Australian Government

Department of Defence

Post Implementation Review

August 2015

Treaty between the Government of Australia and the Government of the United States of America concerning Defense Trade Cooperation

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Post Implementation Review

Purpose

This Post Implementation Review outlines the possible impacts of the *Treaty between the Government of Australia and the Government of the United States of America concerning Defense Trade Cooperation* (the Treaty) on Australian defence industry. At the time of the Treaty's negotiation, implementation details were not available for a Regulation Impact Statement to support the legislative framework development.

Rationale

Over 50 per cent of Australian defence equipment and technology (referred to as 'defence articles') is sourced from the United States (US), and is subject to some form of US Government export control that includes licensing and compliance requirements.

Defence articles may range from complete military platforms, such as aircraft, ships and tanks and their subsystems and components, to small pieces of military equipment, such as handheld Global Positioning Systems and night vision goggles. US export controls also apply to US-origin support and test equipment, technical data, software and the provision of services needed to operate or sustain this equipment.

US export controls are governed by US domestic legislation that includes the *International Traffic in Arms Regulations* (ITAR) for controlled defence articles acquired through commercial arrangements; Section 3 of the *Arms Export Control Act* for US Foreign Military Sales acquired articles; and the *Export Administration Regulations* for less sensitive and dual military/commercial-use technology.

Under these US provisions, every transfer of defence articles to a foreign government or commercial entity is subject to US export controls and requires individual approval and export licensing, or the application of appropriate exemptions or other written authorisations. For defence industry, these are brokered between the initiating company, the US suppliers and the US Government. This negotiation, approval and licensing process can be complex and is time consuming, and may take up to nine months to negotiate a new licence or any variation to an existing licence. Depending upon the nature of the defence articles to be exported from the US, this may result in the Australian Defence Force and Australian defence industry experiencing delays in importing and maintaining US-sourced equipment for operational use.

The Treaty enjoys an exemption under Section 126.16 of the US ITAR and, as a result, provides an opportunity to reduce the regulatory burden and associated approval and licence processing lead-times by creating an 'Approved Community' in Australia and the US within which approved members may export, import, transfer or re-export eligible defence articles without the need to apply for individual licences or authorisations.

The Treaty is a sub-set of the overarching US export controls regime and offers Approved Community members an alternative framework for transacting eligible defence articles. There remain US-origin defence articles that are exempted and cannot be transacted under the Treaty. The regular US export control provisions continue to apply for those articles.

Background

The Treaty was signed by the then Prime Minister of Australia, the Hon John Howard MP, and the then President of the United States of America, George W. Bush, on 5 September 2007.

The Treaty establishes a bilateral framework intended to reduce barriers, including requirements for licences or other written authorisations, for the exchange or trade of eligible defence articles where the Australian Government is the end-user, or for US Government end-use. In this context, non-governmental entities such as Australian defence industry may benefit from the Treaty by becoming an approved Australian Community member and by transacting under the Treaty to support Australian and US government end-use defence programs, projects, military exercises, cooperative programs and equipment sustainment.

The Australian legislative authority to implement the Treaty is provided by Part 3 of the *Defence Trade Controls Act 2012* and the accompanying *Defence Trade Controls Regulation 2013*, which came into effect in June 2013. A non-binding 'Implementing Arrangement' agreed by Australia and the US also came into effect at that time. The Implementing Arrangement supplements the provisions of the Treaty by prescribing detailed procedures and standards to be adopted by both parties.

This legislation and regulation enact the Australian Government's obligations to the US Government under the Treaty. They provide a domestic framework to protect essential national security and defence interests for eligible defence articles transacted under the Treaty framework that otherwise would be subject to Australian export controls, the US ITAR or Section 3 of the US Arms Export Controls Act.

It is important to note that the Treaty and the legislative and regulatory framework do not replace Australian or US export control regulations but act in a complementary manner, providing Australian defence industry with an alternative to move eligible defence articles between themselves and other companies or government agencies that are part of the Approved Community within Australia or the US.

Treaty parameters

The Treaty sets three provisions that determine the eligibility and the ability to transact under its framework:

Membership

Any company seeking to transfer eligible defence articles under the Treaty must be a member of the Approved Community.

Eligible Articles

Articles eligible for export or transfer under the Treaty must be:

- Listed in Part 1 of the Australian Defense Trade Cooperation Munitions List (DTCML), which is derived from the US Munitions List (USML); and

- Not listed in Part 2 of the DTCML that identifies articles excluded from transfer under the Treaty, which is derived from the US Exempted Technologies List (ETL).

Approved Activities

Four scope lists define the Australian and US Government activities under which the transfer of eligible defence articles may be transacted under the Treaty:

- Combined Operations and Exercises List, which lists eligible military and counter-terrorism operations and exercises that include participation by both Australia and the US.

- Cooperative Programs List, which lists eligible research, development, production and support programs related to security and defence that involve cooperation between Australia and the US.

- Australian Government End-Use List, which lists projects and platforms related to security or defence where the Australian Government is the end-user.

- US Government End-Use List, which lists projects related to security or defence where the US Government is the end-user.

These provisions set the parameters for Australian defence industry in deciding whether to transact under the Treaty or maintain their arrangements under extant US export controls.

Approved Community Membership

Under the Treaty, Australia and the US agreed to establish an Approved Community of government and non-government entities. Only members of the Approved Community may operate within the transfer and import/export system established by the Treaty.

Members of the Approved Community that are Australian-based are known as the ‘Australian Community’ or ‘Australian Community members’. The Australian Community is managed by the Australian Department of Defence (Defence) and the US Community is managed by the US Department of State.

Admission to the Australian Community is voluntary and does not affect any existing licensing or contractual or business arrangements a company might have. For Australian companies wishing to join the Approved Community, the application process is a one-off requirement with no sunset clause.

To maintain approved membership, Australian Community members must: complete an annual compliance assessment, as well as on-occurrence reports for any loss, theft, destruction or unauthorised access to Treaty articles; keep appropriate records and mark Treaty articles; notify any changes to foreign ownership, control and influence; and permit an authorised Department of Defence officer to enter specified premises to monitor compliance. These obligations are included in the legislative framework.

Intermediate Consignees

Freight forwarders, customs brokers or other commercial transport providers involved in the movement of Treaty articles are not required to join the Approved Community but require approval as an 'Intermediate Consignee'. Approved Intermediate Consignees may receive Treaty articles from Australian Community members for the purpose of transportation to other Approved Community members.

The application process is a one-off requirement with no sunset clause. Once approved, the major compliance requirement is that the Intermediate Consignee must have a system that is capable of tracking and recording the movement of articles in its possession, including information such as time, date, location and identity of recipient. Such a tracking system is typically employed within the industry as standard business practice and does not represent an additional burden.

Progress since implementation

Since the Treaty came into effect in mid-2013, membership of the Australian Community has steadily grown to 48 members, with 36 non-governmental (defence industry) and 12 government agency members at 30 June 2015. Another 23 industry applications were in progress. Thirty-three Intermediate Consignees were approved in the same period.

Over the last two years, Defence has worked closely with the US Department of State, the US Department of Defense and Australian defence industry to improve the application and operation of the Treaty framework. Measures include having new projects and cooperative programs and government end-use equipment added to broaden the scope of approved Treaty activities, and bringing a greater deregulatory effect by streamlining administrative processes to include self-assessment and compliance reporting to the extent possible.

Defence has also conducted industry outreach activities, particularly during the development and implementation phases of the Treaty. Regular feedback and industry requests are also brokered through telephone and email 'hotlines', and will continue through future outreach and industry association engagement programs.

Expected Benefits of the Treaty

Australian defence industry companies that become Australian Community members under the Treaty may benefit through the opening of new avenues for industrial cooperation and allowing for partnering and technology sharing with their US counterparts. The Treaty provides the opportunity for Australian companies to support work for Australian and US government end-use defence programs, with

timely access to controlled technology, and the ability to share technical data without the need for individual licences or other authorisations. This has a major benefit in reducing lead-times and costs in brokering business opportunities and responding to requests for tender, and may improve the prospects for Australian companies seeking to participate in US defence programs.

The Treaty's regulatory framework places some obligations and potential costs on Australian Community members, such as record keeping, article marking, personnel security clearances and compliance reporting. However, the Treaty provisions may also give rise to a deregulation benefit in reducing administrative and licensing overheads and schedule lead-times related to approval processes that would arise if the eligible transactions were made under other US export control provisions. In addition, much of the Treaty administration between defence industry and Defence is based on SmartForm and online submissions, including self-assessment and exception reporting, to assist in reducing administrative costs and regulatory burden.

Australian Community members may also import, transfer or re-export eligible US-origin defence articles under the Treaty without individual licences, authorisations or referral to Defence, which also represents a significant cost and deregulatory benefit.

Australian defence industry participation in the Treaty framework is voluntary. Companies have no obligation to transact using the Treaty once their Australian Community membership is approved, and are only subject to the regulatory framework if they use the Treaty to transact eligible defence articles.

Each Australian Community member has made a decision to join, and may then use the Treaty based on their individual business decisions. The Treaty is not a regulatory regime imposed on the Australian Community but instead offers an alternative to navigating the US export control system for eligible transactions. However, deregulatory benefits and potential time and cost savings accrue when Australian Community members choose to transact eligible articles under the Treaty framework rather than other US export controls.

Survey

Given the limited data available to Defence, Australian Community members and approved Intermediate Consignees were invited in March 2015 to participate in a voluntary survey designed to ascertain the utility of the Treaty and to identify any regulatory impacts on Australian defence industry. The surveys (one for each cohort) consisted of a one page SmartForm for completion.

At the time of the survey, there were 45 approved Australian Community members (33 defence industry and 12 government agencies) and 29 approved Intermediate Consignees. Twenty-two responses were received from Australian Community members yielding a 49 per cent response rate. Eleven responses were received from approved Intermediate Consignees yielding a 38 per cent response rate. The results of the survey can be found in annexes A, B and C.

Qualitative survey responses also indicate that the Treaty framework has been of most benefit to small and small-to-medium enterprises, possibly because there is little cost to incorporate Treaty framework requirements into existing systems and

processes, and the number of staff to train in Treaty management is generally low. This may provide these companies with a competitive advantage in transacting under the Treaty from the outset. However, the business decisions and assessments as to whether to use the Treaty provisions or not remain the responsibility of individual companies which may also be guided by US suppliers' willingness to transact under the Treaty.

Interest from small and small-to-medium enterprises in joining the Australian Community is proportionately high, although information provided to date is that only a modest number of companies have undertaken transactions using the Treaty. The number of transactions is expected to rise with the increase in Australian Community membership that is currently indicated, and growing awareness of the Treaty's potential benefits.

The survey sample did not result in a 'typical' profile for defence industry (which may range from sole traders to small-to-medium sized companies to large prime contractors) possibly transacting under the Treaty, or provide an assured range of quantitative data. Equally, other data, such as transactional data, is not readily available given that the Treaty does not require individual licences or reporting of Treaty activities to Defence.

A comparative model was therefore developed to estimate the likely costs of regulation under the Treaty and to derive an estimate of the deregulatory benefit in the situation where the Treaty framework was used in place of US ITAR provisions to transact an eligible article.

Assessing regulatory costs and deregulatory benefits

The comparative model used by Defence to estimate the likely costs of the Treaty's legislative and regulatory regime and its deregulatory benefit is consistent with the Government's Regulatory Burden Measurement Framework. The model derives estimated implementation costs, as well as ongoing costs (over a 10 year period) that are brought back to a yearly estimate.

To undertake transactional comparison estimates, the model assumes that an Australian Community member may transact an eligible defence article under either the Treaty or US ITAR provisions.

The comparative model is also based on:

- thirty-three Australian Community defence industry members, which is the number of industry members included in the survey of March 2015;
- staffing and overhead costs of $65.45 an hour, which is the standard regulatory labour wage cost including a 1.75 factor for on-costs; and,
- defence industry members having an estimated turnover of $1 million and profit of 4 per cent directly related to transacting defence articles.

The model's comparative estimates also draw on qualitative and quantitative information provided by survey respondents regarding Treaty and US ITAR

transactions and, in particular, the staff effort and indicative costs associated with negotiation and any licensing approval timelines (comparative delays), record keeping, training and compliance. For Intermediate Consignees, the only costs are in regard to implementation (completing the application form).

While US ITAR and the Treaty frameworks operate under different jurisdictions and regimes, some administrative and compliance aspects are similar. In particular, both require record keeping and training for staff to understand and uphold the legislative, regulatory and security and handling obligations. The comparative model therefore assumes that the costs for these activities are the same and do not present an additional burden on industry, but are included in the comparative tables.

Comparative cost estimates between the Treaty and US ITAR transactional framework drawn from the model are illustrated in the following tables. The activities mainly represent staffing costs:

Comparative estimates

Table 1: Membership, facility and ICT application

Framework	Yearly estimate
Treaty	$4,860
ITAR	Nil

Table 2: Negotiation with suppliers for licence/to transact

Framework	Yearly estimate
Treaty	$192,767
ITAR	$453,569

Table 3: Transition articles/amending licences

Framework	Yearly estimate
Treaty	$110,152
ITAR	$259,182

Table 4: Licencing costs

Framework	Yearly estimate
Treaty	Nil
ITAR	$14,025

Table 5: Security clearances

Framework	Yearly estimate
Treaty	$18,480
ITAR	Nil

Table 6: Annual compliance assessment, reporting and monitoring

Framework	Yearly estimate
Treaty	$26,262
ITAR	Nil

Table 7: Delay costs due to article negotiation and supplier/licence processing lead-times

Framework	Yearly estimate
Treaty	$ 53,768
ITAR	$313,516

Table 8: Intermediate Consignee application

Framework	Yearly estimate
Treaty	$1,424
ITAR	Nil

Table 9: Comparative deregulatory benefit including all activities and costs

Framework	Yearly estimate
Treaty	$ 710,134
ITAR	$1,342,714
Difference	($ 632,580)

Overall, the yearly deregulatory benefit across the Australian Community defence industry membership is estimated to be $0.633 million should eligible defence articles be transacted under the Treaty rather than US ITAR provisions. This is illustrated in the following table.

Table 10: Regulatory burden and cost offset estimate

Average annual regulatory costs (from business as usual)				
Change in costs ($ million)	Business	Community organisations	Individuals	Total change in costs
Total, by sector	($0.633)	$0	$0	($0.633)
Cost offset ($ million)	Business	Community organisations	Individuals	Total, by source
Agency	$0	$0	$0	$0
Are all new costs offset? □ Yes, costs are offset □ No, costs are not offset ☑ Deregulatory—no offsets required				
Total (Change in costs – Cost offset) ($ million) = ($0.633)				

Conclusion

The Australian legislative and regulatory framework to implement the Treaty has met the major bilateral government intent that, under the Treaty:

> …the Parties seek to establish a framework that is necessary for the protection of the Parties' essential security and defense interests and that facilitates the movement of Defense articles within an Approved Community, while ensuring there are proper safeguards against unauthorized release beyond that Approved Community….[1]

The Treaty is enduring, and the Australian legislation and regulation provide an assured framework to protect essential security and defence interests for eligible defence articles transacted under the Treaty that are for Australian Government end-use, or for US Government end-use. Australian defence industry has the opportunity to play a key role within this construct should the Treaty and the nature of eligible defence articles being transacted suit their business models and experience of extant US government export controls.

Australian industry participation in the Treaty framework - and thus becoming subject to its legislative and regulatory compliance and control framework - is voluntary. The Treaty's regulatory framework places some obligations and costs on Australian Community members, but the Treaty also extends potential deregulatory benefits and cost-savings for Australian defence industry in allowing approved Australian Community members to import, transfer or re-export eligible US-origin defence articles without individual approvals or licences required by other export controls. The major benefit flowing from this is the reduction in lead-times that would otherwise be necessary to negotiate licences with US suppliers and obtain approvals, with complementary reductions in delays to business, staffing effort and costs.

Overall, the legislative and regulatory framework has the potential to bring benefits to Australian Community members by providing enhanced opportunities for the supply and sustainment of eligible US export controlled technology to the Australian Government.

Undertaking a definitive assessment of the potential costs or savings under the Treaty for defence industry was constrained by the limited quantitative data available, coupled with the diverse nature of defence industry currently approved as members of the Australian Community. Notwithstanding, a comparative model to estimate the likely costs of regulation under the Treaty and any deregulatory benefit in the situation where the Treaty framework was used in place of US ITAR provisions to transact an eligible article has derived an indicative yearly benefit of $0.633 million to the Australian Community defence industry membership.

Since the legislation and regulation came into effect in mid-2013, the uptake of Australian Community membership among defence industry has been steadily increasing. While the number of transactions undertaken has been modest, recent indications are that they are also steadily increasing. Defence has an outreach program underway to highlight the prospective benefits to defence industry in

[1] Treaty between the Government of Australia and the Government of the United States Concerning Defense Trade Cooperation, 5 September 2007, which is available at the Defence website (www.defence.gov.au/publications/docs/DefenceTradeCooperation_Treaty.pdf).

transacting under the Treaty framework and to encourage Australian Community membership, and continues to receive a steady flow of applications for membership.

Defence will continue to gather qualitative and quantitative data to support and review the utility of the regulation, mindful of not creating an administrative or additional ‘red tape’ burden among Australian Community members when seeking this data.

Annex A

Survey questions and results for Australian Community Members

No.	Question	Response/Result
1	Were there any impacts on your business to gain approval as a member of the Australian Community?	Yes – 31.8% No – 68.2%
1a	If 'yes', what was the nature of the impact and was there any associated cost increase or decrease?	Comments box
2	Have you ever used the Australia-US Defence Trade Cooperation Treaty (the Treaty) to transfer, supply or receive defence goods, services or technologies?	Yes – 27.3% No – 72.7%
2a	If 'yes', how did the Treaty arrangements compare to traditional licensing arrangements e.g. DECO licence, ITAR authorisation such as a TAA?	Easier – 22.7% No change – 9.1% More difficult – 4.5% Not applicable – 63.6%
2b	If 'easier' or 'more difficult', what changed the activity and was there any associated cost increase or decrease?	Comments box
3	Have you been required to make changes to business processes to incorporate transfers under the Treaty?	Yes – 50% No – 50%
3a	If 'yes', was there any associated cost increase or decrease?	Comments box
4	Have you been required to undertake additional formal or information training of staff to manage transfers under the Treaty?	Yes – 45.5% No – 54.5%
4a	If 'yes', was there any associated cost increase or decrease?	Comments box
5	How do Treaty compliance requirements compare to operating under ITAR?	Easier- 40.9% No change – 45.5% More difficult – 9.1% Not applicable – 4.5%
5a	If 'easier' or 'more difficult', what changed the activity and was there any associated cost increase or decrease?	Comments box
6	Would you recommend the Australia-US Defence Trade Cooperation Treaty to other companies as a viable trade option over existing licensing arrangements?	Yes – 90.9% No – 0% Nil response – 9.1%
7	Do you have any additional comments?	Comments box

Annex B

Survey questions and results for Intermediate Consignees

No.	Question	Response/Result
1	Were there any impacts on your business to gain approval as an Intermediate Consignee?	Yes – 9.1% No – 90.9%
1a	If 'yes', what was the nature of the impact and was there any associated cost increase or decrease?	Comments box
2	Have you ever transferred any goods for Approved Community members using the Australia-US Defence Trade Cooperation Treaty (the Treaty) arrangements?	Yes – 27.3% No – 72.7%
2a	If 'yes', how did the Treaty arrangements compare to traditional licensing arrangements e.g. DECO license, ITAR authorisation such as a TAA?	Easier – 0% No change – 18.2% More difficult – 0% Not applicable – 81.8%
2b	If 'Easier' or 'More difficult', what changed the activity and was there any associated cost increase or decrease?	Comments box
3	Have you been required to make changes to business processes to incorporate transfers under the Treaty?	Yes – 9.1% No – 90.9%
3a	If 'yes', was there any associated cost increase or decrease?	Comments box
4	Have you been required to undertake additional formal or information training of staff to manage transfers under the Treaty?	Yes – 18.2% No – 81.8%
4a	If 'yes', was there any associated cost increase or decrease?	Comments box
5	How do Treaty compliance requirements compare to operating under ITAR?	Easier – 0% No change – 81.8% More difficult – 0% Nil response – 18.2%
5a	If 'Easier' or 'More difficult', what changed the activity and was there any associated cost increase or decrease?	Comments box
6	Would you recommend becoming an approved Intermediate Consignee to other companies?	Yes – 90.9% No – 0% Nil response – 9.1%
7	Do you have any additional comments?	Comments box

Annex C

Additional Comments from Australian Community Members

Question 7: At the end of the survey, recipients were asked if they had any additional comments relating to the Treaty. Nineteen comments were received; 16 of which are cited below (the remaining three comments were nil responses). Responses are anonymous.

> "X are involved with projects between Australia and the US and although not having to reference the Treaty directly in our exchange of services to date, have found it valuable in such as being a common reference organisation between parties".
>
> "The Treaty is a game changer for Federal Govt agencies engaged in law enforcement and security especially in the emerging counter terrorism taskings nationally. Its also allows closer inter-operability with ADF/Customs on joint tasks both nationally and internationally due to shared technologies".
>
> "X is grateful the Department has provided this valuable change".
>
> "As not having used the Treaty as yet, I'm looking forward to using and experiencing the changes".
>
> "Would prefer it to cover more sustainment activities (didn't know they could apply to have additional projects/platforms added to GoA [Government of Australia] End Use List)".
>
> "Treaty arrangements appear to have benefitted the Australian end-customer. Greater education of USA-side suppliers would benefit overall process".
>
> "We have only just become Australian Community members so difficult to ascertain comparison to ITAR".
>
> "X is an SME [small-medium enterprise] and has a small throughput of such activities but the changes have been worthwhile".
>
> "We are still waiting on security clearances before we can handle goods under the Treaty so unable to comment on several questions".
>
> "Haven't actually used but are set up and ready to use, keen to use it".
>
> "The control requirements for activities under the Treaty are very similar to ITAR controls and, as an ITAR compliant company, the Treaty is easy to comply with. The Treaty will likely become more useful when more participants are involved, but at this time, it's of limited value to us".
>
> "Very happy with the support we have received and glad to be a member and we will use more and more with whole platforms now added".
>
> "More outreach in the USA please – there is still a high level of reluctance and fear of using the Treaty".

"Have not yet used but have set up and are ready. Intend to do a seminar to learn more".

"The implementation of the Treaty into a predominantly ITAR business will take some getting used to and certainly with inherent teething issues. Not addressed yet is the issue of EAR [Export Administration Regulations] under the Treaty where an article may have both ITAR and EAR components".

"Experiences to date are relatively positive".

Additional Comments from Intermediate Consignees

Question 7: At the end of the survey, recipients were asked if they had any additional comments relating to the Treaty. Ten comments were received; six of which are cited below (the remaining four comments were nil responses). Responses are anonymous.

"Procedures and systems we had in place met the requirements of Intermediate Consignee prior to application".

"We signed up based on the fact that we might use the Treaty in the future but have not used the Treaty yet".

"We are happy with the process. Good changeover. It has helped us obtain business as other companies ask if they are members of the Treaty".

"No comment to any of the above questions. Could not answer them as have no experience of the Treaty".

"Application process was great, quick and streamlined".

"I believe that industry is not totally aware of the advantages and is not putting the opportunity in use. Although we do see requirements to verify whether [X] is an approved Intermediate Consignee, I do not see requests where we make use of the membership".