Modelling Dual-Use Trade Control Systems

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Transnational Consortia For Dual-Use Goods and National Export Control Regimes

Facing Diversity

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In spite of the existence of the EU dual-use Regulation (EC Regulation 428/2009, hereinafter "dual-use Regulation") which has harmonised all export trade with dual-use goods (all economic goods except weapons and defence items) in the EU Common Market, there remain important loopholes, so that national export control law of the EU Member States is still very decisive for the export law in action. This contribution wants to demonstrate some of the consequences of this diversity of different national export law of the EU Member States and what impact it can have on the export law in action.

Case 1: the organisational restructuring and its impacts on export law in action: former situation

Originally, the German company G was operating on its own and shipping its listed goods (especially listed electronic goods) directly to its clients overseas. G has a limited number of customers worldwide, most of them are research organisations which are supplied permanently.

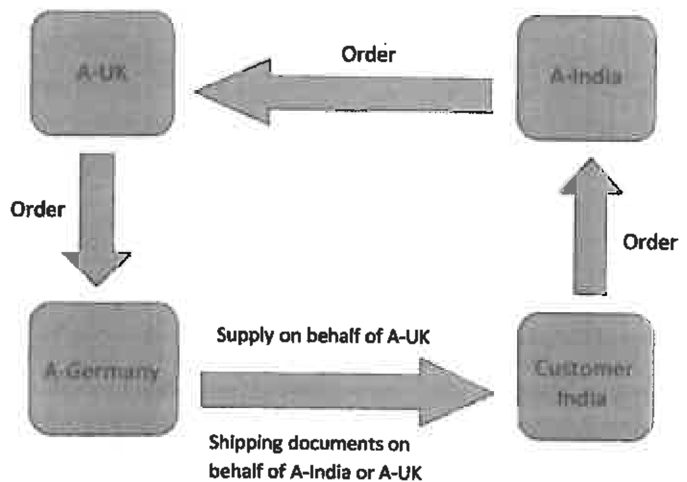
Question: what must G do in order not to always apply for each export licences permanently?

New situation: G was bought by the US consortium A (now G is renamed: A-Germany); this leads to the following organisational restructuring: if a customer in India wants to order these goods from the Indian company A-India, a subsidiary of the US consortium A, A-India will send this order to the centralised ordering company A-UK, another subsidiary of the US consortium A. A-UK is not only collecting all world-wide orders but is also the responsible company for world-wide export controls of the US consortium A. A-UK sends this order to A-Germany, because only A-Germany is producing these goods. A-Germany will produce this

good on behalf of A-UK and A-Germany will send this good on behalf of A-UK to the customer in India. The shipping documents including the bills are filled out by A-India (or if a national subsidiary of A is missing in this country: by A-UK).

Questions: which of these companies is now exporter? And what must this company do under which national law in order not to always apply for each export licence permanently? What are the main differences between former and new situation?

See the following picture:



Case 1 in the former situation: bulk licences under national German export law

In the former situation, it was obvious that German national export law applied to the operating of G's exports: G was not a subsidiary of any international consortium, but was only acting in Germany.

Since the goods are listed, under Article 3 of the dual-use Regulation an export licence is required in each case of export to a third country (outside the EU). The question arises whether German national export law knows any trade facilitation in order to prevent that G has to apply for an export licence in each individual case. It must be checked whether any of the following two German bulk licences could be used by G, either the SAG (*Sammelausfuhrgenehmigung*) or the HBG (*Höchstbetragsgenehmigung*). The main difference between the SAG and the HBG in Germany consists in the fact that under the HBG G can export his goods only to one

customer without applying for an individual export licence, while under the SAG he can do this to several reliable customers if he fulfils the high requirements of the SAG.

The differences between the two German bulk licences SAG and HBG are as follows:[1]

- The SAG can only be applied for in case that the German exporter is regarded as reliable by the German export agency BAFA and if he has received 50 export licences from BAFA within the last year, except that special circumstances can be demonstrated (e.g. that a dramatic increase of export numbers is to be expected). The German exporter must demonstrate that he has an ICP (internal compliance programme) for export controls, including formally nominating the Board's Export Director as responsible person (Ausfuhrverantwortlicher) to the BAFA. The SAG can be used for exports to several enumerated customers, under the two conditions that (1) these customers are regarded as reliable by BAFA and that (2) the German exporter checks whether the customers really comply with the use and end-use location indicated in their EUC (end-use certificate). The SAG is valid for 2 years (and can be extended once again).
- The HBG can only be applied for in case that the German exporter is regarded as reliable by BAFA; there is no need for him to demonstrate that he has received a specific number of export licences from BAFA, also an ICP is not necessarily required (although it is recommended). The HBG can be used for all successive shipments to only one customer. The German exporter must send the framework agreement for these successive shipments and an EUC of this one customer. The HBG is valid for 1 year (and can be extended once again).

Since the formal requirements for the SAG are very demanding, it is very likely that G will apply for the HBG for all customers he will ship to successively. In the case that he has 10 such customers, he will apply ten times for the HBG. Since the application procedure for this is only slightly longer than for individual export licences, it may take between 3 and 6 months to get this HBG from BAFA for these 10 customers.

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1 Cf. German Runderlass Außenwirtschaft 10/2003 of 2 June 2003 (in BAFA (ed.), *HADDEX Handbuch der deutschen Exportkontrolle*, loose-leaf, Vol. 6, No. 730) concerning SAG, and comments by BAFA, in BAFA (ed.), *HADDEX*, Vol. 1, Part 7, No. 495 *et seq.* and No. 560 *et seq.* Cf. also Hohmann, *Angemessene Außenhandelsfreiheit im Vergleich*, Tübingen: Mohr 2002, pp. 243 *et seq.*

Case 1 in the new situation: bulk licences under national British export law

Here, the question which of the companies involved shall be regarded as "exporter" is decisive for the following reason: under Article 9 dual-use Regulation the place of establishment of an export company is decisive for the national export law to be applied for this export.[2] Therefore, it must be decided which of the companies involved shall be regarded as "exporter".

Under Article 2.3 (i) dual-use Regulation, it is decisive who is the "principal" of the export (so-called *procedural exporter*): this is the person "on whose behalf an export declaration is made", the person "who holds the contract with the consignee in the third country and has the power for determining the sending of the item out of the customs territory of the Community" and benefits most from this export. In this case, the export contract is concluded between A-UK and the customers, since the shipping papers regard A-India as supplier, while A-Germany and A-India are acting only as sub-suppliers of A-UK. And A-UK has the power of determining the sending of the item out of the customs territory of the Community. Very likely, A-UK will be regarded as procedural exporter.

Under national export law (Section 2 Paragraph 3 of the German Export Control Act), an additional exporter definition applies especially for purposes of criminal export law. The decisive factor here is which person is acting for the departure of goods from Germany to foreign countries (so-called *material exporter*).[3] It is very likely that A-Germany is regarded as "exporter" in this regard.

The question to decide here, namely what is the "place of establishment of an export company" in the sense of Article 9 dual-use Regulation, the EU definition of "exporter" under Article 2.3 (1) dual-use Regulation must be applied. Therefore, decisive is the place of establishment of A-UK, i.e. national British export law, and no longer national German export law.

British export law offers especially two kinds of bulk licences, namely OIEL (open individual export licence) and GPL (global project licence) – the latter is available only for military goods and defence items. If no bulk

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[2] For all other exports for which an authorisation is required under this Regulation, such authorisation shall be granted by the competent authorities of the Member State "where the exporter is established".

[3] On the differentiation between procedural and material exporter, see Hohmann, John (eds.), *Kommentar zum Ausfuhrrecht*, Beck: Munich 2002, at pp. 289 *et seq.*, 363 *et seq.* and 1229-1231. See in particular: Hohmann, John, "Update Anhang 2 zur Dual-use-VO", note 15 *et seq.*; Just, "Paragraph 4 AWG", note 41 *et seq.*; Balzer, Hohmann, "Paragraph 8 AWV", notes 5 *et seq.*

licence is available, a SIEL (standard individual export licence) must be applied for. A-UK must now check, whether it wants to apply for SIEL or for the bulk licence OIEL. The differences are as follows:[4]

- The SIEL has similar functions as the German individual export licence, including some functions of the German HBG, since SIEL is often used for long-term contracts, projects and repeated business. SIEL is an export licence for controlled goods (especially for listed dual-use goods) specific to one exporter and only one consignee, and it is valid for 2 years. Thus SIEL is an individual export licence which can also be used if the British exporter wants to export these goods to only one customer in several successive shipments (based on a framework agreement) within 2 years.
- By contrast, the OIEL is a bulk licence having similar functions as the German SAG, since the OIEL can be used for the export of multiple shipments of specific controlled goods (especially of listed dual-use goods) to specific destinations, subject to meeting detailed terms and conditions. It may also name the consignees or end-users of the goods concerned – unlike the SIEL which always names these parties. To justify applying for an OIEL, the British exporter must have a record of at least 20 relevant SIEL applications in the previous year; where this is not possible (e.g. in case of new business), the British exporter should argue that there is an increasing number of export shipments. The British exporter should describe his ICP, he should add a list of very few countries to those the OIEL is applicable, and he should add the names and addresses of consignees and if possible of end-users (or at least a list of clients or end-users which could very likely be covered by his exports), and EUC undertakings from the consignees or end-users.

A-UK has now the choice whether it wants to apply for the SIEL; if he has 20 consignees to be delivered successively, he would need 20 SIEL. Or he could apply for the OIEL, in this case, this one bulk licence may be sufficient to undertake the exports to all consignees.

Case 1: main differences between former/current situations (German/British bulk licences)

While it is very cumbersome and time-consuming to apply for a SAG in Germany – already the requirement to have a record of at least 50 individual export licences in the previous year is a high barrier for most

[4] Results of the author's phone calls with the BIS (July 2012).

companies, and the application procedure may take up to 1 year –, nearly the same functions can be received in the UK with the British OIEL, and the application procedure can be done within 60 working days (at least in 60-80% of cases). The conditions for applying the SAG are much higher than for the OIEL. The application procedure for the OIEL is quicker since the British export agency (in contrast to the German BAFA) will not check whether the exporter will fulfil with all requirements, instead BIS will undertake a compliance audit of the British exporter's business within three months after the first OIEL has been granted, and thereafter at intervals of between 3 and 36 months.[5]

The British OIEL is more flexible than the German SAG since not necessarily all end-users must be named during the application procedure, if at least a list of very typical end-users and those very likely to be named thereafter is submitted to BIS. It is no wonder that the number of granted OIELs is much higher than that of SAGs: in 2011, the BIS has issued OIELs to 406 exporting companies, while the number of German companies having a SAG is very limited, ca. 200 – 300 companies altogether, at least for the year 2001.[6]

Example 2: exports of a chemical company

CASE 2 A: The German chemicals company G sells a product to its subsidiary I in Italy. Later I sell this product outside the Community to S in South Africa. Who is the exporter: G or I? What practical steps should G and I take in order to simplify exports?

CASE 2 B: G wants to sell one of its products: a chemical mixture containing 15% aluminium powder, if possible from the stocks of its Italian subsidiary in Italy. This product is listed on position 1C111 lit. a under specific conditions. The interpretation of the German export agency is that it is only listed if at least 30% of this mixture contains aluminium powder. The interpretation of the Italian export agency is that it is already listed if the mixture contains only 10% aluminium powder. What should G do?

Concerning case 2 A

In Case 2 A it is very difficult to see which of the two parties is the procedural exporter, due to a triangle situation: the owner of the good (G) is not the contract partner of S, but G is supplying S, either directly

[5] See: "Open Individual Export Licences OIEL", in: www.businesslink.gov.uk/exportcontrol.

[6] See for these numbers: BIS, "UK Strategic Export Controls Annual Report 2011", at pp. 32 *et seq.*; Hohmann, "Bundestag Ausschuss-Drucksache 17(9) 1053 (neu)", at p. 8 *et seq.* and *Hohmann, op. cit.*, p. 244.

or via I, in both situations G is doing this under the instruction of I. It could be argued that G is procedural exporter, since I derives the power of control only from G, or that I is procedural exporter, since I is the principal. All depends on the contractual relationship and/or the division of labour between G and I.[7] The best recommendation for simplifying exports would be to have very clear contracts. Especially, if G wants to deliver the products directly to S, the best would be to have a contract between G and S. If only I has the contract and would deliver to S, then only I would be regarded as procedural exporter. In addition, the division of labour should be specified, that only the one doing the direct export to S should have control over the export, so that only he is regarded as procedural "exporter".

The question regarding which national export agency is competent also has two aspects: the German export agency BAFA has competence due to the *principle of residence* under Article 9 Paragraph 2 dual-use Regulation since the company's headquarter is in Germany. The other possibility is the *principle of the addressed agency:* that the Italian export agency is competent in case the export application is addressed to the Italian export agency under Article 11 Paragraph 1 dual-use Regulation and if the Italian and the other concerned national export agencies consult with one another. If the German export agency BAFA does not oppose to the Italian competence within 10 (or 30) working days, the Italian competence is accepted (Article 11 Paragraph 1 sentences 4 and 5 dual-use Regulation). In general, the end-use certificate of one country – regularly that of the final end-use (here South Africa) – is sufficient. If however the final end-use is not known at that time, than the EUC of the first destination could be accepted.

Concerning case 2 B

EU export law does not know any definition under which situations a mixture is listed, whether 10% or 30% would trigger this. At least one of the global non-proliferation regimes (MTCR) seems to accept a 30% rule for mixtures. Since there are no binding EU norms saying which mixture is decisive for triggering the match of the list position, EU Member States can decide which %-values is decisive for this. Therefore, there are no legal objections that the Italian export agency accepts a 10% level, while the German export agency accepts the 30% value.

In this case, G has the choice of a strategic selection which of the national export agencies is competent for this export application, depending on what G favours. Since G will prefer the situation not to be forced

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[7] See BAFA, *op. cit.*, Vol. 1, Part 1, note 47 *et seq.*

to apply for an export licence, he will apply to the German export agency. Even if this good is already in the stocks of the Italian subsidiary I, this is possible due to the fact that the headquarters of G is in Germany. However in this case, G should consult with I whether a licence was already denied by Italy in the past. If denied, Germany may only decide on this application after having previously consulted with Italy (in order to meet the no-undercut notification requirement).

Results of case 2

Although the dual-use Regulation wanted to harmonise the conditions for exporting dual-use goods in the EU, it still offers some potential for "forum shopping". In order to apply at the national agency offering the lowest levels of export controls, transnational companies may sell their goods to a subsidiary in another EU Member State. This national export agency is then responsible, at least if it consults with the national export agency of the residence of the headquarters. This condition can be easily fulfilled by waiting 10 (or 30) working days whether the national export agency of the residence will object.

Results of both cases

The EU Common Market for dual-use goods is not yet a level-playing field in which all EU Members face same European conditions – instead the national export law of EU Member States still has a large influence on the export law in action.

- The question which national general licence is applicable or what kind of bulk licence could be used is largely dominated by national export law, in spite of all efforts of harmonisation by the EU. This can lead to results such as that an export licence is required under EU export law, while the national export law of one EU Member State renounces this requirement for all goods with a value below 5,000 EUR (German AG12). Or – as Case 1 shows – this can lead to results that a bulk licence like the British OIEL can be easily applied for within 2 months, while it would require more than 1 year to apply for the German SAG or half a year for the HBG, and in case of the SAG, it may even be too cumbersome or nearly impossible to comply with all conditions for it, while the corresponding British bulk licence gives nearly same advantages, although the bureaucratic burden is much less in case of Great Britain as compared with Germany.
- The question regarding which national interpretation standards will apply is also largely dominated by national export law. In case that EU export control law does not give binding results, all national export agencies can decide on their own which definition

and which standards should apply. As Case 2 shows, the standards in one EU Member can be much lower than in the other. This leads to competitive disadvantages between the EU Members.

- Some EU Member States still accept unilateral export controls which are applicable only in this State, but not in the other EU Members. Especially German export law knows several unilateral export controls which are not shared by the other EU Members.[8] Also in this case, the standards in one EU Member are much lower than in the other. This also leads to competitive disadvantages between the EU Members.
- This national diversity is a fact where especially transnational consortia can take advantage of it.
- They can sell their goods to the stocks of that EU Member having the lowest export control standards and then address the application to this national export agency.
- Or they can, if they want, also ask the national export agency of the headquarters to decide on this export matter. The question which national export agency has competence could be made dependent on the lowest export control standards.
- This can lead to a strategic "forum shopping" that always the national export agency with the lowest standards shall have competence.

Such a strategic "forum shopping" is not acceptable in the EU Common Market. Therefore, the Green Paper for the revision of the EU dual-use Regulation of 30 June 2011 (COM (2011) 393) has emphasised that differences in national approaches to dual-use export controls should be abolished as far as possible. The EU Commission has made clear that this task should cover administrative, substantive and operational measures:[9]

- Administrative: Member States should harmonise their approaches to such issues such as registration requirements and questions which kind of ICP is required for bulk licences.
- Substantive: Member States should harmonise their national authorisations available under the dual-use Regulation, in order to

[8] See especially the licence requirements under Paragraph 9 of the German Export Control Order AWV (for non listed goods if there are "red flags" for a sensitive use in a nuclear installation in a nuclear sensitive country) and under Paragraph 11 Paragraph 2 AWV (for intra-Community transfers of nationally listed dual-use goods if there are Red Flags that these goods will be shipped to third countries); cf. the critical remarks by *Hohmann*, *op. cit.*, at pp. 323 *et seq.* and at pp. 511 *et seq.*

[9] European Commission, "Green Paper", document COM (2011)393, p. 5.

prevent that broad national authorisations are applicable in one Member State which are not available for other EU Members.

– Operational: Member States should harmonise their different interpretations of control list entries and harmonise their use of the catch-all provisions for non-listed goods.

One of the main items of the Green Paper is the "level playing field for EU exporters" within all EU Member States. The EU principles of the economic freedoms (like the free movement of goods), the equality between the Member States, the Single Market with the EU Common Commercial Policy, they all urgently require that this "level playing field for EU exporters" is also created as soon as possible for the export policy in order to avoid facing diversity.