

From *Law360*: Expanding The Scope Of 'Brokering' Under ITAR

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Law360, New York (January 10, 2012, 1:16 PM ET) -- On Dec. 19, 2011, the U.S. Department of State's Directorate of Defense Trade Controls published in the Federal Register^[1] its proposed revisions to the brokering regulations set forth in Part 129 of the International Traffic in Arms Regulations.

The notice includes other proposed changes to Parts 122 and 129 that we anticipate will directly impact registration and other compliance requirements for most DDTC-registered parties, even those that have managed to avoid Part 129 activities in the past. If adopted as proposed, the new brokering rules would clearly apply to more parties involved (even indirectly) in defense trade transactions and require manufacturers and exporters of defense articles to pay closer attention to Part 129 requirements.

Summary of Proposed Changes

The proposed Part 129 revisions have been in the making for eight years. As expected, the proposed rule “clarifies” the broad, extraterritorial reach of Part 129 by removing the qualifying phrase “who acts as an agent for others” from the definition of “broker” in § 129.2, but otherwise leaving intact an immensely broad description of which activities constitute “brokering.”

The key elements of the proposed rule changes include:

- replacing the current definitions of “broker” (including the “agent/acts for others” language) and “brokering activity” with a significantly broader approach — “any action to facilitate the manufacture, export, reexport, import, transfer, or retransfer of a defense article or defense service”;
- adding a new certification requirement in § 126.13, which would require all license applicants to identify all brokers and describe brokering activities related to the transaction(s) to be licensed;
- adding an illustrative (“including, but not limited to”) list of covered brokering activities in § 129.2(b), even though many of these same covered activities (i.e.,

- financing, insuring, transporting or freight forwarding) would be exempt from registration and prior approval requirements under a revised § 129.3(b)(2);
- adding a new § 129.2(e) to separately list activities not considered brokering activities and thus not covered by Part 129 at all, such as domestic transactions by U.S. persons (via an existing provision to the same effect being moved from § 129.2(b)), “official” activities of U.S. government employees (presently addressed as a registration exemption in § 129.3(b)) and certain administrative and legal services;
 - clarifying in a new § 129.2(d) the circumstances in which foreign persons are subject to Part 129, which includes any time the foreign person is present in the United States, brokering U.S. origin defense articles or services outside the United States, brokering outside the United States that will result in imports of defense articles into the United States, or acting on behalf of a U.S. person;
 - exempting “exclusive” brokers (including unaffiliated brokers) from separate registration, but only if they act on behalf of only one DDTC-registered company (and its listed affiliates) and if the registered company lists the exclusive broker in its own statement of registration;
 - removing dual registration requirements for manufacturers and exporters already registered under Part 122;
 - clarifying the types of material changes to information contained in statements of registration that require notification to the DDTC pursuant to § 122.4(a), making notification for all other changes due at the time of the registrant’s next annual registration renewal;
 - removing the concept of “prior notice” and consolidating authorization requirements under one subsection for “prior approvals”;
 - clearly tying prior approval requirements to registration requirements, such that exemption from registration also means exemption from prior approval requirements;
 - clarifying existing exemptions from prior approval requirements and adding a new exemption for brokering of U.S.-origin defense articles and services that are not designated as significant military equipment , provided that the end use is by an international organization or foreign government; and
 - limiting reporting obligations to persons required to register and allowing reports to be submitted either with annual registration submissions or within 30 days thereof.

Likely Impact on ITAR Compliance

The DDTC has been working on this proposed revision to Part 129 for nearly a decade, and has negotiated its content with industry and the Defense Trade Advisory Group. Unfortunately, many of the DTAG's recommendations were not adopted in the DDTC's proposal. We therefore do not expect the DDTC to make substantial revisions between now and publication of the final rule.

Nonetheless, comments are being accepted through Feb. 17, 2012, and may yield some influence on the final rule's content or elicit helpful commentary from the DDTC in the Federal Register notice announcing the final rule. Since few changes of substance or scope are expected, practicing brokers, potential brokers and those that work with them should immediately focus on the steps they must take to prepare for the new Part 129 brokering regime.

There is some good news for DDTC-registered parties in the Dec. 19 proposal. The revision to § 122.4(a) — which is not a brokering-specific provision — will alleviate the burden of § 122.4(a) “material change” notifications for changes in senior management and United States Munitions List categories. In addition, allowing DDTC registrants under Part 122 to identify themselves and their affiliates as brokers in one registration statement would be a welcome and sensible change to the brokering regime.

The ability to add unaffiliated but “exclusive” brokers to one's registration statement may prove to be another useful compliance shortcut. However, it is hard to predict whether independent, third-party defense brokers will prefer being tied to an “exclusive” brokering arrangement to maintaining their own, separate Part 129 registration. The latter would leave open the prospect of representing other DDTC-registered defense article manufacturers.

The rule also, however, broadly expands upon the scope of what activities are considered “brokering” and will bring more parties under the regulatory reach of Part 129. The DDTC is clearly sending a message that non-U.S. sales affiliates and third-party representatives or independent contractors that promote a DDTC registrant's catalog of products and services in nearly any way are going to be covered by the new definition of brokering activity, even if registration and prior approval requirements will be reduced at the same time (recall that anyone not required to separately register would also not be required to seek prior approval for their brokering according to revised § 129.7(a)(1)).

At least the accompanying changes will perhaps make it easier for multinationals to understand registration requirements and manage broker registrations for foreign sales affiliates, even if those registrations are covering a much larger number of parties.

The other change with a potentially large but less obvious impact is the revised § 126.13, which would require each license applicant to disclose brokering activity in export license applications. While not an entirely new requirement, the DDTC's decision to

make this part of the § 126.13 certification and solicit details about brokering activity in connection with every license application could cause delay in approvals where the applicant has disclosed the involvement of an unregistered broker.

Conclusions and Recommendations

If implemented without significant changes, this proposed rule change will both expand the scope of the brokering provisions in the ITAR and streamline associated compliance requirements. Brokers, potential brokers and DDTC-registered manufacturers and exporters should take proactive steps to review their affiliated and nonaffiliated sales and marketing partners and identify those parties that need to maintain separate registrations or can be added to their own (e.g., affiliates that broker and unaffiliated “exclusive” brokers).

Those parties that are registered should review the new registration and prior approval requirements and determine whether their activities allow them to cease separate Part 129 registrations and prior approvals. Given how long this rule has been expected, the DDTC may not show much flexibility on implementation once the final rule is adopted.

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