

The UPDATE Report

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Expertise: How to Handle Export of a Part Brokered by Another Party

A member recently asked how to handle the "direct-ship" export of a part that had been brokered by a non-U.S. distributor but that was destined for direct-shipment to a non-U.S. air carrier.

The transaction looks like this. Company A is a U.S. distributor that has the aircraft part in inventory. A non-US distributor, Company B, calls to purchase the part. The two companies agree to a purchase price of \$2,000.00. Then, Company B asks Company A to directly-ship the part to Company C, a non-U.S. end-user. Company B has sold the part to Company C for \$3,000.00 - an amount that is greater than the amount for which they purchased it.

The question that arises is, when Company A files export documentation, which export price is the price that goes in the electronic export information? Should they use their sales price to Company B (\$2,000.00), or Company B's sales price to Company C (\$3,000.00)? The answer to this question may even impact whether electronic export information needs to be filed, because \$2,000.00 is less than the \$2,500 filing threshold and \$3,000.00 is greater than the \$2,500 filing threshold.

For purposes of this hypothetical transaction, we will assume that the part is a commercial aviation part that is not subject to the ITAR restrictions. We will also

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MESSAGE FROM ASA'S PRESIDENT

THE UPDATE REPORT

is the newsletter of
the Aviation Suppliers
Association.

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members and other aviation
professionals stay abreast of
the changes within the aviation
supplier industry.

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Dear Colleagues,

In the U.S. alone, 11 million people work in the aviation industry, so the health of the aviation industry has a tremendous impact on the economy. The aviation industry also is a bellwether for the economy. If aircraft aren't flying, then that is a sure sign that commerce, in general, is flagging.

Last year's drop in revenue passenger miles and revenue ton-miles of freight was a stark indication of the global recession. And this year's upswing in these two categories is a sure sign that the global economy is healing.

Many ASA members have reported that they are doing much better than last year and they are anticipating rosy times in the near future. One of the most important sectors among our customer base, airlines, are showing increases in net yield and operating margins. But it is important to remember that all business is a calculated risk. Signs of improvement could yield to an economic complacency that might permit a resurgent recession, or at least delay recovery.

There is uneven economic recovery throughout the world, which is why a geographically diverse client base remains important to business stability in our industry.

In the United States, a fragile recovery could easily be tipped by regulations that obstruct business without improving safety. ASA remains committed to working on issues that will benefit the economic conditions of the industry while continuing to support the highest levels of safety. This is why we remain focused on government affairs issues that will help improve the aviation industry's economic situation at the same time that we continue our focus on aviation safety.

Take care, Michele

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REGULATORY UPDATE

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assume that the transaction is not required to be licensed under Bureau of Industry and Security (BIS) or Office of Foreign Asset Control (OFAC) restrictions. Finally, we will assume that no documentation exceptions apply to this transaction.

The short answer to the question is that the exporters at Company A should use the Company A selling price as the export value. However, the answer could change under other factual situations so it is important to understand how we've arrived at this result.

In order to understand the way we have arrived at the answer to the question, we will need to first define a few terms. The first term is "Order Party." An "Order Party" is the person in the United States that conducts the direct negotiations or correspondence with the non-U.S. purchaser or ultimate consignee and who, as a result of these negotiations, receives the order from the non-U.S. purchaser. In our hypothetical case, the Order Party is Company B because Company B conducted all of the direct sales negotiations with the non-U.S. purchaser (Company C).

The BIS' export rules say that if a U.S. Order Party directly arranges for the sale and export of goods to the non-U.S. purchaser, then the U.S. Order Party shall be listed as the United States Principle Party in Interest (USPPI) in the electronic export information filings.

The selling price for goods exported pursuant to sale, and the value to be reported in the electronic export information, is the USPPI's price to the non-U.S. buyer. In this hypothetical case, Company B is the non-U.S. "buyer," even though Company A is directly shipping the part to the end user, Company C.

The Export value of an aircraft part is the value of the part at the time it reaches the U.S. port of export. The regulations specify that the value shall be the selling price if the parts are sold, including freight and insurance. In establishing the selling price for the Electronic Export Information (EEI) system (formerly known as Shipper's Export Declaration), you should deduct from the selling price any unconditional discounts, but do not deduct discounts that are conditional upon a particular act or performance on the part of the non-U.S. buyer.

If goods are not sold (e.g. shipped as part of an exchange or barter), then the cost of goods is used to assess value (the sum of expenses incurred in the acquisition or production of the goods). For goods shipped on consignment without a sale actually having been made at the time of export, the selling price to be reported in the EEI is the market value at the time of export at the U.S. port.

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In our hypothetical transaction, Company A appears to be the USPPI, and therefore Company A should list their selling price (\$2,000.00) as the value on the EEI.

What if we change the facts slightly? Imagine that Company B was a domestic U.S. company, rather than a non-U.S. company. In such a case, Company B may be the US PPI, and Company A may merely be a shipping agent. If Company A is listing the other brokering company, Company B, as the USPPI, then Company A should list the other company's selling price as the value on the EEI.

The facts of every situation must be analyzed carefully to make sure that each party to the transaction is properly characterized, so that the analysis will yield the proper result and the exporter will know how to complete the documentation properly. 

Japan Readies its SMS Rule for Publication.

Japan's Ministry of Land, Infrastructure, Transport and Tourism (MLIT), which is the parent ministry of the Japanese Civil Aviation Bureau (JCAB), is soliciting public comment on forthcoming Japanese rules concerning Safety Management Systems (SMS).

These rules would affect companies that manufacture, maintain or modify civil aircraft and aircraft parts. While these proposed rules would not have a direct effect on distributors (e.g. distributors would not be regulated), they are expected to have a significant indirect effect on distributors.

MLIT intends to impose SMS requirements on MRO companies by April 1, 2011. SMS requirements would be imposed seven and a half months later on manufacturers - the target date is November 14, 2011.

It is presently unknown how these rules would affect non-Japanese companies, but it is possible that Japan could forbid the import of parts made or maintained by companies that do not meet the Japanese SMS requirements. Under normal international standards, this requirement would be waived if the home country of the exporter (1) has published comparable SMS regulations and (2) has signed a bilateral agreement with Japan in which Japan recognizes the SMS regulatory structure of the exporting nation as being comparable to the system implemented in Japan.

We obtained a loosely-translated copy of the Japanese rulemaking publication, and it is available on our website. Interested companies are urged to submit comments to MLIT no later than the deadline of October 4, 2010. MLIT prefers to receive comments in Japanese (sorry—neither MARPA nor the Department of Commerce can recommend a Japanese translation service). 

U.S. Government Sponsors an Aerospace Mission to China

The U.S. Commerce Department has organized an Aerospace Supplier Development Mission to China. For ASA members looking to expand into China, this is an excellent way to make contacts and to learn more about the marketplace.

The Mission is scheduled for November 7-17, 2010, and the government has announced that there are still spaces available. Several ASA members have told us that they plan to participate.

China's aerospace sector ranks among the world's most dynamic, going far beyond the country's massive (Continued on Page 5)

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investment in aircraft (4,000 by 2025). Chinese aerospace companies have rapidly developed into serious players in the industry's global value chain, and they are in a greater position than ever to frequently make their own sourcing decisions.

The primary objectives of the Aerospace Supplier Development Mission to China are:

1. To introduce U.S. companies to Chinese joint venture groups and Western OEMs operating in China;
2. To explore supplier opportunities on current/future aerospace projects in China, and;
3. To participate in Airshow China in Zhuhai

2010 Mission schedule:

- November 7-9 - Shanghai
- November 9-11 - Beijing
- November 11-14 - Xi'an
- November 14-15 - Guangzhou
- November 15-17 - Zhuhai

The full mission schedule is online at <http://www.buyusa.gov/nevada/aeroflyer.pdf>.

This is a great opportunity to meet directly with officials from Chinese aerospace companies and from the Chinese government. Check out the online information, including application instructions for more details at <http://www.buyusa.gov/nevada/aerochina.html>. 

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United and Continental Merger Approved

The stockholders have agreed: United and Continental will merge into a single airline.

To satisfy the political delegation from Ohio, the pre-merger combination announced that they will retain Continental's Cleveland hub for at least two years. But of course, there is always someone who will be upset with a combination like this, and there is a lawsuit pending in California that contends that the merger will illegally decrease competition. The Judge in that case has reportedly announced that he will provide an initial ruling by October 1 on the motion for a restraining order that would prevent the merger.

One of the significant concerns in a merger like this is antitrust compliance (which includes the competition issues). For example, to assuage government regulators, the airlines already agreed to transfer United's old slots at Newark Airport over to Southwest. The Justice Department approved the merger on the grounds that it would not adversely affect competition, so it is likely that the Federal Judge will NOT issue a restraining order that would prevent the merger (although the case can still move forward, and the plaintiffs can still be compensated with some form of relief if they are successful in their suit).

ASA members supporting either or both of these carriers will want to track the merger carefully to make sure that your contacts - and contracts - remain in place. ✈️

Latin American Airlines Plan to Merge

In another consolidation within the airline industry, Latin American air carriers LAN of Chile and TAM of Brazil have announced plans to merge. Both airlines are the market leader in their respective countries. While the two airlines have been working towards closer cooperation, the merger announced on August 13 was still a surprise. The two companies have signed a memorandum of understanding, but the completion of the merger will require regulatory and shareholder approval, which could take six to nine months. Upon completion of the merger, each airline will maintain their brand but will operate under a merged parent company called Latam Airline Group.

The merger will result in the largest airline in South America. In terms of passenger traffic, the combined airline will rank 15th in terms of revenue and 11th in number of passengers.

Combined, the airline will operate 115 destinations to 23 cities, with a fleet of 220 planes. LAN currently operates in Chile, Peru, Ecuador, and Argentina; while TAM operates in Brazil and also serves Paraguay through TAM Mercosur. The two airlines had combined 2009 revenues of \$8.5 billion.

The airlines expect the merger to

(Continued on Page 7)



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place the combined airline in a position to take advantage of the strong growth in demand for air travel in the emerging Latin American markets. The new airline is expecting annual synergies of \$400 million through alignment of passenger networks, growth in cargo operations, and cost savings. Growth is also expected to come from routes from Brazil to Europe and Peru to North America, new hubs to connect to Europe and the United States, and taking advantage of LAN's expertise in cargo coupled with TAM's footprint.

The consolidation endemic to the airline industry was clearly a motivating factor in the merger. "As the world industry consolidates we cannot stand still," said Enrique Cueto, the CEO of LAN who will also be CEO of the merged airline. "Now is our time to capitalize on this trend." 

Global Aviation Industry Continues Recovery in June

After enduring a difficult 2009, the international aviation industry showed strong growth this past summer. This growth came on the heels of unanticipated growth in the late spring, after April had shown weak numbers due to the European airspace interference of the volcanic ash. This strong growth in demand for air traffic is a good omen for those of us who rely on the health of the air carrier industry for our livelihood.

The International Air Traffic Association's (IATA) summer traffic statistics showed improvements in both passenger and freight demand for the entire summer.

PERCENT TRAFFIC CHANGE IN 2010 RELATIVE TO THE SAME MONTH IN 2009

	Int'l Passenger Traffic (Revenue Pax Kilometers) Increase over 2009	Int'l Freight Traffic (Freight Ton Kilometers) Increase over 2009
June	11.9%	26.5%
July	9.2%	22.7%

Total demand in 2010 is now expected to grow by 11% (stronger than the previous forecast of 10.2%) while capacity will only expand by 7.0% (up from the previous forecast of 5.4%).

Passenger demand improved in all regions. Europe's growth in international passenger demand, at 7.8%, was the only region that did not post double digit growth rates in June as compared to the June 2009 data. Additionally, international passenger demand recovered from the financial crisis and returned to an upward growth trend, with passenger volumes now surpassing the pre-recession peak of the first quarter of 2008 by 1-2 percent.

Overall, international freight volume demonstrated even more impressive gains, increasing 26.5% in June and 22.7% in July. This volume surged above the pre-recession highs of early 2008. The increase in freight demand continues to be fueled by the fast growth of demand (relative to 2009 figures) in Asia-Pacific (29.8% growth in June, % growth in July), the Middle East (39.6% growth in June, 30.1% growth in July), Latin America (44.9% growth in June, 25.3% growth in July), and Africa (54.0% growth in June, 35.2% growth in July).

Freight demand in Europe rose (only) 15.3% in June and 12.1% in July (once again, relative to 2009 numbers for those months), but the current low value of the Euro is likely to fuel increases in freight volume in the region in the remaining months of 2010.

North American freight demand in June was 24.2% above June 2009 figures, and in July was 27.1% above July 2009 figures.

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These across-the-board increases in both passenger and freight demand are a welcome sign of recovery to the aviation industry. This growth represents a significantly faster and more robust recovery from the financial crisis for the aviation industry than was previously predicted by the IATA. More revenue passenger miles and more freight ton miles (or kilometers) means more utilization which in turn means more need for maintenance and spare parts. 

FAA Proposes Expanded Icing Certification Standards

The FAA has proposed new icing certification standards for transport category aircraft. A Notice of Proposed Rulemaking (NPRM) was issued by the FAA on June 29, 2010. The purpose of this NPRM is to ensure that an aircraft can safely operate in new icing conditions established by this proposed rule.

The NPRM sets forth new freezing rain and freezing drizzle icing conditions. These new icing conditions are explained by the proposed Appendix O to 14 CFR part 25. The NPRM expands the certification requirements for transport aircraft and components for these aircraft in freezing rain and freezing drizzle conditions - referred to in the NPRM as supercooled large drop icing conditions, ice crystal conditions, and mixed phase conditions. These freezing rain conditions are currently not considered when certifying an airplane's ice protection systems.

Under the proposed NPRM, aircraft and components would need to meet certain safety certification standards in order to be certified for flight in the freezing rain icing conditions. For an aircraft to be certified in the new icing conditions, the proposed NPRM would require evaluating the operation of the airplane in the icing conditions, developing a means to differentiate between different icing conditions, and developing procedures to maintain safe operations while exiting all icing conditions. The proposed regulations would not require an aircraft to be certified for operation in all of the expanded icing conditions. Instead, the aircraft could be certified to operate in some of the proposed icing conditions; or the aircraft could be certified to operate safely upon encountering icing conditions, detect the icing conditions, and operate safely while exiting such icing conditions.

Several components would need to be certified as able to operate within the expanded icing conditions, or if the plane is not certified to operate in that icing condition, to detect and operate safely while exiting such icing conditions. These components include the pilot compartment view, airspeed indication system, static pressure system, angle of attack systems, propellers, and engine induction systems. Applicants for certification can demonstrate compliance with the proposed rule through a combination of laboratory analyses and flight tests. Also, if an applicant has adequate data, a similarity analysis can be used in lieu of testing.

Suppliers of any of the mentioned components should carefully review this NPRM. The FAA is accepting comments on this proposed rule up until September 29. ASA requests that any party filing comments also submit a copy of those comments to ASA, so we can incorporate all of our members' concerns before submitting our own comments.

The NPRM is available at: <http://frwebgate2.access.gpo.gov/cgi-bin/PDFgate.cgi?WAISdocID=VBWG5J/4/2/0&WAISaction=retrieve>. The NPRM also contains instructions for submitting comments. 

Election Results!

ASA would like to congratulate the following people elected to the Board of Directors:

- **Richard Levin**, A.J. Levin Company, Inc.
- **Brent Webb**, Aircraft Inventory Management & Services, Ltd.
- **David Susser**, Seal Dynamics, LLC
- **Mitchell Weinberg**, International Aircraft Associates, Inc.

Expect Significant Hazmat Shipping Changes in 2011

The industry should expect to see significant changes in the instructions for shipping hazardous materials (dangerous goods).

The packing instructions are being renumbered and reordered. A preview of the way that the numbers are being resequenced has been published by ICAO and it is a total resequencing.

In addition, the way that limited quantities are identified will also be changed. Under the current rules, a limited quantity of acetone, for example, would be identified on the outside of the package as "limited quantity acetone." Under the new ICAO/IATA rules, it appears that such a package would be identified by a diamond-shaped marking with the UN number in the center, and the proper shipping name would no longer be required on the outside of the package.

The United States is harmonizing its regulations to be similar to the ICAO/IATA rules. Under a proposal published on August 24, the U.S. rules for identifying limited quantities of hazardous materials would be changed so that the package would be identified with a diamond-shaped marking with wide, black horizontal stripes on the top and bottom, and a "Y" in the middle (this is for transport by aircraft - transport by highway or rail would omit the "Y" on the marking).

Watch carefully - as soon as the final rules are published, ASA will be providing its members with new compliance guidance. 

UPDATE:

After we had completed this issue, Southwest announced that it would acquire Air Tran for 1.4 billion dollars.

Southwest will operate the 86 Air Tran 717s. This will become a departure from Southwest's normal operations which tend to exclusively favor 737s. This is not unprecedented - in 1985, when Southwest acquired Muse Air, they also acquired several DC 9 and MD 82/83 aircraft which Southwest operated under the name TranStar Airlines (those assets were ultimately sold to Frank Lorenzo's Texas Air).

It is too early to know what Southwest will do to with the 717s - in fact it is too early to know much of anything about the effect this purchase will have on the industry - but distributors holding 717 inventory should start introducing themselves to Southwest Airlines if they don't already have connections there.

One interesting note: it appears that Southwest will have to drop the Air Tran routes to DFW. This is because under their Wright Amendment settlement, they are limited to only 16 gates in "North Texas," which means they are effectively precluded from flying out of DFW (unless they give up gates at Love Field). The Wright Amendment restrictions on long-haul flights out of Dallas Love Field are scheduled to be lifted in 2014 (unless the law changes, again).



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