



Pacific Northwest
NATIONAL LABORATORY

*Proudly Operated by **Battelle** Since 1965*

Seminar Summary

International Seminar on Due Diligence, Risk Assessment, and Supply Chain Management: Combatting Nuclear Proliferation

May 2015

G Hund
R Weise

E Kytomaki
M Quint

DISCLAIMER

This report was prepared as an account of work sponsored by an agency of the United States Government. Neither the United States Government nor any agency thereof, nor Battelle Memorial Institute, nor any of their employees, makes **any warranty, express or implied, or assumes any legal liability or responsibility for the accuracy, completeness, or usefulness of any information, apparatus, product, or process disclosed, or represents that its use would not infringe privately owned rights.** Reference herein to any specific commercial product, process, or service by trade name, trademark, manufacturer, or otherwise does not necessarily constitute or imply its endorsement, recommendation, or favoring by the United States Government or any agency thereof, or Battelle Memorial Institute. The views and opinions of authors expressed herein do not necessarily state or reflect those of the United States Government or any agency thereof.

PACIFIC NORTHWEST NATIONAL LABORATORY
operated by
BATTELLE
for the
UNITED STATES DEPARTMENT OF ENERGY
under Contract DE-AC05-76RL01830

Printed in the United States of America

Available to DOE and DOE contractors from the
Office of Scientific and Technical Information,
P.O. Box 62, Oak Ridge, TN 37831-0062;
ph: (865) 576-8401
fax: (865) 576-5728
email: reports@adonis.osti.gov

Available to the public from the National Technical Information Service
5301 Shawnee Rd., Alexandria, VA 22312
ph: (800) 553-NTIS (6847)
email: orders@ntis.gov <<http://www.ntis.gov/about/form.aspx>>
Online ordering: <http://www.ntis.gov>



This document was printed on recycled paper.

(8/2010)

Seminar Summary

G Hund
R Weise

E Kytomaki
M Quint

May 2015

Prepared for
the U.S. Department of Energy
under Contract DE-AC05-76RL01830

Pacific Northwest National Laboratory
Richland, Washington 99352

Abstract

Sixty participants from government, industry, finance, and non-governmental organizations met in Vienna, Austria, on March 12 and 13, 2015, to discuss the role of integrators, suppliers, finance and insurance in nonproliferation; industry and government cooperation on export control; and ways to explore efficiencies in complying with multiple control regimes. Integrators are larger companies that purchase subcomponents from suppliers and “integrate” them into new goods or use those subcomponents to manufacture new goods. The seminar, held under the Chatham House Rule, emphasized the importance of thinking about incentives for companies that excel at compliance, as opposed to punishing companies that have subpar compliance. There were four panel discussions where participants discussed their efforts to date, current challenges, and potential future approaches.

Contents

Abstract	iii
1.0 Introduction	1
2.0 Panel 1: Large Integrators' and Suppliers' Roles in Nonproliferation	1
3.0 Panel 2: Insurers' and Financiers' Roles in Nonproliferation – Identifying and Rewarding High Performers	3
4.0 Continued Discussion on Role of Finance and Insurance	5
5.0 Panel Three: Industry and Government Cooperation – Innovative Means to Increase Market Efficiency of Export Control Regulations	7
6.0 Panel Four: Exploring Efficiency in Complying with Numerous Control Regimes	10
7.0 Challenges and Suggested Solutions	11

1.0 Introduction

Sixty participants from government, industry, finance, and non-governmental organizations met in Vienna, Austria, on March 12 and 13, 2015, to discuss the role of integrators, suppliers, finance and insurance in nonproliferation; industry and government cooperation on export control; and ways to explore efficiencies in complying with multiple control regimes. Integrators are larger companies that purchase subcomponents from suppliers and “integrate” them into new goods or use those subcomponents to manufacture new goods. The seminar, held under the Chatham House Rule, emphasized the importance of thinking about incentives for companies that excel at compliance, as opposed to punishing companies that have subpar compliance. There were four panel discussions where participants discussed their efforts to date, current challenges, and potential future approaches.

2.0 Panel 1: Large Integrators’ and Suppliers’ Roles in Nonproliferation

This panel had three speakers, all of whom work for integrators – two for large private companies and one for a smaller nonprofit organization that works with a number of sensitive technologies. Some integrators have become increasingly interested in promoting supply chain security culture among their suppliers. Supply chain security culture is a concept that embraces traditional notions of “compliance,” but goes further to include anti-proliferation policies and cradle-to-grave custody from corporate board rooms, down to production lines, and throughout the entire (potentially global) supply chain.

One company saw its careful custody of information and items as a societal and cultural imperative to avoid increasing proliferation risks. She described how her organization is internalizing a supply chain security culture. Steps her organization has taken, and others can take, include: issuing corporate statements expressing commitment to nonproliferation and compliance principles; promoting transparency in the procurement process; improving export control training; participating in government rule-makings on export control and other compliance issues; and voluntarily reporting on noncompliance, if it occurs.

One participant, who works for an integrator with thousands of suppliers, spoke about the competing goals of making a profit versus controlling sensitive material. Less regulation reduces unit costs, and while nonproliferation controls are necessary, they slow sales. Industries’ due diligence includes not just screening of its customers, but also its suppliers. Integrators often rely on suppliers to classify their own items properly, so it is problematic if suppliers make mistakes. His company rewards its best suppliers, based on a number of factors, one of which is export control compliance. His company also keeps data on its suppliers, and if a supplier makes too many errors, it is fired.

Another participant who works for a large integrator discussed his company’s approach to compliance. He reiterated that the business goal to keep unit costs low could sometimes come at the expense of export controls. However, he added that companies can profit from export controls, if properly implemented. A corporate culture where employees can report errors without reprisal is one important element. Additionally, integrators should consult with national export control authorities before filling suspicious orders. Large integrators have an interest in promoting the adoption of due diligence and information sharing along the supply chain; it is good for business and improves relationships with regulators. This participant did caution that companies can get “nonproliferation fatigue,” citing various nonproliferation codes of conduct from the NSG, IAEA, etc. However, more carrots and fewer sticks would be welcomed by industry. He also added that more small and medium enterprises (SMEs) should participate in compliance efforts, because these businesses are often the front line against proliferation.

An industry representative said that his company works with suppliers to offer guidance on export control, though many of his company's internal processes are considered proprietary. Participants agreed that large companies tend to have more resources to devote to compliance.

A participant asked if integrators have problems with suppliers making errors. An industry representative answered that large companies rely on suppliers to come forward with errors. Additionally, ensuring that suppliers and integrators agree about item classification is important. Disputes about classification of dual-use items are more common than for military items (which have straight-forward classification, generally). Good communication between integrators and suppliers is crucial. The representative said that disagreements with suppliers over classification have gotten his company into trouble in the past.

Industry representatives indicated a desire for more dialogue with governments before they adopt export control changes. In response, a government representative talked about how the EU is considering amending its export control policies to improve compliance, but is currently researching the matter and is still getting feedback from the private sector.

An industry representative said that companies save money by proactively implementing compliance procedures; those who ignore compliance upfront will have to pay more in the end. Given the large reputational costs of noncompliance, it makes financial sense to invest in compliance programs. Of course companies will want to reduce overhead costs of compliance, but his company believes in the slogan, "Compliance is a competitive advantage." The better a company knows the relevant regulations, the less it costs the company to comply.

Another industry representative said that his company recently centralized its compliance department to better use division resources and improve controls. This new structure has reduced expenditures on outside counsel and consultants, and will allow the company to measure its exact compliance costs.

In response to a question about how integrators ensure their suppliers and employees are actually complying, an industry representative explained that his company has regularly scheduled internal compliance assessments. If trends indicate there may be problems, the compliance department does more targeted assessments. Staff may or may not be told when an assessment is occurring. Other industry representatives said their companies conduct similar internal audits. One of those industry representatives added that his company makes each business function group responsible for compliance issues, so they do not just pass the responsibility to corporate. In this way, everyone is involved in fixing mistakes. One participant suggested that companies could deal with audits more efficiently by combining safety audits with security and other audits.

A participant asked how industry deals with situations where their due diligence suggests a deal is suspicious, but the entities are not blacklisted. An industry representative said that it is not industry's job to identify companies that are not sanctioned. For example, industries are often not in a position to conduct an investigation to determine if a company is 51% owned by a sanctioned entity. He understands the motivation to broaden the impact of sanctions, but believes it is the governments' responsibility to designate entities, not industry's.

A government representative then asked industry representatives about where nonproliferation falls in the corporate governance structure: is it a core part of corporate governance or is it viewed more narrowly as export control and lumped into compliance? The general answer was that it depends. Industry is starting to pay more attention to export controls, but from a transport and services perspective, it is relatively new. One challenge is getting different compliance groups within an organization to see the overall compliance picture. Service providers view compliance differently from manufacturers.

Another participant added that there are drawbacks to lumping all compliance issues together. It is rare for one person to be an expert in all relevant compliance issues. Also, companies may not adequately look at all risks if the risks are grouped, which can be costly. A government representative added that there is no one-size-fits-all approach to compliance – some companies may have success lumping all compliance issues together, and some may not. Seminars like this help companies mix and match to tailor a system to their needs.

While participants agreed that there is no one compliance model, one person noted that successful compliance models will all be transparent and accountable, with adequate oversight to limit risks from rogue employees. Another participant added that compliance efforts are best adopted when it comes from corporate governance. It is best to have internal compliance actions coming from higher up in the company; when rules come from different internal sources and are implemented differently in various departments, mistakes occur.

Participants noted that suppliers are increasingly located in the developing world because costs are lower. However, an integrator's due diligence must remain the same, whether the technology is being produced to specification in a developing country or is simply purchased off the shelf in the home country. Before sourcing from developing countries, companies must assess sanctions and embargoes to see if any apply. The costs saved by working in the developing world can be lost if the company runs into a costly compliance problem.

Industry representatives were asked how they identify compliant suppliers. One industry representative said that for freight forwarders, integrators often have to closely monitor and assess forwarders for compliance. Another industry representative said that his company re-screens its global supply chain weekly; but the audits must be carefully managed and circumscribed so that they do not prevent the compliance team from carrying out its weekly screening. A third industry representative said that his company asks forwarders a series of questions about their compliance processes and sets certain minimum requirements that forwarders must meet before doing business with them. He has found that working with good forwarders is good for business.

A participant asked whether integrators base their compliance on US or EU regulations and compliance costs. One industry representative said that his company uses US regulations as their benchmarks, based on the size of US fines and penalties. Additionally, the US regulations can be clearer than EU controls. Another industry participant agreed.

3.0 Panel 2: Insurers' and Financiers' Roles in Nonproliferation – Identifying and Rewarding High Performers

This panel featured four panelists, one government representative, one trade attorney, one consultant, and one finance representative. The panel discussed ideas about how finance and insurance might incorporate nonproliferation into their due diligence and the potential benefits for doing so.

A government representative presented on how market forces can be used to reduce proliferation risks. By creating a market for goods and services produced with anti-proliferation practices, those who excel at compliance will be rewarded. If finance and insurance companies looked at a potential client's compliance risks before doing business with them, then companies would be encouraged to adopt

stronger compliance practices. Export credit agencies (ECAs) might lead the way for private financial actors, because ECAs straddle the divide between insurance/finance and government.

Another participant discussed the current roles that banks and insurers have regarding trade compliance. While banks and insurers have primarily been focused on anti-money laundering and economic sanctions, export control risks are starting to get more attention. For example, some loans now have contractual requirements that any subcontractor or member of the supply chain is held to the same standards as the direct contractor. Next steps require raising awareness in the finance and banking communities about the importance of export control issues, particularly with export control as a competitive advantage. Additionally, the participant thought that offering discounts for effective compliance programs as opposed to raising premiums for sensitive transactions would be valuable.

Another participant spoke about the role of third party auditors in nonproliferation. Auditors can perform audits that are legally required by regulations and can also perform internal audits to help improve internal processes. The corporate social responsibility (CSR) and conflict minerals movements are examples of how auditors can help companies meet industry or legal standards. The CSR standards are voluntary and are evaluated using Sustainability Accounting Standards. The US Dodd-Frank Act requires companies to report on their use of conflict minerals. Like those two regimes, nonproliferation and export control requirements could be furthered by the use of third party auditors. Those audits could be made available to investors interested in making responsible investments. Clearly presented information about a company's proliferation risks can have significant value for investors.

Next, a representative from the finance industry spoke about how finance assesses risk and conducts due diligence. Banks are required to conduct sufficient due diligence to know who their customers are. Additionally, banks try to determine what is normal for each customer so that they can identify "abnormal" behavior. For example, if a customer reports a \$100,000 salary, the sudden appearance of \$1 million in their bank account is suspicious, though not necessarily illegal. Abnormal activity triggers the bank to conduct enhanced due diligence. While banks can help stop illegal activity, industry, think-tanks and government will have to help banks identify red flags for export control violations and proliferation activity. Once banks have identified suspicious acts, then they can build models to detect those transactions. This participant's final point was that the fines for banking violations are large enough to generate compliance, even without further carrots.

A few participants commented that the relationship between banks and their customers can be complex. For example, when a bank has a long-standing relationship with a customer who then appears on a restricted list, it is unclear exactly how the bank should handle it. Each bank has a different due diligence program, so each may respond differently. A universal standard would simplify matters.

One participant mentioned that the Nuclear Power Plant Exporters' Principles of Conduct includes nuclear nonproliferation as one of the six foundational principles. In the Exporters' outreach to the financial sector, finance responded favorably to the Principles.

A participant asked whether an organization like the U.S. Institute of Nuclear Power Operations (INPO) might work for improving industry export control processes. Though INPO is technically voluntary, nuclear operators must participate or they simply are not competitive. The information produced by INPO is shared with regulators and insurance companies, increasing incentives for companies to perform well according to the voluntary standards.

Another participant thought INPO was a promising model for export control. However, he noted that INPO is successful given its strong talent and expertise, which might be difficult to replicate in new contexts. INPO is one point along the continuum of ideas to explore, ranging from government

regulation to a regime driven by consensus/codes/standards. Multiple ideas along that spectrum should be considered and might not be mutually exclusive.

A third participant commented that while INPO may be a useful model in part, many of the participating nuclear power plants have few or no international transactions. Thus, it would be valuable to think more broadly than INPO for export control considerations. In response, one participant suggested that an organization for suppliers might be useful, where there is a list of qualified suppliers based on their export control from which integrators can choose.

A government representative commented on the importance of spreading the Seminar's ideas of incorporating nonproliferation into financial decisions in Asian banks. He felt the Chinese banks were particularly important in reducing the North Korean threat. One participant suggested that the NSG Participating Governments might work with their ECAs to require more due diligence for exports. Those ECAs could lead the way for the private sector. Another participant commented that the US Export Import Bank is facing some political trouble, but that there is precedent for using ECAs to push "political" agendas.

To further respond to the comment about Chinese banks, a finance representative explained how many large banks are currently engaged in "de-risking" their holdings, meaning that they are terminating all financial relationships in certain risky countries, rather than risk conducting any business in those countries. De-risking can have devastating effects on local communities. Instead of blocking all transactions with those countries, he recommended Western banks work with smaller banks in riskier countries (such as Chinese banks) to help them build compliance programs. This practice may ultimately be worth the costs of implementation.

4.0 Continued Discussion on Role of Finance and Insurance

The following morning, the participants resumed their discussion about the role of finance and insurance in combatting nuclear proliferation, starting with how to identify red flags.

One participant discussed a case where a company's due diligence found nothing wrong with a series of orders from Lebanon. The company was prepared to fill the order, when the UAE freight forwarder noticed that the items were actually intended for Syria. This illustrates that due diligence is occasionally insufficient, and that having trusted partners on the ground, familiar with the region, helped the company avoid a serious problem. American and EU companies would benefit from having more people on the ground in areas of concern.

Another participant pointed out that fraud typologies are not new. By building off of existing models for detecting fraud, such as money laundering, it should be possible to identify proliferation risks.

A different participant added that having multiple data points about transactions is important. For example, knowing that a series of transactions are just below the \$10,000 reporting threshold is meaningful only if companies know more about those transactions. The repeated \$10,000 transactions could be because a company sells video equipment that happens to cost \$9,999. Or the transactions could all be below \$10,000 to avoid reporting requirements because they are part of a money-laundering scheme. Using carefully designed models to conduct automatic first-look screenings is important, and then personnel can conduct further investigation once suspicious transactions have been identified.

An industry representative gave an example where his company's compliance department declined to fill an order, even though the government said that it was permissible. His company was shipping oil to

China, and the Chinese buyer wanted to reroute half of the shipment through Dubai, to an address that was registered as a musical instrument shop. Just prior to shipment, the buyer asked that all identifying labels be removed from the packaging. His company refused to fill the order because it was too suspicious.

One participant with experience in insurance explained that underwriters rarely get specific information about all of a company's risks. Thus, it is difficult for underwriters and insurance brokers to think about incorporating export control into their underwriting policy. Underwriters need more than just red flags – they need clear guidance on what action regulators want them to undertake. Another participant added that underwriters often have little time in which to make an insurance decision. For example, customers seeking hull insurance only provide a rough indication of where the hull will be during the year. The insurance company has no way of knowing for certain if the hull will visit risky ports. Insurance companies must quickly make decisions using the information available to them, often with just one day to decide. Meanwhile, governments take days, or even weeks, to provide guidance to insurance companies. This is problematic.

A participant with finance experience suggested that court documents are useful tools for identifying red flags, since they describe patterns of illicit behavior in detail. In the United States, court documents are usually public. This participant suggested that insurance companies like the one insuring the hull above could perhaps use look-backs, where at the end of a twelve-month period the insurance company could see where the hull had been.

Switching topics, an industry representative explained his company is motivated to invest heavily in compliance because a mistake by one company can result in more government control and interference for the whole industry. For this reason, he does not think that companies actually compete on compliance – though being compliant may be an advantage. Companies have incentives to work collaboratively to improve compliance. This is especially true when it comes to suppliers' compliance – integrators should consider hiring outside counsel to help their suppliers improve export controls. This would reduce risks, and help his company avoid liability should a supplier still violate export regulations.

This same representative also cautioned that best practices or regulatory regimes may cause unintended consequences. For example, the Dodd-Frank Act conflict minerals amendment put Congolese small business miners out of work, deepening poverty.

A compliance consultant thought that rewarding companies for excelling at compliance is great. He asked for examples of possible "rewards." A government representative answered that "rewards" might include increased market share. For example, if a company with excellent compliance created an advertising campaign highlighting their responsible production processes, consumers could favorably respond to that.

But an industry representative cautioned that if countries do not consistently adopt compliance standards, then it will be hard for multinationals to compete. If one country with a large economy does not implement tougher banking standards, then companies that adopt higher standards might not benefit from a competitive advantage.

This industry representative also wanted to know whether SMEs with limited resources would be able to undertake exceptional compliance efforts, or whether there is some type of trusted trading partner certification that all businesses can aspire to achieve. As of yet, there is no "trusted trading partner" certificate, but some thought has been given to developing an ISO standard or creating a new certification entity. Another participant added that there are plans underway to develop uranium stewardship

standards. Many participants supported the further investigation of possible formal compliance certification, though whether it would be industry-generated or government-generated remained unclear.

Participants generally agreed that bringing SMEs to the table regarding compliance would be valuable. SMEs can represent the biggest risks in the supply chain, because often they just do not have the necessary knowledge about the applicable regulations and/or thorough knowledge of the complete supply chains. One person suggested that perhaps holding events like the Seminar at trade fairs or technical conferences might be a good way to reach out to SMEs. Discussions like these at the Seminar need to be more accessible to SMEs. A finance representative suggested that sharing topical discussion pieces on social media might be a good way to reach SMEs. The more information that large companies and government representatives can make available for free or low cost, then the greater chance of SMEs getting on board. Trade associations and trade fairs are good places to reach out to SMEs.

A government representative wondered whether participants thought some type of government-imposed proliferation tax, where taxpayers would pay less when their compliance efforts were better, was feasible. Participants felt this was very unlikely in the United States. However, the US Department of Justice does consider the existence of a company's compliance program a factor to reduce fines for regulation violation, which has an effect that is somewhat similar to the effect of proliferation taxes.

One participant asked whether credit rating agencies might help assess proliferation risks. Another participant answered that she had spoken with credit rating agencies about these risks, but found those conversations unfruitful. The credit rating agency representatives were reluctant to think creatively about how proliferation might impact business risks and practices.

A government representative divided the world of market actors into four categories: (1) bad actors; (2) unaware actors (like SMEs); (3) good guys and (4) "frustrated actors" – those who want to comply but do not want to miss out on business transactions. The frustrated actors demonstrate the incentive for non-compliance being unable to fill orders, or losing business to actors in other regimes with less restrictive regulations.

An industry representative thought that because the fines for export control are not nearly as large as the fines for violating WMD sanctions, it will be hard to raise awareness and encourage banks and insurance companies to engage. Additionally, each institution has different issues that they care about, so the uptake will be unpredictable and uneven. In response, a financial industry representative said that getting a number of big players to adopt a common standard will encourage others to fall in line.

Finally, a participant wondered whether participants thought the Financial Action Task Force was relevant to the discussion about finance. A participant said that the Task Force is tailored to sanctions and the idea from this Seminar was to look at finance and insurance in different ways. Sanctions are another important element of the fight against proliferation, but a deliberate decision was made to focus on export controls as opposed to sanctions at this meeting.

5.0 Panel Three: Industry and Government Cooperation – Innovative Means to Increase Market Efficiency of Export Control Regulations

Four panelists spoke during this session. Two of the panelists were government representatives, one panelist was a consultant for the nuclear industry, and the fourth was an industry representative. Panelists

discussed possible government reforms that could both improve compliance and promote market efficiencies.

A government representative spoke about performance-based approaches to regulation. Performance-based approaches (PBAs) involve the government telling companies what the end goal must be, but then companies having flexibility to determine how to reach that end point. PBAs are a complement to prescriptive approaches to regulation, not an alternative or substitute. PBAs might be applied to export control as a risk-based approach to licensing. Figuring out the proper balance between what regulators want (to spend less time on low-risk transactions) and what industry wants (licensing certainty, license exceptions for intra-company transfers, and reduced overhead expenses) is the difficult part.

A nuclear industry participant told a story to illustrate how restrictive export controls can be when taken to extremes. Company attorneys said that Spanish engineers could not sit next to Japanese engineers at a meeting held in the United States because the US company did not have the necessary licenses to re-export Japanese technology to Spain, even though all the engineers worked for the same company. This participant suggested that INPO is an example of voluntary nuclear operator industry standards where noncompliance of one is bad for the whole industry. A similar model might be adapted to nonproliferation, if designed properly. Clearly, there will need to be focus on the supply side and SMEs. Additionally, governments should reduce the resources used to control low risk items so that more resources are available for controlling the most sensitive items. Many participants supported this sentiment.

An industry representative spoke about the possible use of intra-company transfer authorizations as an incentive to improve export compliance. The US Validated End-User (VEU) Program is an example of an incentive program, where US businesses can export certain dual-use items to VEUs in China or India. Singapore has a trusted trader program, TradeFIRST, which allows actors to easily distinguish between high and low risk transactions. Intra-Company Transfers (ICT) currently require a license to share information with foreign nationals who work for the same company. In 2008, there was an attempt to create an ICT license exception, but the process to qualify for the exception was too onerous and the benefit was seen as too small. The exception was never implemented. The representative proposed the development of a trusted trader program that would provide benefits (like broad general licenses) to companies that adopt “compliance-plus” ICPs. Participating companies would be subject to review and audit.

A participant spoke about how the UK already tries to make obtaining licenses and authorizations easier for companies that excel at compliance by offering open and general licenses. But, she pointed out that the export controls exist for a reason – nonproliferation is important. Companies need to work with the regulatory bodies to fully understand the rules and allow the most efficient operations possible. Companies should realize that licensing applications can be complicated. If companies’ applications were clearer, the licensing process would be faster. The existence of a compliance program only matters so much – the important question is whether the license can be issued or not. This is especially true because compliance programs in a large integrator look very different from what a five-person SME might have.

A participant asked about political outreach efforts to encourage a culture of compliance, particularly within countries that do not regularly participate in meetings like the Seminar. Another participant answered her questions saying that both the UK and US work with other countries to improve their export controls. Each time a new country joins the European Union, the EU helps that country develop regulations that meet EU standards. Also, the EU helps countries that request it. However, this is soft influence, since one country cannot tell another country what to do. Another participant suggested that there might be a role for big multinational companies to go to developing countries to help raise awareness also.

Participants noted that government and industry do not communicate enough. Often the government does not know what industry is doing and vice versa. One participant thought this growing gap between industry and government was related to the increased role of consultants and attorneys. An ICP is not a panacea and should not be the goal in and of itself.

A participant raised the issue of ICT again and asked if the political situation may have changed enough to allow new consideration of ICT; was there any appetite for ICT or similar proposals? Participants seemed to think that there is appetite for ICT-type proposals, except for in the US where ICT is a non-starter currently.

A government representative said that the biggest challenge with ICT is not the transfer itself, but that people do not think about all the times when they may be exporting something: international travel with a laptop, email, etc. Also, when applying for licenses, companies often do not know all the countries they will visit or the markets they will be in. Where ICTs are more straightforward, it is much easier for the government to make a speedy licensing decision.

A government representative agreed that there is an appetite for change in licensing processes, but that passing legislation and writing regulations are costly and time-consuming endeavors. It might be easier to change processes rather than legislation.

One participant noted that the EU is conducting an ongoing review of possibly introducing ICT and VEU programs. The EU will decide by the end of the year whether it will pursue those policies or not, once all the data has been collected and analyzed.

Another participant talked about current efforts by the Wassenaar Arrangement (WA) on conventional and dual-use technologies. Wassenaar is another system that governments can use as a type of collective risk assessment. WA has a number of best practice guidance documents for its members, as well as list of questions to help industry determine whether an export is subject to catchall controls. The challenge for any regime is creating guidelines but still allowing for national discretion in implementation.

A government representative pointed out that governments are not monolithic, and getting licenses through the various divisions often takes time. Admittedly, this is problematic, but where the process can move quickly it does. Sometimes though, the regulators must do more, such as make site visits to verify information, and then the licenses will necessarily take longer. Government-to-government assurances would help speed the licensing processes in some instances. Another idea is to use local diplomatic representatives to assist with site visits – to verify that the business address listed for a recipient is in fact the business that it is claimed to be. Additionally, license applicants can help speed the process by providing well-prepared applications and being forthcoming with information.

A participant asked whether thorough applications, where industry conducts substantial due diligence upfront, can shorten the license review process. Government representatives said that it can, but that confidence is the crucial element. When companies submit thousand-page long applications, asking for more licenses than they actually need, that does not build confidence. Companies should be realistic about the licenses they seek and prepare their applications carefully. Furthermore, even if a company has done its due diligence, the government still needs to review the license application carefully because the government representative must be able to defend a given license decision. One government representative saw no way around the duplication of due diligence efforts between industry and governments.

Industry representatives added that both government and industry have limited resources and need to use a risk-based approach to licensing. There should be a green lane for lower risk items, to free up regulators' bandwidth so they can really focus on higher risk transactions. Industry representatives indicated a willingness to jump through extra hoops in order to get faster licensing decisions. Having a strong reputation for compliance is part of that effort. But, the hoops jumped must be justified by the benefit received. For example, the Automatic Export Information System Pilot requires reporting both pre-and post-shipment; the participant is willing to jump through many hoops to be allowed to only report post-shipment.

Another government representative said not everyone will see the incentives for industry as equally valuable, so there must still be repercussions to not complying. Participants added that making progress on export control and nonproliferation will require increased awareness and efforts to bring in new stakeholders. For example, the Kimberley Process was led by industry and civil society, which then resulted in government action. Without consumer demand and public support for nonproliferation efforts in business, efforts will have limited impact. Others in the Seminar generally supported this comment. However, one participant pointed out that the nuclear power industry is generally not interested in discussing nonproliferation because they do not want the public to make the connection between nuclear power and nuclear weapons. A nuclear industry representative said that the connection is already there, so nuclear power plant operators should stop ignoring the dots.

6.0 Panel Four: Exploring Efficiency in Complying with Numerous Control Regimes

The three panelists addressed the question of how to promote efficiency in complying with multiple control regimes. Panelists discussed how complying with one regime may assist in complying with another regime and the possibility of improving compliance while reducing compliance costs.

An industry consultant spoke about the importance of cooperation and partnership along the supply chain, particularly with transport service providers. These providers often do not know the regulations for the items they ship and must rely on information from the supplier. Multi-jurisdictional and complex regulations make compliance difficult to understand and costly to implement. If companies had a standardized set of trade practices that they could adopt, it would make it easier and more efficient for compliant companies to identify other compliant companies with whom they should partner. It is also important to engage SMEs and make compliance tools less costly.

A government representative responded that he did not think that harmonization across regimes for export control is realistic. The objective of customs is to lower the cost of legitimate trade, while stopping illegitimate trade. Both companies and countries need basic capacity to effectively implement customs. Having a proper commodity identification system is crucial as well. Like with export control, going beyond strict legal compliance is the best way to reduce risks.

A nuclear industry representative then spoke about the various multilateral regimes that exist that are designed to make export controls more consistent. However, different jurisdictions still classify the same items differently. He gave an example of a business traveler with a laptop, sending emails to and from different countries and all the various export control violations that might occur to illustrate the complexity of international export control. He suggested that businesses can leverage compliance in one jurisdiction to aid in compliance in another.

Another participant agreed that by trying to meet U.S. requirements first, it makes it easier to control information in other regimes. This participant then wondered if there was a way to create a multilateral technology control platform? He suggested that government-to-government assurances could make export control more efficient. For example, a company may receive a note verbale from the Nuclear Regulatory Commission and Japan, saying that any re-export will require a new license. However, the notes verbale do not acknowledge that the US has new general authorizations in place for certain technologies. Better coordination at the multilateral level might help here.

Participants generally agreed that technology transfers can often pose more proliferation risks than goods. Once an email has been sent with sensitive technology in it, it cannot really be withdrawn or pulled back. Regulation has not kept up with technological developments.

7.0 Challenges and Suggested Solutions

Throughout the Seminar, participants identified a number of distinct challenges and possible solutions to those challenges. Those challenges and solutions are laid out below. The solutions presented were not necessarily unanimously supported nor thoroughly vetted. Rather they were presented as possible next steps, worthy of further exploration.

Challenge 1: Determining how to promote best standards – through government or industry standards?

- Suggested Solution: Create an entity like INPO, which would set standards and conduct regular inspections of companies to assess their compliance. However, INPOs success is in large part predicated on the talent and expertise of its staff, which may be difficult to replicate in the compliance and export control context.

Challenge 2: Underwriters do not have the necessary information to incorporate compliance risks in their due diligence.

- Suggested Solution: Develop a set of red flags to help underwriters identify compliance and proliferation risks. Include a set of possible actions that underwriters could take in response to identification of a red flag. For example, if the red flag is simply that the company has no ICP, the underwriter could require development of an ICP before offering insurance. If the red flag is more serious, the underwriter could decide not to do business with that entity. This would also help underwriters make smarter decisions quickly.

Challenge 3: When issuing hull or marine insurance, the underwriter is only told where the ship will go in the next twelve months, but there is no mechanism for tracking which ports the ship actually visits.

- Suggested Solution: Insurance companies could have look-back policies. After the insurance period, the insurance company could review the port logs for the period in question. If the ship deviated from the original port plan, the insurance company could adjust the insurance policy going forward.

Challenge 4: SMEs have limited resources to spend on compliance activities.

- Suggested Solution: Large companies may pay for compliance counsel to assist small trading partners to adopt compliance programs. By hiring outside counsel, the larger company will avoid liability that may result if the large company does the training themselves, but will still help the small companies adopt best practices.
- Suggested Solution: Create a trusted trader certification program. Such a program would not only help clarify which SMEs had excellent compliance, but might also offer SMEs assistance in developing and adopting best practices. The trusted trader certification would be available for companies of all sizes. There was no consensus on whether this should be an ISO, a new certification entity, or a government-led certification program.

Challenge 5: SMEs are too often not part of the discussion on compliance.

- Suggested Solution: Undertake more efforts to engage SMEs. A number of ways to engage SMEs were discussed, including holding events like the Seminar at trade fairs or technical conferences. Also, it was suggested that large companies and government representatives could make more information about compliance available to SMEs, perhaps using social media as part of their outreach.

Challenge 6: Each institution (SME, integrator, bank or insurance company) has different issues that they care about, so uptake of best practices may be unpredictable and uneven.

- Suggested Solution: Encourage a few of the larger institutions to adopt a common standard. Once there is a common standard used by some larger players, others will likely follow suit. In discussions about such standards, companies may need to take preventative steps to avoid violating antitrust regulations.

Challenge 7: Currently governments and industry have to expend their limited resources controlling lower risk items, which reduces the time they have to spend controlling higher risk items.

- Suggested Solution: Increase government and industry cooperation to promote practices that allow resources to be channeled more effectively. This is a very broad suggestion, but included ideas like creating more and broader general licenses for lower risk items, intra-company transfers, and expand trusted trading partner programs.
- Suggested Solution: Government-to-government assurances, possibly in notes verbales, might help speed licensing processes by including up-to-date information about which technologies have general licenses. More multilateral coordination on restrictions on various technologies might be useful to reduce licensing confusion.
- Suggested Solution: Governments could ask their local diplomatic representatives to verify information for export licenses, such as verifying a business's physical address.

Challenge 8: It is difficult to engage with developing countries and countries that are not NSG PGs.

- Suggested Solution: Large multinational companies could promote awareness of the importance of compliance in developing countries and non-NSG countries.

Challenge 9: Consumer demand for products manufactured with anti-proliferation processes is currently lacking.

- Suggested Solution: Create an annual award for the top ten anti-proliferation companies. Such an award would draw public awareness to proliferation risks associated with manufacturing and reward companies that are already excelling at compliance. Determining the criteria for evaluation could be a collaborative effort.



Pacific Northwest
NATIONAL LABORATORY

*Proudly Operated by **Battelle** Since 1965*

902 Battelle Boulevard
P.O. Box 999
Richland, WA 99352
1-888-375-PNNL (7665)

U.S. DEPARTMENT OF
ENERGY

www.pnnl.gov