Overview

On March 28, 2005, the Bureau of Industry and Security (BIS) at the U.S. Department of Commerce (Commerce) issued an “Advance Notice of Proposed Rulemaking” (Notice) to expand provisions in the U.S. Export Administration Regulations (EAR) governing the transfer of controlled technology to foreign nationals in the United States or abroad, commonly known as the deemed export rule (the Rule). The Notice was drafted in response to a report issued in March 2004 by the Commerce Office of the Inspector General (OIG) that identified potential gaps in the control of such technology transfers.

While the established Rule imposes export control restrictions on access to U.S. technology based on a foreign national’s current nationality or place of permanent residence, the proposed changes would expand the restrictions to include consideration of a foreign national’s place of birth. In addition, the proposed revisions could expand the circumstances in which an export license is required from the U.S. government to give a foreign national access to technology related to the “use” of items that are controlled under the EAR. As this suggests, the proposed changes could have a significant impact on business operations for many companies and require those most affected by deemed export issues to review and significantly change their export compliance procedures and related business practices.

Background – The Deemed Export Rule

Under the EAR, an export includes the “release” of technology and source code to foreign nationals as an export. Depending on the technology involved and the nationality of the recipient, deemed exports may require authorization, in the form of a license issued by BIS, prior to release. The Rule, however, does not apply to persons lawfully admitted to the United States for permanent residence or to persons otherwise subject to residential protections under the U.S. Immigration and Naturalization Act.

The definition of “release” gives the Rule a very broad scope of application. Under this definition, technology or source code can be “released,” and thereby exported, through any of the following methods:

• the visual inspection by a foreign national of U.S.-origin equipment or facilities
• the oral exchange of information in the United States or abroad
• the application of personal knowledge or technical experience acquired in the United States.

These provisions make it possible for U.S. companies to violate U.S. export controls simply by granting foreign nationals, including employees, access to controlled technology or source codes.

Proposed Changes To The Rule

As required by the FY 2000 National Defense Authorization Act, the OIG conducted an interagency review to assess whether current deemed export control laws and regulations adequately protect against the release of controlled U.S. technology to countries of concern. The OIG also analyzed compliance with the Rule by U.S. industry, academic institutions and federal research facilities. In March 2004 the OIG issued a report that identified certain concerns with current U.S. technology control and provided recommendations to address those concerns.

In response to the OIG report, BIS issued the March 28, 2005, Notice describing certain proposed changes and soliciting public comment on these changes prior to

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the initiation of formal rulemaking. The March 28 Notice covered the following proposed changes to the EAR involving the Rule.

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The OIG has also recommended clarifications to two interpretations of the Rule that are included in Supplement 1 to Part 734 of the EAR. Essentially, the OIG suggested that the answers contained in the Supplement be revised in order to ensure that it is consistent with the proposed definition of “use” and current BIS policy. These changes are limited, however, to circumstances involving government-sponsored and university research.

**Implications For Affected Companies**

The OIG’s recommended changes could significantly expand the activities and persons subject to export licensing requirements under the Rule. As an initial matter, if the changes are implemented, companies with controlled technology will need to review and, as appropriate, revise their export compliance programs to adjust to the revised regulations and/or new policy. The proposed revisions suggest that specific areas of concern for initial review will include screening of foreign employees, business partners and independent contractors (e.g., outsourcing) to ascertain their country of birth. Moreover, technology control plans and any associated systems (e.g., company intranets) will need to be analyzed to ensure that access is restricted for foreign nationals who may perform discrete functions related to controlled equipment maintained by the company (e.g., repairs and maintenance).

Ultimately, the practical impact on individual companies will depend on a number of factors specific to their individual operations, including: (1) the nature and extent of controlled technology maintained by the company – including technology that is required for the “use” of controlled equipment under the EAR, (2) the involvement of foreign nationals in company operations associated with controlled technology and (3) the structure of the company’s current export compliance program, including its related screening procedures and technology control plan. In this regard, the most burdensome impact of the proposed changes is likely to be felt by those companies that utilize significant amounts of sensitive and controlled technologies in their operations and rely on outsourcing in production or servicing, or other employment of non-U.S. nationals. Accordingly, the proposed changes could have a significant impact on many companies in telecommunications, semiconductors, aerospace, financial services and other sectors where such considerations often apply.

**Conclusion**

Because BIS did not propose specific modifications to the language of the regulations in the Notice, the exact contours of any final changes to existing regulations are uncertain at this time. It is also unclear precisely when a final rule will be issued by BIS. However, it is clear that an expansion of deemed export restrictions will be forthcoming. This gives affected companies useful lead time to consider and develop an approach to possible modifications in established provisions of the EAR. Moreover, it is not too late to submit comments to BIS on the possible impact of, and recommended changes in, the approach advanced in the Notice to these issues.

BIS has requested submission of comments on how the proposed rule could affect industry, academic institutions, U.S. government agencies and holders of export-controlled technology. These are due for submission to BIS by May 27, 2005. BIS has in particular requested comments on a number of related issues. These include:

- the impact the proposals will have on technology developers and manufacturers, academic institutions and U.S. government research facilities
- data on the number of foreign nationals in the United States who will face licensing requirements if the OIG’s recommendations are adopted and impact on compliance, e.g., cost, resources, procedures
- any alternative suggestions regarding the concerns raised by the OIG

The comment procedure provides industry with an opportunity to assess preliminarily the impact of the proposed changes and participate in shaping the language of any revisions to regulations or policy at an early stage. Accordingly, if the proposed changes raise significant concerns for your company, the comment period provides an important opportunity to communicate related concerns to officials at BIS responsible for implementing these changes.