



UNITED STATES DEPARTMENT OF COMMERCE
Bureau of Industry and Security
Washington, D.C. 20230

August 2, 2007

Dear _____ :

This is in response to your May 14, 2007 request for an advisory opinion on the application of the foreign direct product rule to exports of encryption technology. In your request, you presented four fact patterns and requested confirmation of your analyses of the application of the foreign direct product rule to exports made pursuant to sections 744.9, 742.15(b) and 740.17(b) of the Export Administration Regulations (EAR).

Section 744.9

As a threshold matter, section 744.9 sets forth a requirement for a "U.S. person" to obtain authorization from the Bureau of Industry and Security (BIS) to provide "technical assistance (including training) to foreign persons with the intent to aid a foreign person in the development or manufacture outside the United States of encryption commodities and software that, if of United States origin, would be controlled for EI reasons under ECCN [Export Control Classification Number] 5A002 or 5D002." "Technical assistance" is generally defined, in part 772 of the EAR, as "technology" that is not in the form of "technical data," and that may take forms such as instruction, skills training, working knowledge, and consulting services. "Technical assistance" may involve the transfer of "technical data."

Using this definition, "technical assistance" for encryption items may be classified as ECCN 5E992 or 5E002.¹ However, while section 744.9 requires authorization from BIS for all "technical assistance," it only requires a license for "technical assistance" that is controlled under ECCN 5E002. The requirement for authorization set forth in section 744.9 may be satisfied by means of a license, license exception, or if the EAR provide that no license is required (NLR). Section 742.15(b) provides authorization for the export of encryption technology classified under ECCN 5E992 to countries other than those designated as state sponsors of terrorism as NLR, as long as certain review and notification requirements are met. If an exporter complies with the requirements set forth in section 742.15(b) for the export of the 5E992 technology, the authorization set forth in section 742.15(b) will satisfy the requirement in section 744.9 that any "technical assistance" for encryption commodities or software be authorized by BIS.

Turning to the fact patterns set forth in your May 14, 2007 letter, Scenario 1 involves

¹ There is no encryption technology classified as EAR99.



technical assistance classified at the ECCN 5E992 level to a Chinese company that results in the manufacture of a Chinese-made ECCN 5A002-level item. Your letter assumes that the provision of the ECCN 5E992 technical assistance requires authorization under section 744.9. However, as explained above, section 742.15(b) authorizes the export of the 5E992 technical assistance described in Scenario 1. Your analysis, based in part on informal telephone discussions with me, concludes that the ECCN 5A002-level foreign product would not be subject to the EAR unless the foreign product contained more than a de minimis amount of U.S.-origin controlled content, as set forth in section 734.4(b) of the EAR. Your analysis also concludes that the foreign direct product rule, set forth in section 736.2(b)(3) of the EAR, would not apply in this instance because the technical assistance is classified under ECCN 5E992. BIS concurs with these conclusions.

Scenario 2 involves technical assistance classified at the ECCN 5E002 level to a Chinese company that results in the manufacture of a Chinese-made ECCN 5A002-level item. Your letter again assumes that this export requires a license under section 744.9. Your analysis, again based in part on informal telephone discussions with me, concludes that the ECCN 5A002-level item would be subject to the EAR by operation of the foreign direct product rule set forth in section 736.2(b)(3) of the EAR. BIS concurs with this analysis. Please note that any export of ECCN 5E002 technical data or ECCN 5E002 technical assistance would require a license for export to China under section 742.15(a), and that license would satisfy the requirement under section 744.9 that any export of encryption technical assistance receive authorization from BIS; therefore, no separate authorization under section 744.9 would be required. Please also note that the license issued under section 742.15(a) would likely include a rider reminding the exporter that foreign direct products made with the licensed technology would be subject to the EAR pursuant to section 736.2(b)(3).

Sections 742.15(b) and 740.17(b)

Under Scenarios 3 and 4 set forth in your May 14th letter, a U.S. company exports ECCN 5E992 technical data to its subsidiary in China under section 742.15(b)(3)(i) without prior notification or review, and/or exports ECCN 5E002 technical data to its subsidiary in China under section 740.17(b)(1) without prior notification or review. You seek confirmation that foreign-made end products resulting from the transfer of ECCN 5E992 technical data from a U.S. parent to its foreign subsidiary under section 742.15(b) are not per se subject to the EAR, but that foreign-made products resulting from the transfer of ECCN 5E002 technical data from a U.S. parent to its foreign subsidiary under section 740.17(b)(1) are per se subject to the EAR. BIS concurs with your conclusion regarding section 740.17(b)(1), and concurs in part regarding your conclusion regarding 742.15(b).

Section 742.15(b)(3)(i) expands the foreign direct product rule set forth in section 736.2(b)(3) to apply to the foreign direct products of ECCN 5E992 technology, when that technology is exported to subsidiaries without prior notification or review of the technology being exported. As you point out in your letter, section 742.15(b)(1) does not similarly expand the foreign direct product rule. Therefore, while the foreign direct product of technology

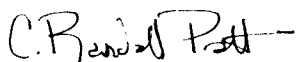
exported under section 742.15(b)(3)(i) is per se subject to the EAR, BIS agrees with your conclusion that the foreign direct product of ECCN 5E992 technology exported pursuant to section 742.15(b)(1) is not per se subject to the EAR. An exporter may choose under which of these provisions to export 5E992 technology.

BIS concurs that foreign-made products resulting from the transfer of ECCN 5E002 technical data from a U.S. parent to its foreign subsidiary under section 740.17(b)(1) are per se subject to the EAR, and that the statement set forth in section 740.17(b)(1)(iii) is in fact an expansion of the direct foreign product rule set forth in section 736.2(b)(3).

Finally, under Scenarios 3 and 4, you request guidance on the regulatory requirements that apply to intra-country transfers of the foreign direct product to third parties in China. As discussed above, if the foreign direct product is produced using technology exported to a U.S. subsidiary in China under section 740.17(b)(1) or 742.15(b)(3)(i), the foreign made product is subject to the EAR. Section 740.17(b)(1)(iii) and 742.15(b)(3)(i) require “review and authorization before sale or transfer outside the U.S. company and its subsidiaries.” Therefore, sale or transfer of the foreign direct product to third parties would be equivalent to an export, and prior review/license exception authorization or a license would be required for such transactions to the same extent it would be required for an export of the item from the United States to the end user.

In rendering this opinion, BIS has relied upon information and representations included in your oral or written communications, including your letter dated May 14, 2007. Any deviation from the factual circumstances as stated in this opinion may result in different regulatory obligations, including license requirements. Please let me know if you have additional questions about these issues.

Sincerely,



C. Randall Pratt
Director
Information Technology Controls Division
Office of National Security and Technology Transfer Controls