V. The role of industry in dual-use and arms trade control

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Governments around the world increasingly recognize that partnership with industry is a prerequisite for preventing—or at least increasing barriers to—the proliferation of nuclear, biological and chemical weapons and their delivery systems, as well as illegal shipments of conventional arms. In recent years, two sets of factors have also shifted the nature of the relationship between governments and the private sector in the field of dual-use arms export controls.

First, there is an ongoing expansion in the range of private sector entities that are potentially subject to trade controls. International and regional legal instruments and guidelines require states to put in place not just export, but also associated transit, trans-shipment and brokering controls for both dual-use items and conventional arms.[1] As a result, export controls affect not just the producers of controlled items, but also brokers and transport service providers.[2] Moreover, today's technological and scientific reality means that academia and research institutions often 'export' controlled items (goods, software and technology) in both tangible and intangible forms. For example, scientists publish research involving controlled items and increasingly do so online. Scientists also exchange advanced technical information about controlled items and transfer controlled items between laboratories, particularly in the biological field.[3] Intangible technology transfer is also a key element of daily interaction in global business structures and supply chains, including their research and development activities. In addition, the range of items that are subject to export controls has expanded in recent years. For example, the recent expansion of controls on the trade in information and communication technology surveillance systems created export control obligations for a range of companies that had little or no prior experience in this area.[4]

Second, today's trading environment is increasingly complex, creating an expanding array of mechanisms through which goods can be transferred and a significant increase in the number of layers of responsibility in relation to the shipment of goods. This makes it increasingly difficult to prevent proliferation through traditional enforcement instruments such as licensing

[1] Included in such instruments and guidelines are the various sanctions regimes and notably United Nations Security Council Resolution 1540, 28 Apr. 2004. See chapter 3 in this volume.

[2] To some extent insurance companies and financial institutions are affected by trade controls, although this is mostly confined to sanctions implementation.

[3] Clevestig, P., *Handbook of Applied Biosecurity for Life Science Laboratories* (SIPRI: Stockholm, 2009).

[4] SIPRI and Ecorys, 'Final report: data and information collection for EU dual-use export control policy review', European Commission, Brussels, 6 Nov. 2015.

requirements and customs controls. For example, new technological developments mean that controlled technology and software can be easily transferred through electronic transactions and stored in clouds. This requires different detection mechanisms, such as company audits, but also preventive action on the part of industry, such as organizing awareness seminars. In addition, the processes through which physical goods are shipped internationally involve a wide range of supply chain actors, such as integrators, shipping companies, shipping agents, freight forwarders and customs agents, as well as air carriers, road transport and fast parcel operators, and brokers. This creates additional mechanisms through which illegal transfers can be concealed but also an expanded range of potential partners for national authorities to engage with in the process of revealing such shipments. Fast parcel trade in particular is increasing and has been used for illegal shipments of dual-use items.[5]

These processes have helped drive two sets of developments among national licensing authorities, although other factors have also played a role. These include resource constraints and consequent efforts to shift more responsibility to companies and ex-post monitoring, and national efforts to reduce the impact of additions to the control list for both administrations and exporters. First, there has been a growing shift towards a reduction in licensing requirements for less sensitive exports, particularly through the use of 'global licences' and 'general licences' as well as other reductions in licensing requirements.[6] Second, there are ongoing attempts to incentivize the adoption of internal compliance programmes (ICPs) in companies and to improve standards in this area. The European Union (EU) has been closely involved in discussions about the first set of developments. There has been some discussion on ICP-related issues within the export control regimes. This section analyses each of these developments in turn, making particular reference to recent developments in Europe and North America, before drawing some initial conclusions about their long-term implications.

Reduction in licensing requirements

In recent years, a number of states have increased the range of exports that are covered by 'global licences' or 'general licences' rather than individual licences. Such licences generally do not require an exporter to submit indi-

[5] British House of Commons, Business, Innovation and Skills, Defence, Foreign Affairs and International Development Committees, 'Scrutiny of Arms Export Controls (2010): UK Strategic Export Controls Annual Report 2008, Quarterly Reports for 2009, licensing policy and review of export control legislation'.

[6] 'Global licences' are granted to a particular exporter and allow for multiple transactions of specified items to a specific end user. 'General licences' cover exports of a particular set of items to a particular set of destinations. Provided certain criteria are met, an exporter does not have to submit an application before using a general licence.

vidual applications for each shipment or transaction, but may attach specific conditions such as compliance measures or specific record-keeping requirements. They cover multiple shipments of specified goods to specified end users or destination countries, are usually valid for several years and may or may not be specific to certain exporters.

The United Kingdom has increased the range of exports that are subject to open licences as opposed to standard individual licences for each individual transaction. The UK has published around 40 Open General Export Licences (OGELs), a type of general licence. In October 2015 it published a new OGEL for companies to use when exporting military goods 'which have been imported into the UK for repair or replacement' as well as spare parts for military equipment previously supplied 'with the approval of the UK licensing authority'.[7] The British Government is preparing at least three new OGELs.[8]

Germany has a long tradition of offering general licences (*Allgemeingenehmigungen*) for both dual-use items and military items to its exporters. Currently, Germany has published 16 general licences: 10 for military items and 6 for dual-use items, which complement the EU's 6 general licences. Most recently, Germany introduced general licences for exports of frequency inverters and specific pumps and valves. In addition, German exporters can apply for global licences, which cover multiple shipments to multiple end users in multiple destinations or, for example, exports to a trader, which have record-keeping requirements regarding the end user. Their use may be subject to conditions such as compliance requirements regarding the end user and, in some cases, even the requirement to name their customers in the licence. Their use is always subject to certain conditions, such as keeping the internal compliance programme up to date.

States are also taking other steps to reduce the regulatory burden associated with the export licensing process. France, which has traditionally had one of the more bureaucratic export licensing procedures in Europe, is reducing the regulatory burden it imposes on exporting companies. In June 2014 France completed the introduction of a range of steps aimed at simplifying the export licensing process as part of its national implementation of the EU's Intra-Community Transfer (ICT) Directive (see below). This included replacing its two-step export licensing procedure for military equipment, which consisted of the *Agrément préalable* [Prior agreement] and the *Autorisation d'exportation de matériel de guerre* [Export authorization

[7] World ECR, 'UK ECO publishes new OGELs', 8 Oct. 2015.

[8] The three new OGELs will cover low-risk military and dual-use electronics and cryptographic products. Tauwhare, R., 'UK export controls and sanctions: a look ahead to 2016', *World ECR*, no. 46 (Dec. 2015).

for war material]—with an individual licence, as well as introducing general and global licences.[9]

In the United States, the ongoing Export Control Reform (ECR) is aiming to reduce the regulatory burden on US industry and focus controls on the most sensitive technologies and destinations. To date, the main focus of the ECR has been to move tens of thousands of items from the US Military List (USML) to the Commerce Control List (CCL), where they will be subject to less stringent licensing controls on exports to trusted destinations.[10] By the end of this process, the US Government plans to have moved the majority of the items on the USML to the CCL or to have decontrolled them completely.[11] At the close of 2015 a number of key elements of the ECR were still to be resolved, including a number of outstanding revisions to the USML.[12] The US Government is aiming to resolve these remaining issues before the end of 2016.[13] The USA uses the licence exception Strategic Trade Authorization (STA) as a form of general licence and removes licensing requirements for the trade in many dual-use items with 36 countries, including 25 EU member states.[14] A number of Asian countries, such as Japan, Malaysia and Singapore, have also introduced different types of general and global licence, called bulk or multiple use permits, in addition to individual licencing.[15]

EU-level processes

A number of EU-level processes have been put in place to facilitate or drive a shift towards a greater use of global licences and general licences among member states. The EU's ICT Directive was agreed in 2009 and forms part of a wider package of EU efforts to reduce barriers to intra-EU cooperation in the defence industry.[16] It encourages EU member states to grant general licences for exports: (*a*) to the national armed forces of another member

[9] Béraud-Sudreau, L., 'French adaptation strategies for arms export controls since the 1990s', IRSEM, Paris Paper no. 10 (Oct. 2014).

[10] Fergusson, I. F. and Kerr, P. K., *The US Export Control System and the President's Reform Initiative*, Congressional Research Service (CRS) Report for Congress R41916, Summary (US Congress, CRS: Washington, DC, 13 Jan. 2014).

[11] White House, Office of the Press Secretary, 'White House Chief of Staff Daley highlights priority for the President's Export Control Reform Initiative', 19 July 2011.

[12] Nilsson, B., Deputy Assistant Secretary for Defense Trade Controls, US Department of State, Bureau of Political-Military Affairs, Statement Before the House Small Business Committee, Hearing on Export Control Reform, 11 Feb. 2016.

[13] Nilsson (note 12).

[14] US Department of Commerce, Bureau of Industry and Security, Export Administration Regulations, 16 Mar. 2016.

[15] See the Center for Information on Security Trade Control (CISTEC), Overview of Japan's Export Controls, 4th edition; Malaysian Ministry of Trade and Industry, Strategic Trade Act 2010, 'Online permit application process flow'; and Singapore Customs, Customs schemes, licences and framework.

[16] Directive 2009/43/EC of the European Parliament and of the Council of 6 May 2009 simplifying terms and conditions of transfers of defence-related products within the Community, *Official Journal of the European Union*, L146, 10 June 2009.

state; (*b*) to a 'certified company' in another EU member state; (*c*) that are taking place for demonstration, evaluation or exhibition purposes; or (*d*) that are being returned to the original manufacturer for maintenance or repair. However, member states insisted on defining the scope of these general licences at the national level and have exempted different sets of items from their coverage, creating a lack of standardization.[17]

Under the Dual-use Regulation, the EU has issued six EU General Export Authorisations (EUGEAs)—a type of general licence. The European Commission's proposal for a revised Dual-use Regulation is expected to include additional EUGEAs for intra-company technology transfers, low-value shipments, large projects, cryptography and specific dual-use items such as frequency changers, among other things.[18] However, reaching EU-wide agreement on new EUGEAs has proved challenging in the past. EU member states differ about which technologies and destinations should be covered by EUGEAs, depending on the size and composition of the national industries affected by dual-use export controls and states' foreign and security policy priorities. Several states prefer to issue nationally defined general licences. Although this is a minority, it includes the EU's biggest dual-use exporters: France, Germany, Italy and the UK.[19]

Developing incentives and standards for ICPs

An ICP is an arrangement that a company puts in place to ensure that 'it is completing legal transactions, obeying the regulations enacted by the government, and fulfilling company export policies'.[20] In order to be effective, the procedures, policies and infrastructure put in place must be based on a broader culture of compliance within the company, especially given that many individuals within a company could violate trade controls. It could be argued that compliance can result in cost reductions due to access to simplified export procedures, the reduced risk of illegal exports and therefore of penalties and damaging the brand or reputation, and the increased potential for attracting customers and investors. Ongoing work in this area

[17] See European Parliament, DG for External Policies Policy Department, 'The impact of the "defence package" directives on European defence', June 2015; and Mampaey, L. et al., 'Study on the implementation of Directive 2009/43/EC on transfers of defence-related products', GRIP, 22 Aug. 2014.

[18] European Commission, Presentation at the 2015 Export Control Forum, Brussels, 5 Dec. 2015.

[19] Information Note, Regulation (EC) no. 428/2009 setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items, Information on measures adopted by member states in conformity with articles 5, 6, 8, 9, 10, 17 and 22, *Official Journal of the European Union*, C51, 13 Feb. 2015, pp. 31–35.

[20] Institute for Science and International Security (ISIS), 'Key elements of an effective export control system', 2003. Depending on the company, export controls may form only one element of a company's compliance systems, which can include a range of other regulations such as anti-corruption policies and safety standards.

is focused on creating additional mechanisms to either incentivize or oblige the adoption of ICPs, and drafting improved standards or creating new ones for sections of industry where none exist.

Some states have gone so far as to require companies to put in place ICPs or specified ICP elements they need to have in place in order to be able to apply for export licences. In Poland, companies are required to have an ICP in place in order to obtain export licences for arms, although no longer for dual-use items.[21] The requirement applies to 'manufacturers, exporters, users and scientific research centres'.[22] Under Romania's secondary legislation, licence applications to export or broker military equipment will be rejected if the applicant does not have an ICP in place.[23] The primary and secondary legislation regulating dual-use exports also contains explicit requirements for an ICP. Similar provisions are also in place in Hungary. German law requires the appointment of an 'export control responsible person' from senior management who will be personally liable for breaches and is thus responsible for establishing an ICP. Austria and Hungary have similar provisions.

EU-level processes

A number of systems have been put in place in the EU in recent years to facilitate trade by 'reliable companies' with solid ICPs, with regard to controls on both conventional arms and dual-use items. Under the ICT Directive, if a company wishes to receive goods exported under a general transfer licence, it must be certified by the national authorities. As part of this process, the company must provide a description 'of the internal compliance programme or transfer and export management system'. However, certification rates have been far lower than was initially hoped, largely due to confusion in industry about the benefits of the process, given the variety in the coverage of member states' general licences (see above). As of 31 January 2016, 48 companies in 14 EU member states had been awarded certified status.[24]

[21] An ICP is, however, strongly recommended for dual-use exporters according to a communication from the Polish licensing authority on 25 Apr. 2016. Article 11 of the Polish law of 25 May 2012 'amending the Act on foreign trade in goods, technologies and services of strategic importance to the security of the State and to maintaining international peace and security and certain other acts' states: 'An entrepreneur applying for an authorization for trade in military goods or using a national general authorization for trade in military goods shall establish and implement an internal system of control and management of trade in military goods, hereinafter referred to as the "internal control system"'. For an English translation of the law, see the Polish Foreign Ministry, National Report on Arms Export 2014.

[22] Polish Ministry of National Economy, [Partnership of entrepreneurs and governmental administration aimed at common security policy realization] (in Polish).

[23] Article 13-h, ANCEX Presidential Order no. 59/2005 for the implementation of Government Ordinance no. 158/1999 on the control regime of exports, imports and other transfers of military goods, approved with amendments by Law no. 595/2004.

[24] European Commission, Register of the Certified Defence-related Enterprises (CERTIDER), [n.d].

Authorized Economic Operator (AEO) status was created by the 2005 amendments to the EU Customs Code and came into force in January 2008. National authorities can award AEO status to manufacturers, exporters, freight forwarders, warehouse managers, customs agents and carriers that meet common criteria in a range of areas, including 'an appropriate record of compliance with customs requirements' and 'appropriate security and safety standards'.[25] AEO status is recognized across the EU and makes the recipient eligible for certain customs control-related benefits, including expedited procedures at entry and exit points and simplified security- and safety-related inspections. However, as with certification under the ICT Directive, uptake has been weak.

Under the EU Dual-use Regulation, granting a global export authorization to a specific exporter must take account of whether the exporter has 'proportionate and adequate means' to comply with the regulation and the authorization (Article 12).[26] Creating additional incentives for ICPs and agreed standards in this area is likely to be a key focus of the Commission's proposals for a revision to the EU Dual-use Regulation (see above).[27]

International processes

The export control regimes have so far had only sporadic interaction with ICP-related issues, for example, through an industry forum of the Wassenaar Arrangement in 2005 and the Nuclear Suppliers Group in 2014. The United Nations 1540 Committee has sought to engage industry through the so-called Wiesbaden process, which was initiated in 2012 with four conferences held in Germany and facilitated by the German Government to date.[28] The dialogue aims to provide a regular forum for exchange and has resulted, among other things, in the creation of the Botticelli project, an industry-led network which was launched in Brussels, Belgium in October 2015. A number of associations, such as the World Nuclear Association, and major exporting companies are involved. The stated aim is to 'forge a better dialogue and cooperation with governments and international institutions to prevent illicit trafficking and harmonize international rules and practices to reinforce competitiveness'. The initiative also seeks to initiate a range of practical steps, such as 'guidelines to help companies implement internal

[25] Regulation (EC) no. 648/2005 of the European Parliament and of the Council of 13 Apr. 2005 amending Council Regulation (EEC) no. 2913/92 establishing the Community Customs Code, *Official Journal of the European Union*, L117, 4 May 2005, p. 15.

[26] Council Regulation (EC) no. 428/2009 of 5 May 2009 setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items, *Official Journal of the European Union*, L134, 29 May 2009.

[27] European Commission, Presentation at the 2015 Export Control Forum, Brussels, 5 Dec. 2015.

[28] Kiessler, K. K., 'Private sector engagement: lessons learnt from the Wiesbaden Process', eds N. Kasprzyk, M. Shadung and N. Stott, *Towards the 2016 Review: Former Experts Assess UNSC Resolution 1540*, Institute for Security Studies (ISS) Monograph no. 191 (ISS: 2015).

compliance programs, offer small and medium-sized enterprises support from a roster of experts and act as a voice for exporters with international institutions'. In the longer term, goals also include enhanced international convergence and simplification for compliant companies.[29]

Potential implications for transparency and regulatory burden

While the attempt to reduce licensing requirements through the use of 'global licences' and 'general licences' may be aimed at reducing the administrative burden attached to the implementation of export controls, it also brings potential reductions in oversight, particularly with regard to public transparency. Since global licences and particularly general licences can be used to ship a wide range of goods to a wide range of destinations, any information that is published about granted licences provides little insight into what is going to be exported and where. For certain licences—particularly for dual-use items—exporters will be required to keep records on how these licences are used, but in many states this information is neither systematically reported to governments nor made public.

Moreover, regulating and administering global licences and general licences involves a shift from pre-licensing to post-licensing controls. Connected to this shift is a greater emphasis on record-keeping and audits, which does not always reduce the administrative burden for companies or authorities. Such requirements, along with the increased emphasis on ICP standards and benefits for companies that are able to comply, may favour larger companies at the expense of small to medium-sized enterprises, while failing to reduce the regulatory burden on national authorities. This comes at a time when resource constraints reinforced by general austerity measures are limiting the administrative capacities of national authorities.

It has been said that exporters are the first line of defence for export control. While it has been recognized that the private sector plays a key role, compliance efforts need to be further adapted to today's technological and trading reality in order to effectively address perceived risks and threats. The insufficient match between company needs and regulatory solutions is partly reflected in the limited uptake of EU instruments. Meanwhile, ICP discussions at the EU level have been mostly focused on the conventional arms side in the context of the ICT Directive. EU-level ICP discussions have been limited in the dual-use area, although this may change during the ongoing review process. Moreover, at both the EU and the international level the focus of ICP discussions has been generally more on company ICPs. To date, research institutions are still largely absent from such discussions. Finally, a certain loss of controllability goes hand in hand with technological

[29] Zero, S., 'Towards smarter nuclear export controls', *World Nuclear News*, 6 Oct. 2015.

developments, and thus the increased availability, speed and complexity of transactions and the reduced control function of physical borders. Effective measures may therefore require a fundamental reassessment of risks, a refocus on the highest risks and tailoring to different types of stakeholder.