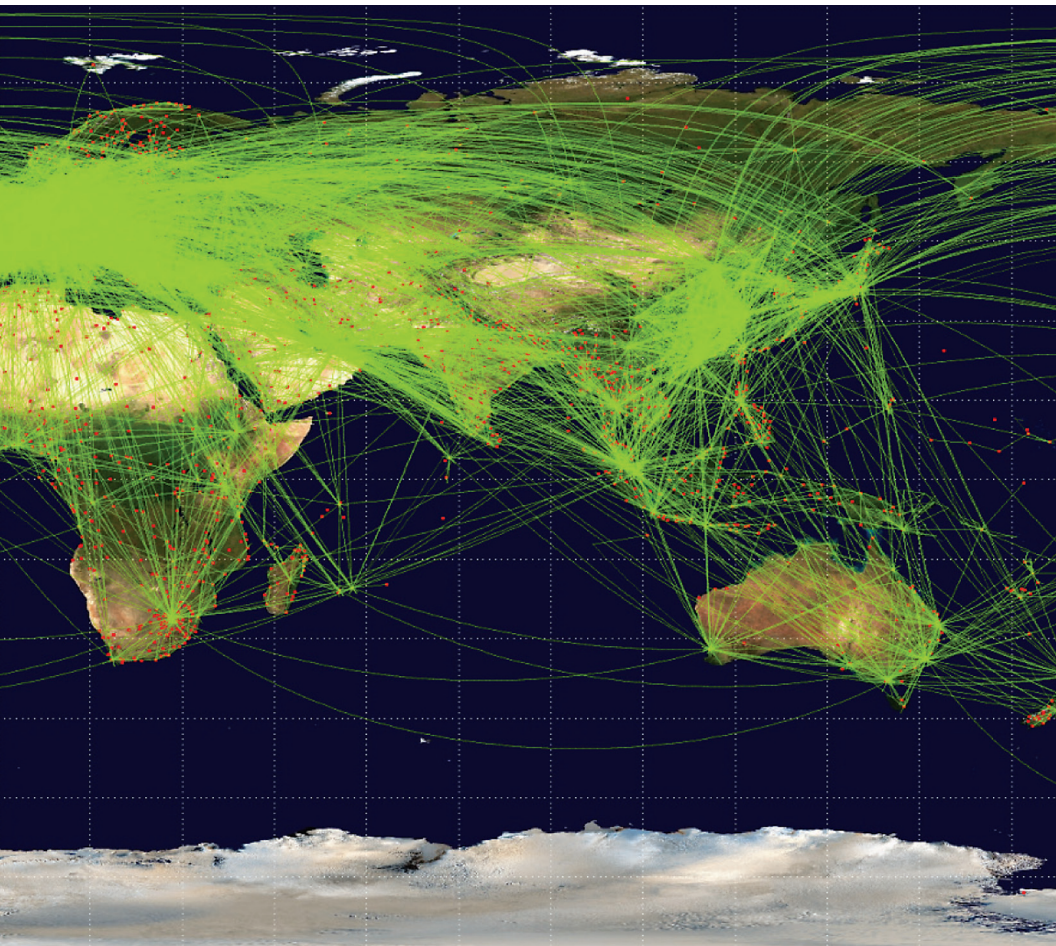


BIS “Best Practices” for Industry to Guard Against Unlawful Diversion through Transshipment Trade



U.S. Department of Commerce
Bureau of Industry and Security
Office of Technology Evaluation



*Where Industry and
Security Intersect*



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BIS “BEST PRACTICES” FOR PREVENTING UNLAWFUL DIVERSION

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BIS Publishes New “Best Practices” for Industry to Guard Against Unlawful Diversion through Transshipment Trade

WASHINGTON, D.C. – The U.S. Department of Commerce’s Bureau of Industry and Security (BIS) today published a new set of “best practices,” developed in cooperation with U.S. industry, to help guard against the diversion of dual-use items shipped to a transshipment “hub,” or to any intermediate country before being shipped to the country of ultimate destination.

Transshipment is a routine and growing part of legitimate world trade with logistical benefits, but also can be used illegally to disguise the actual country of ultimate destination. Transshipment practices may also create a risk that items are diverted to unauthorized end-users or end-uses.

“These new best practices provide a formidable tool to help secure trade through transshipment hubs,” said Assistant Secretary for Export Administration Kevin J. Wolf. “BIS is committed to working with industry to adopt best practices critical to safeguarding U.S. national security interests.”

The following new best practices will help exporters, re-exporters, freight forwarders and other parties to comply with US export control regulations and laws and augment BIS’s Export Management and Compliance Guidelines. BIS is encouraging industry to:

- Pay heightened attention to BIS’s Red Flag Indicators and communicate red flag concerns internally.
- Seek to utilize only those trade facilitators and freight forwarders that administer sound export control management and compliance programs that include transshipment trade best practices.
- Obtain detailed information on the credentials of foreign customers to assess diversion risk.
- For routed transactions, establish and maintain a trusted relationship with parties to mitigate risks.
- Communicate export control classification and destination information to end-users and consignees on government and commercial export documentation.
- Provide the ECCN or the EAR99 classification to freight forwarders for all export transactions and report the classifications in the Automated Export System (AES), if applicable.



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- Use information technology to the maximum extent feasible to augment “know your customer” and other due-diligence measures in combating the threats of diversion and increase confidence that shipments will reach authorized end-users for authorized end-uses.

This set of best practices, aimed at U.S. industry, supports one of ten best practices suggested by the State Department’s Bureau of International Security and Nonproliferation to foreign governments at the Global Transshipment Seminar in Dubai, United Arab Emirates, in March 2011. (See page 24 in booklet.) That best practice suggestion encouraged industry to develop stronger internal compliance programs, conduct focused outreach, and raise awareness of export control obligations.

The 2011 “Best Practices for Preventing Unlawful Diversion of U.S. Dual-Use Items Subject to the Export Administration Regulations, Particularly through Transshipment Trade” are posted on the BIS website <http://www.bis.doc.gov/complianceandenforcement/bestpractices.htm>

BACKGROUND ON U.S. DUAL-USE ITEMS TRANSSHIPMENT TRADE

WHY IS THIS TOPIC IMPORTANT?

■ Many Factors Pose Special Risks of Diversion

- U.S. Exports/Global Trade are/is increasing
- Global Transshipment Hubs are Expanding
- Inexperienced companies are entering the U.S. export market
- Proliferators are seeking High Tech/Dual-Use/Sensitive Items



PREVENTING THE RISK OF UNLAWFUL DIVERSION

Diversion is common in the following types of exports:

■ Transit

- U.S. items that pass through one foreign country en-route to another, without clearing customs



■ Transshipment

- U.S. items usually off-loaded to a warehouse or free trade zone before being shipped and do not clear customs



■ Re-exports

- U.S. items are shipped between two foreign countries, and clear customs in both countries



BIS "BEST PRACTICES" FOR PREVENTING UNLAWFUL DIVERSION

TERMS

Unlawful diversion occurs when an item intended for an authorized end-use and end-user is instead directed toward an unauthorized end-user for an unauthorized end-use. Diversion is most common through transshipment ports because of the size of the ports, their infrastructure and strategic location, and the significant role of intermediaries.

The terms transit, transshipment and re-export are sometimes used in the same context.

All three are common export scenarios in which diversion may occur. The terms are generally understood in the following manner:

Transit: Items from one country are shipped through (or pass through) a second country en-route to a third country. The shipment does not clear customs in the second country.

Transshipment: Items from one country are offloaded (typically in a bonded warehouse or free trade zone) in the second country en route to a third country, the intended destination at the time of export from the first country. The shipment does not clear customs.

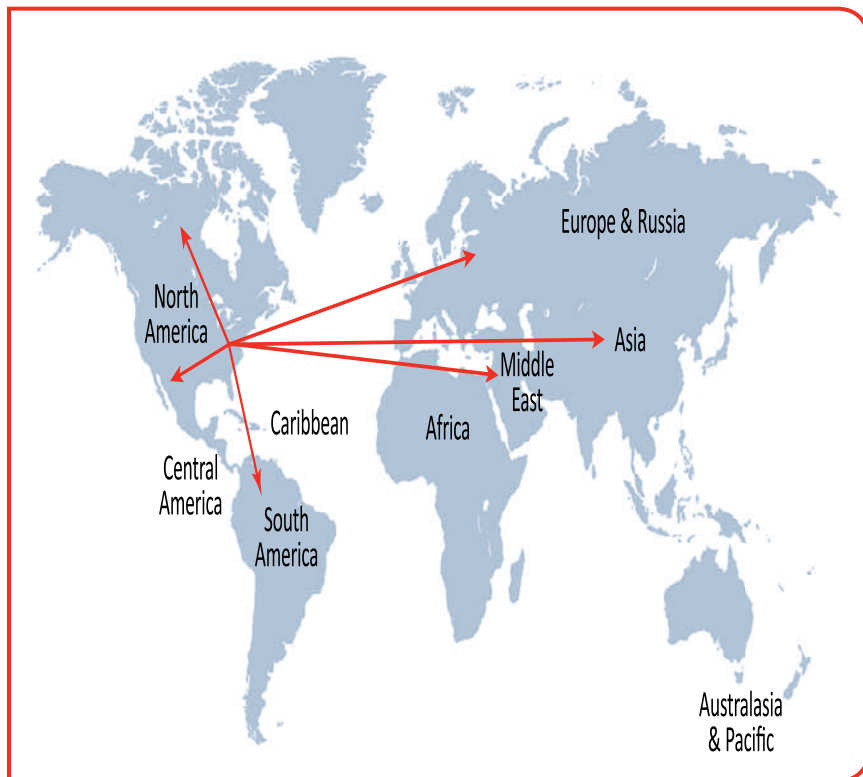
Re-export: Items are shipped between two foreign countries. If the items are subject to the EAR, EAR licensing requirements will apply to the re-export.

Note that an export of items subject to the EAR from the U.S. intended for France that is transshipped through the UK is considered an export from the U.S. to France.



DIRECT EXPORT MODEL

In years past, exporting was simple. An exporter had a buyer in a foreign country and shipped directly to that buyer. There was little involvement of intermediaries who affected delivery of items to their end-destination and no transshipment points.





TRANSSHIPMENT CHALLENGES

- Size and velocity of legitimate transshipment trade is high and growing
- Increasing interest of proliferators in dual-use items
- Challenges in the ability to search, seize and investigate with minimal impact on the high volume of otherwise legitimate trade
- Misperception that adopting and enforcing export transshipment controls is bad for business

IMPORTANCE OF THE ROLE OF INDUSTRY

Outreach to export industry stakeholders as well as regulatory responsibilities are important in reducing the threat of unlawful diversion risk in transshipment trade

- | | |
|----------------------|--|
| ■ Freight Forwarders | ■ Suppliers |
| ■ Brokers | ■ Corporate or government owners of FTZ's, bonded warehouses |
| ■ Custom Brokers | ■ Private companies that function within these or special economic zones |
| ■ Insurers | |
| ■ Financiers | |

Industry cannot be underestimated in the effort to control transshipment, transit, or re-export of sensitive items.



2011 BEST PRACTICES FOR PREVENTING UNLAWFUL DIVERSION OF U.S. DUAL-USE ITEMS SUBJECT TO THE EXPORT ADMINISTRATION REGULATIONS, PARTICULARLY THROUGH TRANSSHIPMENT TRADE

INTRODUCTION

The best practices identified herein are intended to help industry guard against diversion risk. Both government and industry recognize that implementing effective export compliance programs is an important component of responsible corporate citizenship and good business practices.

The success of export control laws rests on well-managed and comprehensive export compliance programs. The diversion of dual-use U.S. origin items from authorized to unauthorized end-uses, end-users, or destinations, even inadvertently, undermines efforts to counter the proliferation of weapons of mass destruction, terrorism, and other threats to national and international security. Global "transshipment hubs" — i.e., countries or areas that function as major hubs for the trading and shipment of cargo — pose special risks due to their large volumes of export, transit, transshipment, and import and re-export traffic. Such hubs make transshipment trade particularly vulnerable to the diversion of sensitive items to unlawful purposes.

To combat diversion risk, the Bureau of Industry and Security (BIS) has exchanged information with industry (including exporters, freight forwarders, carriers, consolidators, express couriers, and others) involved in the export of items subject to the Export Administration Regulations (EAR). BIS consolidated existing best practices and established new practices aimed at preventing diversion. BIS recognizes the importance of soliciting input from industry to define this new set of best practices to prevent diversion.

The publication of these best practices creates no legal obligation to comply with such practices on the part of any person, absent a legal requirement that is set forth elsewhere in the EAR. Compliance with these best practices creates no defense to liability for the violation of the EAR or other export control laws. However, demonstrated compliance with these best practices may be considered in assessing a person's conduct.



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Although BIS issues this guidance on industry best practices as it applies to items and transactions that are subject to the EAR, the guidance clearly has broader potential application. BIS envisions this guidance as a step toward a strengthened dialogue with all members of the export logistics supply chain industry, other agencies that administer export controls, and foreign governments in a manner that may make the guidance pertinent beyond its application to the EAR.

PRINCIPLES

These best practices are based on the following four principles:

- Industry and government should work together in a cooperative partnership on a domestic and global basis to foster secure trade.
- Secure trade will reduce the incidence of diversion of dual-use items to prohibited end-uses and end-users.
- Effective export management and compliance programs will encourage expeditious movement of legitimate trade.
- Industry can achieve secure trade objectives through quality-driven export management and compliance practices.

PRACTICES

The following reflect new best practices that guard against diversion risk, particularly through transshipment trade.

Best Practice No. 1 – Companies should pay heightened attention to the Red Flag Indicators on the BIS Website and communicate any red flags to all divisions, branches, etc., particularly when an exporter denies a buyer’s order or a freight forwarder declines to provide export services for dual-use items.

Best Practice No. 2 – Exporters/Re-exporters should seek to utilize only those Trade Facilitators/Freight Forwarders that administer sound export management and compliance programs which include best practices for transshipment.

Best Practice No. 3 – Companies should “Know” their foreign customers by obtaining detailed information on the bona fides (credentials) of their customer to measure the risk of diversion. Specifically, companies should obtain information about their customers that enables them to protect dual-use items from diversion, especially when the foreign customer is a broker, trading company or distribution center.



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Best Practice No. 4 – Companies should avoid routed export transactions when exporting and facilitating the movement of dual-use items unless a long standing and trustworthy relationship has been built among the exporter, the foreign principal party in interest (FPPI), and the FPPI’s U.S. agent.

Best Practice No. 5 – When the Destination Control Statement (DCS) is required, the Exporter should provide the appropriate Export Control Classification Number (ECCN) and the final destination where the item(s) are intended to be used, for each export to the end-user and, where relevant, to the ultimate consignee. For exports that do not require the DCS, other classification information (EAR99) and the final destination should be communicated on bills of lading, air waybills, buyer/seller contracts and other commercial documentation. For re-exports of controlled and uncontrolled items, the same classification and destination specific information should be communicated on export documentation as well.

Best Practice No. 6 – An Exporter/Re-exporter should provide the ECCN or the EAR99 classification to freight forwarders, and should report in AES the ECCN or the EAR99 classifications for all export transactions, including “No License Required” designation certifying that no license is required.

Best Practice No. 7 – Companies should use information technology to the maximum extent feasible to augment “know your customer” and other due-diligence measures in combating the threats of diversion and increase confidence that shipments will reach authorized end-users for authorized end-uses.



ADDENDUM #1:

BEST PRACTICES FOR PREVENTING UNLAWFUL DIVERSION OF U.S. DUAL-USE ITEMS SUBJECT TO THE EXPORT ADMINISTRATION REGULATIONS, PARTICULARLY THROUGH TRANSSHIPMENT TRADE

SUMMARY: The Bureau of Industry and Security is publishing the guidance entitled, “Best Practices for Preventing Unlawful Diversion of U.S. Dual-Use Items subject to the Export Administration Regulations, Particularly through Transshipment Trade.”

BACKGROUND

On September 1, 2010, the Bureau of Industry and Security (BIS) published a notice of inquiry requesting public comment on its draft *Best Practices for Transit, Transshipment, and Re-export of items subject to the Export Administration Regulations (EAR)* (75 FR 53639). In response to this notice of inquiry, BIS received 5 written industry comments. Between September and December 2010, BIS also received 52 comments through individual meetings and outreach activities with stakeholders, including trade associations, exporters, freight forwarders, carriers, software vendors, advisory committees, and other government agencies.

This effort updates BIS’s Transshipment Countries Export Control Initiative’s efforts that recommended *Best Practices for Transit, Transshipment, and Re-export of Items Subject to the Export Administration Regulations*. BIS published these best practices on its website in November 2003. The best practices were intended to help industry, and in particular Exporters/Re-exporters and Trade Facilitators/Freight Forwarders to contribute to a reduction in unlawful transactions and facilitate legitimate global commerce by increasing the capacity to distinguish between lawful and unlawful transactions.

The 2011 *Best Practices for Preventing Unlawful Diversion of U.S. Dual-Use Items, Particularly through Transshipment Trade* reflects the changes over seven years in the U.S. and global trade facilitation industry’s practices and the growing diversion risks for sensitive dual-use items.



NOTICE OF INQUIRY: BIS'S SUMMARY OF COMMENTS AND RESPONSES

Following is a review of the 5 written industry comments received in response to BIS's notice of inquiry on the best practices as well as the 52 oral comments received through meetings and outreach activities with stakeholders. BIS responds to these comments and where appropriate indicates that it has modified certain best practices or created new best practices.

(PROPOSED) BEST PRACTICE NO. 1 —

Pay heightened attention to the Red Flag Indicators on the BIS Website.

There were very few comments on this best practice. Those received indicated that red flags are raised to a higher level within companies, but most companies cannot detect everything. One commenter indicated that orders for dual-use items placed by potential diversion risk buyers are refused when red flags surface. However, such potential diversion risk buyers will often continue to pursue orders at other divisions/branches of the company until orders are granted. In addition, this commenter noted that these buyers may contact several divisions of a freight forwarding company or several freight forwarding companies until they find one that will facilitate the movement of their items with minimal questions. One commenter focused on risks in the trade practice of split shipments because the carrier may act on its own to split the shipment without the exporter's or ultimate consignee's knowledge and may reduce each parties tracking ability.

As diversion risk grows, BIS will continue the practice of educating exporters on red flag indicators at all forums. BIS notes that companies' compliance units should transmit red flag concerns to all divisions/branches, particularly when an exporter denies a buyer's order or a freight forwarder declines to provide export services for dual-use items. BIS will assess with other government agencies the trade practice of split shipments to better understand the elements of risk and the possible options to reduce them. BIS believes that this element of diversion prevention can be strengthened. For example, BIS initiatives are under consideration to improve exporters' compliance with the EAR that include changing the Automated Export System (AES) requirements, edits and validations, as well as increasing BIS compliance activities with governments and industries both domestically and internationally.

RED FLAG INDICATORS

Things to Look for in Export Transactions

Use this as a check list to discover possible violations of the Export Administration Regulations (EAR). You may also wish to visit our page that provides *"Know Your Customer Guidance"*.



- The customer or its address is similar to one of the parties found on the Commerce Department's [BIS's] list of denied persons.
- The customer or purchasing agent is reluctant to offer information about the end-use of the item.
- The product's capabilities do not fit the buyer's line of business, such as an order for sophisticated computers for a small bakery.
- The item ordered is incompatible with the technical level of the country to which it is being shipped, such as semiconductor manufacturing equipment being shipped to a country that has no electronics industry.
- The customer is willing to pay cash for a very expensive item when the terms of sale would normally call for financing.
- The customer has little or no business background.
- The customer is unfamiliar with the product's performance characteristics but still wants the product.
- Routine installation, training, or maintenance services are declined by the customer.
- Delivery dates are vague, or deliveries are planned for out of the way destinations.
- A freight forwarding firm is listed as the product's final destination.
- The shipping route is abnormal for the product and destination.
- Packaging is inconsistent with the stated method of shipment or destination.
- When questioned, the buyer is evasive and especially unclear about whether the purchased product is for domestic use, for export, or for reexport.

If you have reason to believe a violation is taking place or has occurred, you may report it to the Department of Commerce by calling its 24 hour hot line number: 1 (800) 424-2980. Or if you prefer use our form to submit a confidential tip.

Note: Refer to EAR Supplement No.3 To Part 732—BIS's "Know Your Customer" Guidance and Red Flags.



(PROPOSED) BEST PRACTICE NO. 2 —

An Exporter/Re-exporter should seek to utilize only those Trade Facilitators/Freight Forwarders that also observe these best practices and possess their own Export Management and Compliance Programs (EMCPs). Eleven commenters indicated that there is agreement that freight forwarders belonging to a trusted network or having a certification program should be sought out and utilized. The commenters recommended creating a list of nominated freight forwarders. For example, one commenter pointed out that a standard practice for companies lacking visibility in other countries is to use foreign agent networks or trusted global gateways and counterparts that provide ground, air, and ocean oversight. Five of the eleven commenters support a freight forwarder certification program that includes specific consequences for non-compliance with export laws and regulations. Two other commenters suggested adding export language to the import Customs-Trade Partnership Against Terrorism (C-TPAT) that can be applied to both importers who also export and to brokers who also work as freight forwarders. Commenters suggested that the U.S. Government (USG) should provide programs such as C-TPAT that offer incentives to companies for complying with export control laws and regulations.

As a party to the export transaction, the freight forwarder has a responsibility to report a violation of export control regulations and laws. Therefore, BIS continues to believe that freight forwarders need to be informed of and educated about those regulations and laws and know when they are dealing with a noncompliant party. BIS believes that there is a need for a level playing field in freight forwarding so noncompliant exporters cannot shop around to find one that fails to practice due diligence. The Export Control Reform Initiative (ECR) aims to facilitate more secure trade and identify new approaches to educating exporters such as trade facilitators/freight forwarders on best practices and EMCPs. In 2010, BIS conducted five EMCP conferences. BIS will consider industry's interest in a trusted network/industry program for forwarders as part of its exporter compliance outreach efforts. Also, BIS considers that industry's participation in ECR will provide valuable contributions to understanding and implementing proactive compliance with export control laws and regulations.

Note: Customs-Trade Partnership Against Terrorism (C-TPAT) is a program in which Industry agrees to partner with Customs and Border Protection (CBP) to protect the supply chain, identify security gaps, and implement security measures and best practices that safeguard the world's vibrant



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trade industry from terrorists, and maintain the economic health of the U.S. and its neighbors.

C-TPAT website: http://www.cbp.gov/xp/cgov/trade/cargo_security/ctpat/

(PROPOSED) BEST PRACTICE NO. 3 —

Exporters/Re-exporters should have information regarding their foreign customers. In particular, a company should know if the customer is a trading company or distributor, and inquire whether the customer resells to or has guidelines to resell to third parties. Six commenters indicated that the USG should provide additional education and outreach focused on working with trading companies and distributors. These commenters suggested strengthening foreign distributors’ compliance programs and designation of certain foreign territories as secure points for transshipment. As one commenter stated, “The reseller or distributor in a foreign country should be an extension of the U.S. exporter.” Four commenters noted that the effectiveness of export controls is reduced and diversion threats are heightened when they engage in “indirect selling” (selling to trading companies and distribution centers). Two commenters suggested that new language be inserted into seller contracts with buyers who are trading/distribution companies stating that unauthorized diversion is prohibited. Several commenters suggested that AES be strengthened to include specific, detailed data on ultimate consignees and end-users. Many industry representatives suggested that export compliance among small and medium-size exporters could be strengthened if the USG combined the U.S. screening lists into one consolidated file in one location. Finally, one exporter recommended that knowing a customer well and having professional trust in and a relationship with that customer is a very important business practice to ensure that transshipment of dual-use items occurs in compliance with export laws and regulations.

BIS agrees with these comments and has proposed to the U.S. Census Bureau adding two new data fields to the AES. The two fields are an “end-user” field to identify the end-user from the ultimate consignee when the two data fields are different and an “ultimate consignee type” field to identify whether exporters are doing business with trading companies/distributors, government consumers or government distributors. The Administration has created a consolidated screening list as part of its ECR Initiative on www.export.gov/ECR that includes BIS’s Denied Party List, Unverified List, and Entity List, State Department’s Debarred List and Sanction Lists and Treasury’s Specially Designed Nationals List.



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BIS encourages companies to educate foreign resellers/distributors about their legal obligations and responsibilities under the EAR in preventing the diversion of dual-use items. Such education should include providing detailed and specific guidelines for receiving, handling, reselling, transshipping, and distributing dual-use items.

(PROPOSED) BEST PRACTICE NO. 4 —

With respect to transactions to, from, or through transshipment hubs, Exporters/Re-exporters should take appropriate steps to inquire about the end-user and to determine whether the item will be re-exported or incorporated into an item to be re-exported. Several commenters indicated that BIS should conduct more visits aimed at improving compliance with the EAR for both U.S. exporters and foreign companies targeted as having no, or weak compliance programs involving the export or import of U.S. dual-use items.

One commenter stated that although some foreign companies are knowledgeable about the EAR, others are not, and only companies with effective compliance programs follow this best practice. One commenter noted that current export control regulations do not require communication between third buyers in foreign countries and original U.S. sellers: “communication stops when distributors or trading companies distribute.” One commenter suggested that the U.S. should be more aggressive in requesting import certificates for exported sensitive dual-use items. Other commenters suggested that BIS conduct license reviews whenever there is knowledge that the final destination differs from the ultimate consignee location. Some commenters suggested strengthening the EAR by adding a reseller provision that would strengthen obligations on resellers or alternatively that sellers insert language in contracts with buyers that focuses on foreign companies’ requirements to follow certain procedures when receiving, handling or transshipping dual-use items or munitions.

BIS believes that this best practice No. 4 is consistent with best practice No. 3. Although this best practice No. 4 is directed at items moving to, from, or through transshipment hubs, knowing your customer(s) is an important best practice for shipping to any country. In this regard, customers are defined as purchasers, intermediaries, ultimate consignees or end-users, whether or not they are distributors or resellers. While heightened scrutiny should be applied to exports/re-exports through transshipment hubs, the best practice of knowing your customer should be applied to exports through or to any destination. Therefore, BIS will combine this best practice with best practice No. 3 and modify the resulting content.

(PROPOSED) BEST PRACTICE NO. 5 —

Freight Forwarders should inquire about the details of a routed transaction when asked by a foreign principal party in interest to ship to a country or countries of destination or ultimate consignees that are different from those provided by the U.S. principal party in interest. Industry representatives commented that “drop” shipments to an ultimate consignee other than the foreign principal party in interest (FPPI) are a normal business practice. Six commenters indicated that U.S. exporters and freight forwarders face challenges fulfilling obligations and requirements in drop shipments and routed export transactions. For example, Freight Forwarders asserted that U.S. corporations hide behind the routed export transaction provision of the EAR and Census Bureau’s Foreign Trade Regulations and sometimes refuse to provide information to freight forwarders authorized by FPPIs. Another commenter indicated that exporters often confuse routed export transactions with International Commercial (INCO) Terms. One forwarder indicated that exporters generally classify items as EAR99 and certify shipments as “no license required” (NLR) in routed export transactions destined for distributors. Two commenters also indicated that these types of transactions are not risky if there is trust between the U.S. exporter and FPPI whereby the U.S. exporter recommends a specific freight forwarder for the FPPI to use, and ensures that the freight forwarder fulfills the requirements of export laws and regulations.

A ROUTED TRANSACTION



BIS carefully considered the comments that indicated that U.S. companies face increasing challenges in fulfilling requirements of export laws and regulations in routed export transactions and the comments by freight forwarders and carriers that they will not handle routed export



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transactions because of the risk of noncompliance and potential unlawful diversion. Therefore, BIS amends this best practice by recommending that U.S. exporters and freight forwarders avoid routed export transactions when exporting dual-use items unless a long standing and trustworthy relationship has been built among the exporter, the FPPI, and the FPPI’s U.S. agent.

(PROPOSED) BEST PRACTICE NO. 6 —

An Exporter/Re-exporter should communicate the appropriate Export Control Classification Number (ECCN) or other classification information (EAR99) for each export/re-export to the end-user and, where relevant, to the ultimate consignee. Four commenters

recommended that this information be communicated on the Destination Control Statement (DCS). Another four suggested that the DCS be added to all commercial documents, purchase order confirmations, and certificates accompanying the item.

Nine commenters indicated that §758.6 of the EAR, the provision that describes the DCS and what language it should contain, needed to be strengthened. Another commenter suggested

DCS language should state that “this bill of lading is export controlled” and include the country of destination on the DCS. Certain commenters stated that the current DCS only provides a warning without including detailed and specific information about the items. Two carriers commented that the language on the DCS does not allow them to determine if the containers are loaded with high or low-risk items. Two commenters asserted that additional BIS or private sector classification assistance would be needed to communicate the ECCN to the ultimate consignee. Two other commenters expressed their belief that if providing the ECCN were required, companies might use EAR99 more often. To improve classifications of dual-use items by exporters, these two commenters suggested that BIS

Ocean Bill of Lading			
Exporter		Booking Number	Document Number
Ultimate Consignee		Export References	
Notify Party		Forwarding Agent	
Place of Receipt		Place of Delivery	
Port of Loading		Type of Goods	
Port of Discharge		Type of Vessel	
Marked and Numbered	No. of Packages	Weight (kg)	Measurements
Bill of Lading No. _____ There are _____ packages, including attachments to this Ocean Bill of Lading.			
FREIGHT RATES, CHARGES, WEIGHTS AND MEASUREMENTS			
As between shipper and carrier, the weight and measurements of the goods are as stated on this bill of lading.			
I certify that the above information is true and correct to the best of my knowledge.			



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conduct more visits with exporters targeted as having made mistakes in classification of dual-use items that could result in potential export violations. One commenter indicated that exporters who were not manufacturers frequently get classifications wrong. Another commenter stated that its trade software was not programmed to put the ECCN on any shipping documents.

BIS has amended this best practice to suggest additional language beyond the minimum required language outlined in §758.6 of the EAR in order to address commenters’ concerns. The amended best practice refers to the inclusion of the ECCN and end-user destination on all commercial documents such as invoices and bills of lading or air waybills accompanying the export or re-export. This will help ensure that intermediaries and foreign buyers are knowledgeable of the receipt of dual-use items and abide by U.S. export regulations and laws.

(PROPOSED) BEST PRACTICE NO. 7 —

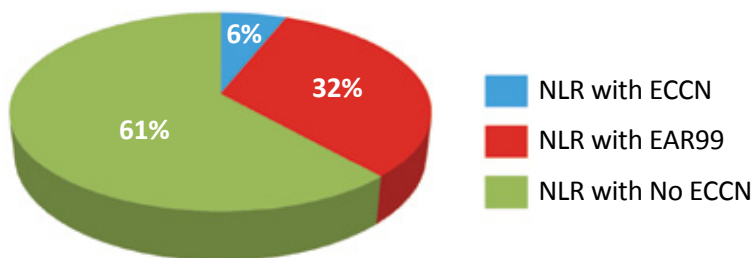
An Exporter/Re-exporter should report such ECCN or the EAR99 classifications for all export transactions, including “No License Required” designations to the Trade Facilitator/Freight Forwarder or enter them in the Automated Export System (AES). Three

commenters stated that this best practice was welcomed and expressed their belief that the EAR’s provisions regarding classification of dual-use items needed to be strengthened. Some exporters commented that it is the forwarder’s duty to provide the service to customers to classify items. Some forwarders commented that they will classify items, but only on a limited, fee-based basis. Two freight forwarders commented that they have to ask exporters repeatedly for classification information. These two forwarders also commented that exporters are aware that there is not a level playing field when it comes to classification requirements. They noted that some freight forwarders will always require classification from exporters while other freight forwarders (competitors) will not. Two freight forwarders also indicated that they do not know when due diligence ends and how much questioning about the items to be shipped is necessary in order to determine whether the classification is correct. On the topic of classification assistance, one commenter indicated that better classification tools are necessary and that forwarders should never classify items. One commenter raised the concept of building a



“crosswalk” between the Harmonized System/Schedule B number (HS) and the ECCN and asserted that it would be unlikely that a crosswalk could be developed, especially in Chapter 85 (electric machinery, etc., sound equipment, television equipment, and parts thereof) of the HS. Note: The term crosswalk refers to the matching of a particular HS number with an ECCN so that the particular item covered by the HS may be covered by a specified ECCN.

BREAKOUT OF CLASSIFICATION TYPES FOR 2010 NO LICENSE REQUIRED (NLR) EXPORTS



BIS recognizes that exporters need proper classification in order to make informed and correct export license determinations. BIS understands that certain commenters support providing or entering classification for EAR99 and CCL items. However, BIS also understands that many items do not fall within the CCL, and requiring exporters to classify to this level for every item would be burdensome. A large number of AES transactions contain no ECCN classification, and being able to identify items by the ECCN is an important tool for BIS to monitor and measure exporters’ compliance with the EAR. Therefore, BIS will continue to discuss with industry what existing tools are available or proposals for new tools that would be beneficial to companies in need of public classification assistance.

OTHER COMMENTS

BIS also received a substantial number of comments that it has addressed by including one additional best practice. This best practice is to improve compliance efforts to avoid unlawful diversion by making use of available information technology.

NEW BEST PRACTICE – Companies should use information technology (IT) to the maximum extent feasible to combat the threats of diversion



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and to increase confidence that shipments will reach authorized end-users for authorized end-uses.

The comments that provide the basis for this new best practice are discussed below.

Four commenters indicated that software is essential to achieve effective, cost-efficient compliance with export and import laws and regulations around the world, especially for large companies. One commenter noted that “without effective IT solutions, some large companies could not perform effective and cost-efficient levels of compliance checks and monitoring of sensitive dual-use exports.” Overall, most commenters stated that compliance software today is very good and some systems have the capability to conduct a check to see if the items shipped have been re-exported without the proper authorization. Three commenters suggested formulating a best practice on operating an IT system that includes adding problem codes, flags, stops, and trigger points in the programs to alert companies of red flags, risks and diversion threats. Two commenters indicated that export compliance software is affordable and a good return on the investment.

BIS agrees that an effective IT system is an essential element in developing and maintaining a successful export and management compliance program. BIS understands that there is a need for such programs in large and medium-sized companies handling a large volume of export transactions. BIS also recommends that small companies seek IT solutions within their budget and take advantage of the recent U.S. Government’s consolidated party screening list to improve compliance. For its part, BIS has and will continue to improve AES functionality to strengthen industry compliance with the EAR.

ADDITIONAL COMMENTS

BIS received other comments that identified additional emerging threats to the security of dual-use international trade. However, many of these comments are outside the scope of the best practices developed by BIS. BIS will look at the list of relevant additional comments and consider the recommendations they contain where feasible to address illegal diversion concerns.

The additional comments are as follows.

- The title of the September 1, 2010 Notice of Inquiry, “Best Practices for Transit, Transshipment and Re-export of Items Subject to the EAR”, is misleading. It gives the impression that diversion is only relevant in



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common transshipment ports. Transshipment trade provides logistical benefits to import/export companies and countries. BIS should consider renaming this document to establish best practices in preventing unlawful diversion in any port around the world, including the United States.

BIS agrees with this proposal and has modified the title of this 2011 document to “Best Practices for Preventing Unlawful Diversion of U.S. Dual-Use Items subject to the Export Administration Regulations, Particularly through Transshipment Trade” to describe more accurately best practices in preventing illegal diversion, particularly in high-risk transshipment trade.

- Another downturn in the economy or resurgence in war will increase the risk of diversion because people will seek methods and opportunities to avoid complying with the EAR.
- More Internet shopping will increase diversion risks because of the growth of buying blind.
- Unintentional mislabeling of packages will cause accidental transshipping.
- Incorporation of U.S. products and the de minimis rule present problems for both U.S. and foreign companies.

BIS agrees that export control agencies and companies are continually challenged by emerging threats, such as those described in the four comments above. For example, during times of economic downturn and war, companies may reduce or drop compliance activities and seek profit only. BIS agrees that detection becomes more challenging when companies receive orders from purchasers ‘buying blind’ via the Internet. These two challenges are the result of profit-driven companies seeking to sell to anyone, and this environment can be exploited by diverters and terrorists.

In addition, mislabeling of packages or misreporting of information may be causes for inadvertent export or re-export of an item to an end-user or end-use of concern (e.g., the use of country code IR (Iran) for Ireland (IE)). In regard to the de minimis rule, which governs the applicability of the EAR to foreign-made items that contain some level of controlled U.S. origin content, some companies may be unaware of or misunderstand the rule or simply guess the percentage of U.S. content in a foreign-manufactured product.

- U.S. Customs and Border Protection should improve U.S. transshipment best practices on the import side, and after implementation share the import best practices with other countries.
- The USG should research and review how other countries handle transits and their transit security programs.



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BIS agrees that government-to-government and government-to-industry exchanges are necessary. These exchanges should focus on developing a set of international best practices based on successful strategic trade controls aimed at preventing diversion of dual-use items. The USG is currently engaged with other countries in bilateral and multilateral activities. BIS agrees that other countries and the USG need to strengthen their collaborative efforts and share the responsibility on the risk to international trade and security posed by the diversion of dual-use items, particularly in transshipment trade.

- BIS should strengthen the EAR regulations and review provisions regarding transshipment policies/diversion for freight forwarders and exporters.

BIS is continuously reviewing the EAR to identify any potential actions, including using AES as a tool, to enhance export control compliance activities.

- Several commenters made the point that Commerce should provide training sessions specifically related to preventing diversion. A commenter stated that BIS should focus more on diversion threats in the EMCP element #2 - Risk Assessment. The commenter believed that the type of training provided needs to be specific and illustrative, with examples of threats to be avoided and best practices to be adopted. Commenters recommended that BIS create special training courses and materials designed, developed and targeted to the small and medium-size exporters that do not normally attend conferences. Comments also suggested that more BIS training emphasis should be directed to training resellers because of potentially higher risks when they are parties to export transactions. Commenters recommended that the USG should develop a methodology for working with other countries that mutually recognize the threats to unlawful diversion of dual-use items to high-risk destinations. Other commenters noted that training will be better attended if offered at low cost or no cost. More webinars delivering the message to industry that employee training is a good return on a company's investment should be encouraged. Commenters indicated that industry-wide awareness of the diversion problem is low or inadequate. As one commenter stated, “the public does not know how bad the situation is, so they are not doing much about it.” Commenters stated that BIS should be highly visible about the risks of diversion so industry takes action to minimize diversion risks nationwide and overseas.
- BIS should implement an expanded compliance review program that deploys a hands-on approach to improving exporters and freight forwarders compliance with the EAR.

Commenters suggested that BIS adopt a program to improve exporters and freight forwarder's compliance of the EAR modeled on the Census Bureau's AES compliance program. Census' program identifies best practices of compliant AES filers (freight forwarders and exporters)



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and common problems of noncompliant AES filers. The Census Bureau also conducts one-on-one visits to both compliant and noncompliant companies and publishes the best practices of the compliant companies and shares them with noncompliant companies and requires an improvement in compliance by a specific deadline. Other commenters suggested that BIS consider allowing export companies to self-assess, similar to the CBP initiative on the import side. A freight forwarder suggested that BIS should consider establishing a freight forwarder technical advisory committee. Freight forwarders explained that over the last decade U.S. and foreign exporters' use of and dependence on freight forwarders grew sharply increasing reliance on forwarders to manage and execute compliance responsibilities for their dual-use customers including some classification of products.

- Companies need to improve their internal training. Industry representatives stated that BIS needs to provide targeted training on diversion risks particularly through transshipment trade and that BIS continue to exchange information on this subject with industry as diversion threats change and new ones emerge.

BIS agrees that essential elements to enhancing outreach and compliance activities should be expanded. These include expanding BIS' capacity to analyze data to identify exporters and foreign re-exporters who pose a risk to national security and provide enhanced outreach and compliance programs to prevent noncompliant activities.



ADDENDUM #2:

TEN “BEST PRACTICES” SUGGESTED BY THE DEPARTMENT OF STATE AS THE BASIS UPON WHICH WE CAN BUILD EFFECTIVE INTERNATIONAL TRANSSHIPMENT SECURITY MEASURES:

- 1.** First to have a transparent and interagency-coordinated legal and regulatory system that comprehensively controls items for export, re-export, transit and transshipment that extends fully to activities within free trade zones, and is consistent with the guidelines and lists of the four multilateral regimes and relevant Security Council Resolutions.
- 2.** Ensure for listed items that licenses are required for the transshipment of all munitions and nuclear items, and for all exports of other listed items at least to countries and end-users identified as being of proliferation concern or those endeavors acting on their behalf. Coordination with the exporting country, as appropriate, to ensure that transshipments of listed items are consistent with the intent of the exporting country.
- 3.** Ensure catch-all authority controls all items in transit and transshipment where there is a reasonable suspicion that the items are intended to be used in weapons of mass destruction (WMD), their related delivery systems, or conventional arms.
- 4.** Adopt internationally endorsed requirements for manifest collection in advance of the arrival of all controlled goods, regardless of their end destination. This would provide the governments the ability to vet transactions against known end users of concern and for inconsistencies that raise suspicion, and do it in time to stop and seize the transaction utilizing catch-all controls if necessary. The World Customs Organization (WCO) SAFE Framework provides a multilaterally accepted data model to simplify for shippers how this information can be selected, formatted, and transmitted.
- 5.** Encourage industry to develop stronger internal compliance programs, and conduct focused outreach to manufacturers, distributors, brokers, and freight forwarders to raise awareness of their export control obligations and the potential penalties for non-compliance. A robust government-industry partnership in the context of transit, transshipment, and re-export is essential to effectively safeguard



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circumstances of transshipment trade from proliferation related activities.

- 6.** Provide adequate resources and training for customs and enforcement officers so that they can identify proliferation-related items, including increasing cooperation between enforcement agencies and licensing authorities and other sources of technical assistance.
- 7.** Fully use inspection authorities for cargos of potential concern, and adopt and deploy appropriate screening technologies—both non-intrusive inspection and radiation detection.
- 8.** Make full use of authorities to seize and dispose of cargos of proliferation concern. Limit enforcement officials’ personal liability for the conduct of routine investigations of shipments.
- 9.** Institute effective penalties sufficient to punish and deter proliferation-related transshipment activities. Prosecute transshipment violations to the full extent of the law and publicize prosecutions as a deterrent.
- 10.** Establish and maintain information sharing exchanges with counterparts in other countries and ensure timely replies to inquiries for assistance.

(The Department of State’s Bureau of International Security and Nonproliferation suggested ten best practices that all nations and jurisdictions should adopt in applying trade controls in transshipment at the March 7, 2011 U.S. Sponsored Global Transshipment Seminar in the United Arab Emirates. <http://www.state.gov/t/isn/rls/rm/158724.htm>)

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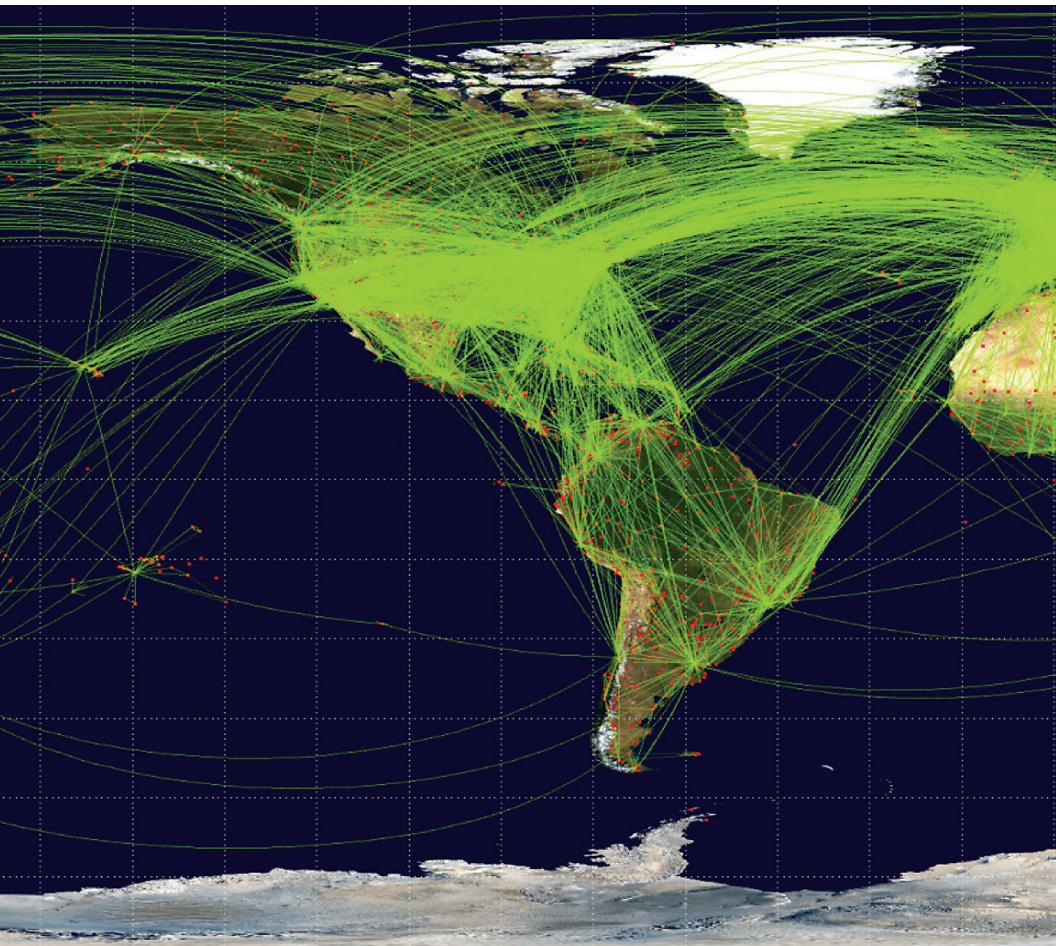
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