies should closely monitor new rules issued by the regulators and industry updates.<sup>19</sup>

## **II. Revisions to the International Traffic in Arms Regulations' Brokering Rules**

On August 26, 2013, DDTC issued an interim final rule substantially overhauling the brokering rules in the International Traffic in Arms Regulations.<sup>20</sup> The interim final rule went into effect on October 25, 2013,<sup>21</sup> and represents a potentially significant—and long-awaited—change for companies and individuals, both in the United States and abroad, that engage in defense trade.

The ITAR's brokering regulations implement the Arms Export Control Act's requirement that persons engaged in the business of brokering arms transfers register with the government.<sup>22</sup> The regulations have generally been considered unclear, in large part because they did not clearly identify the activities that constitute brokering and, thus, that triggered brokering-related registration, reporting, and prior approval requirements. As a result, revisions to the brokering regulations have been under consideration for a decade, with the State Department publishing (formally or informally) proposed revisions in 2009, 2011, and 2012.

The interim final rule that went into effect in the fall of 2013 largely mirrors a 2012 DDTC proposal. The rule expands the scope of covered brokering activities in certain respects, but its most significant amendments are two changes that narrow the scope of the regulations.

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19. *President's Export Control Reform Initiative*, EXPORT.GOV (Jan. 14, 2014), <http://export.gov/ecr/index.asp>.

20. See Amendment to the International Traffic in Arms Regulations, 78 Fed. Reg. 52,680 (Aug. 26, 2013) (to be codified at 22 C.F.R. pts. 120, 122, 126–29).

21. *Id.* at 52,694.

22. 22 U.S.C. § 2778(b)(1)(A)(ii) (2012).

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First, the interim final rule limits the circumstances in which foreign persons are subject to the brokering registration requirement. Previously, ITAR Section 129.3 imposed a registration requirement on anyone who engaged in brokering activities, defined under ITAR Section 129.2 to mean “acting as a broker . . . [including] the financing, transportation, freight forwarding, or taking . . . any other action that facilitates the manufacture, export, or import [of] a defense article or defense service, irrespective of its origin.”<sup>23</sup> ITAR Section 129.2 in turn defined “broker” as “any person who acts as an agent for others in negotiating or arranging contracts, purchases, sales or transfers of defense articles or defense services in return for a fee, commission, or other consideration.”<sup>24</sup> Pursuant to that language, foreign persons were required to register as brokers if they facilitated sales or other transfers of U.S.-origin defense articles, even if those persons were outside the United States and were not owned by a U.S. corporate parent.

Under the newly amended regulations, foreign persons are no longer required to register as brokers merely because they facilitate sales of U.S.-origin defense articles. A broker is now defined to include only a person who “engages in the business of brokering activities” and is a U.S. person (wherever located), a “foreign person . . . located in the United States,” or a “foreign person located outside the United States” and “owned or controlled by a U.S. person.”<sup>25</sup>

Second, the interim final rule excludes from brokering activities those activities performed by one affiliate of an ITAR registrant on behalf of another affiliate of the registrant.<sup>26</sup> This exception is particularly helpful in clarifying that DDTC no longer recognizes the concept of “intra-company brokering,” a departure from a past DDTC position that the brokering rules applied to such intra-company activities. Tracking, reporting, and obtaining authorization for intra-company brokering previously presented a significant challenge for companies in an increasingly international and integrated defense industry, and the new rule largely eliminates those issues.

Beyond those significant changes narrowing the scope of the regulations, the interim final rule also broadens the regulations in some respects. Perhaps most notably, the amended regulations abandon previous language that defined a broker as a person who acts “in return for a fee, commission, or other consideration.”<sup>27</sup> There is no payment/consideration element in the new definitions of “broker” or “brokering activities,” although the definition of “broker” states that brokers are those who “engage in the business” of brokering activities.<sup>28</sup> The interim final rule also broadens the language of the regulations to codify positions previously taken by DDTC. For example, the amended rules clarify that facilitation of an in-country transfer or retransfer or a re-export from one foreign country to another constitutes brokering activity.<sup>29</sup>

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23. Registration and Licensing of Brokers, 22 C.F.R. § 129.2(b) (2013).

24. *Id.* § 129.2(a).

25. Amendment to the International Traffic in Arms Regulations, 78 Fed. Reg. at 52,690 (Aug. 26, 2013).

26. *Id.*

27. *Brokering Controls*, A RESOURCE ON STRATEGIC TRADE MANAGEMENT AND EXPORT CONTROLS, <http://www.state.gov/strategictrade/practices/c43181.htm> (last visited Feb. 17, 2014).

28. Amendment to the International Traffic in Arms Regulations, 78 Fed. Reg. 52,690 (Aug. 26, 2013) (to be codified at 22 C.F.R. pts. 120, 122, 126–29).

29. *Id.*



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Similarly, the amended rules define brokering activities as activities “on behalf of another,”<sup>30</sup> phrasing that is arguably broader than the “act[ing] as an agent for others” phrasing in the original rules. While DDTC had long interpreted the “agent” language to extend beyond the traditional concept of a principal-agent relationship, the revised language provides a stronger basis for DDTC to penalize persons for activity that does not involve acting as the agent of a principal.

Beyond these changes, the amended regulations now provide more guidance than the old regulations on conduct that does or does not constitute brokering activities. Section 129.2(b) provides that brokering activities include “[f]inancing, insuring, transporting, or freight forwarding defense articles and defense services” (subject to certain exceptions) and “[s]oliciting, promoting, negotiating, contracting for, arranging, or otherwise assisting in the purchase, sale, transfer, loan, or lease of a defense article or defense service.”<sup>31</sup> But brokering activities do not include “[a]ctivities by regular employees . . . acting on behalf of their employer”; “administrative services,” including “activities by an attorney that do not extend beyond the provision of legal advice to clients”; and “activities by a U.S. person in the United States that are limited exclusively to U.S. domestic sales or transfers (e.g., not for export).”<sup>32</sup> This latter exclusion is similar to a carve-out in the old brokering regulations for purely domestic activities, but this new exclusion specifies that the activities by the U.S. person must occur “in the United States” to be exempt. Conduct that does not extend beyond acting as an end-user of a licensed article/service or subsequently acting as an authorized re-exporter of such article/service is also now excluded from the definition of brokering.<sup>33</sup>

Finally, the interim final rule makes several notable changes to the registration, notification, and approval processes that brokers must follow, including the following:

(1) In many circumstances, section 129.7 of the old brokering regulations required those engaging in brokering activities to obtain prior approval, which is similar to licensing, from DDTC. Section 129.4 of the amended regulations revise the circumstances in which the prior approval requirement applies, focusing the requirement on brokering of foreign defense articles/services and end-items such as military aircraft, vessels, tanks, and night-vision items.<sup>34</sup>

(2) Under the old rules, certain activities were subject to “prior notification,” as distinct from prior approval. The amended regulations eliminate the prior notification requirement.

(3) Section 129.3(d) of the amended regulations now allows U.S. exporters registered as manufacturers or exporters to include on their Part 122 registration their U.S. and foreign subsidiaries and owned or controlled affiliates that will act as brokers.<sup>35</sup>

(4) Section 127.1(c) of the amended regulations provides that:

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30. *Id.*

31. *Id.*

32. *Id.*

33. *Id.*

34. Compare 22 C.F.R. § 129.7 (2013) with Amendment to the International Traffic in Arms Regulations, 78 Fed. Reg. 52,691, 52,680 (Aug. 26, 2013) (to be codified at 22 C.F.R. pts. 120, 122, 126–29).

35. Amendment to the International Traffic in Arms Regulations, 78 Fed. Reg. at 52,691 (Aug. 26, 2013).

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any person who is granted a license or other approval . . . is responsible for the acts of . . . brokers[ ] and all authorized persons to whom possession of the defense article, which includes technical data, has been entrusted regarding the operation, use, possession, transportation, and handling of such defense article abroad.<sup>36</sup>

This provision appears intended to clarify that license applicants are only responsible for their brokers' compliance with respect to licensed defense articles that come into the brokers' possession, rather than responsible for their brokers' overall compliance with the brokering rules.

### **III. Directorate of Defense Trade Controls Enforcement Actions**

In 2013, the U.S. Department of State settled charges with three companies for alleged violations of the Arms Export Control Act (AECA)<sup>37</sup> and the International Traffic in Arms Regulations,<sup>38</sup> imposing penalties that collectively exceeded \$40 million. In each of the charging letters and consent agreements involving Raytheon Company, Aeroflex, Inc., and Meggitt-USA, Inc., the State Department noted that in recent years, the companies had submitted voluntary disclosures related to the compliance matters to DDTC. Yet, despite those efforts, the companies continued to violate the AECA and ITAR, meriting penalties.<sup>39</sup>

#### **A. RAYTHEON**

On April 30, 2013, Raytheon settled allegations that it violated the AECA and the ITAR in connection with its administration of ITAR agreements and ITAR licenses.<sup>40</sup> DDTC alleged a total of 125 violations, falling broadly into two categories: "failure to properly manage [ITAR] agreements and failure to properly manage temporary export and import [licenses]." Citing "corporate-wide weakness in administering Part 124 agreements and Part 123 temporary import and export authorizations," the consent Proposed Charging Letter addressed to Raytheon noted that the previous remedial efforts undertaken by Raytheon and reported in prior voluntary disclosures were insufficient in that they failed to prevent or detect additional similar violations subsequently disclosed.<sup>41</sup>

Alleged violations related to Raytheon's administration of ITAR agreements included, among others, the manufacture of hardware by Raytheon's foreign subsidiaries greatly in

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36. *Id.* at 52,688.

37. See Arms Export Control Act, 22 U.S.C. § 2778 (2012).

38. See International Traffic in Arms Regulations, 22 C.F.R. §§ 120–130 (2013).

39. Consent Agreement, *In re Aeroflex Inc.*, United States Department of State, Bureau of Political-Military Affairs, 14–16 (Jan. 25, 2013), *available at* [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/Aeroflex%20Executed%20CA.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/Aeroflex%20Executed%20CA.pdf); Consent Agreement, *In re Meggitt-USA, Inc.*, United States Department of State, Bureau of Political-Military Affairs, 17–20 (Jan. 25, 2013), *available at* [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/Meggitt\\_CA.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/Meggitt_CA.pdf); Consent Agreement, *In re Raytheon Co.*, United States Department of State, Bureau of Political-Military Affairs, 15–17 (Jan. 25, 2013), *available at* [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/Raytheon\\_ConsentAgreement\\_13.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/Raytheon_ConsentAgreement_13.pdf).

40. Consent Agreement, *In re Raytheon Co.*, at 2.

41. Letter from Lisa V. Aguirre, Dir., Office of Def. Trade Controls, to William H. Swanson, Chairman and CEO, Raytheon Co., 2–6 (Mar. 21, 2013), *available at* [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/Raytheon\\_PCL\\_13.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/Raytheon_PCL_13.pdf) [hereinafter Raytheon Charging Letter].

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excess of the approved amounts and the failure to timely file sales reports, amendments, and other required documents. Compliance issues related to Raytheon's administration of license authorizations, for which DDTC noted that Raytheon had submitted thirty voluntary disclosures since September 2005, included inaccurate tracking, valuation, and documentation of temporary exports and imports, some of which involved classified defense articles. In some cases, these administrative issues prevented the State Department from properly informing Congress pursuant to the Congressional Notification requirements of the AECA.<sup>42</sup>

Under the terms of the Consent Agreement, Raytheon will pay a civil penalty of \$8 million and implement various remedial measures.<sup>43</sup>

**B. AEROFLEX**

On August 6, 2013, the State Department and Aeroflex entered into a Consent Agreement to settle 158 alleged violations of the AECA and the ITAR<sup>44</sup> in connection with Aeroflex's "unauthorized exports and re-exports of ITAR-controlled electronics, microelectronics, and associated technical data" to various countries, including, in some cases, the re-export of ITAR-controlled defense articles to proscribed destinations.<sup>45</sup>

Over the course of many years, Aeroflex business units submitted multiple voluntary disclosures, disclosing hundreds of ITAR violations to DDTC, many of which were unauthorized exports that resulted from Aeroflex's failure to properly establish jurisdiction over ITAR-controlled defense articles and technical data through the Commodity Jurisdiction process. DDTC found that some of these exports directly supported Chinese satellites and military aircraft and caused harm to U.S. national security. DDTC noted in the Charging Letter that the AECA provides DDTC, in concurrence with the Department of Defense (DOD), exclusive authority to designate defense articles and services that constitute the U.S. Munitions List,<sup>46</sup> and that the Department of Commerce's commodity classification process is not a jurisdictional determination for purposes of the AECA.<sup>47</sup>

Under the terms of the Consent Agreement, Aeroflex will pay a civil penalty of \$8 million and implement various remedial measures.<sup>48</sup>

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42. See Arms Export Control Act, § 22 U.S.C. 2776 (c) – (d); Raytheon Charging Letter, *supra* note 41, at 5–7.

43. Consent Agreement, *In re Raytheon Co.*, at 12–14, 16–17.

44. Consent Agreement, *In re Aeroflex Inc.*, United States Department of State, Bureau of Political-Military Affairs, 21 (Jan. 25, 2013), available at [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/Aeroflex%20Executed%20CA.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/Aeroflex%20Executed%20CA.pdf); Letter from Daniel J. Buzby, Acting Dir., Office of Defense Trade Controls, to Leonard Borow, CEO, Aeroflex, Inc. (July 25, 2013), available at [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/AM%20-%20Aeroflex%20Admin%20Settlement%20-%20Tab%204%20Proposed%20Charging%20Letter.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/AM%20-%20Aeroflex%20Admin%20Settlement%20-%20Tab%204%20Proposed%20Charging%20Letter.pdf) [hereinafter Aeroflex Charging Letter].

45. See 22 C.F.R. § 126.1 (2013) (listing proscribed destinations); Aeroflex Charging Letter, *supra* note 44, at 8–9.

46. Aeroflex Charging Letter, *supra* note 44, at 5; see also 22 C.F.R. § 121.1 (2013).

47. Aeroflex Charging Letter, *supra* note 44, at 5–8.

48. Consent Agreement, *In re Aeroflex Inc.*, United States Department of State, Bureau of Political-Military Affairs, 14 (Jan. 25, 2013), available at [http://www.pmddtc.state.gov/compliance/consent\\_agreements/pdf/Aeroflex%20Executed%20CA.pdf](http://www.pmddtc.state.gov/compliance/consent_agreements/pdf/Aeroflex%20Executed%20CA.pdf).

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C. MEGGITT

On August 19, 2013, Meggitt and several of its subsidiaries, which are owned by United Kingdom company Meggitt PLC, settled sixty-seven charges of violating the AECA and ITAR “in connection with the unauthorized export of defense articles, including technical data; the unauthorized provision of defense services; violation of the terms of provisos or other limitations of ITAR licenses; and failure to maintain specific records involving ITAR-controlled transactions.”<sup>49</sup>

DDTC noted that the majority of the violations occurred prior to Meggitt’s acquisition of certain subsidiaries. Further, Meggitt subsidiaries and business units voluntarily disclosed hundreds of ITAR violations beginning in the mid-1990s.<sup>50</sup> But DDTC noted in its Charging Letter that given the “breadth of violations included in the disclosures, the extended duration of certain violations, and the recurrence of certain types of violations[,]” administrative action against Meggitt was warranted.<sup>51</sup>

Under the terms of the Consent Agreement, Meggitt will pay a civil penalty of \$25 million and implement various remedial measures.<sup>52</sup>

**IV. Ending Trafficking in Persons**

On September 26, 2013, the Federal Acquisition Regulatory Council published (1) a rule proposed by DOD, General Services Administration, and National Aeronautics and Space Administration amending the Federal Acquisition Regulations (FAR)<sup>53</sup> and (2) a related rule proposed by DOD amending the Department of Defense Federal Acquisition Regulation Supplement (DFARS),<sup>54</sup> both of which implement Executive Order 13627, Strengthening Protections Against Trafficking in Persons in Federal Contracts<sup>55</sup> and Title XVII of the National Defense Authorization Act for Fiscal Year 2013.<sup>56</sup> The proposed FAR amendments expand the Government’s existing zero-tolerance policy for trafficking in persons<sup>57</sup> and establish a requirement for certain contractors to maintain and certify a

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49. Letter from Daniel J. Buzby, Acting Dir., Office of Defense Trade Controls, to Eric G. Lardiere, Senior VP, Sec’y, and Gen. Counsel, Meggitt-USA, Inc., 1–2 (Aug. 19, 2013), *available at* [http://www.pmdtc.state.gov/compliance/consent\\_agreements/pdf/Meggitt\\_PCL.pdf](http://www.pmdtc.state.gov/compliance/consent_agreements/pdf/Meggitt_PCL.pdf) (“Meggitt PLC, a corporation organized under the laws of England and Wales and the ultimate parent of the Meggitt group of companies . . .”) [hereinafter *Meggitt-USA Charging Letter*].

50. Media Note, U.S. Dep’t of State, Dep’t of State Concludes Settlement of Exp. Violations by Meggitt-USA, Inc. (Aug. 23, 2013), *available at* <http://www.state.gov/r/pa/prs/ps/2013/08/213483.htm>.

51. Meggitt-USA Charging Letter, *supra* note 49, at 2, 7.

52. Consent Agreement, *In re* Meggitt-USA, Inc., United States Department of State, Bureau of Political-Military Affairs, 17 (Jan. 25, 2013), *available at* [http://www.pmdtc.state.gov/compliance/consent\\_agreements/pdf/Meggitt\\_CA.pdf](http://www.pmdtc.state.gov/compliance/consent_agreements/pdf/Meggitt_CA.pdf).

53. Ending Trafficking in Persons, 78 Fed. Reg. 59,317 (proposed Sept. 26, 2013) (to be codified at 48 C.F.R. pts. 1, 2, 9, 12, 22, 52).

54. Defense Federal Acquisition Regulation Supplement: Further Implementation of Trafficking in Persons Policy, 78 Fed. Reg. 59,325 (proposed Sept. 26, 2013) (to be codified at 48 C.F.R. pts. 203, 204, 212, 222, 252).

55. *See generally* Exec. Order No. 13,627, 77 Fed. Reg. 60,029 (Sept. 25, 2012). For additional discussion see Mark J. Nackman et al., *Aerospace and Defense Industries*, 47 INT’L LAW. 279, 286–87 (2013).

56. National Defense Authorization Act for Fiscal Year 2013, Pub. L. No. 112-239, 126 Stat. 1632 (2013).

57. *See* Victims of Trafficking and Violence Protection Act of 2000, 22 U.S.C. §§ 7101–7113 (2012).

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compliance program designed to target trafficking activities.<sup>58</sup> The proposed DFARS amendments further require contractors to display hotline posters prepared by the DOD Office of the Inspector General and post a notification of enumerated employee rights in work spaces.<sup>59</sup>

Current law prohibits contractors, subcontractors, their employees, and their agents from “engaging in severe forms of trafficking in persons, . . . procuring commercial sex acts, . . . [and] using forced labor in the performance of [a] contract.”<sup>60</sup> The proposed FAR rule expands this to include acts such as denying an employee access to his identity or immigration documents, “using misleading or fraudulent recruitment practices,” and charging recruitment fees.<sup>61</sup> Further, it requires contractors to provide for return transportation or cover the costs of return transportation at the end of employment, barring some limited exceptions.<sup>62</sup> Under the proposed rule, when providing housing, a contractor must meet the housing and safety standards of the host country.<sup>63</sup> Finally, employment contracts and similar work documents must be provided in the employee’s native language prior to the employee’s departure from his country of origin and should include a description of the work, wages, location, and employee’s rights.<sup>64</sup>

For any contract or subcontract in which the value of the supplies acquired or services performed outside the United States exceeds \$500,000, a contractor or subcontractor must, under the proposed rule, certify that it has implemented a compliance plan “appropriate to the size and complexity of the contract and the nature and scope of its activities.”<sup>65</sup> The certification must be presented prior to the award of a contract and requires that contractors perform due diligence to certify that “either (i), to the best of the contractor’s knowledge and belief, neither it nor its agents, nor any of its subcontractors nor their agents, has engaged in any [prohibited] activities, or (ii), if abuses have been found, the contractor or subcontractor has taken the appropriate remedial and referral actions.”<sup>66</sup> The proposed rule includes the minimum requirements for an adequate compliance plan: (1) an awareness program informing employees of the prohibited activities, (2) a process for employees to report abuses, (3) a recruitment and wage plan restricting the use of recruitment companies, prohibiting recruitment fees, and ensuring the enforcement of legal wage requirements, (4) a housing plan meeting the housing and safety standards of the host-country, and (5) procedures to prevent trafficking in persons abuses among any of the contractor’s agents or subcontractors.<sup>67</sup> Once established, a contractor must post details of the compliance plan at the workplace and on its website.<sup>68</sup>

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58. Ending Trafficking in Persons, 78 Fed. Reg. at 59,322–23.

59. Further Implementation of Trafficking in Persons Policy, 78 Fed. Reg. at 59,327.

60. FAR 22.1703(a)(1)–(3) (2014).

61. Ending Trafficking in Persons, 78 Fed. Reg. 59,317, 59,322 (proposed Sept. 26, 2013) (to be codified at 48 C.F.R. pts. 1, 2, 9, 12, 22, 52).

62. *Id.*

63. *Id.*

64. *Id.*

65. *Id.* at 59,322–23.

66. *Id.* at 59,322.

67. Ending Trafficking in Persons, 78 Fed. Reg. 59,317, 59,324–25 (proposed Sept. 26, 2013) (to be codified at 48 C.F.R. pts. 1, 2, 9, 12, 22, 52).

68. *Id.* at 59,325.

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The proposed amendments to the DFARS provide three additional requirements of covered DOD contracts. First, when performing contracts exceeding \$5 million, with the exception of commercial item procurements, a contractor is required to display "DoD Combating Trafficking in Persons and Whistleblower Protection hotline posters prepared by the DoD Office of the Inspector General."<sup>69</sup> The posters must be displayed in common work areas and on the contractor's website in English and any foreign languages spoken by a significant portion of the employees, if English does not suffice.<sup>70</sup> Second, for all solicitations and contracts that exceed the simplified acquisition threshold, a contractor must submit a representation that it will not engage in prohibited trafficking activities, has policies in place to protect the rights of its employees, and has notified its employees and subcontractors of their responsibilities and protections when reporting abuses.<sup>71</sup> Lastly, for contracts in which DFARS clause 252.225-7040 (Contractor Personnel Authorized to Accompany U.S. Armed Forces Deployed Outside the United States) applies,<sup>72</sup> a contractor must openly post in English and appropriate foreign languages an employee bill of rights establishing employees' rights, as follows: (1) maintain possession of identity and immigration documents, (2) timely receive agreed upon wages, (3) "take lunch and work-breaks," (4) "terminate employment at any time," (5) "identify grievances without fear of reprisal," (6) possess a copy of the employee's employment contract in a language the employee understands, (7) receive wages at or above the legal wage limit of the host-country, (8) be notified of the employee's rights prior to signing an employment contract, and (9) live in housing that meets the housing and safety standards of the host-country.<sup>73</sup>

In the event a contractor does not establish the necessary compliance plan and abide by the contractor's certified responsibilities, the Government has a number of remedies available to it, including terminating the contract for default or cause or suspending or debarring the contractor.<sup>74</sup>

The initial deadline for public comments on the proposed rules was November 25, 2013,<sup>75</sup> but it was subsequently pushed back to December 20, 2013.<sup>76</sup> Final rules will be issued in the forthcoming months after public comments are reviewed and addressed.

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69. Defense Federal Acquisition Regulation Supplement: Further Implementation of Trafficking in Persons Policy, 78 Fed. Reg. 59,325, 59,327 (proposed Sept. 26, 2013) (to be codified at 48 C.F.R. pts. 203, 204, 212, 222, 252).

70. *Id.*

71. *Id.*

72. See FAR 225.7402-5(a).

73. Further Implementation of Trafficking in Persons Policy, 78 Fed. Reg. at 59,327.

74. Ending Trafficking in Persons, 78 Fed. Reg. 59,324 (proposed Sept. 26, 2013) (to be codified at 48 C.F.R. pts. 1, 2, 9, 12, 22, 52).

75. *Id.* at 59,317.

76. Ending Trafficking in Persons, Extension of Time for Comments, 78 Fed. Reg. 69,812 (proposed Nov. 21, 2013) (to be codified at 48 C.F.R. pts. 1, 2, 9, 12, 22, 52).

**V. National Institute of Standards and Technology Preliminary Cybersecurity Framework**

On October 22, 2013, the National Institute of Standards and Technology (NIST) released a Preliminary Cybersecurity Framework<sup>77</sup> (Framework) as directed by Executive Order 13636 Improving Critical Infrastructure Cybersecurity, issued by the White House in February 2013.<sup>78</sup> The Framework seeks to help owners and operators of “critical infrastructure”<sup>79</sup> in industries such as electric power generation, transportation, and telecommunications by communicating cybersecurity expectations based on current best practices.<sup>80</sup> The ultimate goal is to provide a common language by which organizations can describe their current and target cybersecurity postures, identify opportunities for improvement, and measure progress.<sup>81</sup> It is meant to complement, not replace, existing cybersecurity risk management programs and act as a guide for organizations developing nascent cybersecurity programs.<sup>82</sup>

The Framework presents a three-pronged approach comprised of a Framework core spanning infrastructure sectors, a Framework profile specific to the practices of a particular system or organization, and Framework implementation tiers characterizing the progress of cybersecurity risk management within an organization.<sup>83</sup> The Framework core is a compilation of standards and best practices for organizations to manage cybersecurity risk in five functions—identify, protect, detect, respond, recover—along with underlying categories and subcategories.<sup>84</sup> Functions are also provided with corollary methodologies for addressing privacy and civil liberties considerations.<sup>85</sup> Each organization’s Framework profile represents the alignment of the Framework core with the business practices and resources of the organization and is intended to help an organization close gaps between its “current” profile and its “target” profile.<sup>86</sup> Finally, the Framework implementation tiers allow an organization to select its desired level of “rigor and sophistication in cybersecurity risk management practices” such that “selected levels meet the organizational

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77. Press Release, Jennifer Huergo, Nat’l Inst. of Standards & Tech., NIST Releases Preliminary Cybersecurity Framework, Will Seek Comments (Oct. 22, 2013), *available at* <http://www.nist.gov/itl/cybersecurity-102213.cfm>; *see generally* NAT’L INST. OF STANDARDS & TECH., U.S. DEP’T OF COMMERCE, IMPROVING CRITICAL INFRASTRUCTURE CYBERSECURITY EXECUTIVE ORDER 31636: PRELIMINARY CYBERSECURITY FRAMEWORK (Dec. 16, 2013), *available at* <http://www.nist.gov/itl/upload/preliminary-cybersecurity-framework.pdf> [hereinafter PRELIMINARY CYBERSECURITY FRAMEWORK].

78. Exec. Order No. 13,636, 78 Fed. Reg. 11,739, 11,740–41 (Feb. 12, 2013).

79. *Id.* at 11,739 (defining “critical infrastructure” as “systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems and assets would have a debilitating impact on security, national economic security, national public health or safety, or any combination of those matters”).

80. Patrick Gallagher, Acting Deputy Sec’y, U.S. Dep’t of Commerce, Under Sec’y for Standards & Tech., and Dir., Nat’l Inst. of Standards and Tech., Press Briefing: Preliminary Cybersecurity Framework (Oct. 22, 2013), *available at* <http://www.nist.gov/director/speeches/cybersecurity-framework-remarks-102213.cfm>.

81. PRELIMINARY CYBERSECURITY FRAMEWORK, *supra* note 77, at 1, ¶¶ 95–99.

82. *Id.* at 2, ¶¶ 100–104.

83. *Id.* at 2–3, ¶¶ 111–158.

84. *Id.* at 13–27.

85. *Id.* at 28–35.

86. *Id.* at 7–8, ¶¶ 292–298.

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goals, reduce cybersecurity risk to critical infrastructure and are feasible and cost-effective to implement.”<sup>87</sup>

The Preliminary Cybersecurity Framework recommends that an organization, after reviewing the Framework core, (1) identifies its objectives and overall risk approach, (2) creates a “current” profile, (3) conducts a risk assessment of its operational environment, (4) creates a “target” profile, (5) determines, analyzes, and prioritizes gaps, and (6) implements an action plan to close these gaps.<sup>88</sup> In this manner, the Framework serves to provide organizations “a way to set goals so that they can map out a progression and strengthen their security, lower risks, and protect themselves and their customers.”<sup>89</sup> The Framework “is not about eliminating cyber risks, it is about managing them effectively.”<sup>90</sup>

NIST developed the Framework by reviewing feedback gathered through a Request for Information issued in February 2013, a number of workshops held throughout the country, and stakeholder engagement.<sup>91</sup> Most recently, NIST issued a Request for Comments on the Preliminary Cybersecurity Framework on October 29, 2013,<sup>92</sup> and it contemplates having a final version of the Framework published by February 2014.<sup>93</sup>

**VI. *Shell Oil Co. v. United States*: Liability for Environmental Cleanup on WW-II Era Defense Contracts, Part Deux**

In *Shell Oil Co. v. United States*,<sup>94</sup> the U.S. Court of Federal Claims (CoFC) held that the “Taxes” clause of World War II (WW-II)-era defense contracts for aviation gas, or “avgas,” did not provide indemnification for environmental cleanup costs incurred decades later under the Comprehensive Environmental Response, Compensation, and Liability Act of 1978<sup>95</sup> (CERCLA).<sup>96</sup> In doing so, the CoFC essentially reversed course on its ruling in a previous *Shell Oil Co. v. United States*<sup>97</sup> case, as well as *Exxon Mobil Corp. v. United States*,<sup>98</sup> which was discussed in the 2011 Year in Review.<sup>99</sup>

The plaintiffs in this case were Shell Oil Company, Atlantic Richfield Company, Texaco, Inc., and Union Oil Company of California.<sup>100</sup> During WW-II, the U.S. Government urged the plaintiffs to enter into contracts to produce large amounts of avgas to fuel military aircrafts, which “unquestionably aided the war effort of the United States.”<sup>101</sup>

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87. PRELIMINARY CYBERSECURITY FRAMEWORK, *supra* note 77, at 9–10, ¶¶ 323–330. The Tiers progress from Partial to Risk-Informed to Risk-Informed and Repeatable to Adaptive. *Id.* at 9–11.

88. *Id.* at 11–12.

89. Gallagher, *supra* note 80.

90. *Id.*

91. PRELIMINARY CYBERSECURITY FRAMEWORK, *supra* note 77, at 40, ¶¶ 650–652.

92. Request for Comments on the Preliminary Cybersecurity Framework, 78 Fed. Reg. 64,478 (Oct. 29, 2013).

93. Press Release, Huergo, *supra* note 77.

94. *Shell Oil Co. v. United States*, 108 Fed. Cl. 422 (Fed. Cl. 2013).

95. 42 U.S.C. § 9601 (2012).

96. *Shell Oil Co.*, 108 Fed. Cl. at 425–26.

97. *See generally* *Shell Oil Co. v. United States*, 93 Fed. Cl. 439 (Fed. Cl. 2010), *vacated*, 108 Fed. Cl. 422 (Fed. Cl. 2013).

98. *See generally* *Exxon Mobil Corp. v. United States*, 101 Fed. Cl. 576 (Fed. Cl. 2011).

99. Mark J. Nackman et al., *Aerospace and Defense Industries*, 46 INT’L LAW. 287, 298–300 (2012).

100. *Shell Oil Co. v. United States*, 108 Fed. Cl. 422, 424 (Fed. Cl. 2013).

101. *Id.*



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Unfortunately, the production process for avgas generated “significant acid waste material” that was subsequently deposited at a location in Fullerton, California, referred to as the “McColl site.”<sup>102</sup> The plaintiffs’ contracts were terminated at the end of WW-II.<sup>103</sup> Many years later, the McColl site was subject to significant environmental cleanup under CERCLA and similar laws in the State of California, the costs of which were ultimately incurred by the plaintiffs after significant litigation.<sup>104</sup>

CoFC’s previous pro-plaintiff recovery decision in *Exxon Mobile Corp.* was based on a “broad interpretation” of a similar “Taxes” clause and rejection of the Government’s argument that the Anti-Deficiency Act (ADA) prohibited an open-ended indemnification.<sup>105</sup> The plaintiffs’ case centered around the word “charge” in the first sentence of the “Taxes” clause, which states,

Buyer shall pay . . . any new or additional taxes, fees, or *charges*, other than income, excess profits, or corporate franchise taxes, which Seller may be required by any municipal, state, or federal law in the United States . . . to pay by reason of the production, manufacture, sale or delivery of [avgas].<sup>106</sup>

CoFC rejected the plaintiffs’ interpretation that environmental cleanup costs were a “charge” under the clause, applying a plain meaning standard and ruling that the “Taxes” clause was meant for just that, taxes, and that environmental cleanup costs did not qualify.<sup>107</sup> CoFC also ruled that the plaintiffs’ rights to indemnification were discharged when their contracts were terminated at the end of WW-II.<sup>108</sup> Finally, CoFC agreed with the argument that the Government was not authorized to waive the ADA when it entered into the avgas contracts with the plaintiffs.<sup>109</sup>

This most recent holding in *Shell* would seem to significantly limit a previously viable theory of recovery for environmental cleanup costs for government contractors under WW-II era “Taxes” clauses. While both *Shell* and *ExxonMobil* involved WW-II production of avgas and its byproducts, this most recent CoFC interpretation of the “Taxes” clause would likely extend to other contaminants and possibly other wartime periods.

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102. *Id.*

103. *Id.*

104. *Id.* The court added that “[o]ddly, neither party cited this highly relevant decision in the briefs or at oral argument in this case”. *Id.* at 429 n.2.

105. *Shell Oil Co.*, 108 Fed. Cl. at 429 n.2.

106. *Id.* at 424–25 (emphasis in original).

107. *Id.* at 425.

108. *Id.* The court added that the plaintiffs had also stipulated as much during the course of related CERCLA litigation. *Id.* at 434–35.

109. *Id.* at 436–37.

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