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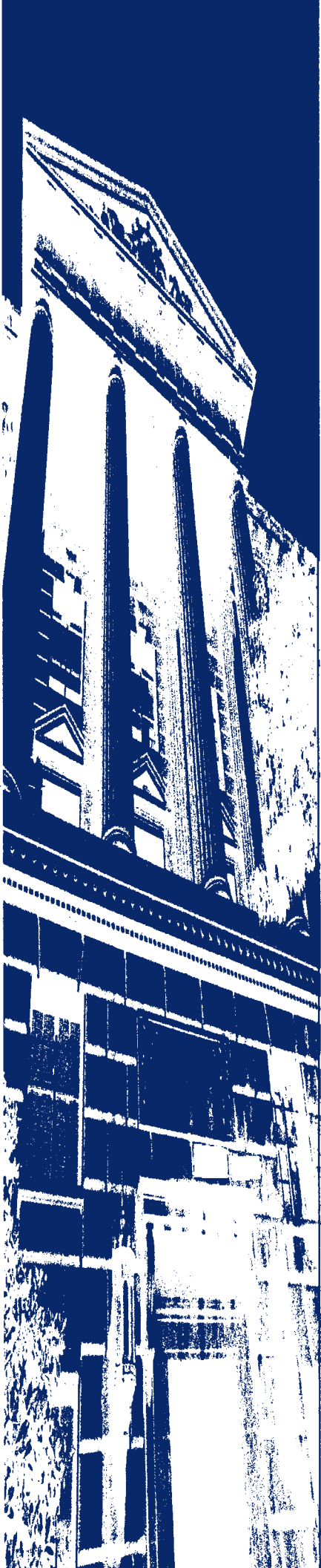
***BUREAU OF EXPORT ADMINISTRATION***

*Improvements Are Needed to Meet the Export  
Licensing Requirements of the 21<sup>st</sup> Century*

*Final Inspection Report No. IPE-11488/June 1999*

**PUBLIC  
RELEASE**

*Office of Inspections and Program Evaluations*





**UNITED STATES DEPARTMENT OF COMMERCE**  
**The Inspector General**  
Washington, D.C. 20230

June 18, 1999

**MEMORANDUM FOR:** William A. Reinsch  
Under Secretary for Export Administration

**FROM:**   
Johnnie E. Frazier  
Acting Inspector General

**SUBJECT:** Final Report: *Improvements Are Needed to Meet the Export Licensing Requirements of the 21<sup>st</sup> Century* (IPE-11488)

As a follow-up to our May 7, 1999, draft report, this is our final report on our program evaluation of BXA's export licensing efforts. The report includes comments from your June 3, 1999, written response. A copy of your response is included in its entirety as an attachment to the report.

While our report highlights some areas that are working well in BXA, it also highlights problems that hamper BXA's efforts to effectively and efficiently carry out its export licensing responsibilities. The report offers a number of specific recommendations that we believe, if implemented, will better prepare BXA for the export licensing requirements of the 21<sup>st</sup> century.

Please provide your action plan addressing the recommendations in our report within 60 calendar days. If you have any questions or comments about our report or the requested action plan, please contact me on (202) 482-4661.

We want to thank your entire staff for their assistance and courtesies extended to us during our review.

Attachment

cc: William M. Daley, Secretary of Commerce

**Final Report**

***Improvements Are Needed to Meet the  
Export Licensing Requirements of the 21<sup>st</sup> Century***

**June 1999**

**Report Number IPE-11488**

**U.S. Department of Commerce  
Office of Inspector General  
Office of Inspections and Program Evaluations**

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## **EXECUTIVE SUMMARY**

In August 1998, the Chairman of the Senate Committee on Governmental Affairs requested that the Inspectors General from the Departments of Commerce, Defense, Energy, State, the Treasury, and the Central Intelligence Agency conduct an interagency review of the export licensing process for dual-use commodities and munitions. The Committee Chairman specifically asked the six Inspectors General to update a 1993 special interagency Office of Inspector General review of the export licensing process and answer 14 questions.<sup>1</sup> (See Appendix A for questions and answers.) In addition to addressing the committee's questions, we expanded our review to perform a complete program evaluation of the Department's export licensing process, focusing on the effectiveness of the current policies, procedures, and practices in its licensing of dual-use goods and technologies.

Dual-use commodities are goods and technology determined to have both civilian and military uses. The Department of Commerce's Bureau of Export Administration (BXA) administers the U.S. government's export control licensing and enforcement system for dual-use commodities for national security, foreign policy, and nonproliferation reasons. It does so under the authority of several different laws, including the Export Administration Act of 1979, as amended. Although that statute expired in September 1990, Presidents Bush and Clinton have extended existing export regulations by executive order, invoking emergency authority contained in the International Emergency Economic Powers Act. These controls continue in effect today through Executive Order 12924, dated August 19, 1994, and Executive Order 12981, dated December 15, 1995.

Since early 1990, both the Congress and the Administration have tried to rewrite the basic law that authorizes the President to regulate exports from the United States. The principal focus of the continuing policy debate pertains to national security export controls that are used to restrict exports of dual-use technologies to successor states to the Soviet Union, Eastern Europe, and the People's Republic of China. There is a wide range of opinions on how the government's export control policies and practices should balance the need to protect national security and foreign policy interests with the desire not to unduly hamper U.S. trade opportunities and competitiveness. Striking this balance poses a significant challenge for the parties involved. Furthermore, some critics of the export licensing process argue that Commerce has an apparent conflict of interest in promoting and regulating exports. For instance, while China is viewed by the U.S. export control licensing agencies as a potential technology transfer risk, China is also seen as an important trading partner, and as such, Commerce has made great efforts to encourage and help U.S. companies entering the Chinese market.

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<sup>1</sup>*The Federal Government's Export Licensing Processes for Munitions and Dual-Use Commodities*, conducted by the Offices of Inspector General at the U.S. Departments of Commerce, Defense, Energy, and State, September 1993.

Our review found the licensing of U.S. dual-use exports to be a balanced multi-agency review process that attempts to bring divergent policy views and information to bear on decision-making for export licenses. That process includes not just Commerce, but also Defense, Energy, Justice (for encryption exports), State, the U.S. Arms Control and Disarmament Agency (ACDA),<sup>2</sup> and the Central Intelligence Agency's Nonproliferation Center. Under Executive Order 12981, Defense, Energy, State, and ACDA have the authority to review any export license application submitted to Commerce under the Export Administration Act and regulations. The executive order also established mandatory escalation procedures when agencies disagreed about dual-use export license applications and refined the timelines for this process.

We determined that the interagency referral and the escalation processes are working reasonably well. There are four levels of escalation for dual-use cases: the Operating Committee (OC) at the senior civil service level, the Advisory Committee on Export Policy (ACEP) at the assistant secretary-level, the Export Administration Review Board (EARB) at the Cabinet level, and the President. Each level of the escalation process is required to consider all matters referred to it, giving consideration to foreign policy, national security, and domestic economy concerns as well as concerns about the proliferation of weapons of mass destruction. With an orderly procedure to resolve interagency disputes, the export licensing process has been greatly improved since the 1993 special interagency OIG review.

Throughout our review of the export licensing process, we found BXA personnel to be extremely burdened by oversight reviews and multiple requests for information from congressional committees, the General Accounting Office, and outside organizations, including extensive Freedom of Information Act requests. In spite of these demands, BXA personnel have been able to successfully perform their normal duties of reviewing export license applications and issuing export licenses. While we noted significant areas of improvement, we also found the following problems that warrant management's attention.

**Current export control legislative authority, executive orders, and regulations need attention.**

The 1990s have brought dramatic changes in worldwide economic and political conditions, as well as in the environment for controlling the export of U.S. commodities and technology. However, as we examined the legislation, executive orders, and regulations used to control U.S. exports, we found several weaknesses that need to be addressed in order to strengthen the export licensing and enforcement process.

First and foremost, new legislative authority is needed to replace the expired Export Administration Act and accurately reflect current export control policies. In providing this authority, one issue to be addressed is whether the Congress should consider allowing BXA to review dual-use items that may fall under the U.S. Munitions List administered by the State

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<sup>2</sup>ACDA was a separate agency until April 1999, when it became a part of the Department of State.



Department, thereby increasing the transparency of the government wide licensing process. In addition, the requirement to conduct a post shipment verification for every high performance computer shipped to Tier 3 countries, as mandated by the 1998 National Defense Authorization Act, may not be the most effective use of government resources. We also determined that minor changes are needed to Executive Order 12981 with regard to the impact of the U.S. Arms Control and Disarmament Agency's merger with State, as well as clarification on agency representatives at the assistant secretary-level Advisory Committee on Export Policy. Finally, we believe that the export control policy and regulations regarding the release of technology to foreign nationals—commonly referred to as “deemed exports”—are ambiguous and need to be revised. (See page 23.)

**More transparency is needed in the commodity classification process.**

While BXA holds the exporter responsible for classifying an export item, it will advise an exporter whether an item is subject to the Export Administration Regulations and, if applicable, identify the appropriate Export Control Classification Number. Exporters may verbally inquire about a commodity classification (e.g., telephone call), but only written inquiries result in binding determinations. During our review, we found that BXA had instituted a front-end review mechanism to pre-screen commodity classifications before distributing them to the appropriate engineer for review.

This initial step serves as an important quality control measure, but we have identified two areas that still need improvement. First, Export Administration's processing of exporters' commodity classification requests is untimely, resulting in delays for exporters. Second, and more importantly, BXA needs to work with both Defense and State to ensure that the CCATS process is more transparent with regard to items or technologies specifically designed, developed, configured, adapted and modified for a military application, or derived from such items as called for in the NSC guidance. Therefore, we recommend that BXA, in conjunction with the Defense and State, work with the NSC to develop specific criteria and procedures for the referral of munitions-related commodity classifications to Defense and State. Otherwise BXA leaves this process vulnerable to incorrect classifications (e.g., the 1995 investigative report on the crash of a Chinese rocket carrying a satellite for which BXA mistakenly determined no license was required). (See page 39.)

**Licensing officers' analysis of export applications could be enhanced.**

One of BXA's core missions is to analyze and process export license applications. Proper case analysis is critical in ensuring that the appropriate export policy and procedures are followed for individual applications. However, during our review, we found it difficult to determine whether some applications were being thoroughly analyzed by licensing officers in the initial review period because there was little indication in the license history about how they reached their conclusions.

The lack of information in the licensing history does not necessarily indicate that licensing officers did not take into consideration the necessary elements, such as the reasonableness of the end use or background of the end user. However, without this critical information in the history, referral agencies cannot make the most informed decisions. We believe that better policies and procedures, as well as additional training, could enhance licensing officer analysis and documentation of applications. (See page 47.)

**Export license application review process has improved, but some weaknesses need to be addressed.**

In fiscal year 1998, BXA referred 85 percent of export license applications to other agencies for review, up from 53 percent in fiscal year 1995. While we believe the overall referral process is generally effective, we did identify some areas that need management attention including (1) licensing officers amending existing licenses without interagency review; (2) inadequate review time provided to the CIA's Nonproliferation Center for its end user checks; (3) BXA not providing its licensing officers with the latest CIA guidance outlining what license applications should not be referred to the Nonproliferation Center; and (4) BXA canceling pre-license checks without notifying the referral agencies when they have approved a license conditioned on a favorable end use check. In addition, we highlight two other areas of concern that require interagency attention.

First, while the intelligence community plays a critical role in license review and threat analysis, we found that the CIA and its Nonproliferation Center do not review all dual-use export applications or always conduct a comprehensive analysis of export license applications they do receive. In addition, the current dual-use licensing process does not take into account the cumulative effect of technology transfers. While individual technology sales may appear benign, combining technology sales over a long period of time may allow U.S. adversaries to build weapons of mass destruction or other capabilities that could threaten our national security. We believe this type of cumulative effect analysis, while difficult to make, would be valuable to have during the export license application decision-making process. BXA should work with the intelligence community, including the CIA, Defense, and Energy, to determine the feasibility of developing a mechanism to better track and assess the cumulative effect of dual-use exports to a specific country or region.

Second, as we have reported in the past, another key element missing from the export licensing process is the screening of all parties to pending license applications against the Treasury Enforcement Communication System (TECS) database maintained by the Treasury Department's U.S. Customs Service. TECS was created to provide multi-agency access to a common database of enforcement data to satisfy a recognized need to promote the sharing of sensitive information between federal law enforcement agencies. Screening every export license applicant and consignee against TECS during the initial phases of the licensing process would give licensing and enforcement authorities early warning of any potential concerns Customs may have. (See page 57.)

**Dispute resolution process gives referral agencies a meaningful opportunity to escalate licenses.**

The four-level dispute resolution process has been effective. From fiscal years 1991 to 1998, the number of cases escalated to the Operating Committee increased by 353 percent, while the number of cases escalated to the Advisory Committee on Export Policy decreased by 62 percent. In addition, only 21 license applications have been escalated to the Export Administration Review Board during this time period; however, only one has been escalated since 1991. The fact that there has been a significant increase in the cases escalated to the Operating Committee, and a decrease in cases escalated to the ACEP and EARB, indicates that this process is working well.

We found that the Chair of the Operating Committee affords each agency—including BXA—the opportunity to present its recommendation on every application the OC reviews. While the OC Chair has been given the authority to decide all cases at this level without having to reflect the recommendations of the majority of the participating agencies, the decisions of the Chair are usually based on interagency consensus. However, we did identify several areas that need management attention: (1) the OC Chair's role needs to be clarified, (2) agency delegations of authority cause delays at the OC, (3) the process of returning escalated cases to the licensing officers requires additional quality control. (See page 77.)

**BXA has sought interagency guidance during review of exporter appeals, but a more formal process is needed.**

Once an export license application has been formally denied, the exporter has the right to appeal to the Under Secretary, whose decision is considered final. Although BXA informally confers with the referral agencies on appeals, there is no requirement that this decision be made in consultation with the other referral agencies involved in the export licensing process.

However, this part of the exporter appeals process raises a legitimate question as to whether an exporter could use the process to circumvent the interagency referral process (i.e., a case denied during the interagency license review could be approved during an appeal, with no formal interagency review). While we found no evidence to suggest that this has happened, we believe that for the sake of transparency in the export licensing process, the referral agencies should be formally included in the appeals process. (See page 87.)

**BXA needs to improve its monitoring of license conditions with reporting requirements.**

The ability to place conditions on a license is an important part of the license resolution process, as well as an additional means to monitor certain shipments. While 28 standard conditions can be placed on an export license, there are only 7 that actually require the exporter to provide documentation to BXA for shipments made against the license. Export Administration is

responsible for monitoring six of these conditions, and Export Enforcement the remaining one. However, BXA is still not adequately monitoring license conditions as first reported in the 1993 special interagency OIG review.

Specifically, both Export Administration's and Export Enforcement's follow-up subsystems were out of date because they had not followed up on expired licenses. In addition, most licensing officers (except for those responsible for deemed exports and encryption) are not involved in monitoring conditions they place on the licenses. Licensing officers also did not have access to exporters' compliance history in order to make the most informed decision about an export license application. By not having an adequate monitoring system in place, BXA cannot assure itself that the goods were not diverted to an unauthorized end user, and exporters may receive new licenses even though they did not comply with previous licenses. (See page 93.)

**End use checks are a valuable tool, but some improvements are needed.**

End use checks, an important part of the license evaluation process, are used to verify the legitimacy of export transactions controlled by BXA. A pre-license check is used to validate information on export license applications by determining if an overseas person or firm is a suitable party to a transaction involving controlled U.S.-origin goods or technical data. Post shipment verifications strengthen assurances that exporters, shippers, consignees, and end users comply with the terms of export licenses and licensing conditions, by determining whether goods exported from the U.S. were actually received by the party named on the license and are being used in accordance with the license provisions. These checks, which help prevent and detect illegal technology transfer, are generally conducted by Commerce's U.S. and Foreign Commercial Service (US&FCS) officers stationed at overseas diplomatic posts and BXA's export enforcement agents through its Safeguard Verification program.

This review found some of the concerns identified in previous OIG reports with respect to end use checks conducted by US&FCS. Among these concerns are (1) untimely end use checks, (2) US&FCS's use of foreign service nationals and personal service contractors to conduct some checks, (3) failure to perform on-site checks, and (4) insufficient US&FCS coordination with other parts of the embassy and host governments in conducting checks.

In addition, while Export Enforcement's Safeguard Verification program enhances the end use checks because of the "enforcement" element it brings to the process, we have a number of suggestions that could make this program more effective: (1) better initial trip planning, (2) better in-country consultations, (3) clearer guidance or a standard format for trip reports, and (4) faster and wider dissemination of Safeguard check results, especially negative findings. We also believe that BXA should use the Safeguard visits as an opportunity to better train US&FCS staff on conducting end use checks. Our report also highlights specific conditions regarding end use checks in China, Hong Kong, and Israel. (See page 103.)

**Other OIG concerns are related to the export licensing process.**

Our review identified two areas in the export licensing process that have raised enforcement concerns. The first issue is BXA's practice of returning some export license applications without action after an unfavorable pre-license check was received. A second issue is Export Administrations's untimely processing of license determination requests from BXA's export enforcement agents and the Customs Service. (See page 125.)

**BXA needs a new automated export licensing system.**

The Export Control Automated Support System, developed by BXA in 1984, is a large database system that provides license processing and historical license information to BXA and the referral agencies. We determined that the system's internal controls are generally adequate and that its data are sufficiently reliable. However, we have identified some controls that need strengthening or further implementation. In addition, although the export licensing referral process has been working reasonably well and become increasingly transparent over the past five years, the agency automation systems are lagging way behind. We strongly agree with BXA that it needs a new system to process export license applications efficiently and effectively. While we encourage BXA and the Congress to move ahead with the development and funding of a new system as soon as possible, we believe that BXA should concurrently ensure that it considers the best available options, including a classified system. We also urge BXA to coordinate its system development efforts with the other export licensing agencies to ensure that all of the systems are compatible and, at a minimum, are able to interact with each other. (See page 133.)

On page 157, we offer detailed recommendations to address our concerns.



In BXA's June 3, 1999, written response to our draft report, the Under Secretary for Export Administration generally agreed with most of our recommendations. The Under Secretary reported that for some recommendations, the benefits of changing BXA's current practice are not readily apparent or the changes may be difficult to implement, such as those relating to "deemed exports," or providing for TECS screening of pending license applications. We disagree.

With regard to the "deemed export" rule, our review determined that not only are the regulations for deemed exports ill-defined, but the export control policy concerning deemed exports itself appears to be ambiguous. The lack of understanding regarding deemed exports could damage national security if sensitive technology is released to inappropriate end users. We strongly urge BXA to move expeditiously to clarify this requirement with the National Security Council and provide clearer guidance to U.S. research laboratories and industry.

In addition, since we first identified the weakness related to BXA's failure to screen its licensing data against TECS, we have not seen any real improvement in this process. As a result, we have again recommended that BXA update the 1993 MOU between BXA and Customs to provide for TECS screening of pending license applications. Screening every applicant and consignee against TECS during the initial phases of the licensing process would give licensing and enforcement authorities early warning of any potential concerns Customs may have. We believe that as the agency with the ultimate responsibility for issuing U.S. dual-use export license applications, BXA has an obligation to take every precautionary measure to ensure that all potential export enforcement concerns within the U.S. government are considered before issuing a license. By not doing so, BXA is making licensing decisions based on incomplete information. We do not understand why BXA has not implemented this three-year-old recommendation since the problem is not fixed.

The Under Secretary also stated that a critical shortcoming in our report is that virtually none of our recommendations, whether BXA agrees with them or not, includes any assessment of the budgetary impact. We are not convinced that the majority of our recommendations would require substantial budget increases, with the exception of the development of its new automated licensing system. We also contend that all of our recommendations will improve the efficiency and effectiveness of the export licensing process.

Finally, while the Under Secretary indicated a concern that our answers to Senator Thompson's questions do not precisely track the body of the report, we disagree. Obviously, as BXA points out, the report is a more detailed document than the answers to the specific questions. For each question, we refer the reader back to the applicable section of the report for more details.

Where necessary, we have made changes to the report and recommendations. BXA's complete response has been included as Appendix D to this report.

## INTRODUCTION

In August 1998, the Chairman of the Senate Committee on Governmental Affairs requested that the Inspectors General from the Departments of Commerce, Defense, Energy, State, and the Treasury and the Central Intelligence Agency conduct an interagency review of the export licensing process for dual-use commodities and munitions. The committee chairman specifically asked the six Inspector General offices to update a 1993 interdepartmental OIG review of the export licensing process<sup>3</sup> and answer 14 questions. (See Appendix A for a complete listing of the 14 questions and answers.) In addition to addressing the committee's questions, we expanded our review to perform a complete program evaluation of the dual-use export licensing process which is administered by the Department's Bureau of Export Administration.

Program evaluations are special reviews the OIG undertakes to give agency managers timely information about operations, including current and foreseeable problems. By highlighting problems, the OIG hopes to help managers move quickly to address them and to avoid similar problems in the future. The evaluations are also conducted to detect and prevent fraud, waste, and abuse and to encourage effective, efficient, and economical operations. Program evaluations may also highlight effective programs or operations, particularly if they may be useful or adaptable for agency managers or program operations elsewhere.

We conducted our evaluation from October 1, 1998, through April 15, 1999. This evaluation was conducted pursuant to the authority of the Inspector General Act of 1978, as amended, and in accordance with the *Quality Standards for Inspections* issued by the President's Council on Integrity and Efficiency. During our review, we found that BXA personnel felt extremely burdened by oversight reviews and multiple requests for information from congressional committees, the General Accounting Office, and outside organizations, including extensive Freedom of Information Act requests. According to BXA, in fiscal year 1998, it had 141 Freedom of Information Act requests including several time-consuming ones from Judicial Watch; 77 congressional requests; 8 General Accounting Office requests; and 4 Inspector General requests. BXA provided the House Select Committee on U.S. National Security and Military/Commercial Concerns with the People's Republic of China (commonly known as the Cox Commission) with information for over nine months. In spite of these demands, BXA personnel have performed their normal duties of reviewing export license applications and issuing export licenses. However, during our review, we found that some BXA personnel felt under siege and were somewhat defensive in responding to our requests for information. Nonetheless, we also found that most of BXA's managers, licensing officers, and systems personnel were cooperative. At the conclusion of the program evaluation, we discussed our observations and recommendations with BXA's Under Secretary and other bureau officials.

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<sup>3</sup>The Federal Government's Export Licensing Processes for Munitions and Dual-Use Commodities, conducted by the OIGs at the Departments of Commerce, Defense, Energy, and State, September 1993.





## **PURPOSE AND SCOPE**

The purpose of our program evaluation was to assess the interagency export licensing process for dual-use commodities and determine whether current practices and procedures are consistent with established national security and foreign policy objectives. The scope of our program evaluation included assessing the adequacy of (1) compliance with the current legislative authorities and federal regulations regarding dual-use commodities, (2) the interagency export licensing process for dual-use commodities, including the escalation and appeals processes, (3) exporter compliance with export license conditions, (4) monitoring the stated end use and end users of licensed commodities, and (5) the licensing information management system, including security of data transmitted between the various agencies.

To coordinate the review of interagency licensing issues and determine the work performed by each OIG team, the six OIGs formed an interagency working group and held monthly meetings. Representatives of the six OIG review teams also met several times with the Staff of Senator Fred Thompson, Chairman of the Senate Committee which requested the review. We discussed the scope and procedures of the review with the committee staff, but not our findings prior to issuance of the reports. A decision was made by the six OIGs that each OIG would issue a report on the findings of its agency review, and there would also be a consolidated report on crosscutting issues that all six OIGs would contribute to and approve.

### BXA's export control legislation

We examined current and prior legislation, executive orders, and related regulations, including the Export Administration Act of 1979, the Export Administration Regulations, the International Emergency Economic Powers Act, and Executive Orders 12924, 12981, and 13026 to assess the roles and responsibilities of the governmental agencies and departments involved in dual-use export licensing. We also examined (1) BXA annual reports for fiscal years 1993-97, (2) Presidential Budget Submissions for Fiscal Years 1993-99 and the Office of Management and Budget's Fiscal Year 2000 budget submission for BXA, and (3) BXA's strategic plan for fiscal years 1999-2004 to determine how BXA is carrying out its responsibilities.

### Export licensing process for dual-use commodities

We interviewed more than 50 BXA officials, including most of the bureau's senior managers and two of its attorneys; regulatory officials, licensing officials, and analysts in Export Administration; and enforcement agents and analysts in Export Enforcement to assess BXA's export licensing process. We also interviewed officials at the Departments of Defense, Energy, Justice, State, and the Treasury; the U.S. Arms Control and Disarmament Agency; the General Accounting Office; the National Security Agency; the Nonproliferation Center of the Central Intelligence Agency; and the U.S. Postal Service.

To further assess the strengths and weaknesses of the export licensing process, we sent out a questionnaire to survey all Export Administration licensing officers (LOs) and their supervisors, and reviewed LO operating manuals, personnel position descriptions, performance plans, training plans, and vacancy announcements. We examined prior reports on dual-use and munitions export licensing processes prepared by our office and the General Accounting Office. In addition, we reviewed reports prepared by BXA's task force that examined commodity classifications, export licensing, license determinations, and the Operating Committee (OC).

In addition to our interviews, survey and document review, we examined BXA's licensing process, including (1) commodity classification, (2) non-referred licensing, (3) referral process, (4) escalation process, (5) appeals, and (6) license determinations. To understand the above six components of the licensing process, we sampled and reviewed licenses for some components, or because of a small number, reviewed all license applications for other components.

- The Departments of Defense and State both indicated to the other OIG team members a need for more transparency in the commodity classification process. To address their concerns and evaluate whether BXA is generally making the correct classification, we reviewed a sample of 103 commodity classification line items out of 6,161 done during fiscal year 1998.
- To determine whether the licensing and referral process is generally operating as mandated by current export control legislation, orders and regulations, we reviewed a sample of 60 non-referred export licenses and 179 referred licenses during the period January - June 1998. The objective of our sample design was to address Senator Thompson's Question 7 regarding license application referrals. The tested conditions were whether (1) applications referred out of Commerce for review by other U.S. agencies should not have been and (2) those not referred should have been. Our review used a stratified sample structure to accommodate the fact that each application may be referred to two or more federal organizations outside of Commerce. We conducted our review based on the referred/non-referred distinction. Within each stratum (referred and non-referred), we used a simple random sample.
- To determine whether the escalation process is generally operating as mandated by Executive Order 12981, we reviewed 26 license applications out of 266 that were escalated to the OC and all 8 escalated to the Advisory Committee on Export Policy (ACEP) during the same time period as our license sample. We also attended three OC meetings and two ACEP meetings. Because the Export Administration Review Board (EARB) did not convene during our evaluation, we did not attend any of its meetings.
- If an exporter disagrees with the final licensing decision, they can appeal the decision; we reviewed 23 appeals by exporters that were resolved during the period October 1997 - December 1998.

- To address the concerns of Export Enforcement staff regarding the long time it takes Export Administration to complete a license determination, we examined the records for 212 license determinations referred to Export Administration by Export Enforcement.

#### Exporter compliance with conditions placed on licenses

The 1993 special interagency OIG review of BXA's export licensing process pointed out a lack of exporter compliance with conditions on export licenses. To determine whether BXA corrected this problem, we interviewed Export Administration and Export Enforcement personnel responsible for monitoring exporter compliance. We also analyzed samples of 39 licenses in Export Administration's Compliance Follow-Up Subsystem, 20 licenses in Export Enforcement's Compliance Follow-Up Subsystem, and 42 licenses from the sample of referred licenses.

#### End use check guidelines, procedures, and practices

We examined Commerce's monitoring of licensed items and end users by reviewing 12 Safeguard trip reports<sup>4</sup> and prior OIG reports, sampling 124<sup>5</sup> out of 331 completed/canceled pre-license checks as listed on an October 1998 ECASS printout, and sampling 18 out of 109 completed post shipment verifications as listed on an October 1998 ECASS printout. Commerce's United States and Foreign Commercial Service (US&FCS) overseas personnel and Export Enforcement agents conduct end use checks. To understand how both groups perform end use checks, we surveyed commercial officers at 27 US&FCS posts, observed end use checks performed by US&FCS personnel in Israel, and observed end use checks performed by Export Enforcement personnel in Malaysia. We also discussed the performance of end use checks by other US&FCS officers during our conduct of recent OIG inspections of US&FCS posts in China and Hong Kong.

#### BXA's Export Control Automated Support System

We reviewed the operation of the Export Control Automated Support System (ECASS), BXA's automated licensing information management system, by reviewing the system's operations and procedures manuals. To assess data integrity and system integrity, we reviewed the ECASS database management controls related to data management, database management, database integrity, database operations, and database security. We also interviewed BXA information technology personnel and BXA system contractor personnel about implementing a new system

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<sup>4</sup>BXA's Office of Export Enforcement agents prepare Safeguard reports after each overseas trip they conduct to monitor or check on the end use and end users listed on dual-use export licenses.

<sup>5</sup>Originally, we selected 166 PLCs to review, but only 124 were initially found in BXA's files. Except for our discussion in Section IX, our sample analyses are based on these 124 PLCs. BXA later found and submitted supporting documents for all but one of the 166 sample PLCs requested.

and performing actions to make ECASS Year 2000 compliant. We did not review BXA's specific Year 2000 actions to date; we only determined what Year 2000 actions have occurred.

We also interviewed numerous BXA managers and licensing officers to obtain their comments, issues, and concerns about ECASS. We interviewed computer personnel at the referral agencies who are responsible for receiving information from and transmitting information to BXA on dual-use export licenses. We also interviewed the Department's Chief Information Officer to discuss BXA's system development efforts.

## **BACKGROUND**

The United States controls the export of dual-use commodities for national security, foreign policy, and nonproliferation reasons under the authority of several different laws. Dual-use commodities are goods and technology determined to have both civilian and military uses. The primary legislative authority for controlling the export of dual-use commodities is the Export Administration Act of 1979, as amended. Under the act, the Department of Commerce's Bureau of Export Administration (BXA) administers the Export Administration Regulations (EAR) and the U.S. Government's export control licensing and enforcement system for dual-use commodities.

The Export Administration Act has been expired since September 1990, except for a brief time in 1994 when it was reinstated. However, during periods in the past when one version of the act has expired and a new version has not been enacted, the authority for imposing export controls is derived from the International Emergency Economic Powers Act (IEEPA). Most recently, IEEPA has enabled BXA to control exports for the period from August 1994 to the present while the Congress continues to debate enactment of a new export control act. (See Section I for a further discussion of the impact of the Export Administration Act's expiration.)

BXA is a regulatory agency that enhances the nation's security and its economic prosperity by controlling exports for national security, foreign policy, and short supply reasons. BXA administers the Export Administration Act by developing export control policies, issuing export licenses, and enforcing the laws and regulations for dual-use exports.

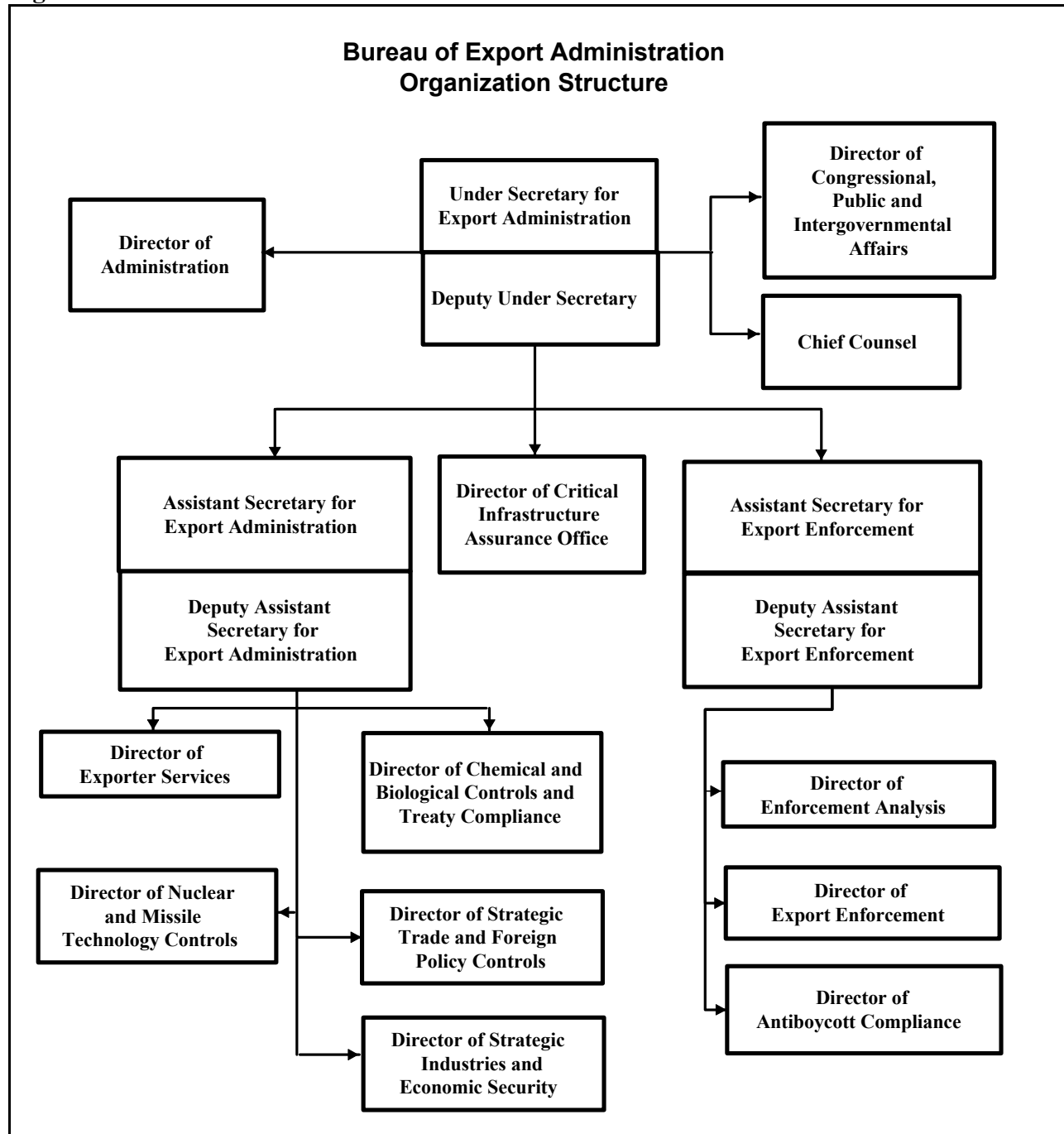
BXA was established in 1987 in response to a congressional mandate to ensure adequate separation of the Department of Commerce's export control and export promotion roles and responsibilities. Before that time, the Department's export control functions were performed by the International Trade Administration, which continues to be responsible for the Department's trade promotion activities. Despite the separation, there is still much debate about whether the Commerce Department and BXA maintain the appropriate balance between promoting U.S. trade and exports and controlling the export of goods and technology that could be detrimental to our national security interests.

### **I. BXA's Organizational Structure**

BXA's two principal operating units, Export Administration and Export Enforcement, as well as its Office of Administration, have undergone significant reorganization in recent years in an effort to reform and streamline the export control system. Before October 1994, the export control function within BXA was separated into three elements: policy, licensing, and enforcement. In October 1994, BXA's new leadership combined policy and licensing into units with specific areas of concern: (1) nuclear and missile technology, (2) chemical and biological weapons, and (3) strategic trade and foreign policy. BXA's new structure was designed to

provide better coordination between BXA export policy and licensing decisions. Enforcement is still a separate functional element. (See Figure 1.)

Figure 1



Source: 1999 Organization Chart, Bureau of Export Administration.

## **Export Administration**

Export Administration is composed of five offices: (1) Exporter Services, (2) Nuclear and Missile Technology Controls, (3) Chemical and Biological Controls and Treaty Compliance, (4) Strategic Trade and Foreign Policy Controls, and (5) Strategic Industries and Economic Security.

### ***Office of Exporter Services***

The Office of Exporter Services is responsible for Export Administration's outreach and counseling efforts to help ensure exporters' compliance with Export Administration Regulations, and coordination of policy within Export Administration. To educate exporters about the requirements of U.S. export control laws and regulations, Exporter Services personnel develop brochures and other written guidance and distribute them in workshops, exporter seminars, and on BXA's website. This office also provides exporter counseling. The Office of Exporter Services codifies regulatory policy, revises the existing regulations, drafts new regulations, and coordinates with other federal agencies on the clearance of all changes to Export Administration Regulations. In addition, Exporter Services is responsible for the receipt, screening, and data inputs of all export license information into ECASS, BXA's automated licensing information system, and the issuance of all export licenses once approval has been obtained. This office is also responsible for following up to determine exporters' compliance with license conditions.

### ***Office of Nuclear and Missile Technology Controls***

The Office of Nuclear and Missile Technology Controls has a full range of responsibilities associated with the licensing of exports controlled for nuclear or missile technology reasons and proposed exports subject to the Enhanced Proliferation Control Initiative.<sup>6</sup> The office has two divisions: (1) the Nuclear Technology Controls Division and (2) the Missile Technology Controls Division.

The Nuclear Technology Controls Division is responsible for licensing items that is responsible for licensing items that fall under the Nuclear Referral List and the Nuclear Suppliers Group (NSG). The Nuclear Referral List are items subject to the EAR that could be of significance for nuclear explosive purposes if used for activities other than those authorized at the time of export or reexport. The NSG—established in 1992 and composed of 34 member countries—sets controls on nuclear material, equipment, and technology unique to the nuclear industry, and dual-use items that have both nuclear and non-nuclear commercial and military applications. The Nuclear Suppliers Group published guidelines and an annex setting forth how members should proceed in imposing restrictions on affected exports and listing the items that each member nation should

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<sup>6</sup>This initiative's provisions require that all exporters obtain a license if they have knowledge or are informed by BXA that a proposed export could be used in nuclear, chemical, or biological weapons or missile activities.

make subject to export controls. The guidelines establish the underlying precepts of the regime, provide a degree of order and predictability among suppliers, and help ensure harmonized standards and interpretations of NSG controls. The Nuclear Technology Controls Division reviewed more than 1,300 licenses in calendar year 1998.

The Missile Technology Controls Division is responsible for all licensing of items that relate to the Missile Technology Control Regime. The Missile Technology Control Regime was formed in 1987 by the United States and 6 other countries (now totaling 29 members) to limit the proliferation of missiles capable of delivering weapons of mass destruction. Although the current members are not bound by a treaty, they have agreed on guidelines to coordinate their national export controls to prevent missile proliferation. The guidelines provide licensing policy, procedures, review factors, and standard assurances for missile technology exports and form the basis for U.S. missile technology controls. Licensing authority for most of these items lies with the Department of State. A considerable portion of the license applications reviewed for missile-related concerns by BXA are for commercial aviation exports, including avionics, navigation, telemetry, composite materials, and test equipment. The Missile Technology Controls Division reviewed approximately 840 licenses in 1998.

### ***Office of Chemical and Biological Controls and Treaty Compliance***

The Office of Chemical and Biological Controls and Treaty Compliance, consisting of the Chemical and Biological Controls Division and the Treaty Compliance Division, reviewed approximately 2,100 licenses in calendar year 1998. The Chemical and Biological Controls Division administers export controls and develops policy relating to the Australia Group. The Australia Group is a forum of 30 industrialized countries that cooperate in curbing the proliferation of chemical and biological weapons through the coordination of export controls, the exchange of information, and other diplomatic actions. Australia Group members have agreed to adopt controls on dual-use chemicals and equipment and biological microorganisms and related equipment. The Treaty Compliance Division is responsible for outreach efforts to develop industry awareness about the impact of the Chemical Weapons Convention, which became effective on April 28, 1997, including providing information about industry's rights and obligations, and completing on-site inspection protocols.

The Office of Chemical and Biological Controls and Treaty Compliance also oversees the Foreign Nationals Program and the Short Supply Program. The Foreign Nationals Program administers export controls and develops policy relating to "deemed exports." According to the Export Administration Regulations, any release to a foreign national of controlled technology or software that is subject to the regulations is "deemed to be an export" to the home country of the foreign national. In such instances, the U.S. host(s) would generally be required to obtain an export license before providing the foreign national access to such technology or software.<sup>7</sup> The

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<sup>7</sup>Per 15 CFR 734.2(b)(2)(ii), this deemed export rule does not apply to persons lawfully admitted for permanent residence in the United States and does not apply to persons who are protected individuals under the Immigration and Naturalization Act (8 U.S.C. 1324b(a)(3)).



Short Supply Program administers the short supply export controls as mandated by the Export Administration Act, such as western red cedar and crude oil.

### ***Office of Strategic Trade and Foreign Policy Controls***

The Office of Strategic Trade and Foreign Policy Controls comprises three divisions that reviewed over 6,000 licenses in 1998. The Strategic Trade Division is responsible for implementing the multilateral export controls under the Wassenaar Arrangement, the successor regime to the Coordinating Committee on Multilateral Export Controls, which deals with conventional arms and related dual-use items. The Wassenaar Arrangement, consisting of 33 member states, including Russia, attempts to respond to the new security threats of the post-Cold War era. It does this by seeking to control exports of armaments and sensitive dual-use items, such as computers, machine tools, and satellites.

The Foreign Policy Controls Division implements and oversees U.S. export controls imposed for foreign policy reasons, including controls for crime control, antiterrorism, and regional stability. As such, this division is also responsible for administering controls on exports to terrorist states such as Iran, Iraq, Libya, and North Korea. The Encryption Policy Division develops encryption control policy, licenses commercial encryption products, and regulates key recovery agents.

### ***Office of Strategic Industries and Economic Security***

The Office of Strategic Industries and Economic Security oversees issues relating to the health and competitiveness of the U.S. defense industrial base by assisting U.S. companies to diversify from defense-related products and industries to commercial production and markets, promoting the sale of U.S. weapons systems to U.S. allies, analyzing the impact of export controls on key industrial sectors, and conducting primary research and analysis on critical technologies related to defense-related sectors. This division does not review export licenses.

## **Export Enforcement**

Export Enforcement is composed of three offices: (1) Export Enforcement, (2) Enforcement Analysis, and (3) Antiboycott Compliance.

### ***Office of Export Enforcement***

The Office of Export Enforcement (OEE) investigates alleged export control violations of the Export Administration Act, apprehends violators, and coordinates with other federal agencies, including the Department of Justice and its Federal Bureau of Investigation, the Department of the Treasury and its Customs Service, and the Department of State. The Office of Export Enforcement has a headquarters office in Washington, D.C. and eight field offices staffed with

federal criminal investigators empowered to make arrests, carry firearms, execute search warrants, and seize goods about to be exported illegally. OEE agents also go overseas to conduct end use or Safeguard checks to monitor the end use and end users listed on dual-use export licenses.

### ***Office of Enforcement Analysis***

The Office of Enforcement Analysis is the central point for the collection, research, and analysis of classified and unclassified information on end users who are of export control concern. Office of Enforcement Analysis specialists review license applications and shipper's export declarations and develop preventive enforcement programs. This office also analyzes intelligence information and determines when pre-license check and post shipment verification checks should be requested. OEA also assists OEE special agents with research and analysis on investigative matters.

### ***Office of Antiboycott Compliance***

The Office of Antiboycott Compliance monitors compliance with the 1977 provisions of the Export Administration Act by seeking to counteract the participation of U.S. citizens in other nations' economic boycotts or embargoes that the United States does not sanction. To enforce the antiboycott provisions, the Office of Antiboycott Compliance investigates violations, such as companies refusing to deal with blacklisted businesses and religious discrimination. This office pursues the pertinent administrative or criminal sanctions against violators of the antiboycott provisions, including civil penalties, the imposition of export denial for specific periods, and referral to the Department of Justice for criminal prosecution.

### **Office of Administration**

The Office of Administration is responsible for BXA's overall administrative management. The office manages administrative functions in support of headquarters, domestic, and overseas operations; maintains liaison for administrative services provided by the Department's Chief Financial Officer and Assistant Secretary for Administration; prepares budget submissions; coordinates the administrative aspects of BXA programs involving other departments and agencies; provides supervision and guidance for BXA's security program; supports the Under Secretary and Deputy Under Secretary in developing BXA programs related to Department and government wide initiatives such as diversity, quality management, and foreign technical assistance and reinvention; and manages ECASS.

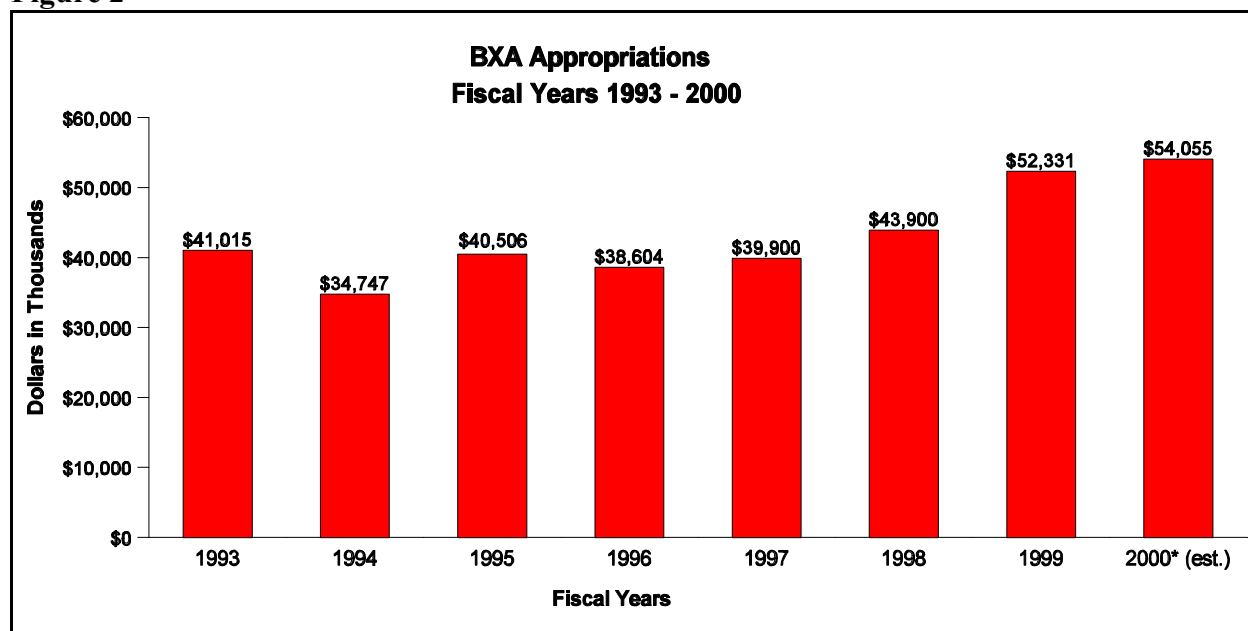
### ***BXA Appropriations***

If BXA's estimated funding for FY 2000 is realized, funding from FY 1993 through FY 2000 will have increased almost 32 percent, from \$41.0 million to \$54 million. In FY 1993 BXA's appropriation was \$41 million. From FY 1994 to FY 1998, BXA's appropriations fluctuated

from a low of \$34.7 million in FY 1994 to a high of \$43.9 million in FY 1998. BXA's budget also increased to \$52.3 million in its FY 1999 budget and to \$54 million in its FY 2000 budget request. (See Figure 2.) BXA's funding growth for FY 1998 through 2000 is primarily for new programs in Export Administration and Export Enforcement.<sup>8</sup>

Export Administration's budget for FY 1998 was \$20.3 million, and its FY 1999 budget increase of \$1.4 million is mainly to support its responsibilities under the Chemical Weapons Convention. Export Administration's FY 2000 increase, if enacted, will provide over \$1.3 million in additional funding for the Chemical Weapons Convention.

Figure 2



Source: President's Budget Submission to the Congress, FY 1995 - 2000.

Export Enforcement's budget has also grown from \$20.6 million in FY 1998 to \$21.6 million in FY 1999. Part of this increase was to cover (1) new enforcement responsibilities related to

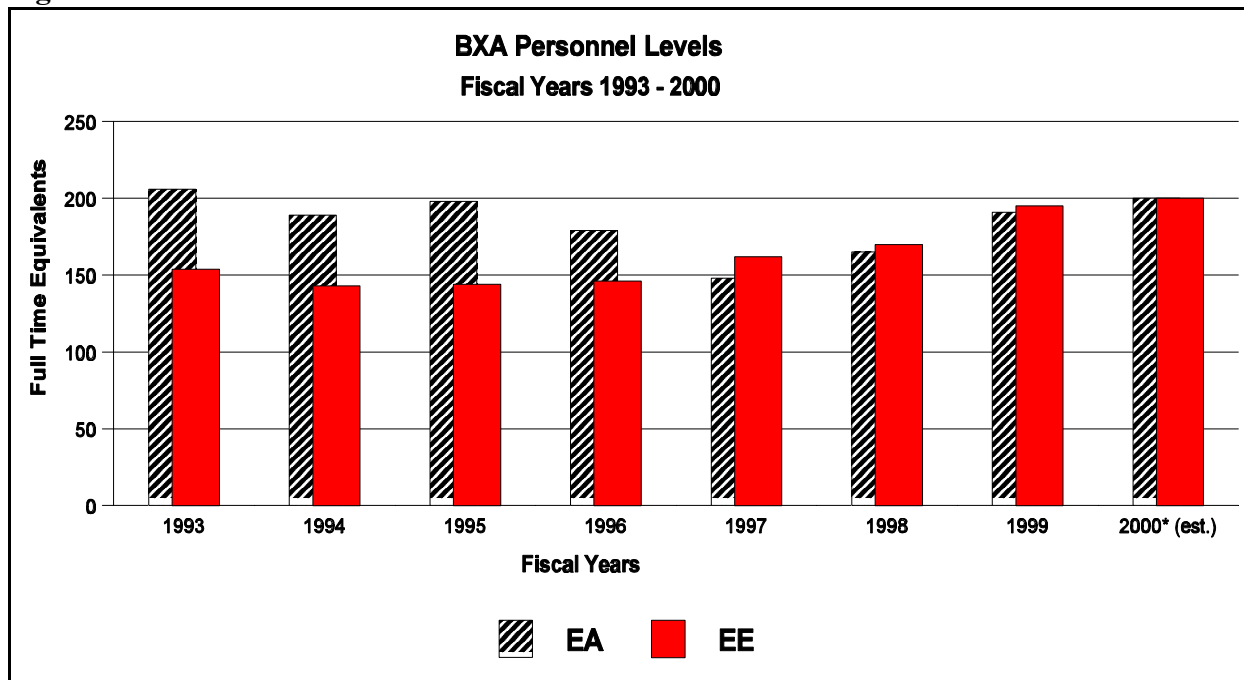
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<sup>8</sup> Not included in the FY 2000 budget estimate above is \$6.4 million for the establishment of a new office in BXA to implement the Critical Infrastructure Program. Presidential Decision Directive 63 calls for a national effort to assure the security of the increasingly vulnerable and interconnected infrastructures of the United States. Such infrastructures include telecommunications, banking and finance, energy, transportation, and essential government services. PDD 63 instructs the Department of Commerce to establish the Critical Infrastructure Assurance Office to support the National Coordinator's work with government agencies and the private sector and to develop a national plan. Within Commerce, the CIAO is located in BXA whose Director reports to the Under Secretary as well as the Secretary of Commerce and the National Coordinator at the National Security Council.

encryption controls and the Fastener Quality Act,<sup>9</sup> (2) staffing field offices including overseas enforcement support, to meet increased responsibilities (e.g., counter-terrorism); and (3) monitoring shipments to Hong Kong to identify possible diversions of strategically controlled goods to China. Export Enforcement's FY 2000 increase, if enacted, will provide additional funding of \$1 million for the post shipment verifications of high performance computers as mandated by the National Defense Authorization Act.<sup>10</sup>

Figure 3 illustrates the personnel levels of Export Administration and Export Enforcement from FY 1993 through 2000. In FY 1993, Export Administration supported 206 full time equivalents (FTEs). The personnel levels fluctuated slightly during FY 1994 through FY 1996 and then dropped to 148 FTEs in FY 1997. Personnel levels for Export Administration have grown in FY 1998 and 1999 and are projected to reach 200 FTEs in FY 2000, approximately the same number of FTEs that Export Administration had in FY 1995. Most of the growth in Export Administration personnel levels is due to its responsibility for implementing the Chemical Weapons Convention (38 FTEs).

**Figure 3**



Source: President's Budget Submission, FY 1995 - 2000.

<sup>9</sup> The Fastener Quality Act of 1990, as amended, requires that certain threaded fasteners meet specified technical standards and that they be tested by an accredited laboratory.

<sup>10</sup> Under the National Defense Authorization Act for FY 1998, EE must undertake time-sensitive analytical screening of pre-export notifications and conduct post shipment verifications on exports of high performance computers to 50 countries, including China, India, Israel, Pakistan, and Russia.

Personnel levels for Export Enforcement was 154 in FY 1993 and fluctuated between 143 and 146 from FY 1994 through FY 1996, but increased to 162 in FY 1997 and 170 in FY 1998. The number of FTEs is estimated to increase to 195 in FY 1999 and 200 in FY 2000, representing a 39 percent increase since FY 1994. The growth in EE personnel levels between FYs 1998 and 2000 is mainly in staffing for the National Defense Authorization Act and field investigative units.

### ***Export Control Automated Support System***

BXA developed the Export Control Automated Support System in 1984 to expedite the license approval process and better serve the U.S. exporter. ECASS, which is managed by the Office of Administration, is a large database system used to process, store, and transmit dual-use export licensing information, running on a mainframe at the departmental computer center in Springfield, Virginia. ECASS is an unclassified system that supports over 600 users, including BXA headquarters and field offices; the U.S. Arms Control and Disarmament Agency;<sup>11</sup> the Central Intelligence Agency; and the Departments of Defense, Energy, State, and the Treasury. During its life cycle, ECASS has been upgraded to permit manual, electronic, and optical character recognition data entry of license applications and commodity classification requests. (See ECASS Section X of the report for a further description and discussion of the system.)

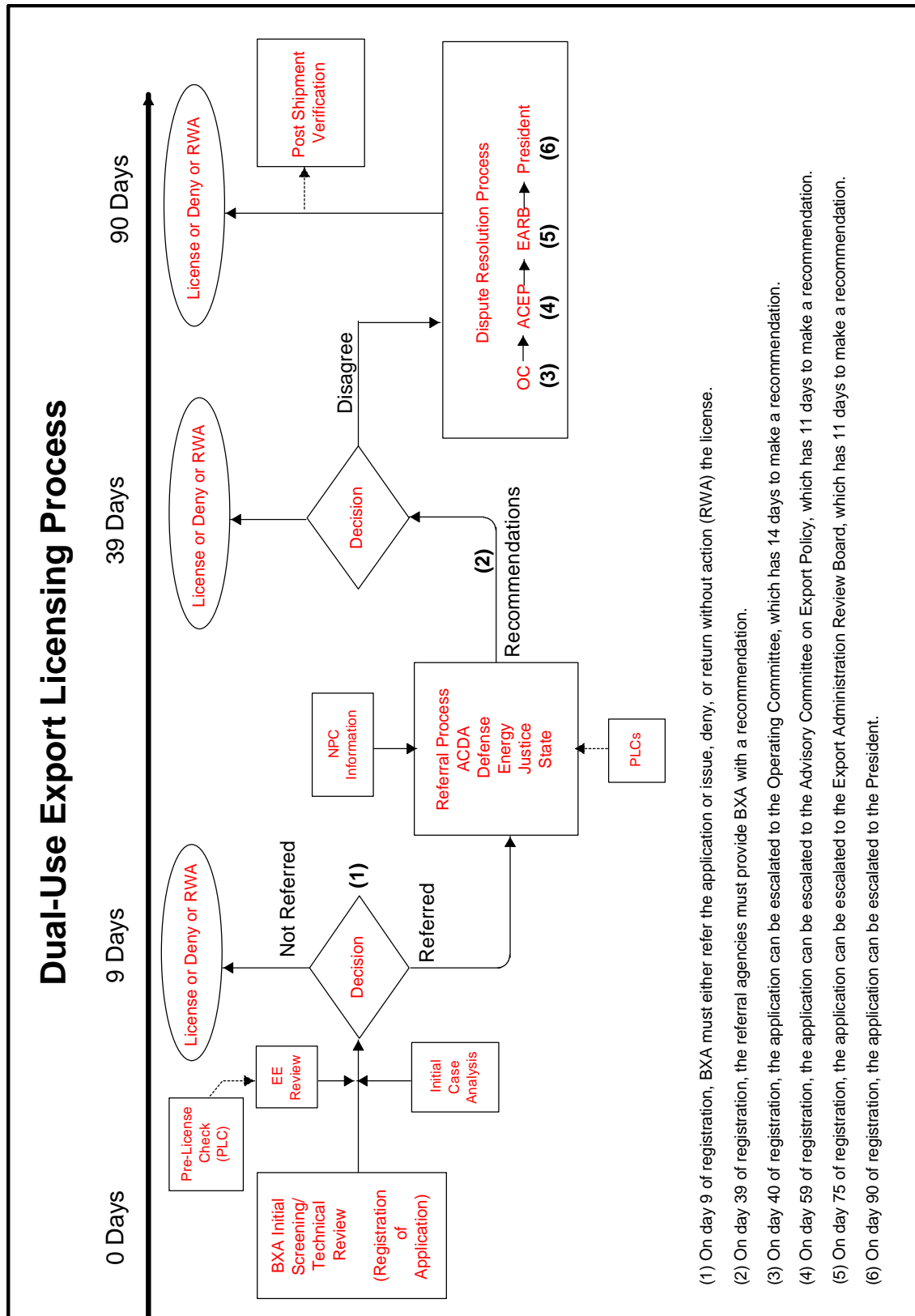
## **II. Interagency Export Licensing Process**

The Export Administration Act of 1979, as amended, gives authority to the Secretary of Commerce to issue rules and procedures for processing dual-use export license applications. The Congress intended that a determination concerning an export license application be made to the maximum extent possible by the Secretary of Commerce without referral to any other government department or agency. Authority to manage the dual-use export licensing process was delegated by the Secretary to BXA. On December 5, 1995, the President issued Executive Order 12981, in response to the need for more transparency in the dual-use export license process. Specifically, it authorized the Departments of Defense, Energy, and State and the Arms Control and Disarmament Agency to each have the authority to review any license application received by Commerce. In addition, the executive order established mandatory escalation procedures for all dual-use export license applications under interagency dispute and refined the time line for this process. (See Figure 4.)

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<sup>11</sup>The U.S. Arms Control and Disarmament Agency was dissolved on April 1, 1999. Its licensing review function was moved to the Department of State.

Figure 4



(1) On day 9 of registration, BXA must either refer the application or issue, deny, or return without action (RWA) the license.

(2) On day 39 of registration, the referral agencies must provide BXA with a recommendation.

(3) On day 40 of registration, the application can be escalated to the Operating Committee, which has 14 days to make a recommendation.

(4) On day 59 of registration, the application can be escalated to the Advisory Committee on Export Policy, which has 11 days to make a recommendation.

(5) On day 75 of registration, the application can be escalated to the Export Administration Review Board, which has 11 days to make a recommendation.

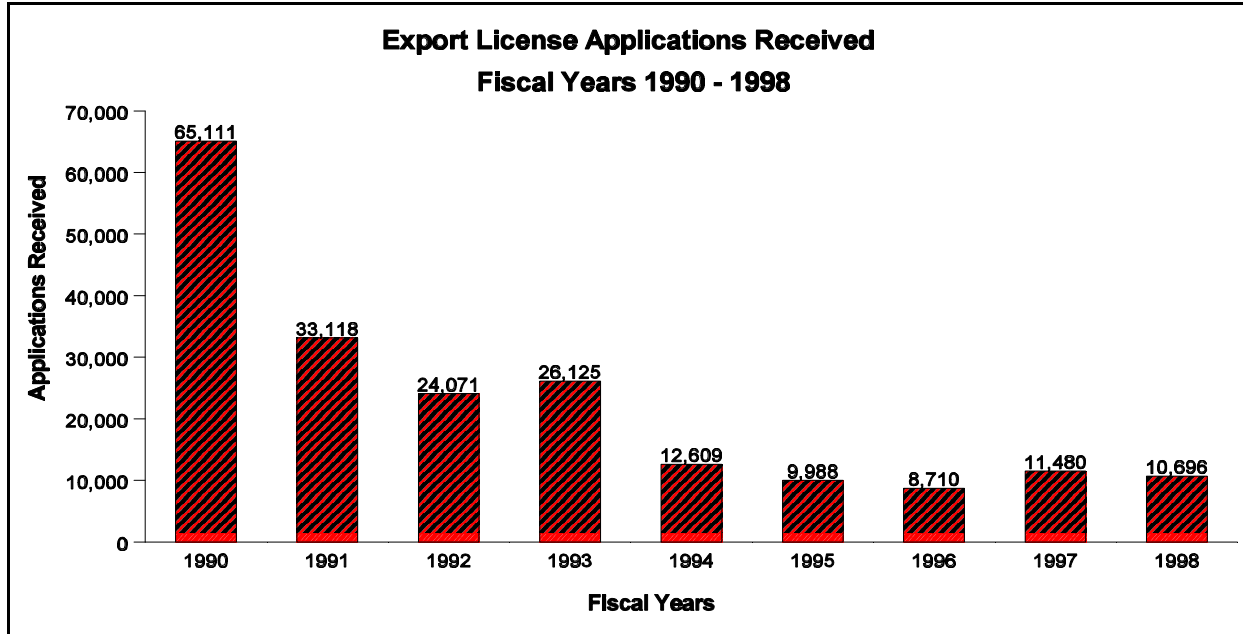
(6) On day 90 of registration, the application can be escalated to the President.

Source: Export Administration Regulations, Bureau of Export Administration.

## **BXA Review Process**

The number of export license applications that BXA receives has decreased from 65,111 in fiscal year 1990 to 10,696 in fiscal year 1998, primarily due to the loosening of export controls at the end of the Cold War. (See Figure 5.)

**Figure 5**



**Source:** Office of Administration, Bureau of Export Administration.

After a license application is received by BXA it is entered into ECASS, either manually or electronically. ECASS automatically tries to match the parties listed on the application to parties already in the system in order to assign it the same identification number (see Section X for further discussion). For parties not recognized as already in the system, the system refers them to the Office of Enforcement Analysis. On a daily basis, ECASS automatically screens all new applications against the watchlist to identify any “flags” on the parties.<sup>12</sup> Applications flagged by the system are automatically referred to the Office of Enforcement Analysis or the Office of Export Enforcement for further review and simultaneously to licensing officials in Export Administration. Applications that are not flagged are automatically referred to licensing officials for processing.

According to Executive Order 12981, BXA has nine days to conduct its initial case review and refer the case to other reviewing departments or agencies if appropriate. Within the nine days, licensing officers conduct an initial screening of the export license application to determine if

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<sup>12</sup>BXA’s watchlist contains the names of parties that have been identified as warranting increased scrutiny for export license purposes.

there is sufficient information to process it. If so, the licensing officer then verifies the exporter's commodity classification—a critical step in the export licensing process because the commodity classification determines the appropriate policies and procedures to apply. In addition, the licensing officer will (1) determine the reasonableness of the end use specified by the exporter, (2) document the licensing history of the exporter, (3) document the licensing history of the ultimate consignee or end user(s), (4) analyze the reasonableness of the end use of the goods, (5) document the reason(s) for not referring a license application to the other agencies if applicable, and (6) provide a written recommendation.

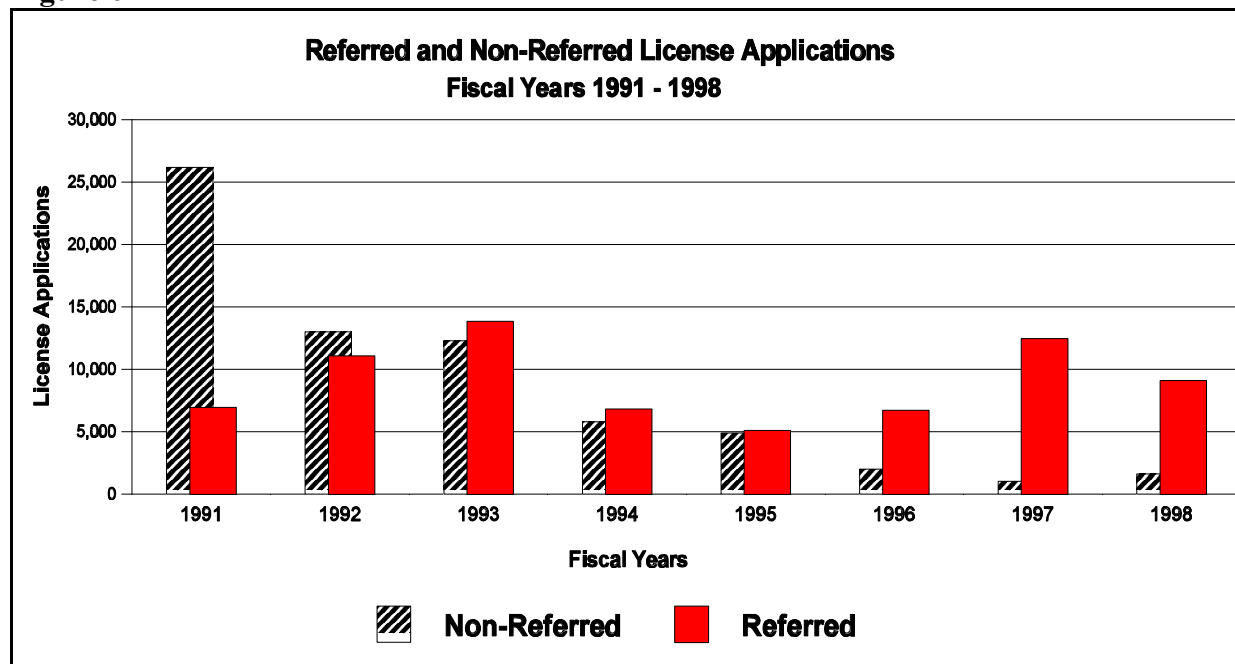
### **Referral Process**

While the four referral agencies can now see all export license applications, they have provided Commerce with delegations of authority for certain types of applications based on the level of technology, the appropriateness of the item's stated end use, and the country of destination. Even with the delegations, Defense receives and reviews almost all export license applications. Applications with items controlled under the Nuclear Referral List and the Nuclear Suppliers Group are referred to Energy. Applications for all items controlled for "foreign policy" reasons are referred to State. ACDA gets all referrals of applications with items subject to "regional stability" and "terrorism" controls; applications with items subject to certain "national security" controls; applications with items controlled by the Australia Group, the Missile Technology Control Regime, and the Nuclear Suppliers Group.

BXA also sends applications that have potential missile, nuclear, chemical, and biological proliferation concerns to the Central Intelligence Agency's Nonproliferation Center for an end user review. In addition, since the transfer of jurisdiction of commercial encryption products from State to Commerce in November 1996, the Department of Justice has been included in the referral process for encryption exports. See Figure 6 for a comparison of referred and non-referred license applications from fiscal years 1991 through 1998.



Figure 6



Source: Office of Administration, Bureau of Export Administration.

Under the executive order time frames, referral agencies must provide a recommendation to approve or deny the license application to the Secretary of Commerce within 30 days of receipt of the referral and all the required information. To deny an application, the referral agency is required to cite both the statutory and regulatory basis for denial, consistent with the provisions of the Export Administration Act and the Export Administration Regulations. An agency that fails to provide a recommendation within 30 days is deemed to agree with the decision of the Secretary of Commerce.

Most export licenses are issued with conditions that require the exporter to abide by certain restrictions. The conditions are primarily used to control proliferation of the commodity by limiting the end use or restricting access of the commodity to specific end users. There are 28 standard conditions that BXA can place on an export license. When BXA refers the export license application to the referral agency, it attaches the conditions for the agency to review. The referral agencies can also recommend additional conditions to be placed on the export license before it is issued. If any agency disagrees, the agency can escalate the application to the dispute resolution committee(s).

### Interagency Working Groups

If any of the referral agencies, including the intelligence community, wish to address a potential proliferation concern about a particular application before escalating the matter, the export license application may be referred for discussion to one of the three interagency working groups, all of

which are chaired by the Department of State: (1) the Subgroup on Nuclear Export Coordination which reviews nuclear related dual-use cases, (2) the Missile Technology Export Control Group which reviews missile technology dual-use export license applications, and (3) the Shield which reviews dual-use export license applications related to the possible proliferation of chemical or biological weapons.

### **Dispute Resolution Process**

If there is agency disagreement on whether or not to approve a pending license application after the 30-day interagency review period, the application is automatically escalated to a higher-level interagency working group called the Operating Committee. Under Executive Order 12981, the OC members are comprised of representatives from the Departments of Commerce, Defense, Energy, and State. The Chair of the OC is appointed by the Secretary of Commerce. Non-voting members of the Operating Committee include representatives of the Nonproliferation Center and the Joint Chiefs of Staff. The OC meetings occur weekly. The Chair of the OC considers the recommendations of the reviewing departments before making a decision on the export license applications. The OC Chair's decision does not have to be based on the majority vote. (See Section V for further discussion on the dispute resolution process.)

Any reviewing department may escalate the decision of the OC Chair, within five days of that decision, to the Advisory Committee on Export Policy. The ACEP, which meets monthly, is chaired by the Commerce Assistant Secretary for Export Administration, and members include assistant secretary-level representatives from the Departments of Defense, Energy, State, and ACDA. Appropriate representatives of the Nonproliferation Center and the Joint Chiefs of Staff are non-voting members of the committee. Any dissenting department or agency may appeal the majority decision of the ACEP to the Export Administration Review Board within five days.

The Export Administration Review Board is chaired by the Secretary of Commerce, and its members include the Secretaries of Defense, Energy, State and the Director of ACDA. The Chairman of the Joint Chiefs of Staff and the Director of the Central Intelligence Agency are nonvoting members of the EARB. The EARB's decision is based on a majority vote. Again, within five days of this decision, any dissenting agency may make a final appeal to the President.

### **End Use Checks**

End use checks help determine if the overseas parties or representatives of U.S. exporters are suitable for receiving sensitive U.S. items and technology and will likely comply with appropriate end use conditions and retransfer restrictions. As a result, end use checks are an important component of the export licensing process. End use checks consist of pre-license checks (PLCs) and post shipment verifications (PSVs). PLCs are conducted before the approval of a license application to obtain information about a foreign end user or intermediary consignee. PSVs are conducted after goods have been shipped to determine whether the licensed item or technology was received and is being used appropriately by the party named on the license or shipper's export

declaration (SED) or whether it was diverted to an unauthorized end user. The results of PLCs are factored into the licensing recommendation that Export Enforcement makes to the licensing offices. A PSV is used to verify whether the commodity is being used in accordance with the license provisions.

Most PLCs and some PSVs are conducted by the Department's International Trade Administration's U.S. and Foreign Commercial Service (US&FCS) personnel stationed in the country where the check is to take place or by State Department personnel if US&FCS has no office in the country. In addition, most PSVs and some PLCs are conducted by OEE's enforcement agents under the Safeguard Verification Program. In Fiscal Year 1998, approximately 258 PLCs and 60 PSVs were conducted by US&FCS personnel, and 25 PLCs and 286 PSVs were conducted by BXA Safeguard teams. A total of 283 PLCs and 346 PSVs were completed. The end use checks can be initiated or requested by any of the parties involved in the license review process, including BXA's licensing or enforcement personnel, referral agencies, or members of interagency groups to which a license has been referred.

### **III. Problems Previously Identified in the Export License Application Process (1993)**

In our September 1993 special interagency OIG report, we identified a number of problems in the license process, including continued disagreement among most of the agencies regarding which applications should be referred for comments and inconsistencies in the databases at BXA and Energy. We recommended that Commerce, Energy, Defense, and State, in cooperation with the National Security Council, develop appropriate procedures for addressing the referral issues and determine the feasibility of, and potential benefits from, expanding the use of ECASS for dual-use export information licensing data.

Our 1993 report also stated that BXA was not (1) maintaining sufficient documentation to provide a reliable audit trail of the actions taken on applications, (2) taking actions to ensure that exporters had complied with conditions placed on licenses, and (3) taking measures to ensure that the PLC or PSV programs were as effective as they should be.

BXA generally agreed with our 1993 review findings, but it stated that further efforts to streamline the referral procedures should be handled by the National Security Council. We were satisfied that BXA's planned efforts should improve its audit trail of the actions taken on applications. In addition, Export Administration officials agreed to improve the number of compliance conditions on licenses that they would follow-up on within their budget constraints, and to review the need for improved guidance for its end use check program. During our current review, we have followed up on each the findings from the 1993 report to determine the adequacy of the actions BXA has taken.



## OBSERVATIONS AND CONCLUSIONS

### I. Current Export Control Legislative Authority, Executive Orders, and Regulations Need Attention

The 1990s have dramatically changed the United States export licensing environment through global and economic change. However, as we examined the legislation, executive orders, and regulations that are used to control U.S. exports, we found several weaknesses that need to be addressed in order to strengthen the export licensing and enforcement process. First and foremost, we believe that new legislative authority is needed for export controls to replace the expired Export Administration Act, to accurately reflect current export control policies. In doing so, consideration should be given to allowing the Bureau of Export Administration to review dual-use items that may fall under the U.S. Munitions List administered by the State Department. In addition, we believe that the requirement to conduct a post shipment verification for every high performance computer shipped to every Tier 3 country, as mandated by the National Defense Authorization Act of 1998, may not be the most effective use of government resources.

We also determined that minor changes are needed for Executive Order 12981 with regard to the impact of the U.S. Arms Control and Disarmament Agency's merger with State, as well as clarification on agency representatives at the assistant secretary-level Advisory Committee on Export Policy. Finally, we believe that the export control policy and regulations regarding the release of technology to foreign nationals—commonly referred to as “deemed exports”—are unclear and ambiguous. We discuss these issues in more detail below.

#### A. Congress should renew legislative authority for export controls

Since World War II, the United States has controlled exports for three reasons: to preserve national security, to prevent domestic shortages and inflation, and to further foreign policy. The first major postwar export control law, the Export Control Act of 1949, authorized a virtual embargo on exports to Communist countries. The enactment of the Export Administration Act of 1979 maintained U.S. export controls, but called for removal of controls on goods and technologies freely available to Communist countries from non-U.S. sources and on items that do not contribute significantly to the military strength of potential adversaries. The Export Administration Act reaffirmed the need for national security, foreign policy, and short supply controls while also emphasizing the importance of exports to the economic well-being and national interest of the United States.

When the Export Administration Act of 1979 expired in September 1990, President Bush extended existing export regulations by executive order, invoking emergency authority contained in the International Emergency Economic Powers Act. As required by IEEPA, the President declared a national emergency “...with respect to the unusual and extraordinary threat to the national security, foreign policy, and economy of the United States...” posed by the act's

expiration. IEEPA-based controls were later terminated during the extension of the Export Administration Act in 1994, but after the final expiration of the act later that year, President Clinton reimposed controls under IEEPA. These controls continue in effect to date through Executive Order 12924, dated August 19, 1994, and Executive Order 12981, dated December 15, 1995.

However, under IEEPA BXA has less authority than under the Export Administration Act. Specifically, BXA states that its penalty authorities, both criminal and civil, are substantially lower than those for violations that occur under the Export Administration Act. Another limitation of IEEPA concerns the police powers (e.g., the authority to make arrests, execute search warrants, and carry firearms) of its enforcement agents. Those powers lapsed with the expiration of the act and BXA agents must now obtain Special Deputy U.S. Marshal status in order to exercise these authorities and function as law enforcement officers.

Since early 1990, both the Congress and the Administration have tried to rewrite the basic law that authorizes the President to regulate exports from the United States. The focus of the continuing policy debate pertains to national security and proliferation based controls that are used to restrict exports of dual-use technologies to the successor states to the Soviet Union, Eastern Europe, and the People's Republic of China. There is a wide range of opinions on how the government's export control policies and practices should balance the need to protect U.S. national security and foreign policy interests<sup>13</sup> with the desire not to unduly hamper the U.S. trade opportunities and competitiveness. Striking this balance poses a significant challenge for the parties involved.

#### Export Administration Act has expired

The Export Administration Act of 1979 was enacted at the beginning of the Cold War primarily to help block the export of critical goods and technologies to the Communist bloc for national security reasons. During the eighties and early nineties, the United States worked in concert with the international body known as the Coordinating Committee on Multilateral Export Controls (CoCom) in this endeavor. Section five of the act, "National Security," references this relationship often with regard to U.S. dual-use exports controlled for national security reasons. However, CoCom disbanded in 1994, and its replacement group, the Wassenaar Arrangement on Export Controls for Conventional Arms and Dual-Use Goods and Technologies, has few of the national security protections of CoCom.<sup>14</sup> In addition, whereas CoCom tried to block exports to Russia, that nation is now a member of the Wassenaar Arrangement. Since the end of the Cold War, many of the threats to the U.S. national security and foreign policy goals stem from rogue

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<sup>13</sup>Foreign policy export controls relate to the broad issues of human rights, anti-terrorism, regional stability, chemical and biological warfare, missile technology, and nuclear nonproliferation.

<sup>14</sup>For example, under CoCom, proposed exports were vetted among the member partners, and if one objected, the export was denied. However, there is no such provision under the current regime.

countries and groups who seek to acquire weapons of mass destruction and delivery systems and employ or support international terrorists.

As the United States encourages other countries, such as those in Eastern Europe and Southeast Asia, to implement export controls, it must set the example by sending a clear, unambiguous message that it is committed to export controls. However, it has been 10 years since the expiration of the Export Administration Act,<sup>15</sup> and, in our opinion, this could send the wrong signal to these countries as well as our allies that the United States is not truly committed to export controls. As the current Under Secretary for Export Administration stated in his written testimony on March 3, 1999, before the Subcommittee on International Economic Policy and Trade of the House International Relations Committee, the lack of an Export Administration Act "...can undercut our credibility as leader of the world's efforts to stem the proliferation of weapons of mass destruction."

However, the statement made by a former Under Secretary for Export Administration in recent testimony on the reauthorization of the act probably sums this issue up the best. Specifically, he stated,

"The fact that the Export Administration Act was last amended in 1988, a year before the collapse of the Soviet Union, would seem reason enough to justify the effort to draft and adopt a new Export Administration Act to guide export controls in the 21<sup>st</sup> Century."<sup>16</sup>

### Suggestions for new export control legislation

The Export Administration Act gives decision-making authority for dual-use license applications to Commerce and encourages Commerce to carry out its authority with limited referral to other agencies. The act also states that the Secretary of Commerce will seek recommendations from government agencies that have an important bearing on exports. As we reported in the special interagency review conducted by four OIGs in 1993, this ambiguity led to many conflicts regarding the referral issue between the various export control agencies.

However, Executive Order 12981 clearly defines the export licensing referral process by authorizing the Departments of Defense, Energy, and State, and the U.S. Arms Control and Disarmament Agency to review any license application received by Commerce. As a result, each agency has an opportunity to provide its individual perspective (e.g., national security or foreign policy) about a potential dual-use export transaction, thus making the process more transparent.

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<sup>15</sup>Except for a brief time period in 1994 when the EAA was temporarily extended by the Congress.

<sup>16</sup>Prepared Testimony of Dr. Paul Freedenberg at the Senate Banking, Housing and Urban Affairs Committee, Subcommittee on International Trade and Finance, Hearing on the Reauthorization of the Export Administration Act and Managing Security Risks for High Tech Exports, March 16, 1999.

As we discuss in Section IV of this report, all of the licensing agencies involved in reviewing export license applications (including Commerce) believe the process works much better now than it did in the early 1990s because of the transparency in the licensing process. Therefore, we believe that any new legislation for export controls should maintain the openness in the licensing process by continuing to allow all licensing agencies the ability to review all export license applications.

In addition, the expired act does not contain an interagency escalation process. Executive Order 12981 also clearly outlines a dispute resolution process. Specifically, any dissenting agency can escalate its concerns about any particular license applications to various ascending levels of review all the way to the President. Again, as we discuss in Section V of this report, we found the interagency dispute resolution process to be working well. Therefore, we believe that any new legislation on export controls should include a dispute resolution process.

Furthermore, although the other export licensing agencies have the opportunity to participate in the dual-use export licensing process, BXA lacks the same opportunity to participate in the munitions licensing process. The Arms Export Control Act of 1976 authorizes the President to control the commercial export of goods and technologies that are on the U.S. Munitions List. The authority for administering the export control functions of this act was delegated to the Secretary of State. State's Office of Defense Trade Controls (DTC) administers the International Traffic in Arms Regulations, which govern the export of munitions.

The Office of Defense Trade Controls refers license applications to other agencies or bureaus for review because of concerns about technical or policy issues related to the applications. Referrals are made to Defense, Energy, the Arms Control and Disarmament Agency, the National Aeronautics and Space Administration, or State Department bureaus. DTC does not refer any license applications to BXA for review.

According to BXA officials, some items are controlled by the multilateral regimes (e.g., Wassenaar Arrangement and the Missile Technology Control Regime) as "dual-use" but licensed in the United States as munitions items. One example is image intensification tubes. Since these items are treated by our foreign partners as dual-use, and BXA administers U.S. dual-use exports, BXA believes that State could benefit from BXA's technical expertise for these items. In addition, BXA officials believe that along with national security and foreign policy concerns, commercial issues should also be addressed, since U.S. companies may face foreign competitors whose governments have less stringent export controls.

In addition, the Export Administration Regulations indicate that there are a limited number of items that may be subject to both the International Traffic in Arms Regulations and the Export Administration Regulations.<sup>17</sup> For any item (e.g., rad-hardened chips) where the dividing line is

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<sup>17</sup>15 CFR 734.6.



not clearly defined between the Commerce Control List and the U.S. Munitions List, we believe both Commerce and State could benefit from having a complete picture of what is being approved or denied for consistency's sake. BXA could not tell how large of a problem this is since it does not see State licenses.

Although we are not suggesting that BXA be consulted on export licenses for "arms," we do believe that BXA, in conjunction with the other referral agencies, should evaluate the benefits of making the munition licensing process more transparent with regard to those items that may be dual-use but fall under the U.S. Munitions List. We would encourage BXA to discuss this issue with the applicable congressional committees while they are considering new legislation for the dual-use process.



In its written response to our draft report, BXA concurred with our recommendation to continue to work closely with the Congress and the Administration to renew export control legislative authority and stated that it has testified several times recently on the importance of renewing the Export Administration Act.

With regard to our suggestion that the Congress and the Administration evaluate the benefits of making the munition licensing process more transparent with regard to those items that may be dual-use but fall under the U.S. Munitions List, BXA reaffirmed its position that Commerce's involvement in those dual-use licenses currently under State's jurisdiction is appropriate. Specifically, BXA stated that as the Department of Defense becomes increasingly dependent on commercial-off-the-shelf procurements, the viability of the commercial sector (whose growth has been export driven) becomes a national security issue.

In addition, BXA points to a 1996 decision memorandum from the National Security Council on commodity classifications and commodity jurisdictions which indicates that the State Department should refer to BXA any munitions license applications that might more properly be controlled under the Commerce Control List. BXA indicated that to date it has received no such referrals. The fact that BXA has received no referrals does not necessarily indicate that the State Department is not adhering to the guidance, but it does illustrate one benefit that would come with more transparency in the munitions export licensing process.

***B. Post shipment verifications mandated by the 1998 NDAA are a questionable use of resources***

The Congress added provisions to the National Defense Authorization Act for fiscal year 1998 requiring exporters to notify BXA of their intent to export or reexport high performance computers (HPCs) with a performance capability of between 2,000 and 7,000 Million Theoretical

Operations Per Second (MTOPS) to Tier 3 countries.<sup>18</sup> Export control policy for HPCs organized countries into four Tiers with Tiers 3 and 4 including countries of concern to U.S. security interests. The four Tier listings are as follows:

- Tier 1 Most of the industrialized democracies in Western Europe and Japan. Exports may proceed without prior government review (i.e., export under a license exception) and with no limitation on MTOPS.
- Tier 2 Countries in Asia, Africa, Latin America, and Central and Eastern Europe with low risk proliferation records and export control concerns. No government review for exports up to 10,000 MTOPS.
- Tier 3 Countries such as China, India, Pakistan, Israel and Russia posing proliferation or other security risks. Licenses are not required (unless a referral agency objects to the export) for HPCs up to 7,000 MTOPS exported to civilian end users for civilian end uses, while exports above 2,000 MTOPS to end users of concern for military or proliferation of weapons of mass destruction reasons require a license. (See Appendix B for a complete listing of Tier 3 countries).
- Tier 4 Terrorism-supporting countries, such as Cuba, Iran, Iraq, Libya, North Korea, Sudan, and Syria. Exports to these countries are generally prohibited.

In addition, the National Defense Authorization Act mandated that BXA (1) issue a “one-time” report on HPC exports to the Congress in fiscal year 1998, (2) perform post shipment verifications on all HPCs greater than 2,000 MTOPS exported to Tier 3 countries, and (3) submit an annual report to the Congress on all HPC exports to Tier 3 countries.

Under the Act, the Departments of Commerce, Defense, Energy, and State and the Arms Control and Disarmament Agency have 10 days to review each exporter notification, and if no agency raises an objection, the exporter may proceed with the transaction without obtaining a license. If an agency objects to the transaction, the notification will automatically be converted to a license application and BXA will advise the exporter or re-exporter that a license is required. The license application is then processed under the normal export license application review process (including intelligence community review, as appropriate). Whether or not a license is required, the exporter is required to provide a written report containing shipping information to BXA after shipment of the goods. BXA uses this information to initiate a PSV for those HPCs above 2,000 MTOPS.

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<sup>18</sup> National Defense Authorization Act, 1998, P.L. 105-85, Sections 1211–1215, 111 Stat. 1629, November 18, 1997.

In the *National Defense Authorization Act First Annual Report to Congress*, issued in December 1998, BXA reported that there were 390 HPC exports made to Tier 3 countries in fiscal year 1998 (up from 279 in 1997). Of these 390 exports, 288 HPCs were shipped under license exceptions, and 102 HPCs under an export license. Based on these exports, BXA identified nine categories for how HPCs are being utilized as well as the percentage breakdown of each. (See Table 1.)

In addition, BXA reported that of the 390 reported exports, there were only 104 PSVs performed (27 percent). Table 2 illustrates the Tier 3 countries, number of HPCs shipped, and number of PSVs conducted. While close to half of these HPCs shipments were made to China, only one PSV was actually performed there. As we discuss in Section VII of this report, the United States has historically had problems with conducting end use checks, especially PSVs, in China. In fact, while the Chinese government has allowed some pre-license checks in the past, it had never allowed post shipment verifications until September 1998. BXA officials have attributed the ability to have performed the PSV on the one HPC shipment to the End Use Visit Arrangement agreed to in July 1998 as part of the U.S.- China summit.

**Table 1: End Uses/End Users for High Performance Computers Sold to Tier 3 Countries (U.S. Exports, Fiscal Year 1998)**

End Use/End User Categories	Percent Sold
<b>Communications &amp; Utilities</b> —telephone companies, television stations, television program production, advertising agencies, movie production, online shopping, Internet service providers, Internet access, radio stations, news bureaus, newspapers, and gas/electric suppliers	35
<b>Financial Industry</b> —banks, savings and loan, credit unions, insurance, pension, stock brokers, and stock exchanges.	21
<b>Manufacturing &amp; Software Development</b> —administration, manufacturing research, product development, and software development.	13
<b>Seismic Research &amp; Petroleum Industry</b> —oil exploration, oil production and refining, petroleum product distribution, seismic research, and earthquake prediction.	7
<b>Demonstration &amp; Resale</b> —includes HPCs purchased for demonstration purposes or for resale.	6
<b>Civilian Government Agencies</b> —patent, trademark, customs, taxation authorities; weather services; transportation including railroads and police departments.	4
<b>Academia</b> —includes colleges, universities, research centers, basic research, and medical research.	4
<b>Distribution</b> —includes retail and wholesale distribution of items other than HPCs (distribution of HPCs is under “ <b>Demonstration &amp; Resale</b> ”) and petroleum products (distribution of petroleum products is under “ <b>Seismic Research &amp; Petroleum Industry</b> ”).	3
<b>Other</b> —includes military, hospitals, some special comprehensive licenses, and instances where end use is not specified.	7

Source: Export Enforcement, Bureau of Export Administration.

An obstacle the Chinese government has placed on this process is the requirement of an End User Certificate issued by its Ministry of Foreign Trade and Economic Cooperation for any exports that the United States wants to perform a PSV on in China. However, End Use Certificates have only been associated with “licensed” exports from the United States, and most of the HPC exports shipped to China fell under a License Exception. To accommodate the Chinese insistence of requiring end use certificates for PSVs, BXA recently amended the Export Administration

Regulations to require exporters of HPCs to China to obtain an end user certificate issued by China before exporting if the HPC is to be exported under the authority of an export license or License Exception.

**Table 2: Number of PSVs on HPCs to Tier 3 Countries in Fiscal Year 1998**

Country	HPCs Shipped	PSV	No PSV
China	191	1	190
Egypt	11	2	9
India	29	20	9
Israel	82	42	40
Russia	33	21	12
Saudi Arabia	8	2	6
United Arab Emirates	20	11	9
Other <sup>19</sup>	16	5	11
<b>Total</b>	<b>390</b>	<b>104</b>	<b>286</b>

Source: BXA's First National Defense Authorization Act Annual Report to Congress, December 1998.

In addition to the 190 HPC shipments to China that did not have a PSV check, 96 other PSVs were not performed on the HPC exports to Tier 3 countries. The status of these checks is as follows:

- PSVs are planned for the coming year (47).
- PSVs are still pending at overseas posts (28).
- Original PSV indicated consignee sold the HPC; new PSVs are pending (13).
- HPCs have not been delivered to customer (2).
- HPCs were returned to U.S. ownership (6).

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<sup>19</sup>The other 12 countries are: Algeria, Angola, Azerbaijan, Bahrain, Croatia, Kazakhstan, Kuwait, Lebanon, Oman, Pakistan, Serbia, Ukraine.

All 104 PSVs conducted were reported as favorable, in that the checks found no discrepancies between the stated and the actual end use. However, one discrepancy was found in a check that was only partially completed during the reporting year. While we do not have any reason to believe that the HPCs were not physically at the stated facilities, we do question if these checks can truly identify how the HPCs are being used. Again, as we discuss further in Section VIII, we believe that end use checks are an appropriate tool to use if the U.S. government wants to verify the physical location of a commodity and learn more about the foreign entity.

However, determining the actual end use of a commodity in some cases may be difficult. For instance, a computer can be networked with other computers or machines in other facilities to increase its capabilities. More specifically, a computer at Facility ABC could be networked with a more powerful computer at Facility XYZ through a Local Area Network (LAN), giving the computer at Facility ABC more computing power. With the increased computing power, a networked computer can be used for multiple purposes (commercial or military applications), and the information can be stored on a computer at a different location through the LAN. A physical check of the HPC most likely would not detect this. This dilemma points out the inefficiency of some end use checks as well as the futility of certain controls.

Another reason that contributed to BXA's inability to perform all of the required PSVs was resources. At the time the 1998 National Defense Authorization Act was passed, BXA's appropriations for fiscal year 1998 were already enacted and the fiscal year 1999 budget submission had already left the Department of Commerce, so BXA has had to operate the program within existing resources. BXA officials informed us that they did not request a supplemental appropriation for fiscal year 1999. However, this requirement essentially forced BXA to divert some of its enforcement resources to conduct PSVs on some lower end HPCs that could have otherwise been used for targeting end use checks on the HPC shipments of greater concern or on more critical commodities and technologies. According to the Under Secretary for Export Administration,

“The resultant burden of on-site visits for each computer is an example of good intentions leading to wasteful government expense and no improvement to national security.... Requiring BXA to visit every site where an HPC is installed, regardless of what business the end user is in or how many times it has been visited before, is ineffective.... BXA needs to target its enforcement resources where they will do the most good.”<sup>20</sup>

Nonetheless, to meet this Congressional mandate, the Assistant Secretary for Export Enforcement created a high performance computer team to coordinate the PSV checks and compile the annual congressional report. The HPC team currently has two members. Most of the burden of actually conducting the National Defense Authorization Act PSVs fell to BXA's export enforcement

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<sup>20</sup>*Growing Demand for U.S. High Performance Computers*, January 8, 1999, BXA Press Release.

agents through its Safeguard Verification Program, as well as Commerce's United States & Foreign Commercial Service staff located in the Tier 3 countries (see Section VIII for more information on end use checks).

In its fiscal year 2000 budget submission, BXA has requested an additional five full time equivalent positions and approximately \$1 million in outlays to perform time-sensitive screening of pre-export notifications and conduct PSVs for HPCs. However, BXA officials claim that with small desk-top computers, as well as laptop computers, rapidly approaching the 2,000 MTOPS level, it will drastically increase the number of future PSVs. They are still concerned that even with these additional resources, they will not be able to meet the requirements of performing a PSV for every HPC shipment.

We believe that the NDAA requirement to conduct a PSV for every HPC shipped to Tier 3 countries is not the most effective use of government resources. Since this requirement cannot be adjusted by the executive branch, we would encourage BXA to seek relief from the Congress on this issue.



BXA's response to our draft report stated that it concurred with our recommendation to work with the Congress to revise the 1998 NDAA requirement to conduct PSVs for every computer meeting the threshold levels in Tier III. It also pointed out that when the 1998 NDAA passed, the PSV requirement affected some mainframes, high end workstations, and powerful servers, but now dual processor desktop workstations that exceed 2,000 MTOPS are captured under this requirement. BXA's response reiterated that the requirement calls for a U.S. government employee to visit all high performance end users no matter how many times they have been visited in the past, to judge whether their computers are being used for weapons development. As a result, BXA believes that the burden of these visits becomes disproportionate to the benefits derived from them. We agree that some modification to the current PSV requirement should be given serious consideration.

***C. Some clarification is needed for Executive Order 12981 pending new legislation***

During our review, BXA management expressed its frustration to us regarding the failure of referral agencies to send the appropriate representation level to the Advisory Committee on Export Policy meetings. Specifically, they directed us to the Executive Order 12981 language that specifies that the Advisory Committee on Export Policy (ACEP),

“...shall have as its members the Assistant Secretary of Commerce for Export Administration, who shall be Chair of the ACEP, and assistant secretary-level representatives of the Departments of State, Defense, and Energy, and the Arms Control and Disarmament Agency. Appropriate representatives of the Joint Chiefs

of Staff and of the Nonproliferation Center of the Central Intelligence Agency shall be nonvoting members of the ACEP.”

However, upon further examination of the executive order, we found that it also states, “Regardless of the department or agency representative’s rank, such representative shall speak and vote at the ACEP on behalf of the appropriate Assistant Secretary or equivalent of such department or agency.” A Department of Energy official we spoke with stated that the above language gives agencies the flexibility to decide who should attend these meetings. BXA officials disagree with this interpretation and insist that it was the intent of the drafters of the executive order for representatives at ACEP to be at the assistant secretary-level or its equivalent. To settle this dispute, we believe that BXA should request the National Security Council to clarify this issue in an amendment to the executive order.

In addition, the merging of the U.S. Arms Control and Disarmament Agency into the State Department in April 1999, leaves ACEP with only four standing voting members. Since ACEP decisions are based on a majority rule, the committee faces a potential problem if a decision comes down to a tie vote. We encourage BXA to request that the National Security Council review this issue and provide a procedure to follow in the event of a tie vote.



In its written response to our draft report, BXA concurred with our recommendation to request the NSC to provide a procedure to follow in the event of a tie vote at the ACEP and it indicated that a review is currently underway. BXA also agreed that the advisory agencies need to improve the level of representation at the ACEP and that it is working toward that end. However, BXA indicated that it does not believe that this issue should be referred to the NSC because the cited language Energy relies upon to send less than assistant-secretary representation is taken out of context. We are not convinced that the language in the Executive Order is clear on this issue. Furthermore, the fact that BXA and Energy have different interpretations of this language is precisely the reason why the NSC should be asked to clarify this issue. Therefore, we reaffirm our recommendation to BXA that it refer this issue to the NSC for clarification.

***D. Export control policy and regulations for foreign workers need clarification***

According to the Export Administration Regulations, any release to a foreign national of technology or software that is subject to the regulations is “deemed to be an export” to the home



country of the foreign national. These exports are commonly referred to as “deemed exports.”<sup>21</sup> Technology or software can be “released” for export through:<sup>22</sup>

- Visual inspection by foreign nationals of U.S.-origin equipment and facilities;
- Oral exchanges of information in the United States or abroad; or
- The application to situations abroad of personal knowledge or technical experience acquired in the United States.

Items not subject to the Export Administration Regulations include publicly available technology and software, except software controlled for encryption item reasons on the Commerce Control List, that (1) are already published or will be published, (2) arise during or result from fundamental research, (3) are educational, or (4) are included in certain patent applications.<sup>23</sup>

However, we found the definitions and subsequent regulations for “fundamental research” to be vague and ambiguous. According to the regulations, fundamental research is defined as

“...basic and applied research in science and engineering where the resulting information is ordinarily published and shared broadly within the scientific community. Such research can be distinguished from proprietary research and from industrial development, design, production, and product utilization, the results of which ordinarily are restricted for proprietary reasons or national security reasons.”

While the regulations indicate that research conducted by scientists, engineers, or students at a university will normally be considered fundamental research, there are various exceptions to this rule (e.g., certain situations where prepublication reviews of the research is required). In addition, research conducted by scientists or engineers working for a federal agency or a Federally Funded Research and Development Center may be designated as “fundamental research.” Finally, research conducted by scientists or engineers working for a business entity will be considered “fundamental research” at such time and to the extent that the researchers are free to make scientific and technical information resulting from the research publicly available without restriction or delay based on proprietary concerns or specific national security concerns outlined in any funding arrangement by the U.S. government.

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<sup>21</sup>The deemed export rule does *not* apply to persons lawfully admitted for permanent residence in the United States (e.g., persons carrying a green card).

<sup>22</sup>15 CFR 734.

<sup>23</sup>15 CFR 734.

### Potential loophole to the deemed export regulation

According to the regulations, educational information is not subject to these regulations if it is released by instruction in catalog courses and associated teaching laboratories of academic institutions. We see this as a potential loophole in the regulations. Specifically, while a proprietary course on design and manufacture of high performance machine tools is subject to the Export Administration Regulations because the proprietary business does not qualify as an “academic institution,” this same information, if taught as a university graduate course, would not require a license even if some of the students were from countries to which an export license is required. One could argue that if a foreign country wanted to gain as much knowledge about U.S. technology as it could, this could be done, in part, by sending “professional” students to the United States.

### Compliance with deemed export controls

Deemed export license applications make up approximately 10 percent of all export license applications processed by BXA. One BXA official estimates that 25 U.S. companies submit most of the total number of deemed export applications that BXA processes, implying that there might be many more high technology companies out there that may not be compliant with the regulations due to a lack of knowledge or understanding of the regulations or simply an unwillingness to comply.

In addition to the limited number of U.S. companies that have applied for these licenses, we also learned that only one federal agency has submitted deemed export license applications in connection with foreign nationals visiting its research labs. Specifically, in fiscal year 1998 two of the federal labs under the Department of Energy submitted a total of two deemed export license applications to BXA. The first export license application was returned without action due to insufficient information, while the second was approved.

Given the high volume of foreign visitors that visit Energy laboratories who might have access to export-controlled technology and/or software, BXA officials raised the concern that Energy may not be complying with the deemed export regulations. During this review, Energy’s Office of Inspector General informed us that most of the Energy laboratories are federally funded research development centers. As such, some of these laboratory officials claim that most of their work is “fundamental research,” which exempts them from this regulation. We discussed this issue further with an Energy official who is an active participant in the dual-use export licensing process. This official considers the deemed export provisions in the Export Administration Act to be difficult to interpret, and therefore, understands the laboratories’ confusion in determining if deemed export licenses are needed for some of its foreign visitors. More recently, another Energy lab applied for two deemed export licenses involving foreign nationals from China. At the time of this writing, the license applications were pending review at the Advisory Committee on Export Policy.

We would also like to point out, however, that BXA has not received any deemed export license applications from any other federal laboratories, including those at Commerce's National Institute of Standards and Technology; Defense's Army, Navy, and Air Force laboratories; and Health and Human Services' Centers for Disease Control and Prevention. While we have no evidence to suggest that these or other federal agencies are noncompliant with the deemed export rule, based on Energy's lack of understanding about this rule, we wonder whether other federal agencies may have the same problem.

### *Summary*

Having examined the general provisions specified in the Export Administration Regulations, and after discussions with BXA officials on this topic, we believe that not only are the regulations ill-defined, but the export control policy concerning deemed exports itself appears to be ambiguous. The lack of understanding regarding deemed exports could damage national security if sensitive technology is released to inappropriate end users. BXA should work with the National Security Council to determine what the United States' goal is with regard to requiring deemed export licenses and to ensure that the policy and regulations are clear and do not provide any avoidable loopholes that foreign countries can use to obtain proscribed sensitive U.S. technology inappropriately.

We believe that it would be prudent for BXA to open up dialogues with the federal scientific community to ensure that these agencies fully understand the deemed export requirements and to help them determine if foreign visitors to their laboratories require a deemed export license. In addition, while BXA has published deemed export guidance on its web site and developed a course on technical data on software that deals with the hiring of foreign nationals in the United States, we believe that if the U.S. government's own federal laboratories do not understand these regulations then it is plausible that industry might not as well. Therefore, we believe that BXA needs to be more proactive by conducting a series of outreach visits to high technology companies or industry associations it feels are appropriate candidates for deemed export licenses.



In its response to our report, BXA did not disagree with our observations that the regulations for "deemed exports" are ambiguous or the fact that U.S. companies and other federal agencies may be noncompliant with the regulations. However, BXA raised the issue of the constitutionality of the "deemed export" regulation, specifically as it pertains to prior restraint of free speech. While we did not address the constitutionality of this regulation, if BXA believes this regulation is unconstitutional, it has an obligation to raise this issue with the Department of Justice.

In addition, BXA stated that our report ignores the “most serious aspect of the issue which is the current standard being employed for triggering ‘deemed export’ license applications.”<sup>24</sup> We disagree. Again, we recommended that BXA work with the NSC to determine what the United States’ goal is with regard to requiring deemed export licenses. By determining what the goal is, we contend that policymakers would also have to review the reasonableness of the current “deemed export” rule. Therefore, we reaffirm our recommendation to BXA that it should work with the National Security Council to determine what the United States’ goal is with regard to requiring deemed export licenses and to ensure that the policy and regulations are clear and do not provide any avoidable loopholes that foreign countries can use to obtain proscribed sensitive U.S. technology inappropriately.

Finally, while BXA agreed to expand its outreach efforts, it conditioned this action upon the resolution of the concerns it cited in its response. We agree that the regulations regarding deemed exports should be clarified before BXA expands its outreach efforts. But we urge BXA to move expeditiously to clarify that requirement with the NSC and provide clearer guidance to U.S. research laboratories and industry.

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<sup>24</sup>The current standard requires an export license for hiring a foreign national when he or she will be exposed to technology in the United States that would require export authorization if it were to be transferred to his or her home country.

## II. More Transparency Is Needed in the Commodity Classification Process

As the agency responsible for administering the Export Administration Regulations, BXA is responsible for determining whether an item or activity is subject to these regulations and, if so, what licensing or other requirements apply. Such a determination affects only Export Administration Regulations requirements, and not the applicability of any other regulatory programs. For example, the item may fall under the U.S. Munitions List and therefore be subject to the controls of the International Traffic in Arms Regulations under the licensing jurisdiction of State's Office of Defense Trade Controls. If an item falls under the U.S. Munitions List, BXA will forward the request to State.

In general, BXA holds the exporter responsible for classifying an export item. However, BXA will advise an exporter whether an item is subject to the Export Administration Regulations and, if applicable, identify the appropriate Export Control Classification Number. When making written commodity classification requests, exporters must provide descriptive literature or brochures, precise technical specifications, or papers that describe the items in sufficient technical detail to enable BXA engineers to accurately classify the items. BXA also responds to many phone inquiries about commodity classifications, but they are not binding determinations.<sup>25</sup>

Exporters can submit written requests electronically or in paper form. These are entered into BXA's Commodity Classification Automated Tracking System (CCATS). CCATS is commonly used by BXA officials to refer to classification requests from exporters. In fiscal year 1998, BXA responded to 2,723 CCATS requests with 6,161 line items.<sup>26</sup>

During this review, we found that BXA had instituted a front-end review mechanism to pre-screen commodity classifications before distributing them to the appropriate engineer for review. This was an important quality control measure, but we identified two areas that still need improvement. First, we found that Export Administration's processing of CCATS is untimely, resulting in delays for exporters. Second, and more importantly, we found the commodity classification process is not transparent, leaving it vulnerable to incorrect classifications.

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<sup>25</sup>We reviewed only written commodity classification requests, and our recommendations pertain only to such requests.

<sup>26</sup>According to 15 CFR 748.3, each classification request should be limited to five items, but exceptions may be granted by BXA on a case-by-case basis for several related items if the relationship between the items is satisfactorily substantiated in the request.

**A. *BXA's processing of commodity classifications has improved, but timeliness is still a problem***

Before 1998, commodity classification requests were being assigned to one of Export Administration's seven licensing divisions by nontechnical support staff in the Office of Exporter Services. However, due to a concern that CCATS were being assigned to incorrect divisions, a 1997 Export Administration task force determined that a quality control mechanism was needed to pre-screen CCATS before distributing them for analysis. Essentially, this quality control mechanism consists of a front-end technical review of the commodity classification by an engineer before they are distributed to the appropriate licensing division.

While this process was implemented briefly in 1998, it was interrupted when the key staff person assigned to this function departed in September 1998. This procedure was reinstated again in February 1999. BXA management has stated that as a result of this quality control mechanism, commodity classification requests are now being routed to the appropriate division for review. We believe that Export Administration has taken a positive step toward improving the commodity classification process by implementing the front-end review. However, it needs to ensure that this procedure is not affected in the future by absences of key staff persons.

In-house delays in CCATS processing

According to the Export Administration Regulations, commodity classifications submitted by exporters (with the exception of encryption products) must be completed within 14 calendar days.<sup>27</sup> However, we found that the average CCATS in fiscal year 1998 took BXA 37 days to process. Delays in commodity classifications could delay U.S. exporter shipments unnecessarily if it is determined that no license is required. According to one senior Export Administration official, the primary reason CCATS processing is delayed is that the licensing officers give priority to license applications because they are expected to adhere to strict time frames in processing applications under Executive Order 12981. We found that a lack of written procedures for assigning CCATS to multiple licensing divisions also contributes to processing delays.

First, with regard to commodity classifications not being a priority, licensing officers need to understand that while the Executive Order 12981 mandates timely processing of export license applications, the Export Administration Regulations require timely processing of CCATS. We believe that BXA managers must communicate to LOs the importance of processing CCATS in a timely manner and hold them accountable for doing so. However, BXA's managers have informed us that they cannot tell from the ECASS management reports they receive if a CCATS is overdue as a result of LO inaction or if the CCATS is legitimately "on hold" because the LO is

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<sup>27</sup>15 CFR 750.2.

waiting for additional information from the exporter necessary to complete his review.<sup>28</sup> Unlike the automated export license application process, ECASS has not been programmed to allow an LO to place a CCATS in a “hold without action” status, thus “stopping the clock” with regard to mandated processing times. We believe BXA should program ECASS to allow for the “hold without action” feature.

Second, when a commodity classification is subject to controls in more than one licensing division, it must be reviewed by all applicable divisions. In fiscal year 1998, there were 133 CCATS that were referred to multiple divisions. There are no written procedures in place that outline the requirements for reviewing commodity classifications that involve more than one division. As a result, we have been told, misunderstandings have occurred resulting in processing delays. We encourage Export Administration to develop policy and procedures for the intra-agency review of commodity classifications, as it has for intra-agency licensing review.

#### CCATS Delays at the National Security Agency

A different time line has been established for processing commodity classification requests for the export of certain mass market encryption software that falls under “Encryption Item” controls. If the software product meets certain criteria, the request is supposed to be processed within 15 working days from receipt of a properly completed request.<sup>29</sup> The criteria are as follows: (1) the software product must be mass market software, (2) the software must be designed for installation by the user without further substantial support by the supplier, and (3) the software includes encryption for data confidentiality. BXA shares these classification requests with the National Security Agency for a technical review of the encryption product.

However, the 15-day turnaround time for processing encryption CCATS requests has not always been met. As of March 1999, there were 107 pending encryption classification requests, and BXA had been waiting an average of 69 days for a technical review of them by the National Security Agency. According to a National Security Agency official, the delay in the agency’s review of these CCATS was due to BXA changing its regulations on encryption exports effective January 1999. Because of these changes, many exporters submitted commodity classification requests to learn if they qualified for license exceptions. The official said that the agency received more requests in the first three months of 1999 than in all of 1998 and was overwhelmed by the workload. However, many of the requests were one-time requests, and the Agency expects the

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<sup>28</sup>Although both the Export Administration Regulations and BXA’s web page make clear that a commodity classification request requires the applicant to submit appropriate technical specifications of the commodity, software, or technology in order for BXA to evaluate the request, there are instances when the exporter does not submit sufficient information.

<sup>29</sup>Supplement No. 6, 15 CFR 742, paragraph (a)(1).

workload to return to prior levels. The official said that approximately 75 percent of BXA's pending encryption classification requests have been cleared as of mid-April 1999.



In its written response to our draft report, BXA generally concurred with our recommendations to improve its in-house processing of commodity classifications. BXA stated that its goal is to complete all commodity classifications within the 14 days stipulated in the EAA but that this has been difficult to do in recent months due to the external demands placed on the agency, including requests for information from the Congress and the public.

With regard to our recommendation for BXA to program ECASS to allow commodity classifications to be put on "hold without action," BXA stated it was an interesting suggestion that it would review as it balanced the interest of the timely completion of commodity classifications with the need for accurate time accounting. However, we believe that the "hold without action" feature will help BXA managers determine why a CCATS has been delayed and hold the licensing officers accountable for their inactions. Therefore, we reaffirm our recommendation that BXA program ECASS to allow commodity classifications to be put on "hold without action."

**B. Commodity classification referral criteria need to be clarified**

A 1996 memorandum from the National Security Council (NSC) set forth guidance for processing commodity jurisdiction and commodity classification requests. Included were procedures for initial screening, transparency, escalation and deadlines. Regarding initial screening, the previous policies for both processes were maintained. Specifically, the NSC guidance directed the State Department to continue to refer to Defense and Commerce all commodity jurisdiction requests. A commodity jurisdiction request is used to determine whether an item or service is subject to the export licensing authority of the EAR, as administered by BXA, or the ITAR, as administered by State's Defense Trade Controls.<sup>30</sup> There are more liberal deadlines for commodity jurisdictions than for CCATS. According to the NSC guidance, Defense Trade Controls has 90 days to make a commodity jurisdiction determination. There is also a three-level escalation process outlined by the memo, starting with the Assistant Secretary level, to the Under Secretary or Secretary level, and finally to the President. During fiscal year 1998, Defense Trade Controls processed 276 commodity jurisdiction requests, and all were referred to Commerce for comments.

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<sup>30</sup>While BXA is the primary licensing agency for dual-use exports, Defense Trade Controls licenses defense-related or munitions articles and services.



The NSC guidance also continued the process of allowing exporters to initiate commodity classification requests with Commerce to determine whether items are subject to the Export Administration Regulations. Again, BXA has 14 days to make a CCATS determination. While there were no general provisions for Commerce to refer commodity classification requests to Defense or State, the NSC guidance did state that Commerce “will share with State and Defense all commodity classification requests for items/technologies specifically designed, developed, configured, adapted and modified for a *military application*, or derived...” from such items or technologies [emphasis added].

Furthermore, the guidance instructed Commerce to refer these munitions-related commodity classification requests to State and Defense, allowing them a two-working-day turnaround time. At the end of those two working days, silence will be deemed to be consent, and Commerce may proceed with the processing of a final and binding commodity classification in accordance with its own regulations, practices, and policies. Since the 1996 NSC guidance, BXA has referred 27 CCATS to Defense Trade Controls.

Subsequent to the NSC guidance on this subject, Defense informed BXA in 1996 that it did not want the opportunity for an initial review of munitions-related commodity classifications and instead requested that Commerce provide, on a weekly basis, a copy of such completed commodity classifications requests and decisions to Defense.<sup>31</sup> Defense OIG has informed us that the Defense Threat Reduction Agency has received 12 such completed commodity classifications since the 1996 ruling.<sup>32</sup> BXA did not provide us with any contrary figures. According to the NSC guidance, Commerce should be referring appropriate commodity classification requests to both State and Defense. However, BXA did not explain the discrepancy between the 12 completed munitions-related CCATS referred to Defense and the 27 munitions-related CCATS referred to State.

Defense’s current position on the commodity classification process is significantly different than it was in 1996. Both Defense and State have indicated to us a need for more transparency in the CCATS process. Specifically, they believe that this process should be completely opened for interagency review similar to the export licensing process. Since there is no way for Defense or State to question commodity classifications that are not referred, they are concerned that BXA may be advising exporters that munitions-controlled items are licensable by Commerce or require no license at all. To illustrate the need for more transparency, the agencies point to a case in 1995 in which BXA mistakenly determined that an investigative report on the crash of a Chinese rocket carrying a satellite as needing no export license. BXA allowed the release of this report without consulting the referral agencies. BXA has since admitted that its commodity classification

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<sup>31</sup>Memorandum dated May 13, 1996, from the Director of Defense Technology Security Administration to the Deputy Assistant Secretary for Export Administration.

<sup>32</sup>Until October 1998, the Defense Threat Reduction Agency was known as the Defense Technology Security Agency.

determination was incorrect because the accident occurred in part of the rocket, not in the satellite being carried, and the release of the report should have been authorized by the State Department.

As part of our review, we sought to determine whether past commodity classification determinations by BXA did, in fact, support the concerns of Defense and State. We invited analysts from Defense Trade Controls and the Defense Threat Reduction Agency to review a sample of 103 CCATS line items and second-guess the original CCATS determinations made by BXA.<sup>33</sup> The sample was reviewed by analysts from the Defense Threat Reduction Agency in preparation for a joint review session. The Commerce and Defense OIGs convened the joint BXA-Defense Threat Reduction Agency review session in which 13 of the cases—those that the Defense Threat Reduction Agency found most troublesome of the 103 CCATS line items—were discussed. The Defense Threat Reduction Agency disagreed with BXA’s decision in 5 of the 13 cases. In two of the five cases, the agency argued that the items were not under the Commerce Control List, and the CCATS should have been referred to Defense Trade Controls as commodity jurisdiction requests.

The first case was for a ruggedized, portable, encrypted radio. Commerce officials stated that the radio had not been built to military standards and therefore was not a munitions item under the jurisdiction of the ITAR. Defense officials stated that the literature accompanying the request described the radio as militarized and that other radios built by the manufacturer were subject to munitions export licenses. The second request was for an antenna. Commerce officials stated that the antenna was not a munitions item, despite company literature describing it as militarized. Defense officials stated that the literature satisfied ITAR criteria for a “defense article” (munitions) and that the manufacturer had a history of exporting products under the munitions export licensing process.

Regardless of whether these items fall under the ITAR or CCL, we believe that BXA should have at least referred these two CCATS to State per the 1996 NSC guidance—especially since the manufacturers’ own literature describes them as “militarized.” Again, the NSC guidance requires BXA to share with State and Defense all commodity classification requests for items or technologies specifically designed, developed, configured, adapted and modified for a *military application*, or derived from such items or technologies.

In the remaining three cases, the Defense officials agreed that the items fell under the Commerce Control List but disagreed with BXA’s export control classification number. BXA ultimately agreed with Defense’s classification for one of the three CCATS but maintained its original position on the other two.

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<sup>33</sup>Officials from State’s Defense Trade Controls chose not to participate in the review.

The opinions expressed by senior Defense Threat Reduction Agency and BXA officials after this review illustrate the different perspectives held by these two agencies. In the opinion of the Deputy Director, Technology Security Directorate, Defense Threat Reduction Agency, this exercise demonstrated that while in the vast majority of CCATS cases there was no difference in the conclusions of the Defense Threat Reduction Agency and BXA, there is an opportunity for mistakes as highlighted above.

In the opinion of the Deputy Assistant Secretary for Export Administration, this exercise showed that BXA made appropriate classifications in 99 percent of the sample cases (indicating that the Defense Threat Reduction Agency's analysis did not convince BXA that it was wrong in the other four CCATS). He also stated that while it is important to have participation by referral agencies in the export license application process for policy considerations, BXA can handle the CCATS and judge what is under the Export Administration Regulations without help from its colleagues at these agencies. In response, the Defense Threat Reduction Agency official stated that the process, as currently set up, could undercut its review of potential International Traffic in Arms Regulations items, which could affect its license review rights. In further discussions with BXA officials on this subject, it appears that they are concerned that referring all CCATS to Defense and State would unnecessarily slow down the review process. BXA believes any delays would discourage exporters from submitting CCATS requests, the submission of which are voluntary.

However, as our sample demonstrates, BXA appears to not have fully complied with NSC's 1996 guidance to refer all munitions-related commodity classification requests to State. Furthermore, per Defense's request, BXA has not referred all of the completed commodity classifications for such items to Defense. At this time, we are not convinced that BXA should refer all CCATS to both Defense and State given the fact that these agencies may not have adequate resources to review all CCATS in a timely manner. However, we strongly believe that BXA needs to work with both Defense and State to ensure that the CCATS process is more transparent with regard to items or technologies specifically designed, developed, configured, adapted and modified for a military application, or derived from such items as called for in the NSC guidance. Therefore, we recommend that BXA, in conjunction with the Defense and State, work with the NSC to develop specific criteria and procedures on how to implement its 1996 guidance for the referral of munitions-related commodity classifications to Defense and State. In addition, we believe BXA should consult with Defense to determine if it wants to continue its delegation to BXA on munitions-related CCATS or withdraw it.



In its written response to our draft report, BXA concurred with our recommendation that the NSC 1996 memorandum should be revisited to clarify the guidance on the referral of munitions-related commodity classifications to Defense and State. However, it disagreed with some of our analysis.

Specifically, BXA's response pointed out that the fundamental difference between CCATS and license applications is that the former are technical determinations that, in its opinion, should be divorced from policy or politics. It further stated that whether or how an item appears on the CCL is an empirical judgment well within the expertise of a BXA licensing officer and this should not be the subject of interagency negotiation. On the other hand, BXA stated that licensing determinations are policy decisions and that the perspectives of different agencies are important in these decisions. While we generally agree with BXA that a CCATS determines what a product is and where it appears on the CCL, we also believe that this decision could ultimately impact policy decisions—especially if BXA incorrectly informs an exporter through a CCATS that no license is required, as it did with the investigative report on the crash of a Chinese rocket carrying a commercial communications satellite under Commerce's jurisdiction.

While BXA contends that the crash investigative report is not a true commodity classification because it pertained to a previous export license, we disagree. The exporter requested a written commodity classification determination from BXA regarding whether this item required an export license. The licensing officer provided the exporter with a written determination on two different occasions using the CCATS form. There is no mention of a prior license anywhere on the written CCATS. Thus, we contend this decision is an example of a CCATS, and it clearly would have been beneficial if it would have been reviewed by the referral agencies.

### **III. Licensing Officers' Analysis of Export Applications Could Be Enhanced**

BXA's core mission is to analyze and process export license applications. Significant changes have occurred in BXA over the past several years that have affected how export license applications are processed. First, BXA's 1994 reorganization combined the once separate policy and licensing functions into units of specific areas of concern, such as nuclear and missile technology, chemical and biological weapons, and strategic trade and foreign policy. Second, the Executive Order 12981 mandated stricter time frames with regard to processing export license applications and gave referral agencies the right to full review and to provide recommendations on any export license application. Third, and perhaps most important, the complexity of export license application reviews has increased due to rising proliferation threats, requiring licensing officers to make a more comprehensive analysis.

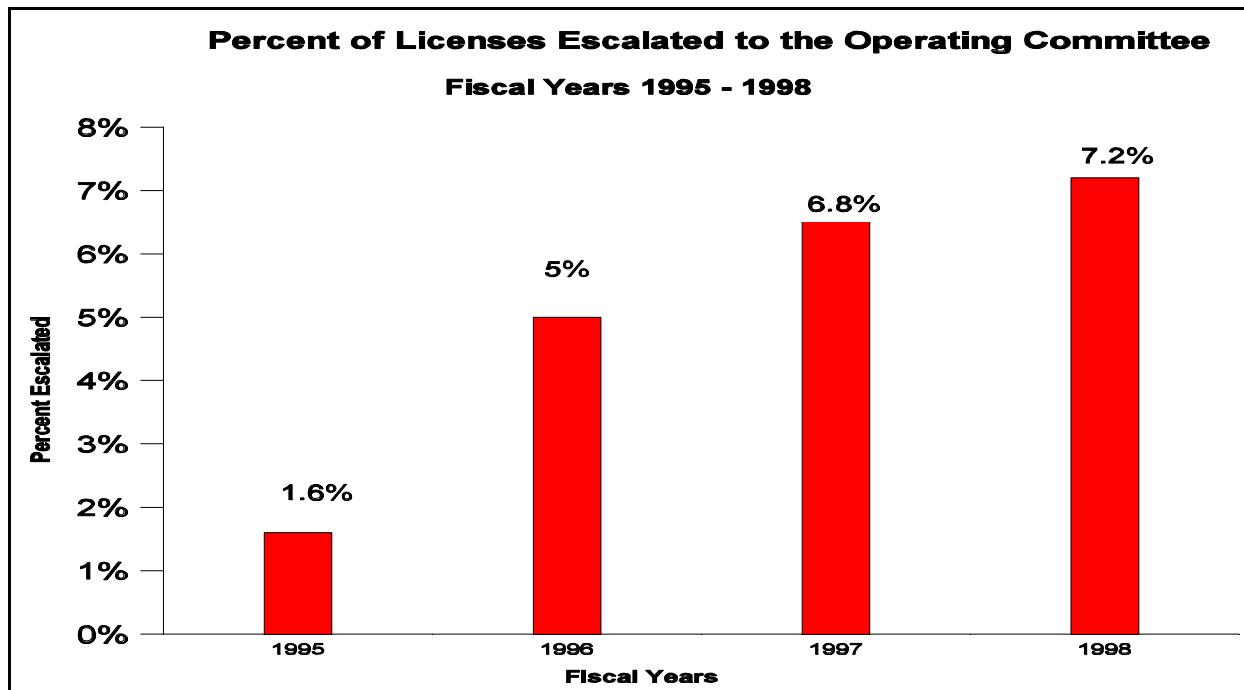
Proper case analysis is critical in ensuring that the appropriate export policy and procedures are followed for individual export license applications. According to Executive Order 12981, BXA must either refer the application to other agencies or dispose of the application within nine days of the registration of a license application. While the Executive Order does not preclude the LO from continuing to seek additional information about the end use or end user after the nine days, it is within this period that BXA must make the necessary decisions to help ensure that cases are processed appropriately during the interagency review. Within the first nine days, LOs (1) determine if there is sufficient information to process the application; (2) refer the application to the Central Intelligence Agency's Nonproliferation Center for end user checks, if appropriate; and (3) analyze the information and document their conclusions about the license application.

However, during our review of export license applications, we found it difficult to determine whether applications were being thoroughly analyzed by LOs in the initial review period because there was little indication in the license history about how they reached their conclusions. For example, in some cases LOs omitted critical information in their referral comments or notes section, with regard to (1) the reasonableness of the end use specified by the applicant, (2) detailed characterizations of the ultimate consignee or end user(s), and (3) the detailed licensing history of the applicant or the foreign entity. While the lack of information in the licensing history does not necessarily indicate that the LOs did not consider the above elements, without this critical information, referral agencies cannot make the most informed licensing decisions.

The consequences of incomplete analysis or documentation by LOs in this initial review period are significant. One result, according to some BXA officials, is that more and more license applications are being disputed by the referral agencies and escalated to the Operating Committee because LOs either (1) do not know all they can about a transaction (e.g., legitimacy of the end user or end use) before they make their decision and refer it out for interagency review or (2) are not providing this critical information to the referral agencies. Based on our review of 26 export license applications that went to the OC during the period January 1 to June 30, 1998, our observations from three OC meetings we attended, and the percentage of licenses escalated to the

OC between fiscal years 1995 and 1998, this seems plausible. (See Figure 7.) We believe that better policies and procedures as well as additional training could enhance LOs' analysis and documentation of export license applications.

Figure 7



Source: Office of Administration, Bureau of Export Administration.

**A. Better policies and procedures are needed to assist licensing officers**

We found that the policy and procedures used by licensing officers varied. The *Licensing Officers Operating Manual*, dated October 1, 1995, has become an assortment of outdated or superseded documents and is no longer user friendly. Many of our OIG survey respondents, as well as those we interviewed throughout the review, identified the lack of up-to-date guidelines as one of BXA's major weaknesses. We also found that the contents of individual licensing officers' operating manuals varied among LOs as well as from one of the BXA employees responsible for drafting new guidance.<sup>34</sup> Export Administration officials stated that after the LO operating manual was modified per Executive Order 12981 in 1995, it was not updated again for almost a year and a half due to resource constraints. They also informed us that pertinent sections of the

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<sup>34</sup>The OIG team conducting this review also had difficulty getting a complete up-to-date licensing officer manual. On November 20, 1998, we were provided a copy of the operating manual from the Director of the Office Exporter Services, who informed us that it was a complete and updated copy. However, in March 1999, we learned that several key sections of the operating manual, such as case analysis, were missing from our copy. On March 25, the Office of Exporter Services provided us with the missing sections.

LO operating manual, such as case analysis and administrative procedures, are still valid but they conceded that these sections need to be updated.

The operating manual being used by LOs at the time of our review included a small section entitled "Case Analysis Guidance," which outlined eight points that must be addressed as part of an LO's analysis of an export license application and be included in the initial referral comments to all advisory agencies:

1. Export Control Classification Number(s) and reason for control.
2. Brief background statement highlighting licensing history involving the applicant and or/item, previous working group consultations, issues of interest, any precedent setting aspects of the proposed transaction.
3. Characterization of the end user(s) including type and relationship with applicant, if any (e.g. bank, motel, U.S. subsidiary).
4. Number of end users and reasonableness of end use.
5. Reason for not referring to an agency.
6. The LO's written recommendation.
7. Statement as to whether or not conditions are appropriate and, if so, identification of the specific conditions the Department of Commerce would suggest.
8. LO's name, telephone, and facsimile numbers.

While we believe these are the appropriate areas that the LOs should focus on during their review, guidance as to how they should accomplish these objectives is lacking. For instance, the third item tells the LO to "characterize the end user," but it does not provide any suggestions about how the LO should go about acquiring this information beyond that which was submitted by the applicant (e.g., researching the entity on the Internet) or what types of questions the LO should be addressing when dealing with end users in dynamic markets such as China and Russia. For example, since there is an increasing number of export license applications involving joint ventures between China and western partners, one BXA official stated that LOs need to take into account fundamental information about the joint venture including (1) whether the joint venture is in a formative stage or already established with the necessary authorizations and licenses from the Chinese Government; (2) the type of joint venture; and (3) elements that each joint venture partner contributed to the enterprise, such as capital, fixed assets and equipment, resources, and management. We believe this type of information would be especially helpful to the referral agencies as they do their own follow-up checks on end users, and also pertinent if the Central Intelligence Agency's Nonproliferation Center reports, "No comment" or "No intelligence

information was found on the entity.” (See Section IV for more discussion on the Central Intelligence Agency’s role in the export licensing process.)

To supplement this “eight-point” policy and procedures, BXA’s Chemical and Biological Controls Division (CBCD) issued specific guidance for its LOs as a reference during case analysis. CBCD’s guidance provides more comprehensive and descriptive case analysis guidelines than appear in the LO operating manual. For example, the guidance states that indicating a “university” is not a complete description of an end user, unless the LO specifies the school or laboratory within the university. CBCD’s guidance also requires that any decision made as a result of contacts with various individuals and organizations or review of supporting documentation must be documented in LO notes. CBCD also created a “Commodity Classification and License Determination Guide” to assist LOs in determining the appropriate Export Control Classification Number for items controlled for chemical and biological warfare reasons. In the absence of comprehensive policy and procedures for all LOs, we compliment this office for creating useful reference materials for LOs to use during case analysis.

In an effort to improve LO guidance for case analysis, on March 31, 1999, Export Administration officials implemented new procedures that emphasize the importance of obtaining sufficient information before processing a case and identify the types of facts and details that must be documented in LO notes. We found the new procedures to be more detailed than the prior guidance—expanding upon the original “eight points” outlined above. For instance, with regard to the end user, the new guidance states that simultaneously with the Nonproliferation Center review, the LO should seek additional information on the business nature and reliability of end users through Dun and Bradstreet, Lexis/Nexis, or the Internet and include this information in the referral history for the reviewing agencies.

The new guidance also stresses that LOs should document all relevant facts and details in notes throughout the review and analysis of an export license application, including discussions with the applicant, supervisors, or senior technical staff; summary of relevant end use check cables reviewed; and information obtained from the Internet, Dun and Bradstreet, or other open sources. The guidance also provides clearer instructions for interoffice referrals, pre-license checks, and referrals to the Operating Committee. While the new license application analysis procedures are more thorough than the previous case analysis procedures, we believe it would also be beneficial to provide LOs with specific questions they should be contemplating when processing export license applications to specific countries (e.g., China joint ventures described above). The new procedures are also more comprehensive than the existing procedures with regard to licensing history. The new procedures require LOs to specify details about both the prior licensing history for item(s) and/or consignees, including license identification numbers and number of licenses. However, we believe the new procedures should also require that LOs include the most recent dates of prior licenses or denials in the license history.

Export Administration is also currently creating an electronic library to store new policies and procedures. The library will be an on-line licensing officer manual and will include policies and



procedures related to commodity classifications, case analysis, license determinations, country policy, referral policies, and record keeping.

The policies and procedures in the electronic library are intended to be generic and will be applicable to all Export Administration licensing divisions. However, some divisions may find a need to customize the policies and procedures for specific issues relevant to their division, and all will need to update their specific policies and procedures as necessary. LOs will be able to access the electronic library via the case analysis screen in ECASS. The first guidance entered in the electronic library is policy and procedures for hold without action, return without action, and denials. The library is not yet available on-line for LOs' use, but BXA officials have stated that this action is imminent.

We applaud Export Administration for taking the initiative to update its policies and procedures and to improve the initial licensing review by LOs. We also believe that the electronic library will be a valuable reference tool for LOs to access while preparing the case analysis. Once all the new policies and procedures are approved and entered into the library, they need to be periodically updated to ensure that they are consistent with current issues and new regulations. Export Administration should develop a long-term plan for maintaining the library, including who will be responsible for updating the procedures, when they will be updated, and what procedures will be followed for updates.



In its written response to our draft report, BXA indicated it is willing to explore the implementation of our recommendation to provide a check list for licensing officers and require them to include the dates of the most recent approval or denials in the licensing history. Specifically, BXA's response stated that since each case is unique, a list of questions may not fit every contingency. However BXA agreed to pursue the development of such a list with licensing officers as part of its training on case analysis. In addition, BXA states that its recent guidance to licensing officers on case analysis requires that a past licensing history be considered. However, this guidance does not require that the most recent dates of prior licenses or denials be included in the license history. Therefore, we reaffirm our recommendation that BXA require LOs to include those dates in the licensing history.

Finally, BXA agreed with our recommendation to update policies and procedures regularly and fully implement the BXA electronic library. BXA's response indicated that the library is nearing completion, and it believes the library will go far in improving the consistent and timely provision of guidance to licensing officers.

**B. BXA needs a formal training program for its licensing officers**

BXA has not emphasized the need to develop and maintain a corps of highly qualified LOs who have the skills and competencies required for optimal case analysis of export license applications. The export licensing function requires a continuous structured training program to ensure that the LOs' critical thinking and knowledge of export control issues and concerns are the best possible. During our review, we found training in Export Administration to be inconsistent and unresponsive to LO needs.

LO training needs have not been properly identified or prioritized

BXA needs to identify and prioritize the current and future learning needs of its licensing officers and then establish a formal training program to meet those needs. Any training program BXA establishes must take into account the mission of the organization and identify the training necessary to achieve this mission. In addition, BXA should designate a specific office and staff, and provide the necessary resources to enable them to manage and implement this program.

All of the managers we spoke with in Export Administration said they place a strong emphasis on training—pointing out that the training budget for the last several years has been more than adequate. Actual obligations for training have increased from \$31,621 in fiscal year 1997 to \$84,746 in fiscal year 1998. In addition, Export Administration managers stated they rarely decline a request for training. However, we still believe that management's commitment to training has not been adequately communicated to all LOs, and has not resulted in quality and relevant training for most of them.

The LOs we talked with perceive that training within Export Administration is a low priority. In response to the questionnaire that we sent to all licensing officers, 25 of 39 respondents noted that over the last three years they received an average of only 75 hours of training. This included two experienced LOs and one new LO who responded that they received no formal training at all within the last three years. In addition, some supervisors told us that the types of courses LOs have taken did not always improve their ability to conduct more thorough analyses. We noted that many of the training classes cited in the responses did not appear useful for improving LOs' ability to review license applications. Some LOs we spoke with who want to improve their technical expertise feel it is far too difficult to obtain approval to attend workshops, technical seminars, or symposia that would improve their skills.

While training is a requirement in the LOs performance plans, the requirement is vague and inconsistent among the three licensing offices in Export Administration. For example, the Office of Strategic Trade and Foreign Policy Controls requires one training class per year, while the other two offices do not specify how much training is required. In addition, this training requirement does not specify the types of training that are required. Some LOs informed us that the training required in their performance plans is not taken seriously and, as a result, they are not held accountable for taking the training classes that will improve their ability to process export

license applications. Export Administration management needs to be more specific as to the amount and content of required training and should include this in a training plan for the office and also a training plan for each LO.

#### Training for new employees is inconsistent between Export Administration divisions

We were particularly concerned about the adequacy of training for new employees. Such training for new LOs and other Export Administration employees was generally left up to the individual divisions. LOs told us that new officer training generally consists of reading the Export Administration Regulations and learning on the job by directing questions to experienced staff. While a couple of divisions offered some additional training for their new employees, we found one in particular that provides more extensive training. Specifically, the Encryption Policy Division in the Office of Strategic Trade and Foreign Policy Controls provides a comprehensive training program for all of its new analysts. Initially, new analysts spend three weeks answering phones and sitting in on other calls in the Exporter Counseling Division. They also observe and answer exporters' questions via the speaker phone with the division director for two hours a day for one month. The new analysts also attend a two-day regulations seminar and a half-day technology seminar sponsored by BXA for exporters. In addition, new analysts observe interagency working group meetings and industry meetings. Lastly, new analysts attend BXA educational seminars provided to exporters to teach the licensing regulations. While we recognize that training needs to be flexible to allow for a variety of learning methods in a variety of disciplines, we recommend that Export Administration consider using this kind of training program for all new LOs.

We believe a training program—consisting of courses that are relevant to Export Administration at the group level, at the division level, and to new employees—is critical to maintain a standard of high quality export licensing decisions. In addition, we believe BXA needs to designate either a training team or training coordinator to manage and implement an Export Administration training program.

We also found that some LOs record their training hours using a training project code, while others do not track their hours. BXA may also want to consider requiring all LOs to use a project code for training, to be recorded on LO timesheets, so that upper level management can automatically track the hours spent on training.

#### Suggestions for training topics

Based on the responses to our survey and interviews with LOs and managers, we have identified a number of areas where we believe training would improve LOs' performance. Some of the basic courses include those that would improve their (1) communications skills, including writing and negotiating, and (2) research skills for obtaining additional information on companies and products, such as use of the Internet. Ongoing training on changes and updates to the Export Administration Regulations is also needed.

We believe that LOs also need more training in the policy arena, including international trade, international business, economics, and proliferation issues. Another important area includes ongoing technical training for BXA engineers to keep them abreast of constant changes in technology. For example, BXA LOs could visit companies or associations to obtain information on new or cutting edge technologies, or visit Commerce's National Institute of Standards and Technology for data encryption information. Such contacts would be especially helpful in key technical areas such as biotechnology, encryption software, chemical and drug manufacturing, and optical computing.

Export Enforcement sponsors training programs each year to which all its employees are invited. One of the advantages of Export Enforcement's training program is that it brings together all the agents, analysts and support personnel to hear from key speakers from the referral agencies, law enforcement community, Export Administration, and the Office of the Chief Counsel for Export Administration to discuss issues concerning export controls. We believe Export Administration may want to consider a similar program.

In addition, Export Administration should work with its counterparts at the other export control agencies to institute regular briefings by the various agencies. We believe this forum could be used to provide LOs the opportunity to learn more about other agencies' licensing functions as well as to discuss current export control issues from different perspectives (e.g., national security or nonproliferation concerns). This could help LOs gain a better understanding of how their function fits into the "bigger" picture and improve LO working relationships with their counterparts at the referral agencies. In that regard, we also suggest that Export Administration explore the possibility of brief exchanges of licensing personnel among the referral agencies, or even short-term assignments of BXA's LOs to another agency's licensing office or the Nonproliferation Center.

Finally, Export Administration should consider implementing a temporary internship for new LOs to work in the Operating Committee to observe the types of questions and issues that will be raised by the referral agencies. This assignment should better prepare the new LOs for what to consider in their initial review of an export license application.



In its response to our draft report, BXA concurred with our recommendation to develop and implement a training program for its licensing officers. Specifically, BXA informed us that its Licensing Officer Task Force is organizing an extended formal training program for all licensing officers that will include briefings by other agencies, such as the NPC.

BXA disagreed with our finding that it "has not emphasized the need to develop and maintain a corps of highly qualified LOs..." and stated that the current diversion of resources to respond to the extraordinary external requests for information placed on the agency has affected its ability to

conduct formal training programs. We do not believe that BXA can attribute the lack of a formal training program or training coordinator solely to the drain on its resources from these requests in fiscal year 1998. In addition, BXA stated that our report did not adequately highlight that its primary method for training (especially new LOs) is on-the-job training with a senior licensing officer. We disagree with this comment. We state in our report that “new officer training generally consists of reading the Export Administration Regulations and learning on-the-job by directing questions to experienced staff.” However, our report emphasizes that more than on-the-job training is needed. We highlight as a best practice the efforts of one BXA licensing division to provide a more comprehensive training program for all of its new analysts. Such training includes attending seminars and interagency or industry meetings, and working for a time in the Export Counseling Division. We again recommend that BXA consider using this kind of training program for all new LOs.

Finally, BXA stated that we may have reached our conclusions about LO training as a result of comparing the training programs of EE and EA. As part of our review we did obtain a basic understanding of EE’s training program and determined that its practice of bringing together all of its personnel on an annual basis for briefings from the referral agencies, law enforcement community, and the Office of Chief Counsel for EA to discuss issues concerning export controls was a sound idea. While we agree that EA must tailor its training on a more individual basis because of its widely different areas of expertise and responsibilities, we contend that there are still opportunities for centralized training.



#### **IV. Export License Application Process Is More Transparent, but Some Weaknesses Need to Be Addressed**

The dual-use export licensing process is more transparent today than it was in 1993. In fiscal year 1993, 53 percent of export license applications were referred by BXA. In fiscal year 1998, 85 percent were referred. In the 1993 special interagency review, the OIGs pointed out that there was not complete accord between Commerce and most of the other federal agencies regarding which license applications should be referred for comments to the other agencies which may have important information bearing on exports. The report recommended that the Secretary of Commerce, in cooperation with the National Security Council and the Secretaries of Defense, Energy, and State, direct the appropriate officials to provide a mechanism for (1) resolving referral criteria disputes at progressively higher levels and (2) periodically reviewing the referral criteria and resolving future disputes. The report also recommended that the Congress clarify the roles of the various agencies involved in the dual-use export licensing process.

In 1995, the President issued Executive Order 12981, which authorized the Departments of State, Defense, and Energy, and ACDA to each have the authority to review any export license application submitted to the Department of Commerce under the Export Administration Act and the Regulations. The Secretary may refer license applications to other U.S. government departments or agencies for review as appropriate.

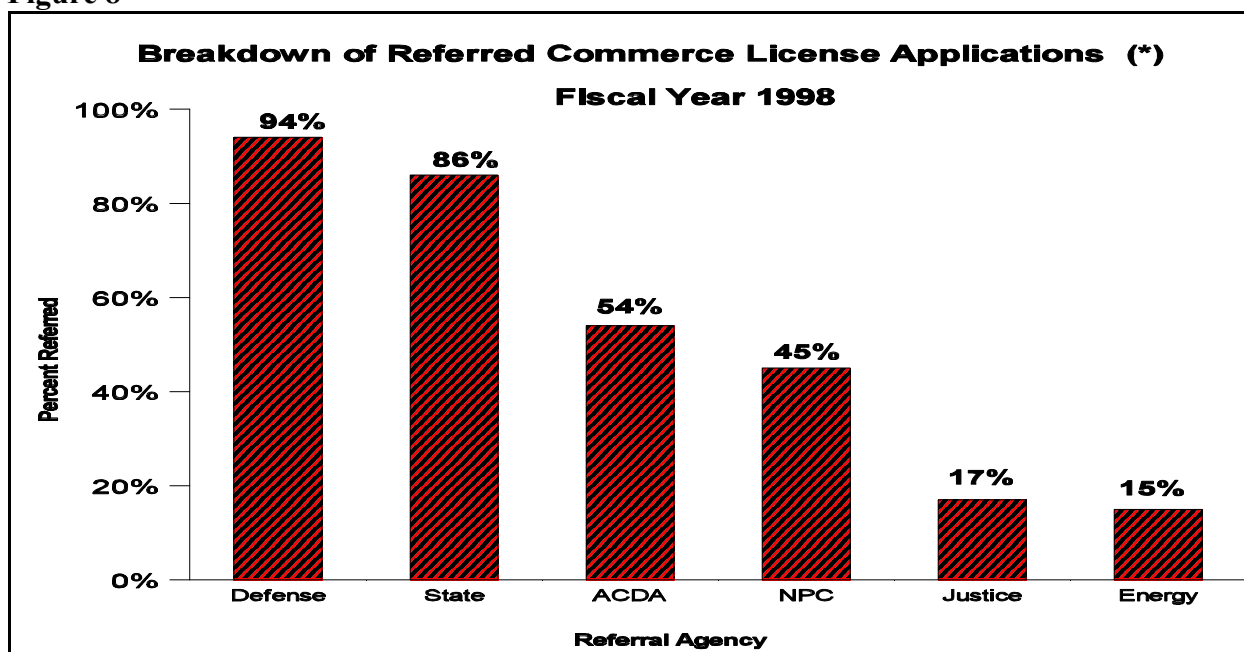
While the four referral agencies can now see all applications, they have provided Commerce with delegations of authority for certain types of applications, based on the level of technology, the appropriateness of the items for the stated end use, and the country of destination. With the delegations, most export license applications are still referred to Defense. Applications with items controlled by the Nuclear Suppliers Group are referred to Energy. Applications for all items controlled for "foreign policy" reasons are referred to State. ACDA got all referrals of applications with items subject to "regional stability" and "terrorism" controls; applications with items subject to certain "national security" controls; applications with items controlled by the Australia Group, the Missile Technology Control Regime, and the Nuclear Suppliers Group; and all applications for computers. Since the transfer of jurisdiction of commercial encryption products to Commerce in 1996, the Justice Department and the National Security Agency have a role in the license review process for encryption license applications.<sup>35</sup> In addition, applications for items that do not fall under the Commodity Control List but are determined to be related to the Enhanced Proliferation Control Initiative are referred to all agencies.

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<sup>35</sup>Executive Order 13026, *Administration of Export Controls on Encryption Products*, November 15, 1996, authorizes the Department of Justice to review any export license applications pertaining to encryption items. In addition, the National Security Agency was delegated authority by the Defense Threat Reduction Agency to review most encryption item exports referred to the Defense Department, but DTRA retains its authority for handling these cases during the escalation process.

In fiscal year 1998, 11,015 license applications were processed by Commerce. Of these, 9,405 applications were referred to the four agencies, as specified in Executive Order 12981, and Justice as specified in Executive Order 13026, and the Nonproliferation Center of the Central Intelligence Agency. Most export license applications are referred to more than one agency. Figure 8 shows the percentage of the referred applications that were referred to the Departments of Defense, State, Justice, Energy, ACDA, and the Nonproliferation Center. In fiscal year 1998, 1,610 (or approximately 15 percent) of export license applications processed were not referred to any other agency.

Figure 8



(\*) This does not reflect 15 percent (1,610 applications) not referred to any agency.

Source: Office of Administration, Bureau of Export Administration.

While we believe the overall referral process is generally effective, we did identify some areas of weaknesses that need management attention, including (1) LOs amending existing licenses without interagency review; (2) inadequate review time provided to the Nonproliferation Center for its end user checks; (3) lack of guidance provided to LOs with regard to the Nonproliferation Center referrals; (4) vulnerabilities associated with not screening parties against the Customs Service's TECS database during the initial review period; and (5) canceling pre-license checks without notifying the referral agencies when they approve a license with the condition of a favorable end use check. In addition, we highlight two other areas of concern that require BXA management's attention. First, the intelligence community could provide a more comprehensive analysis on end users. The current dual-use licensing process does not take into account the cumulative effect of technology transfers. To obtain the greatest benefit from the intelligence community, all export licenses should be referred to the Central Intelligence Agency, which could distribute them to other units in addition to the Nonproliferation Center. Secondly, we identified



a high number of “pullbacks” from one of State’s licensing units. We discuss these issues in more detail below.

**A. Sufficient justification exists for most of the non-referred cases**

In fiscal year 1998, BXA did not refer about 15 percent of license applications processed. As part of our review of the export licensing process, we looked at a randomly selected sample of 60 non-referred cases to determine whether BXA had sufficient justification for not referring those applications. BXA officials provided a number of reasons for the non-referred cases, e.g., they were mostly incomplete applications that were returned to the exporter without action, some automatic denials, and a small number of routine cases that the other agencies have elected to delegate to Commerce.

The most common reason export license applications in the sample were not referred was that they lacked sufficient information to evaluate the application and were returned to the exporter. Nineteen applications (or 32 percent of the sample) were not referred for this reason. The other reasons for non-referral include:

- The items were classified as “EAR 99” and qualified for “no license required” based on the destination. These applications were “returned without action.” “EAR 99” is the classification used for items subject to the Export Administration Regulations that are not on the Commerce Control List.<sup>36</sup> If an item is classified as “EAR 99” and certain prohibitions do not apply, then the exporter is allowed to ship with “no license required.”<sup>37</sup> For example, a microwave switch not described in the Commerce Control List was classified as “EAR 99.” Because it was being shipped to Switzerland, the application was found to be “no license required” (10 cases).
- The items had export control classification numbers but qualified for “no license required” based on the destination and end use. All were returned without action (8 cases).
- The items were included in a delegation of authority from the referral agencies. For example, the referral agencies have delegated their authority to Commerce to review most applications for crime control items, e.g., polygraph systems (6 cases).

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<sup>36</sup>A license or other requirement applies only in those cases where other parts of the Export Administration Regulations impose a licensing or other requirement on such items or activities. For example, a license is required for an EAR 99 item whose destination is Cuba.

<sup>37</sup>General Prohibitions Four through Six of 15 CFR 736 include actions prohibited by a denial order, prohibited end uses or end users, and export or reexport to embargoed destinations.

- The items qualified for license exceptions and applications were returned without action. A “License Exception” is an authorization that allows the exporter to export or reexport, under stated conditions, items subject to the Export Administration Regulations that would otherwise require a license<sup>38</sup> (3 cases).
- Applications were rejected based on an outright denial policy for certain items going to India. On May 13, 1998, Presidential Determination No. 98-22 determined that India detonated nuclear explosive devices and directed that all licenses and other approvals to export or otherwise transfer defense articles and defense services from the United States to India or transfer U.S. origin defense articles and defense services from a foreign destination to India be revoked immediately (3 cases).
- Applications were returned without action at the request of the exporters (3 cases).
- Items involved “short supply” commodities, which are not specified as one of the types of applications to be referred under Executive Order 12981. Examples of “short supply” commodities include crude oil, other petroleum products, and unprocessed western red cedar. Both of these applications were approved with conditions (2 cases).
- Applications were duplicates of pending export license applications and were returned without action (2 cases).
- Item was determined to fall under U.S. Munitions List and was returned without action after BXA advised the applicant that the commodity was under State’s jurisdiction. (1 case).
- Application was for a special case requiring last-minute approval for flights by a news organization to Cuba to cover a papal visit. BXA verbally discussed this case amongst the referral agencies in order to expedite the exporter’s request (1 case).
- Applications were treated as amendments to previous licenses. One was approved with conditions, and the other was returned without action (2 cases).

In addition, the Departments of Defense and Energy and the Nonproliferation Center also reviewed our sample of 60 non-referred cases. While the Nonproliferation Center had no concerns about any of the non-referred cases in the sample, the Departments of Defense and

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<sup>38</sup>According to 15 CFR 740.1, items that would otherwise require a license are those falling under General Prohibitions One, Two, or Three (Exports and Reexports, Parts and Components Reexports, Foreign-Produced Direct Product Reexports), as indicated under one or more of the export control classification numbers in the Commerce Control List in 15 CFR 774.

Energy expressed some concerns about six of the 60 not referred to them. Two of these cases involved amendments to previous licenses, and four cases raised procedural concerns.

Amendments to existing licenses need interagency review

Two of the 60 export license applications not referred raise concerns because they involved amending original licenses agreed to by the referral agencies. However, BXA did not seek concurrence from the referral agencies who reviewed the original licenses.

The first case dealt with an application to export a work station to be used by a lab in Israel. The application was meant to replace a validated license which had been reviewed and agreed upon by the Missile Technology Export Control Group<sup>39</sup> with the conventional condition of “no missile related end uses.” However, the exporter had failed to notify BXA that the ultimate consignee was a missile division and thus this condition would not be acceptable. BXA informed the exporter to resubmit a new application with this information. According to the LO notes for the newer application, the licensing officer wrote:

“...I was disappointed that there was no expanded end use or reason the condition was not acceptable. When I called the exporter, I was able to reach a compromise with [the exporter] to add a clarifying sentence to the previous case. I had it reopened and approved it with this clarification, rather that (sic) start all over again with agency referrals and lengthy explanations.”

According to BXA management, the “clarification” referenced above was that there should be “no category one missile end use.” BXA decided to reopen the existing, interagency-approved license to modify the condition with this clarification, and returned the new application without action. The Deputy Director of the Defense Threat Reduction Agency stated that the Export Administration Regulations treat amendments to existing licenses as replacement licenses, which should be referred to Defense and any other appropriate reviewing agencies. However, BXA stated it was justified in not referring this case because it was just a clarification of the originally agreed to conditions, not a change in scope. Nonetheless, Defense stated that if Commerce makes substantive changes to licenses, Defense would like the opportunity to review such changes. If the changes are simply grammatical, Defense indicated that it does not need to see them.

Similarly, the second case dealt with an export license application to amend one of the conditions placed on an existing license to export an aircraft navigation system to Taiwan. Specifically, the exporter wanted to add an additional aircraft series onto the existing license. Instead of reopening the existing license in this case, the licensing officer decided to process the new application. The

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<sup>39</sup>An interagency group chaired by State that primarily reviews applications involving items controlled for missile technology reasons.

licensing officer notes indicated that the amendment did not constitute a major change so interagency review was not warranted because all of the other facts in the case remained the same. Therefore, the export license application was approved with conditions without interagency review. Again, Defense believes this case should have been referred to it.

We agree with Defense that these two cases should have been referred. In our opinion, determining what is a substantive change is a subjective process. We believe that whether BXA processes amendments to existing licenses as new applications or reopens the existing licenses, it must ensure that licensing officers refer or consult with the applicable reviewing agencies in order to avoid allegations that its licensing decisions are not transparent.

#### Some non-referred export license applications raise procedural questions

As previously mentioned, BXA indicated it did not refer three export license applications, destined to India, because they fell under the Administration's policy of denial. However, the Deputy Director of the Defense Threat Reduction Agency considered these non-referrals to be procedural oversights. He explained that in 1998, when the President imposed sanctions on India and Pakistan for conducting nuclear tests, the Deputy Assistant Secretary for Export Administration had suggested in writing that, under the presidential sanctions, Defense could delegate to Commerce the authority to deny these license applications outright. However, Defense did not respond to the Commerce suggestion. Thus, in its opinion, it should still continue to receive these applications. While Defense stated that it probably would not have challenged Commerce's decision to deny these cases, Defense believes the proposed transactions would have provided it useful background knowledge. We agree that such license applications should be referred to Defense. We believe that BXA needs to remind licensing officers to reread BXA's referral procedures and to follow them in the future to address the concern expressed by Defense in the license referral process.

In addition, Energy expressed concern about one of the 60 export license applications from our sample. Specifically, the export dealt with repairs and replacements of components to a civilian nuclear power plant in Russia. According to BXA, this application was not referred because it believes that such plants fall under the International Atomic Energy Agency<sup>40</sup> safeguards. Since Russia is a member of the Nuclear Safeguard Group, BXA concluded that the items did not require a license and returned without action this application. However, Energy specified to Commerce in a June 5, 1997, memo that applications intended for nuclear end uses or end users should continue to be referred to Energy regardless of the reason for export control. In addition, Energy officials indicated that while they do not necessarily have a concern with the shipment

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<sup>40</sup>The International Atomic Energy Agency serves as the international inspectorate for the application of nuclear safeguards and verification measures covering civilian nuclear programs. In 1962, the United States transferred safeguards responsibilities for its own bilateral nuclear export agreements to IAEA. With Soviet support, IAEA became the first international inspection system supported by both the East and the West.

itself, it believes that Commerce should have referred the export license application for its evaluation per the executive order. We agree that such license applications should be referred to Energy. We believe that BXA needs to remind licensing officers to reread BXA's referral procedures and to follow them in the future to address the concern expressed by Energy in the license referral process.



In its written response to our draft report, BXA agreed with our recommendation to instruct its licensing officers to follow BXA's referral procedures, and refer all appropriate license applications including amendments. BXA said it will consider issuing new guidance requiring that they be routinely referred. However, we disagree with BXA's assertion that our review demonstrated that "in every case BXA made the correct decision" with respect to referring export license applications to the appropriate agency.

In fact, our review demonstrates that 6 of the 60 non-referred cases from our sample should have been referred to either Defense or Energy. As our report discusses, 2 of the 6 export license applications not referred raised concerns because they involved amending original licenses agreed upon by the referral agencies, but BXA did not seek concurrence from the referral agencies who reviewed the original licenses. In addition, three non-referred applications were considered to be procedural oversights by Defense, and a fourth was considered to be a procedural oversight by Energy. With respect to the different opinions of BXA and the Defense Threat Reduction Agency on the referral of applications denied under the India and Pakistan sanctions, we recommend that BXA and Defense clarify referral procedures for applications that are generally denied under Administration policy.

***B. Review of export license applications by the intelligence community is limited***

The Director of Central Intelligence is responsible for directing the Central Intelligence Agency as well as coordinating the diverse activities of all U.S. intelligence agencies. The intelligence community refers collectively to those Executive Branch agencies and organizations (e.g., the Departments of Defense, Energy, and State) that conduct the varied intelligence activities that make up the total U.S. national intelligence analysis effort. According to the Central Intelligence Agency, the primary objective of intelligence analysis is to minimize the uncertainty with which U.S. officials must grapple in making decisions about American national security and foreign policies.<sup>41</sup>

However, we found that the intelligence community has not been fully engaged in the export licensing process, which could lead to the licensing of dual-use commodities to unsatisfactory end

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<sup>41</sup>Central Intelligence Agency Home Page.

users. Specifically, we found that (1) the Central Intelligence Agency, at its own request, does not review all dual-use export license applications, (2) the Nonproliferation Center does not always conduct a comprehensive analysis of export license applications it reviews, and (3) the intelligence community agencies are conducting only a limited assessment of the cumulative effect of dual-use export licenses issued. We would encourage BXA to open up discussions about these apparent weaknesses in the dual-use licensing process with not only the Director of the Nonproliferation Center but the Director of the Central Intelligence Agency as well.

#### CIA's review of dual-use export license applications

In September 1991, the Central Intelligence Agency established the Nonproliferation Center to be the focal point for all intelligence community activities related to nonproliferation.<sup>42</sup> The Nonproliferation Center is responsible for supporting the dual-use export licensing process by providing license reviewing agencies with intelligence information on potential end users. However, according to a 1995 Memorandum of Understanding (MOU) between the Nonproliferation Center and BXA, the Nonproliferation Center does not review those items or end users which fall outside its nonproliferation mission or commodities which are generally available and not likely to make a difference in proliferation. As a result, only 45 percent of all dual-use export license applications disposed of in fiscal year 1998 received any input from the Nonproliferation Center and subsequently the Central Intelligence Agency.

While the remaining 55 percent of applications not reviewed by the Nonproliferation Center are those to which the Nonproliferation Center believes it cannot add any value, we question why these applications—which are controlled for national security and foreign policy—are not reviewed by any other Central Intelligence Agency units (e.g., its regional offices). According to its web site, the CIA “...has unique analytic capabilities that exist nowhere else inside or out of government.” Since, the export licensing agencies rely on intelligence information as part of their decision-making process for determining whether an export license application should be approved or denied, we believe it is imperative that the reviewing agencies have access to all appropriate intelligence information for all appropriate export license applications in order for them to make the most informed decision. We would encourage BXA to engage in discussions with the Central Intelligence Agency on this important matter.

#### More detailed intelligence information would be helpful for licensing decision making

We found that the substance of intelligence information provided by the Nonproliferation Center on the applications it reviews varies from case to case. Specifically, some of the Center's reports, known as trade reviews, appeared to provide very thorough and detailed information, while other trade reviews reported, “No comment.” From our licensing officer questionnaire, we received 19 responses with regard to our question of whether BXA LOs have enough information from the

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<sup>42</sup>Internet web address: <http://www.odci.gov/cia>.

Nonproliferation Center to make a reasonable license determination. Among the flaws cited by licensing officers in the information provided by the Nonproliferation Center were:

“Intelligence community data is historic and has not been updated in most cases and while it may reflect the activities of past years it may not reflect present conditions.”

“The Nonproliferation Center tends to focus on very limited activities, rather than looking at the full structure and functions of the end users.”

“Sometimes they [do] not research the end user fully...”

“The Nonproliferation Center end user reports are based on dated intelligence, drafted in language which raises inferences concerning certain activities which suggest proliferation in nuclear, missile, or CBW, but are not relevant to the transaction under review...Increasingly, the Nonproliferation Center end user intelligence reports do not attempt to assess what such dynamic economic or restructuring changes may mean in light of earlier inferences of activities which may have raised proliferation concerns.”

“Greater access to intelligence (perhaps through on-line capability), a more timely response and better quality of analysis would help.”

“The Nonproliferation Center information is late, incomplete, and not definitive. This is a major complaint from all licensing officers.”

In addition, licensing officers reported that in those cases where the Nonproliferation Center provides substantial information, the referral agencies interpret the information differently. To alleviate this problem, one BXA official recommended that the Center’s analysts “rate” the risk of diversion or use in a proliferation project on some kind of quantitative (0-10) or qualitative (high, moderate, low) scale, thereby giving BXA’s licensing officers and referral agencies a better idea of the likelihood of diversion.

While the Nonproliferation Center disagrees with most of the characterizations made by the licensing officers, noting that BXA does not understand “intelligence” information, we believe that the Nonproliferation Center—and the Central Intelligence Agency as a whole—could potentially provide more information to the licensing process (i.e., *routinely* seeking licensing-related information from analysts in the regional offices who specialize in particular countries). Furthermore, we believe that some export license applications dealing with countries of concern may warrant soliciting information on particular foreign entities from overseas posts.

During our review, we identified other factors that may be hindering the Nonproliferation Center analysts from conducting a more comprehensive search, including a lack of time to perform their reviews and a lack of resources.

***Nine-day time frame is inadequate for review by the Nonproliferation Center***

Currently, the Nonproliferation Center has nine days to conduct its review of end users for export license applications. The intent behind this short time frame (as compared to the 30 days provided to the other referral agencies) is to enable BXA licensing officers the opportunity to review the intelligence information prior to referring the export license application to the reviewing agencies with their recommendation.

Based on our referred sample of 179 export license applications, 82 of these applications were referred to the Nonproliferation Center. Of these, approximately 50 percent took longer than nine days for the Nonproliferation Center to respond. Twenty-five of these applications, destined to China and India, took an average processing time of 23 days. Nonproliferation Center officials informed us that nine calendar days to review end users is not enough time, particularly for countries of concern like China and India. Several licensing officers indicated to us that they would rather have the Nonproliferation Center take additional time to provide a trade review report with more details on the end user or end use than one that reports "No comment." Therefore, we believe that BXA should work with the Nonproliferation Center to establish a more realistic time frame for its review of end users especially in countries of concern.

***Nonproliferation Center has resource constraints***

While the Central Intelligence Agency's OIG is addressing the shortage of analysts in the Nonproliferation Center licensing branch in its report on the export licensing process, we believe there is another factor contributing to its resource constraints. Specifically, the Central Intelligence Agency OIG determined that BXA was unnecessarily referring some export license applications to the Nonproliferation Center contrary to the 1995 and 1997 conditions outlined in the interagency agreement between the two agencies.

According to senior BXA officials, its licensing officers were provided guidance describing the referral policy for the Nonproliferation Center. While it is not an exact copy of the 1995 MOU, we determined that the guidance distributed, *clearly* outlines what is to be referred and not referred. However, we found that not all LOs have a copy of the Nonproliferation Center's 1997 addendum to the MOU which further reduced the number of referral cases. As a result, the Nonproliferation Center claims that it has seen a dramatic increase in the number of end users sent in for review that are contrary to the MOU. During this review, we notified BXA's Deputy Assistant Secretary of this matter and subsequently, a memorandum was issued on April 21, 1999 outlining the Nonproliferation Center's 1997 addendum and the current policy on license applications and end users that should be sent to the Nonproliferation Center for review.



However, Export Administration managers informed us that the MOU does provide some flexibility for licensing officers to refer a particular license application to the Nonproliferation Center if they have concerns about it, even if it normally would not be referred. Export Administration managers further stated that they would rather have the license officers be overly cautious than not when it comes to nonproliferation concerns. We agree with this philosophy; however, we also believe that BXA needs to instruct its LOs to indicate in the license application referral history the reason they believe the Nonproliferation Center should review an end user when it is contrary to the MOU.

#### Cumulative effect assessment for exports of dual-use commodities is needed

Cumulative effect refers to the impact resulting from a proposed export when added to other past exports to a country of concern. A cumulative effect can result from individually minor but collectively significant export actions taking place over time. We found that BXA licensing officers appear to have institutional knowledge about what goods and technologies specific end users or countries are receiving because they tend to process similar export license applications dealing with the same commodities, exporters, and end users over time. However, according to the survey responses from licensing officers, they do not routinely analyze the cumulative effect of proposed exports or receive such assessments to use during license reviews.

On the basis of our review, it appears that the Energy Department's seven laboratories conduct a limited cumulative effect assessment review for nuclear dual-use exports, but there is no coordinated effort to conduct such an assessment for all commodities. In addition, we learned that Defense has a requirement to perform annual assessments of the total effect of transfers of goods, munitions, services, and technology on U.S. security, but it had not yet performed such reviews. Therefore, we believe that BXA should work with the intelligence community, including both Defense and Energy, as well as the CIA, in developing some sort of mechanism to analyze and track this cumulative effect of dual-use exports to specific countries and regions.



In its written response to our draft report, BXA agreed with our recommendation to engage in discussions with the Director of the Central Intelligence Agency to seek ways to strengthen the role of the intelligence community in the export licensing review process, including (1) referring all appropriate license applications, (2) performing risk assessments on end users, and (3) obtaining more detailed intelligence information. However, BXA deferred to the intelligence community on the costs and feasibility of implementing our recommendations. BXA also stated that it would reiterate its current guidance for documenting the reasons why referrals are made to NPC when the established guidance would normally preclude referral.

In addition, while BXA did not disagree with our recommendation to establish a more realistic time frame for the NPC's review of end users in countries of concern, it stated that additional time

for review must be reconciled with the competitive realities that U.S. exporters face and their need for prompt decisions from the government. While we understand that U.S. exporters face strong competition in the world today and deserve prompt decisions from the government, we do not believe that this should be done at the expense of national security. In addition, providing additional time for NPC does not necessarily mean that exporters will be delayed. Considering the current resource constraints at the NPC, we reaffirm our recommendation that BXA work with NPC to establish a more realistic time frame for its review of end users in countries of concern, when necessary.

Finally, BXA agreed that tracking and assessing the cumulative effect of dual-use exports are desirable but difficult to do. It further stated that since cumulative effect results not only from the transfer of items under approved licenses, but also as the result of the provision of items not requiring a license and shipments from foreign suppliers that would not be caught by our licensing system, it believes that the assessment of cumulative effect should be made in the multilateral list review process (e.g., Wassenaar Arrangement) instead of on each individual license application. While we maintain that tracking and assessing the cumulative effect for proposed exports to certain countries are critical, we also believe that conducting this type of assessment during the list review process could be advantageous.

Nevertheless, BXA's response stated that it agreed with our overall position and indicated that it has included as part of its 2001 budget request the resources that it would need to conduct such assessments. We also want to reiterate the importance of BXA working with the intelligence community in developing any mechanism to analyze and track this cumulative effect of dual-use exports.

### **C. Concerns are raised about the Department of State's ability to review cases**

One shortcoming identified in the 1993 special interagency OIG report on the export licensing process was unnecessary delays caused by referral agencies in processing of applications. Executive Order 12981 addressed this by holding agencies accountable for delays. Specifically, it states that within 30 days of receipt of a referral and all required information, a department or agency shall provide the Secretary with a recommendation to either approve or deny the license application. A department or agency that fails to provide a recommendation within 30 days shall be deemed to have no objection to the Secretary's decision. In our opinion, the executive order time limit is adequate for agencies to conduct their reviews. If any additional information is necessary, any agency can "stop the regulatory clock" by simply posing relevant questions for the applicant or other sources (e.g., pre-license check). There is no limit on the number of questions that can be posed or the time available to answer them.

Commerce relies on the various referral agencies for their expertise in foreign policy, national security, and nonproliferation matters to determine the potential risks of exporting sensitive commodities to specific end users. However, if an agency does not respond within the mandated 30 days, its position need not be taken into account.

When the referral agency does not respond to a license application in the specified time period, the application is automatically “pulled back” from the agency.<sup>43</sup> Of our sample of 179 referred export licenses from the period January 1 through June 30, 1998, we found that three of the four referral agencies experienced some “pullbacks.” Table 3 illustrates the total number of cases referred to each agency, the number of cases pulled back, and the percentage of cases pulled back. Among the three agencies, State had the greatest number of pullbacks in the sample.

Within the State Department, Office of the Under Secretary for Arms Control and International Security, Bureau of Political Military Affairs, there are three groups that review dual-use license applications: (1) the Office of Export Controls and Conventional Arms Nonproliferation Policy reviews export license applications for encryption products, deemed exports, supercomputers, and electronic devices; (2) the Office of Chemical, Biological, and Missile Technology reviews export license applications for chemical, biological, or missile commodities; and (3) the Office of Nuclear Energy Affairs reviews export license applications for dual-use nuclear commodities. A fourth group, the Office of Energy Sanctions and Commodities, in the Bureau of Economic and Business Affairs, reviews export license applications for crime control commodities. The Office of Export Controls and Conventional Arms Nonproliferation Policy receives approximately 50 percent of all dual-use licenses referred. Based on our sample, this office reviewed 91 out of the 153 cases referred to the State Department and failed to respond on 24 percent of those cases, although the overall pullback rate for all State Department referrals was approximately 12 percent.

**Table 3: Sample of Export License Applications Pulled Back from Referral Agencies**

<b>Referral Agency</b>	<b>Total Referred Cases</b>	<b>Number of Cases Pulled Back After 30 days</b>	<b>Percentage of Cases Pulled Back</b>
<b>State</b>	153	19	12.4%
<b>Energy</b>	56	2	3.6%
<b>Defense</b>	172	3	1.7%
<b>ACDA</b>	97	0	0

**Source:** Office of Administration, Bureau of Export Administration.

We raised this issue with an official from that office who informed us that there was only one licensing officer assigned to handle all of the dual-use license applications referred to this office. This individual is also State’s representative to the Operating Committee and must handle all of

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<sup>43</sup>While BXA can technically proceed with processing the application, in the past its LOs have occasionally sent the case back to the applicable agency to ensure that there were no concerns.

those cases as well. Thus, we believe a major reason for the number of State's "pullbacks" is a lack of resources devoted to looking at these export license applications. Upon discussing our concerns with State's Office of Inspector General team, we learned that as a part of ACDA's dissolution, one of its personnel will be assigned to this office to help with its export license application review. We believe this should help resolve the resource issue in the Office of Export Controls and Conventional Arms Nonproliferation Policy; however, we encourage BXA to periodically check State's pullback record to monitor this situation.



In its written response to our draft report, BXA agreed to periodically review State's pullback record to monitor this situation. However, it also noted that since State has requested to review certain cases under the Executive Order, it is incumbent on that agency to determine how to meet its own responsibilities. We agree.

**D. License applications should be screened against Customs Service's TECS database**

While the export licensing process is clearly more transparent today than it was in 1993, we believe that one key element is missing from this process—the screening of all parties to pending license applications against the Treasury Enforcement Communications System (TECS) database maintained by the Treasury Department's U.S. Customs Service. TECS was created to provide multiagency access to a common database of enforcement data supplied by the participating agencies, such as Customs, the Drug Enforcement Administration, and the Bureau of Alcohol, Tobacco, and Firearms. Screening every applicant and consignee against TECS during the initial phases of the licensing process would give licensing and enforcement authorities early warning of any potential concerns Customs may have. We first identified this weakness in the licensing process in 1996, and again in 1997, during our reviews of BXA's Watchlist.<sup>44</sup> While BXA agreed with our overall conclusion that it is important for policy-makers to have all information available to them in order to reach a licensing decision, it disagreed with our recommendation to screen all parties to export license applications against TECS.

According to Section 12(c)(3) of the 1985 amendments to the Export Administration Act, Commerce has the authority to refer pending export license applications to Customs. Specifically it states: "The Secretary [of Commerce] and the Commissioner of Customs, upon request, shall exchange any licensing and enforcement information with each other which is necessary to facilitate enforcement efforts and *effective license decisions*." [Emphasis added.]

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<sup>44</sup>Report to the Congress on the Department of Commerce's Export License Application Screening Process (IPE-8647), September 1996 and *Export Application Screening Process Could Benefit from Further Changes* (IPE-9524), September 1997.

In addition, Executive Order 12981 clearly states that “the Secretary may refer license applications to other United States Government departments or agencies for review as appropriate.” We are not suggesting that Customs make licensing recommendations as do the existing referral agencies, but we do believe that both the law and executive order authorize Commerce to exchange names of parties associated with pending licenses with Customs in the initial phases of the licensing process to give BXA licensing and enforcement authorities early warning of any potential concerns Customs may have. Again, TECS was created to provide multi-agency access to a common database of enforcement data to satisfy a recognized need to promote the sharing of sensitive information between federal law enforcement agencies. Furthermore, since the intelligence community is unable to collect information on U.S. citizens or companies, it is also unable to collect information on U.S. subsidiaries overseas, even in countries of concern. However, Customs *is* allowed to collect such information which it stores in TECS, thereby giving BXA another valuable source of information to check export application parties against.

As the agency with the ultimate responsibility for issuing U.S. dual-use export license applications, we believe BXA has an obligation to take every precautionary measure to ensure that all potential export enforcement concerns within the U.S. government are considered before issuing a license. By not doing so, it leaves itself and the Secretary of Commerce vulnerable to criticisms of making licensing decisions based on incomplete information.

We therefore reaffirm our recommendation that BXA work with Customs to provide for the transmission of names, addresses, and telephone numbers from pending license applications to Customs for screening against TECS for at least a two-year trial period. This will enable the agencies to determine if TECS can add valuable information to the screening process.

#### Customs involvement in BXA’s current license application screening process

Under the 1993 MOU between BXA and Customs, Customs receives a daily tape of ECASS licensing data for all cases approved, denied, or returned without action, which Customs then enters into TECS. This information is supposed to be available for Customs’ enforcement personnel in the field (e.g., an inspector at a U.S. port) to check the validity of certain export shipments. However, we learned during our current review that this has not happened.

In addition, the MOU allows Customs to add to BXA’s watchlist any derogatory or adverse information about the suitability of a party to participate in an export transaction involving dual-use, U.S.-origin goods or technology. The procedures, as laid out in the MOU, are as follows:

- A Customs special agent recommends, through Customs headquarters, that BXA’s Office of Enforcement Analysis (OEA) place on BXA’s screen the name of a party in which the agent has an enforcement interest.
- OEA places the name on the screen. The name is now “flagged.”

- A license application is received by Export Administration and is entered into ECASS.
- The application contains the name of a party of concern to the Customs special agent; for example, the ultimate consignee.
- ECASS matches the license application to the name on the screen. This is often referred to as a “screen hit.”
- ECASS refers the license application to OEA’s queue. The license is held in this queue until the enforcement concern is resolved. The license cannot be approved until OEA lifts the “flag.”
- OEA notifies the Customs headquarters contact of the screen hit and provides this contact a copy of the relevant license application. Customs provides to OEA any derogatory information Customs may have on the license application in question.
- If Customs does not respond to OEA’s notification within four working days, the OEA lifts the flag and releases the application to Export Administration for normal processing, based on the assumption that Customs has no information to prevent Export Administration from considering the application on its merits.
- If Customs believes it has information that would support a negative licensing action, for example, a rejection of the application by Export Administration in order to prevent a possible violation of the Export Administration Regulations, Customs provides the information to the OEA.

However, as we stated in 1996 and again in 1997, we believe the screening process can be easily expanded to incorporate the screening of parties to pending license applications against TECS.

#### Enhancing the current license application screening process

As a result of the technological improvements in the direct cable connection between BXA’s and Customs’ mainframes in recent years, we believe the screening of pending license applications against TECS is much more feasible. BXA can more easily download a daily transfer of application information from BXA to Customs if sent during off-peak hours, such as at night. As a result, we believe that BXA can readily screen TECS and not slow its normal export license process. As we suggested in 1997, we propose that BXA adopt the following, or similar, procedures for accomplishing this task:

- License applications are received by Export Administration and automatically entered into ECASS.

- Each night, ECASS would be programmed to create a batch file of all parties, including addresses and phone numbers, associated with the new pending applications for that day.
- The file would be electronically sent to Customs via the hard-line access to TECS and then automatically screened against the database, or those portions of the database that BXA and Customs have agreed are relevant.
- TECS is set up to automatically notify a Customs agent if there is a screen hit on any parties the agent may have flagged. Thus, if there is a screen hit in TECS for any of the parties sent over from BXA, the agent would be notified.
- In the interim, Export Administration would continue to process the license application.
- If Customs has information that might support a negative licensing action, such as a rejection of the application by Export Administration in order to prevent a possible violation of the Export Administration Regulations, Customs would provide the relevant information to OEA within four working days of the screen hit.
- If Customs does not provide derogatory information to BXA within four working days, the license application will continue through its normal processing, based on the assumption that Customs has no information to prevent Export Administration from considering the application on its merits.

Like the current procedures providing for Customs' involvement in adding parties to the watchlist, this proposal puts the onus on Customs to notify BXA of any derogatory information. However, under these procedures, BXA will be able to take additional precautionary measures to ensure that all enforcement concerns are addressed.

BXA's justification for not implementing our recommendation is not warranted

In responding to our draft report in 1997, BXA disagreed with our recommendation to screen all parties against TECS. Specifically, its response argued that "to refer all license applications to Customs for review in TECS effectively makes Customs a referral agency. This would not be consistent with the President's goal to streamline the export licensing process as expressed in [Executive Order 12981]."

We do not believe that the additional screening of parties against TECS is inconsistent with Executive Order 12981, which states that "the Secretary may refer license applications to other United States Government departments or agencies for review as appropriate." In our opinion, this provision clearly provides the authority for BXA to exchange pending license application information with Customs. We note that the executive order does not specifically provide for Commerce to refer license applications to the intelligence community, but BXA does so because it makes sense.

Second, BXA argued that “[Executive Order 12981] responded to the needs and concerns of American exporters by ensuring that strict standards and deadlines are imposed on the review and escalation of cases.” We agree. However, our proposal gives Customs a four-day time period (the established time frame under the current MOU) in which to notify BXA of any enforcement concerns. The four-day time frame is also compatible with the application processing times established by Executive Order 12981. If Customs reports back to BXA within the four-day time frame that it has an enforcement concern regarding a particular party, we do acknowledge that the processing time for that application may be extended to address the enforcement concerns. However, this is the current practice for applications in which Customs and/or Export Enforcement agents have concerns. We believe that this process is consistent with the executive order and that it was not the President’s intent to streamline export controls at the expense of national security.

Third, BXA’s 1997 response indicated that this important issue should be discussed within the MOU framework between Customs and BXA at its quarterly meetings. BXA stated that it would remind Customs of its obligation to provide BXA with the relevant information that can be used to screen license applications. BXA contends that it is Customs’ responsibility to provide its enforcement concerns to BXA—not BXA’s responsibility to provide all pending license applications to Customs. Yet it took from October 1997 until February 1999 for Customs to provide BXA with two diskettes, one containing business names and one containing individual names. While there were approximately 3,500 business names provided on the one diskette, the second diskette containing individuals’ names was unreadable. As of March 1999, BXA systems personnel informed us that none of this information has been imported into ECASS.

However, if all parties to pending license applications were run against the TECS database, the issue of Customs not providing BXA the names of parties about which Customs has an enforcement concern is a moot point. Under our proposal, these parties will automatically be identified during the screening process against the TECS database. If there is a “hit” and a party is flagged, the appropriate Customs agent will automatically be notified that a party they were monitoring has applied for an export license. The Customs agent will then have to make a decision as to whether there is enough derogatory or adverse information on the party to notify BXA about Customs’ concerns with that license application.



In its written response to our draft report, BXA disagreed with our recommendation to update the 1993 MOU between BXA and Customs to provide for TECS screening of pending license applications. BXA contends that since our 1997 report to BXA on this issue, Customs has provided BXA with data to add to its watchlist and therefore does not believe that our alternative solution is necessary.



However, since we first identified this weakness in the licensing process in 1996 and again in 1997 during our reviews of BXA's Watchlist, we have not seen any real improvement in this process. In fact, it took from October 1997 (the date of our last watchlist report) until February 1999 (during this review) for Customs to provide BXA with two diskettes—one of which was unreadable. As of June 1999, BXA systems personnel informed us that none of this information has been imported into ECASS due to other priorities.

Screening every applicant and consignee against TECS during the initial phases of the licensing process would give licensing and enforcement authorities early warning of any potential concerns Customs may have. We reiterate that as the agency with the ultimate responsibility for issuing U.S. dual-use export license applications, we believe BXA has an obligation to take every precautionary measure to ensure that all potential export enforcement concerns within the U.S. government are considered before issuing a license. By not doing so, it leaves itself, the Secretary of Commerce, and the Administration vulnerable to criticisms of making licensing decisions based on incomplete information. We do not understand why BXA has not implemented this three-year-old recommendation since the problem is not fixed.

Since it appears that the only time BXA proactively seeks any names from Customs is when we are conducting a review in this area, we reaffirm our recommendation that the 1993 MOU between BXA and Customs be updated to allow the screening of all parties to pending license applications against TECS.

***E. Some licenses were issued without meeting conditions of Department of Defense***

During this review, we reviewed 331 PLCs listed on an October 1998 ECASS printout that were completed or canceled during fiscal year 1998. Of the 56 PLCs canceled, four were part of conditional approvals from Defense, pending favorable outcomes of the checks. Although the PLCs were canceled and never conducted, BXA approved all four license applications with conditions without notifying Defense that their condition could not be met. The locations and the reasons given by BXA for these four canceled PLCs are shown in Table 4.

**Table 4: PLC License Conditions Canceled by BXA**

<b>Destination</b>	<b>Date of Defense Conditional Approval</b>	<b>Date License Approved by BXA</b>	<b>Reason for Cancellation of PLC</b>
<b>India</b>	06/03/97	12/04/97	Post was unable to reply in a timely manner.
<b>Syria</b>	09/10/97	12/25/97	Post was unable to reply in a timely manner.
<b>Russia</b>	04/17/98	05/30/98	Cost was prohibitive; PLC canceled by headquarters.
<b>China</b>	09/15/98	10/21/98	PLC could not be initiated without an end use certificate; PLC canceled by headquarters. <sup>45</sup>

**Source:** Office of Enforcement Analysis, Bureau of Export Administration.

According to the Deputy Director of the Defense Threat Reduction Agency, Defense expects to be notified when a PLC is canceled if it was a condition of its approval for a license. In his opinion, these four cases were important, and Defense might have reversed its decision if it had known that the PLCs had been canceled. We believe BXA should discuss the Defense Threat Reduction Agency's concerns with these four cases. We also believe that BXA should immediately notify any referral agencies which conditioned approvals of licenses with favorable PLCs if the PLCs are canceled and obtain the agency's concurrence to proceed with closing out the license.



In its written response to our draft report, BXA agreed with our recommendation to notify referral agencies when pre-licensing checks (which were licensing conditions) are canceled.

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<sup>45</sup>Licensing officer notes state, "Applicant to provide to DOC with documentation that the end user exists. When this info is provided, we'll cancel the PLC - this agreement was reached between the LO & ... of DOD on 9/15/98." However, there is no indication in the ECASS record that this information was submitted.

## V. Dispute Resolution Process Gives Referral Agencies Meaningful Opportunity to Escalate Licenses

Executive Order 12981 established mandatory escalation procedures for all dual-use export license applications involving interagency disputes and refined the time lines for this process. There are four levels of escalation for dual-use cases: Operating Committee at the senior civil service level, Advisory Committee on Export Policy at the assistant secretary-level, Export Administration Review Board at the Cabinet level, and the President. Each level of the escalation process is required to consider all matters referred to it, giving consideration to foreign policy, national security, and domestic economy concerns as well as concerns about the proliferation of weapons of mass destruction.

Overall, we found that the interagency escalation process for disputed license applications allows officials from dissenting agencies a meaningful opportunity to seek additional review of such cases. From fiscal years 1991 to fiscal years 1998, the number of cases escalated to the OC increased by 353 percent, but the number of cases escalated to the ACEP decreased by 62 percent. (See Table 5.) The fact that the number of cases escalated to the OC has increased, while the number of cases escalated to the ACEP has decreased, indicates to us that this process is working well.

**Table 5: Number of Export License Applications Escalated Fiscal Years 1991 - 1998**

Fiscal Year	Export License Applications Received	OC	ACEP	EARB
1991	33,118	169	89	20
1992	24,071	333	105	0
1993	26,125	493	142	0
1994	12,609	281	97	0
1995	9,988	161	68	0
1996	8,710	435	71	0
1997	11,480	784	38	1*
1998	10,696	766	34	0

\* Although this case was escalated to the EARB, the EARB never convened. Subsequently, the final vote on this case defaulted to the ACEP majority vote of approval with conditions.

Source: Office of Administration, Bureau of Export Administration.

However, we did identify several areas that need management attention, including (1) the need to clarify the OC Chair's objectivity, (2) agency delegations of authority cause delays at OC, and (3) the process of returning escalated cases eliminates quality control.

**A. *Operating Committee is effective but some matters need attention***

When the reviewing agencies do not agree on a final disposition of a license application, the case is escalated to the Operating Committee. The Department of Commerce serves as the OC Chair. The voting members of the OC are the Departments of Commerce, Defense, Energy, Justice (for encryption cases), and State, and the Arms Control and Disarmament Agency. Representatives of the Director of the Central Intelligence Agency and the Chairman, Joints Chief of Staff, are nonvoting members.

The OC meetings are held weekly. Based on the three OC meetings we observed, we found that the OC Chair affords each agency—including BXA—the opportunity to present its recommendation on every application. We generally found that the meetings build consensus through healthy exchanges and debates. The OC Chair has been given the authority to decide all cases at this level without having to reflect the recommendations of the majority of the participating agencies.<sup>46</sup> Thus, agencies must justify their positions or risk being overruled.

However, we found that the decisions of the Chair are usually based on interagency consensus. Specifically, only about five percent of the OC decisions decided by the Chair are contrary to the majority decision, and virtually all of these cases were escalated to the ACEP for a final decision. BXA records indicate that of the 70 cases escalated to the ACEP between February 1997 and February 1999, only 6 actually overturned the chair's decision.

We examined 26 of the 266 cases escalated to the OC during the period January 1, 1998 through June 30, 1998. Of the 26 cases, 3 were settled before the OC meeting, 20 were approved with conditions, and 3 were denied. (See Table 6.) Two of the 26 OC cases were escalated to the ACEP, and they were both unanimously approved with conditions (although the ACEP revised the conditions approved by the OC). We determined that the positions put forward initially by agencies are preliminary, and the information assembled at the OC generally satisfies their concerns. In addition, we found that typically agencies who maintain a denial, but do not wish to escalate the case to the ACEP, often play a key role in crafting the conditions placed on the approved licenses. In many cases, individual agency concerns are addressed by adding or modifying license conditions.

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<sup>46</sup>However, the Executive Order does require a majority vote decision in the case of license applications for commercial communication satellites and hot-section technologies.

**Table 6: OC Decisions from OIG Sample Cases**

Approved With Conditions (20)			Denied (3)		
Majority	Unanimous	DTRA voted to deny*	Unanimous	Majority	BXA voted to approve
18	13	14	1	2	2

\*As mentioned in the text above, Defense only escalated 2 of the 14 cases to the ACEP. The destination for the 14 licenses included Canada (1), China (2), India (4), Israel (3), Russia (3), and Sweden (1).

**Source:** ECASS printouts of OC license histories.

A notice of the Operating Committee license decision is sent to the designated person in each participating agency. Any decision not escalated to the ACEP by a dissenting agency within five days of the notification of the decision will become final.

Objectivity of OC Chair is critical

Authority for handling encryption export policy and licensing was transferred from the Department of State to the Department of Commerce in 1997. Executive Order 12981 was amended on November 15, 1996, by Executive Order 13026, “Administration of Export Controls on Encryption Products,” to allow for Justice to review any export license application submitted to Commerce and be a voting member of EARB and ACEP, and a full member of the OC, with respect to such encryption products. Defense’s Defense Threat Reduction Agency also delegated its review authority for export license applications for certain export control classification numbers subject to “Encryption Item” controls to the National Security Agency.<sup>47</sup> However, the Defense Threat Reduction Agency maintained its sole authority for providing the Defense recommendations and votes at the OC and ACEP.

During this review, both Justice and the National Security Agency raised concerns about the objectivity of the OC Chair with regard to encryption export license applications. While both agencies believe the OC Chair is doing a good job, they believe she is under pressure to promote trade over national security with regard to these exports. According to the National Security Agency and Justice officials, these concerns stem from the fact that the OC Chair has indicated to them that any OC decisions written in the passive voice (e.g., “It has been decided....” versus “The Chair determines....”) can be interpreted to mean that BXA management told her how to decide a case and, therefore, it was not “her” decision.

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<sup>47</sup>The National Security Agency was established by Presidential directive in 1952 as a separate agency within Defense under the direction, authority, and control of the Secretary of Defense.

After sitting down with National Security Agency officials to go over the six export license applications that they believed raise questions about the OC Chair's independence, we determined that the cases were handled properly. Specifically, five of the licenses dealt with end users in Germany, Finland, Japan, Sweden, and the United Kingdom. The remaining one dealt with end users in 43 different countries. All six license applications were approved by the OC Chair, and none is written in the passive voice. In addition, of the five cases escalated to the ACEP by Defense, three were approved by an unanimous decision at that level, while a fourth was approved by a majority decision (with the exception of Defense, which maintained its denial). The final license application was returned without action because the exporter lost the sale to a European competitor and no longer needed an export license. When asked, the OC Chair did not indicate that there was a problem with these cases.

National Security Agency officials later provided us with an OC license decision written in the passive voice. After reviewing this case, we determined that *all* of the participating OC agencies approved the license application with conditions formulated by Justice (including Defense/National Security Agency) except Commerce. While Commerce agreed with most of the conditions, it did not agree with Justice's recommendation to exclude two countries (Chile and the Czech Republic) from the end user list. The OC license decision reflects the Commerce position, which was to approve the license with all of Justice's conditions except the one excluding these two countries. Having said that, the procedures outlined in the Executive Order 12981 allow the OC Chair to overrule the majority and decide the final disposition of the case unilaterally. In addition, as noted previously, no matter what the OC's license decision was for this case, all agencies (including the National Security Agency and Justice) had the right to escalate this case to the ACEP. None of the agencies escalated the case even though at least one of them had concerns about the two countries it wanted to exclude as a recipient of this product.

When we questioned the OC Chair about these allegations, she confirmed that she writes in the passive voice when she believes management has told her how to decide a case. However, she also indicated that this is a rare occurrence and generally it involves a situation where she believes more information is needed about the transaction before a final decision can be made. We discussed this issue with both the Assistant Secretary for Export Administration and his deputy, who informed us that they have never "told" the OC Chair how to vote on a particular case but stated they may have instructed her or provided her guidance as to the applicable policy for a particular export transaction—especially since the export control policies for encryption items are constantly changing to reflect advancement in technologies—in an effort to expedite the license decision. By doing so, they indicated that they wanted the referral agencies to escalate the case to the ACEP in order to force a policy discussion on them. In theory, policy decisions made at the ACEP are supposed to set precedents for similar export license applications in the future.

Our review indicated that the OC plays a pivotal role in the export licensing process. Overall, we heard only positive feedback about both the committee and its Chair. In addition, we were impressed with the OC Chair's willingness to stand firm on the licensing decisions she makes. For

instance, in one recent case, the OC Chair approved a license with conditions over the objections of all of the participating agencies—including BXA. While the case was escalated to the assistant secretary-level ACEP, it illustrates that the OC Chair does not give in easily if she firmly believes in her decision.

Nonetheless, no matter what the rationale is, we believe that the OC Chair should be free to independently decide a case. If the OC Chair makes a decision that BXA disagrees with, BXA should escalate the matter to the ACEP as allowed by the executive order. BXA management should definitely not give the impression that it is instructing the OC Chair on what licensing decisions to make. We encourage BXA to use the avenue afforded it under the executive order to escalate cases to the ACEP in order to avoid any misconceptions that this part of the process is not transparent.



In its written response to our draft report, BXA did not address our recommendation to ensure that it uses the avenue afforded it under the Executive Order to escalate cases to the ACEP in order to avoid any misconceptions that this part of the process is not transparent. However, it did state that both the Assistant Secretary and the Deputy Assistant Secretary have a responsibility to ensure that the OC Chair carries out her responsibilities efficiently and in concert with U.S. regulations and policy. As a result, the response indicated that from time to time, those BXA management officials have instructed the OC Chair on the provisions of the regulations or on changes in U.S. licensing policy to ensure that her actions are consistent with USG rules and policies or to bring a case review to closure by making a decision (e.g., where the loss of a sale is imminent or a case has exceeded the time frames of the Executive Order).

We agree with BXA's statement that our review did not find significant problems with management influence over the vote of the OC Chair. However, we also believe that one could interpret the role of the OC Chair as outlined in the Executive Order to be "independent" since the procedures call for the OC Chair to preside over the OC meeting and listen to all of the reviewing agency arguments—including BXA's—before rendering a decision on a case. Nonetheless, we do recognize that the OC Chair is a BXA employee and that the Executive Order recognizes that an OC decision is a Commerce decision that can be escalated by a dissenting member agency. However, we strongly believe that the main reason the OC review process is so successful is because of the current OC Chair's willingness to be objective in her decisions and not necessarily just vote the "Commerce" position. As a result, the OC Chair's decisions are usually based on interagency consensus.

#### Agencies That Have Given DOAs to BXA During Initial Review Cause Delays at OC

Many LOs and managers in BXA have raised a concern about agencies that provide BXA a Delegation of Authority (DOA) in the initial referral process but reserve their right to review and

vote on these same export license applications in the dispute resolution process. BXA's concerns stem from the fact that since these agencies are not involved in the "debate" early on, they are not familiar with the details of the case and subsequently hold up the licensing process in order to essentially get caught up. As a result, it often takes two to three OC meetings to reach a decision on such cases.

We discussed this issue with Energy licensing officials since they have provided a DOA for most applications that do not involve nuclear end users or end uses. While they understand the frustration of BXA, they believe that if a case is to be decided at a higher level, they feel an obligation to participate. Nonetheless, they are working on expanding Energy's review of applications, and they believe this will work toward correcting the problem. We encourage BXA to work with those agencies which have provided DOAs to find a way to expedite late reviews by these agencies.



In its written response to our draft report, BXA agreed to work with the advisory agencies that have delegated authority to BXA during the initial review of a case to expedite reviews by these agencies if escalated to the OC so that cases are not unnecessarily delayed.

***B. Advisory Committee on Export Policy is working well***

Any request for ACEP review must be signed by an official of the requesting agency who was appointed by the President, with the advice and consent of the Senate. The Assistant Secretary for Export Administration serves as the Chair of the ACEP. The ACEP voting members also include the designated Assistant Secretaries or equivalent officer of the Departments of Commerce, Defense, Energy, Justice (for encryption cases), State, and ACDA. Representatives of the Director of the Central Intelligence Agency and the Chairman of the Joint Chiefs of Staff are nonvoting members.

We believe one of the main reasons agencies escalate a case to the ACEP is because they want the case to be decided at higher levels because of policy implications raised by the proposed transaction. ACEP decisions are based on recommendations of the majority of the agencies.

For the eight export license applications that were disposed of by the ACEP during the period January 1 through June 1, 1998, we found that all of the agencies concurred with approval in seven of the cases. In the remaining case, Defense was the only objecting agency. Similar to the OC process, agency concerns were generally addressed in these cases by adding to or modifying the proposed license conditions. No cases were escalated to the EARB level during fiscal year 1998.



**C. BXA's process of returning escalated cases to LOs lacks quality control**

Under the current process of returning export license applications from the OC, BXA's LOs, and not the OC staff, perform most tasks associated with export licensing cases once a case is approved, denied, or returned without action, regardless of the level at which the licensing decision was made. This also includes incorporating conditions or preparing denial notifications agreed to at OC, ACEP, or EARB meetings. We found that this process is disjointed and adds time, causes errors, and eliminates OC quality control for each case.

The Export Administration Regulations require exporters, consignees, and end users to comply with all license terms and conditions.<sup>48</sup> However, if the conditions on a final license given to an exporter do not match the OC license decision, the parties to a license do *not* have to comply with the decision. Currently there is no mechanism to ensure that conditions agreed to by the OC are placed on the license by the LO. As a result, we found cases where conditions agreed to by the OC had been changed, added, and deleted by the LOs. Examples of such cases include:

- One OC license decision indicated an approval of an export license application with 10 conditions. However, one of the conditions on the official license was worded differently than on the OC license decision. Specifically, the OC decision stated the commodity may be exported to banks, financial institutions, and U.S. subsidiaries in certain countries, but the actual license only stated the commodity may be exported to banks in certain countries, omitting "financial institutions and U.S. subsidiaries."
- Another license decision indicated an approval of an export license application with four conditions. In the first condition, the decision incorporated a reference to the consignee's end use statement to reaffirm that the commodity may only be used for the stated purpose. However, the official license omitted this reference.
- A third decision indicated a denial of an export license application based on missile proliferation concerns. However, the denial notice sent to the exporter stated the application was rejected for U.S. foreign policy reasons.
- A fourth decision indicated that an export license application should be returned without action because the item sought to be exported was licensable under the International Trade in Arms Regulations, which is administered by State. The OC license decision encouraged the applicant to submit a license application to State; however, the return without action notice did not reiterate this and instead stated the reason for the return without action was "per the exporter's conversation with the Director of the Office of Strategic Trade and Foreign Policy Controls."

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<sup>48</sup>15 CFR 750.7.

In addition, the OC Chair informed us that in one contentious case involving an export to China, the license was issued without agreed upon Defense conditions. However, this was not realized until the OC reviewed a second license application from the same exporter, to the same project. As a result, Defense required that the first license application be reopened to incorporate the original conditions agreed to before it would approve the second license application. In their defense, some LOs have informed us that changes get made to “clarify” conditions, reflect “their” opinion on case conditions, or to “relax” conditions that are sometimes made more stringent by the OC Chair (and not agreed to by the whole committee). However, in the OC Chair’s opinion, once a case is reviewed and disposed of through the dispute resolution process, no agency—including BXA—can unilaterally adjust or modify the decision. BXA’s Office of General Counsel supports the OC Chair’s position, stating that while LOs and supervisors can suggest changes to conditions placed on a license through the dispute resolution process, they have no authority to add, change, and/or delete these conditions.

BXA’s License Processing Task Force reviewed the issue of whether the OC’s responsibility over cases it reviews should be expanded.<sup>49</sup> The task force evaluated three options: (1) retain the current practice of LOs processing interagency decisions, (2) increase OC responsibility for processing only denials, and (3) increase OC responsibility for processing all licensing decisions made by the OC, ACEP, and EARB.

After evaluating each option, the task force recommended to BXA management that the OC be given responsibility, and additional resources, for processing *all* licensing decisions made by the OC, ACEP, and EARB in order to increase quality control for these cases.<sup>50</sup> The task force also recommended that draft and final OC decisions should be posted on BXA’s Intranet to quickly provide case decisions to LOs, division directors, and office directors. This would reduce OC time spent photocopying and distributing OC licensing decisions to the referral agencies; and provide a searchable archive of interagency decisions for future reference. In response to these task force recommendations, the Office of Exporter Services issued draft policies and procedures in January 1999, including final sign-off responsibility for the OC Chair for cases handled under the dispute resolution process. However, on March 31, 1999, the Deputy Assistant Secretary for Export Administration issued the final policies and procedures, but omitted this final sign-off procedure by the OC Chair. BXA officials stated that this procedure was rejected due to lack of resources in the OC.

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<sup>49</sup>*Task Force: Strategy for Improving the Licensing System*, Bureau of Export Administration, August 1997.

<sup>50</sup>With Option 1, the task force believed that although the LOs would continue issuing intent to deny letters and handling rebuttals to intent to deny letters, the OC would continue to lack control over cases it has voted on, increasing inaccuracies in interagency-agreed upon conditions or in denial reasons in intent to deny letters. With Option 2, the task force stated that the OC would have to be given additional resources for the new responsibility. The OC would retain complete control over its denied applications, and the content of the intent to deny letters and handling of rebuttals.

Without a process to ensure that conditions agreed to by the OC are actually placed on the license, quality control of OC cases will suffer. We strongly encourage BXA management to reconsider this recommendation to give the OC responsibility and adequate resources to become a “one-stop shop” for processing all licensing decisions made by the OC, ACEP, and EARB. This would include receiving and deciding OC cases, countersigning cases, inputting OC licensing decisions on BXA’s network, and processing escalated cases to the ACEP and EARB.



In its written response to our draft report, BXA indicated that our recommendation to let the OC become a “one-stop shop” for licensing decisions brought before that body was a complex issue that is under review by its Licensing Officer Task Force. However, as we mentioned in our draft report, the task force already recommended to BXA management in March 1998 that the OC be given responsibility, and additional resources, for processing *all* licensing decisions made by the OC, the Advisory Committee on Export Policy, and the Export Administration Review Board. This recommendation was based on the need to increase the quality control of processing licensing decisions made by the OC.

BXA managers have questioned how the OC (primarily the OC Chair) could make licensing decisions and then independently countersign the same licensing decisions. To be effective, the OC would require an independent countersigning mechanism, similar to managers countersigning licenses in the licensing divisions. However, we believe that since the OC Chair has the authority to unilaterally make licensing decisions—unlike any other licensing official—we believe that there is a different threshold for internal controls. Essentially, unless a dissenting agency, including BXA, escalates a decision made by the OC, that decision is final. To ensure accuracy for OC cases, we still believe that the OC licensing officer should sign off on the license application and the OC Chair should counter-sign all license applications. If BXA still disagrees, another alternative would be for the OC Chair to sign off on a case and the Deputy Assistant Secretary for Export Administration could counter-sign these cases. Therefore, we reaffirm our recommendation that BXA provide the OC with the responsibility and resources to process all licensing decisions made by the Operating Committee, the Advisory Committee on Export Policy, and the Export Administration Review Board.



## **VI. BXA Has Sought Interagency Guidance During Review of Exporter Appeals, but a More Formal Process Is Needed**

As part of the license process, if BXA intends to deny a license application, it issues a written notification to the applicant of the “intent to deny” decision. According to Section 750.6 of the Export Administration Regulations, the exporter is allowed 20 days from the date of the notification to respond to the decision before the license application is denied. Once a formal denial has been made, an exporter has the right to appeal to the Under Secretary no later than 45 days after the date appearing on the written notice of administrative action.<sup>51</sup> The appeal must include a written statement as to why the exporter believes that administrative action has a direct and adverse effect and should be reversed or modified. The Under Secretary may request additional information that would be helpful in resolving the appeal, and may accept additional submissions. At the time an appeal is filed, an appellant may request an opportunity for an informal hearing and the Under Secretary may grant or deny the request.

The Under Secretary’s decision on an appeal is considered final, and there is no requirement in either the Export Administration Act, or the Export Administration Regulations that this decision be made in consultation with the other referral agencies involved in the export licensing process. However, we found that BXA informally confers with the referral agencies in the appeals decision process. From October 1, 1997, through December 31, 1998, 23 exporter appeal cases were resolved. These involved 22 license applications and one commodity classification request. Of the 22 appeal cases involving license applications, the original interagency decisions to deny the applications were sustained in 17 cases. Of the five remaining cases, one case was withdrawn by the exporter, one case was not treated as an appeal case by BXA, and three cases resulted in reversals of the original decision.

The exporter appeals process raises a question as to whether an exporter could use the appeals process to circumvent the interagency referral process; i.e., a case denied during the interagency license review could be approved during the appeals process, which has no formal interagency review procedure. While we found no evidence to suggest this has happened, we believe that for the sake of transparency in the export licensing process, the referral agencies should be formally included in the appeals process.

### ***A. Authority for exporter appeals process is valid***

According to Section 10(j) in the Export Administration Act, “The Secretary [of Commerce] shall establish appropriate procedures for any applicant to appeal to the Secretary the denial of an export license application of the applicant.” However, officials at Defense have informally

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<sup>51</sup>Under 15 CFR 756, any person directly and adversely affected by an administrative action taken by BXA may appeal to the Under Secretary for Export Administration for reconsideration of that administrative action. This does not apply to denial or probation orders, civil penalties, sanctions, or other actions under 15 CFR 764 and 15 CFR 766.

questioned this authority now that the Export Administration Act has expired. As a result, Defense has stopped participating in the appeals process.<sup>52</sup> In an attempt to clarify this matter, BXA's Under Secretary sent a memorandum to the Under Secretary of Defense Policy, dated February 5, 1998, stating:

"I do not share the view that Executive Order 12981, in either letter or intent, abrogates exporters' appeal rights. The appeals process is provided for in the Export Administration Act (whose provisions have been continued by Executive Order 12924) and the Export Administration Regulations. It is not included in Executive Order 12981. The Executive Order 12981 procedures deal with the timely processing of export license applications and the escalation of disputes among agencies during the license application review process, while the appeals process for license denials is intended to provide a right of review to the exporting community."

When the Export Administration Act expired in 1990, President Bush extended existing export regulations by executive order, invoking emergency authority contained in the International Emergency Economic Powers Act (IEEPA). President Clinton reimposed controls under IEEPA with Executive Order 12924, dated August 19, 1994. Section one of this Executive Order states:

"...the provisions of the Export Administration Act, and the provisions for administration of the Export Administration Act, shall be carried out under this order so as to continue in full force and effect and amend, as necessary, the export control system heretofore maintained by the Export Administration Regulations...."

We agree with the Under Secretary's interpretation that Executive Order 12981, dated December 15, 1995, deals with streamlining the export licensing review process while making the process more transparent to all relevant agencies. We do not share Defense's view that because the executive order fails to mention the exporter appeals process—which we believe to be separate and distinct from the interagency dispute resolution process—that somehow this process is invalid. Specifically, we believe that section one in Executive Order 12981 clearly continues the powers and authority of the Secretary of Commerce as conferred in the 1979 Act when it states:

"To the extent permitted by law and consistent with Executive Order No. 12924...the power, authority, and discretion conferred upon the Secretary of Commerce...under the Export Administration Act to require, review, and make final determinations with regard to export licenses, documentation, and other forms of information submitted to the Department of Commerce pursuant to the Act and the Regulations or under any renewal of, or successor to, the Export

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<sup>52</sup>An attorney from the Office of the Chief Counsel for Export Administration told us that Defense has never formally challenged this authority.

Administration Act and the Regulations, with the power of successive redelegation, shall continue.”

Based on our discussions with BXA officials and our own review of the Export Administration Act, and Executive Orders 12924 and 12981, we believe the current exporter appeals process is authorized and appropriate. However, because Defense has stopped participating in the appeals process, the process does not have the benefit of its comments.

***B. Overturned appeals had support from majority of the referral agencies***

Two of the appeal cases that were overturned in fiscal year 1998 involved the same exporter, commodities, and destination. In its appeal request, the exporter submitted additional technical information involving the commodities destined for India. The Under Secretary sent the two cases to the Advisory Committee on Export Policy for its *guidance*, which in turn, remanded them to the Operating Committee for its evaluation.

In the interim, Defense conducted a new technical assessment based on the additional information and, at a Missile Technology Export Control Group<sup>53</sup> meeting in September 1997, reported that the equipment involved would not make a material contribution to missile projects of concern. However, Defense still believed the equipment raised national security concerns. The other group participants agreed that the export license applications did not raise Enhanced Proliferation Control Initiative-related missile concerns, and that the final disposition of the case should be based on national security grounds. After reviewing the results of the group meeting, the majority of OC participants—Commerce, Energy, and State—agreed that the denials could be withdrawn and the applications approved with conditions. However, two OC participants—ACDA and Defense—maintained their original denials based on regional stability concerns.

In letters to the Under Secretary of Energy, the Under Secretary for Political Affairs at State, the Under Secretary for Policy at Defense, and the Director of ACDA, BXA’s Under Secretary wrote that “national security” is not an appropriate regulatory ground to deny these cases when there is no indication of a diversion out of India to a country targeted by our national security controls. In addition, he stated that the items covered by these license applications were not controlled for regional stability reasons and there was, therefore, no basis in the Export Administration Regulations to deny these cases. Consequently, BXA’s Under Secretary overturned the denials and granted the two appeals.

The third appeal case that was overturned involved a furnace to be used in a commercial electric power generator in China. BXA originally denied this case in August 1996, with the agreement of

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<sup>53</sup>An interagency working group that reviews missile-related export license applications.

all agencies. The applicant appealed the denial, and an informal hearing was held in November 1996. While all of the referral agencies were invited to participate in the hearing, only the Departments of State, Energy, and ACDA were represented, as Defense declined to participate. At the hearing, the participating agencies held to their original views that the license should not be granted; however, they informed the exporter that they might change their minds if U.S.-China relations on nuclear matters improved. The exporter then requested that BXA hold the case open in the hope that an improvement in U.S. relations with China would increase the chances that this application could be approved in the future.

In the fall of 1997, the President decided to move forward on the 1985 U.S.-China Agreement for Nuclear Cooperation Concerning Peaceful Uses of Nuclear Energy and made the necessary certifications and reports to the Congress as required by law. In light of these developments, BXA's Under Secretary sought the *guidance* of the OC for this case in December 1997. Defense representatives at the OC refused to participate, citing their belief that Executive Order 12981 prevented BXA's Under Secretary from acting on export license appeals.

However, in view of the improvement in U.S.-China relations over nuclear matters, ACDA, Energy, and State representatives supported BXA's view that the appeal be granted and the license be approved with appropriate conditions. Based on this advice, BXA's Under Secretary granted the appeal in February 1998.

### ***C. Some reopened cases have characteristics of exporter appeals***

In fiscal year 1998, BXA reopened 120 closed license applications for various reasons. Three of these reopened cases were license applications that had the characteristics of appeal cases, i.e., they were initially denied, but upon the submission of additional information by the applicant, the denials were overturned. However, they were not processed as formal appeal cases, and the Under Secretary for Export Administration did not make the final decision to overturn the original denial.

In the first case, BXA issued an "intent to deny" letter in June 1997 and a formal denial letter in September 1997 for an application to export chemicals to a plant in India. Later in September, the applicant provided additional technical information to BXA, which it shared with the Subgroup on Nuclear Export Coordination<sup>54</sup> for a preliminary review of the information. The Subgroup, based on favorable responses from the participating agencies at the meeting, concurred with BXA that the original decision should be overturned. After two OC meetings in October 1997, Commerce, State, and Energy representatives voted to approve the application with conditions; Defense voted to maintain its denial; and ACDA took no position. The OC Chair recommended that the application be approved with conditions, and BXA reopened the case to reflect the OC decision.

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<sup>54</sup>An interagency working group that reviews nuclear-related cases.



In the second case, BXA issued an intent to deny letter in September 1997 and a formal denial letter in October 1997 for an application to export a chemical to an American subsidiary in Belgium. This case was originally rejected unilaterally by Commerce based on initial end user concerns. In February 1998, upon receipt of a rebuttal letter from the exporter and end use information from the end user, BXA took the case to the Missile Technology Export Control Group for preliminary review in February. According to the licensing officer's notes in this case, the Missile Technology Export Control Group was "comfortable allowing the export to the end user providing the end user conformed to specified procedures and did not export the chemical in the form received."<sup>55</sup> Based on this concurrence, BXA managers reopened the case and the application was officially approved with conditions.

In a more recent case, BXA issued an intent to deny letter in June 1998 and a formal denial letter in July 1998 for an export license application to supply environmental monitoring equipment for use in connection with decontaminating a nuclear test site in China. The applicant submitted new information about the end user in its August 1998 rebuttal letter requesting a reversal of this denial. In September 1998, BXA reopened this case and returned it for a second review to the OC, which had issued the original denial. The license was ultimately approved with conditions by the OC Chair in October 1998, with ACDA, Energy, and State concurring with the approval and Defense maintaining its denial.

Unlike the formal appeal cases, in which the Under Secretary makes the final decision after informally *consulting* with referral agencies through the ACEP, OC, or other means, the final licensing decision in the three reopened cases were made by the OC Chair or other BXA managers. A senior BXA official informed us that BXA's main objective in the third reopened case discussed above was to facilitate the reversal of the denial. Since it had the majority of interagency support for this decision, BXA determined it was faster to reopen the case and place it back into the export license review process rather than handling it under the formal appeal process. According to one of BXA's attorneys, there are no regulations prohibiting BXA from reopening cases based on new information and reversing previous licensing decisions.

While we do not believe that the end result would have been any different for the three reopened cases had they been reviewed under the appeals process, we question what rights the exporters would have had if the reviewing agencies had decided to maintain the original decision to deny the license. Since these cases would not have been technically treated as "appeals," would the exporter be allowed to "appeal" a second time? In our opinion, having two different processes to handle exporters' appeals obscures BXA's formal appeals process and leaves BXA susceptible to charges that its process lacks fairness and transparency.

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<sup>55</sup>However, it is unclear whether all the Missile Technology Export Control Group parties or just a majority agreed with this recommendation.

**D. Lack of clear procedures obscures BXA's appeals process**

In the six export licensing cases discussed above that resulted in reversals of prior denials—the three formal appeal cases and the three reopened cases--BXA consulted with referral agencies before reversing the prior denials. With the three formal appeals cases, BXA's Under Secretary sought the views of the referral agencies through the ACEP or the OC representatives. With the three reopened cases, two cases were approved with conditions by the OC after a second review of the export license application, while the third case was approved by BXA after a review by an interagency working group.

However, officials from the referral agencies have still expressed the concern that appeal cases are not *subject* to interagency review. Although we found no evidence indicating that BXA does not consult with the referral agencies before overturning a denial, we believe it should avoid any misconceptions that its appeals process lacks fairness and transparency. Therefore, we suggest BXA work with the National Security Council to amend Executive Order 12981 or obtain a new directive, to establish formal procedures to include the referral agencies in the appeals process. The new export licensing legislation should also include a formal interagency appeals process.



In its written response to our draft report, BXA stated that it did not object to our recommendation that the referral agencies be brought into the appeals process in a more formal way, and it is prepared to work with the NSC on this matter. While BXA disagreed with one of our observations about a case we cited where BXA informally handled the appeal through the OC in lieu of action by the Under Secretary, we can accept BXA's argument that the exporter would not have lost its appeal right.

## VII. BXA Needs to Improve Its Monitoring of License Conditions

During our current review of the export licensing process, we found that BXA is still not adequately monitoring license conditions as first reported in the 1993 special interagency OIG report. The Export Administration Regulations state that a transaction authorized under an export license may be further limited by conditions appearing on the license itself. The ability to place conditions on a license is an important part of the license resolution process as well as an additional means to monitor certain shipments. Frequently, the conditions are the result of lengthy negotiations among the referral agencies.

While there are 28 standard conditions that could be placed on an export license, only seven actually require the exporter to submit documentation back to BXA concerning any shipment made against the license. Table 7 illustrates the seven conditions with their reporting requirements. The "Write Your Own" condition allows licensing officers to specify unique requirements for the license, including reporting requirements. For the other six reporting conditions, a standard message is automatically put on the license indicating the reporting requirements. The remaining 21 conditions do not require the exporter to submit any documentation or information to BXA but may require the exporter to perform certain actions or to ensure certain rules are followed. For example, one condition stipulates "No reexport of the items listed on this license is authorized without prior authorization by the U.S. Government," while another one stipulates, "The items authorized for export by this license/authorization are not to be used by nuclear end users or for nuclear end uses." These types of conditions are only monitored when export enforcement agents perform Safeguard visits overseas or when US&FCS personnel perform post shipment verifications.

To track licenses with reporting conditions, BXA uses a computer-controlled monitoring system, called the Conditions Follow-up Subsystem.<sup>56</sup> The subsystem is divided into two modules that have restricted access. Export Administration and Export Enforcement have their own independent modules in the subsystem. Each office is responsible for following up on specific license conditions. Export Administration's conditions generally require an exporter to report back to BXA regarding the export, whereas Export Enforcement's condition requires the exporter to submit shipping documents so that a post shipment verification of the export in the country of destination can be conducted.

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<sup>56</sup> Conditions Follow-Up Subsystem, also known as Subsystem and/or Follow-Up Tickler Queue.

**Table 7: License Conditions with Reporting Requirements**

Condition	Requirements
<b>Write Your Own</b>	Special reporting requirements written by the licensing officer on the license.
<b>Temporary or Demonstration</b>	Authorization is granted for shipment of the described items to the specified country of destination only on a temporary basis for demonstration. At the conclusion of the demonstration or exhibit, the items must be returned to the U.S., to the country from which originally shipped, or to another specifically authorized country, no later than one year from the date of export. Prompt notification of an item(s) return must be given to BXA.
<b>Delivery Verified</b>	The delivery verification (DV) procedure is required for all shipments made under this license. The DV must be obtained from the appropriate government of the country of ultimate destination. The original copy of the DV must be sent to BXA after the last shipment has been made against the license.
<b>Temporary Sojourn</b>	Upon return of the aircraft, immediate written notification must be sent to BXA's Office of Exporter Services.
<b>Encryption</b>	The applicant must report to BXA biannually the item description, quantity, value, and end user name and address of all transactions made under this license. The reports shall cover exports made during six-month periods spanning from January 1 through June 30 and July 1 through December 31.
<b>Deemed Exports</b>	1. Access to International Traffic in Arms Regulations (ITAR) controlled defense articles, defense services, and technical data is not authorized. ITAR controlled software source code and/or source code documentation is not releasable. 2. Approval is limited to release of only unclassified information, and any activity that may lead to possible disclosure of U.S. Government classified information would be the subject of additional government review and must be approved by the U.S. Government in advance. 3. The applicant shall maintain a record of when the foreign national obtains his/her permanent resident status (i.e., green card) or leaves the company prior to obtaining a green card. This information shall be made available to the U.S. Government upon request. 4. The applicant shall submit another export license application if the foreign national's duties require access to controlled technologies other than those authorized by this license. 5. The foreign national is allowed access to technology for the development of civilian dual-use encryption technology and products. However, the applicant must seek U.S. Government approval for access to any encryption technology related to government contracts, including military activities. 6. The applicant shall inform the foreign national in writing of all license conditions and his/her responsibility not to disclose, transfer, or reexport any controlled technology without prior U.S. Government approval. 7. The applicant will establish procedures to ensure compliance with the conditions of this license, particularly those regarding limitations on access to technology by foreign nationals. A copy of such procedures will be provided to BXA. Commerce will monitor to ensure that the applicant's compliance is effective.
<b>Post Shipment Verification</b>	After the first shipment is made against the license, the applicant must send one copy of its Shipper's Export Declaration and Bill of Lading or Airway Bill to the Office of Enforcement Analysis.

**Source:** Office of Administration, Bureau of Export Administration.

The 1993 special interagency OIG review disclosed that (1) Export Administration's subsystem did not contain all of the licenses that should be tracked, (2) Export Administration was not

following up on expired licenses in its subsystem, (3) licensing officers were improperly flagging licenses indicating follow-up was required, when in fact none was required, and (4) Export Enforcement did not update its subsystem even after the exporter submitted the required documentation. We recommended then that BXA track all licenses with reporting conditions, follow-up with exporters who did not comply with the reporting conditions, train licensing officers to properly flag licenses if follow-up was required, and close out old licenses from the follow-up subsystem. BXA agreed with all of the recommendations, but it indicated that it did not have the resources to follow-up with every exporter who did not comply. Unfortunately, we found similar problems still existing today.

**A. *Export Administration is not adequately monitoring exporter compliance with license conditions***

We found several weaknesses in Export Administration's monitoring of exporter compliance with license conditions. First, we discovered that the follow-up subsystem is incomplete and out of date due to (1) the low priority placed on this function by Export Administration's Office of Exporter Services, (2) the improper flagging of licenses requiring reports from exporters, and (3) the subsystem not tracking two major reporting conditions.

Second, we determined that most licensing officers (with the exception of those responsible for deemed exports and encryption) are not involved with monitoring conditions they place on the licenses. We found that licensing officers do not access the subsystem or the reports submitted by exporters. Without this information, LOs are unable to determine the compliance history of an exporter which we believe is important in making any licensing decisions. Without an adequate monitoring system in place, exporters may receive new licenses even though they did not comply with previous license conditions.

Monitoring of reporting conditions has been a low priority of Export Administration

Office of Exporter Services (OEXS) is responsible for performing compliance follow-up for four of the seven reporting conditions: Write Your Own, Temporary or Demonstration, Delivery Verified, and Temporary Sojourn. One of our review objectives was to determine how well the Office of Exporter Services has been monitoring exporter compliance with license conditions that have reporting requirements, including whether the Office of Exporter Services has been requesting and receiving reports owed by exporters.<sup>57</sup>

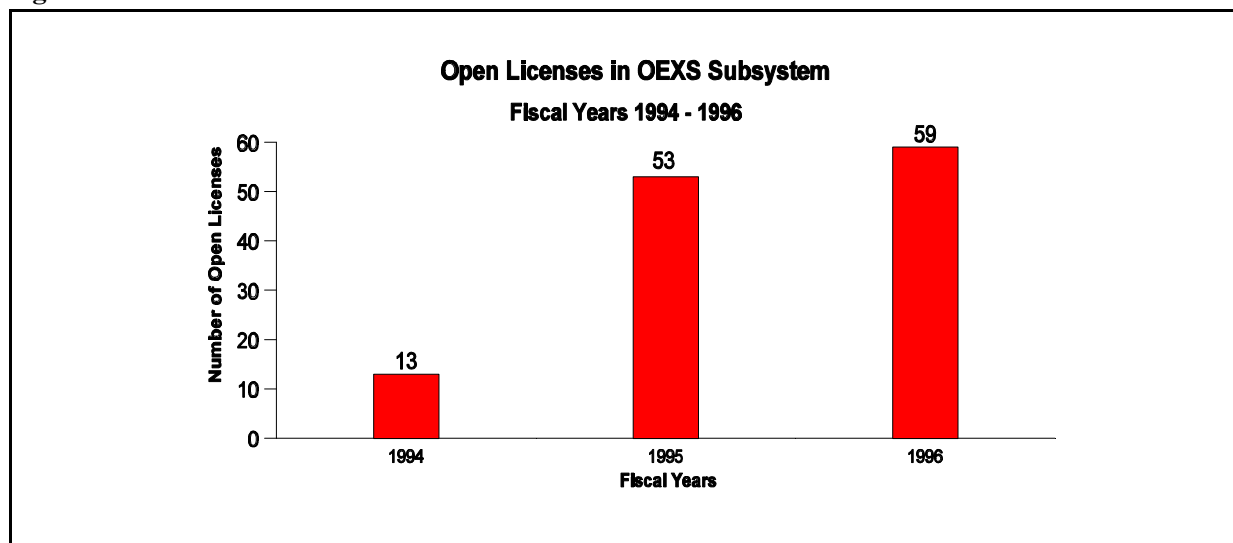
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<sup>57</sup>We did not determine how well exporters were complying with licenses containing follow-up conditions.

The Office of Exporter Services personnel informed us that they did not routinely follow-up with exporters who owed BXA reports before the licenses expired due to resource constraints.<sup>58</sup> In addition, we found that the Office of Exporter Services had not adequately followed up with exporters whose licenses had expired in order to determine whether the exporter had shipped against the license. Within the Office of Exporter Services this responsibility has been tasked to one employee, whose performance plan lists managing the subsystem as a minor task (giving it a weight of 10 out of 100 possible points). More importantly, this employee, in the presence of her supervisor, told us that she has not received any written procedures or guidelines for maintaining the subsystem. Office of Exporter Services management told us that no analysis had been done to determine the resources needed for monitoring these conditions.

In November 1998, we requested a listing of all export licenses in the Office of Exporter Services' subsystem to ascertain if any had expired. In December 1998, the Office of Exporter Services provided a listing of 406 licenses in its subsystem dating back to 1994.<sup>59</sup> Based on a breakdown of the 406 licenses in the subsystem, we determined that 125 licenses issued between fiscal year 1994 and 1996 were still in the subsystem. (See Figure 9.) Although the licenses had expired, the Office of Exporter Services had not contacted the exporters to verify whether the exporters shipped against the licenses.

Figure 9



Source: Office of Exporter Services, Bureau of Export Administration.

<sup>58</sup>With the exception of those related to encryption licenses, export licenses are generally valid for two years.

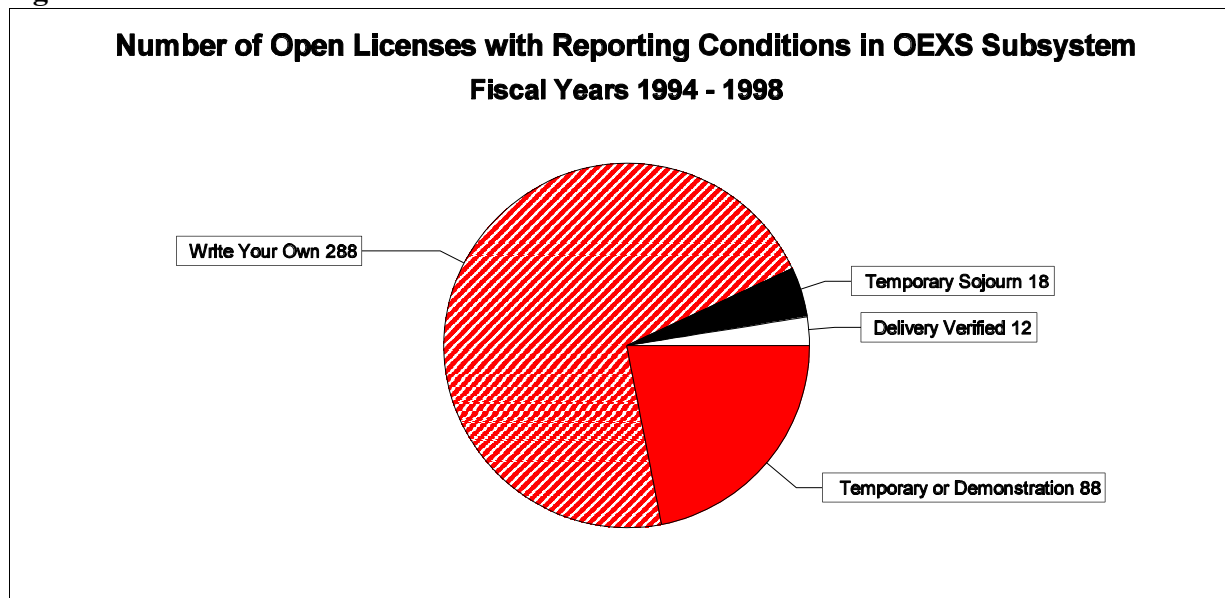
<sup>59</sup> In January 1999, we learned that the Office of Exporter Services' subsystem actually contained an additional 194 licenses dating back to 1992 bringing the total number of licenses in the subsystem to 600.

We also randomly selected 39 of the 406 licenses from all four condition categories to review. Of the 39 licenses, 28 had not expired so it is possible that the exporter had not shipped yet and therefore would not have provided BXA any documentation. However, we could not confirm this because, as mentioned above, the Office of Exporter Services does not routinely follow-up on licenses that have not expired. We did find that 5 of the 39 licenses had expired, and the Office of Exporter Services informed us that it tried to contact one of the exporters associated with these licenses to determine if it had shipped against the license, but it was unable to get a hold of the exporter so it gave up. The Office of Exporter Services had not attempted to contact the remaining four companies. We believe that the Office of Exporter Services needs to purge the subsystem of expired licenses and in doing so, should contact the exporters to determine whether shipments were made against the licenses. We would also encourage the Office of Exporter Services to perform a random spot-check on licenses in the subsystem that have not expired in an effort to inform exporters that BXA is serious about monitoring exporter compliance with conditions placed on export licenses.

#### Licensing officers are improperly flagging licenses with “Write Your Own” conditions

In the remaining six licenses, (15 percent) of our subsystem sample, we found that the LO flagged the wrong box associated with “Write Your Own” conditions, indicating that a report was needed from the exporter. When the licenses were issued, ECASS automatically sent them to the subsystem. Upon examining the six licenses, we determined that there was no reporting requirement written into the condition. The Office of Exporter Services informed us that this is a common mistake made by LOs. Thus, with the vast majority of follow-up conditions in the subsystem being “Write Your Own,” we question how many more are in the subsystem incorrectly. (See Figure 10.) While we understand that mistakes can happen, these licenses can needlessly burden the subsystem. BXA needs to remind LOs and supervisors (who are responsible for countersigning these licenses) of the importance of not flagging licenses with “Write Your Own” conditions unless a reporting requirement is included.

Figure 10



Source: Office of Exporter Services, Bureau of Export Administration.

#### Encryption and deemed export licenses were not being tracked by the subsystem

Frequently, licenses issued for encryption and deemed exports have reporting conditions placed on them as part of the license requirement. During our sample analysis, we found that these conditions were not automatically being tracked by the subsystem. ECASS database managers stated that they were unaware that encryption and deemed exports licenses were issued with conditions that required exporters to submit reports to BX. However, immediately after we reported the problem to them, a software modification to ECASS was made, and now both conditions are being tracked by the subsystem.

#### LOs are removed from the compliance process

A second major weakness we identified in Export Administration's monitoring of exporter compliance is that LOs (with the exception of those in the encryption and deemed export divisions) are generally not involved in this process. LOs generally deal with specific industries and often issue numerous licenses to the same company over time. However, we found that most LOs neither review compliance reports submitted by exporters nor have access to the subsystem to review the compliance history of a company.

Although the subsystem was not tracking conditions placed on encryption or deemed export licenses, we determined that the individual licensing divisions were closely monitoring them. Based on a sample of referred licenses during the period January 1 through June 30, 1998, we identified 27 licenses with either encryption or deemed exports reporting conditions.



Of the 27 licenses, 17 dealt with encryption exports. The encryption division had already received reports from exporters for six of these licenses. The Division Director informed us that for the remaining 11 licenses, shipments had not occurred so no reports were necessary. The encryption licensing staff monitor conditions by making follow-up telephone calls to exporters reminding them of their reporting requirements. They also use this opportunity to keep the exporters informed about pending policy changes and to find out how new regulations are affecting their businesses.

Furthermore, all 10 of the deemed export licenses from our sample were closed out. Based on the documentation provided by the exporters, we believe the companies were compliant with the conditions. As mentioned earlier in this report, deemed export licenses are unique because they involve foreign nationals working for entities in the United States. The supervisor in charge of this program believes it would be a good idea to conduct on-site visits with these companies to verify that security procedures and safeguards, as required by the license conditions, have been put in place to protect controlled technology. We agree. In late 1998, the director informed us that he was able to perform one on-site visit with a company who had received the most deemed export licenses over the past several years. We encourage BXA to routinely spot-check these companies to physically verify that security procedures are indeed in place and meet the established criteria.

As reported above, we believe the steps taken by LOs involved in monitoring exporter compliance with encryption and deemed exports license conditions should be used as a best practice by the other licensing divisions. The compliance rate among exporters seems to be higher when the licensing officers and their supervisors are actively involved in this process. In addition, LOs must have readily available access to exporters' compliance history in order to make the most informed decision about an export license application including denying a license based on noncompliance.

At a minimum, LOs need to have "read-only" access to the subsystem so they can verify the exporter's compliance history and deny a license based on noncompliance. In addition, LOs should review all reports submitted by the exporter and be involved with contacting exporters who do not comply with the reporting conditions.



In its written response to our draft report, BXA agreed with our overall recommendation to improve its monitoring of license conditions. It stated that BXA has recently implemented a new Licensing and Enforcement Action Program (LEAP) designed to deal with the vast majority of the problems with assigning conditions and their follow-up. BXA attached a copy of the LEAP objectives as a part of its response to our draft report, but due to time constraints we were unable to verify the validity of this program. However, based on our review of the objectives of the program, it does not appear that it will address all of our recommendations in the compliance

area. Therefore, we reaffirm our specific recommendations for BXA to (1) notify licensing officers and supervisors of the importance of not flagging licenses with “Write Your Own” conditions for follow-up if they have no reporting requirement, (2) routinely spot-check companies related to deemed exports, to verify that security procedures are indeed in place and meet the established criteria, (3) utilize the steps taken by licensing officers involved in monitoring exporter compliance with license conditions for encryption and deemed exports as a best practice by the other licensing divisions, (4) provide licensing officers with “read-only” access to the compliance subsystem so that they can verify an exporter’s compliance history and deny a license based on noncompliance, if necessary, and (5) ensure that licensing officers review all compliance reports submitted by the exporter and be involved with contacting exporters that do not comply with the reporting conditions.

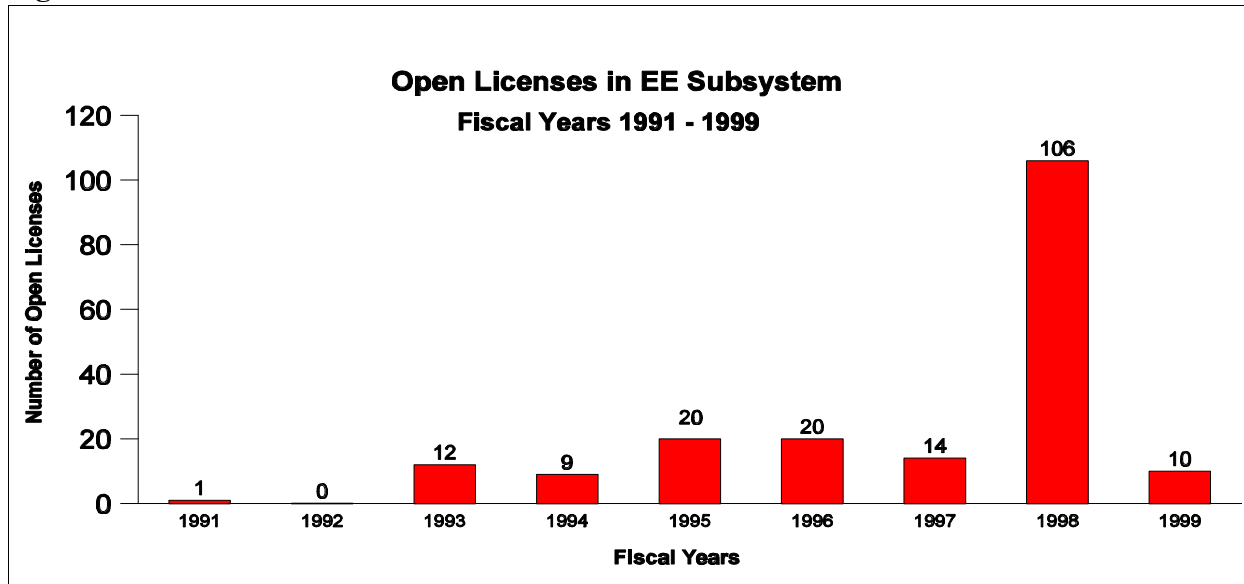
In addition, we are concerned that BXA will only fully implement LEAP, and take interim steps to improve monitoring of conditions, based on budgetary funding. We believe that monitoring exporter compliance overall, and specifically following up on license conditions, is one of BXA’s core functions that should be carried out as part of its export control responsibilities.

***B. Export Enforcement also needs to step up its monitoring efforts***

Export Enforcement’s Office of Enforcement Analysis (OEA) has exclusive responsibility for monitoring condition 14 in the Conditions Follow-up Subsystem. This condition requires an exporter to submit a copy of the Shipper’s Export Declaration and Bill of Lading or Airway Bill directly to OEA once a shipment against the license has occurred. Upon receiving the shipping documents, OEA, with minor exceptions, initiates a post shipment verification to verify the end use. The 1993 special interagency OIG review revealed that OEA was not closing out licenses from its subsystem after the licenses had expired. Our current review uncovered a similar problem.

In January 1999, we received a printout of all the licenses in the OEA subsystem, showing the license number, exporter name, and date of issuance. We found that of the 192 licenses appearing in the subsystem, 66 had expired. (See Figure 11.) After the OIG pointed out the problem, Export Enforcement took immediate action and began contacting the exporters who held these licenses.

Figure 11



Source: Office of Enforcement Analysis, Bureau of Export Administration.

As of March 1999, 57 of the 66 licenses had been closed out of the subsystem. The following is a breakdown of the licenses:

- Exporter advised OEA that no shipments had been made against the license (23).
- Shipping documents have been submitted and a PSV has been initiated (19).
- Exporter could not be located/contacted, and licenses are currently pending referral to Office of Export Enforcement for action (10).
- Licenses had already been referred to Office of Export Enforcement for action (3).
- Licenses involved reexports and because shipper's export declarations are not applicable for this type of transaction, it was determined that condition 14 had been placed on the license in error (2).

Regarding the nine expired licenses remaining in the follow-up subsystem, OEA informed us that they contacted the exporter and are currently waiting for the requested shipping documents. We believe condition 14 is one of the most critical conditions placed on a license, because somewhere in the licensing process it was determined that a post shipment verification was warranted to determine if the goods or technology was actually being used in accordance with the provisions of that license. By not adequately monitoring this condition, BXA cannot assure itself that the goods were not diverted to an unauthorized end user. In addition, exporters may continue to receive licenses even though they were non-compliant on prior licenses. For example, we

discovered that at least three of the exporters who were associated with the 66 expired licenses continue to receive licenses. Thus, it is imperative that the Office of Export Enforcement perform timely follow-up work to verify compliance among exporters and uncover any noncompliance.

In July 1998, the Office of Enforcement Analysis hired a supervisory export compliance specialist to, among other things, monitor exporter compliance with regard to condition 14. However, we found no mention of the compliance monitoring follow-up task in the employee's performance plan. We would encourage the Office of Enforcement Analysis Director to incorporate this responsibility into the supervisor's performance plan to ensure accountability.



In its written response to our draft report, BXA disagreed with our recommendation to incorporate this responsibility as a specific function in the supervisory export compliance specialist's performance plan. It stated that OEA has specific written instructions in place for the individual to perform this function, and BXA believes these are sufficient without making them part of the performance plan. We disagree. We found that BXA personnel were not following the written instructions. By not incorporating this function into the supervisor's performance plan, we believe it will be difficult for BXA to hold anyone accountable for this function. As a result, we reaffirm our recommendation.

### VIII. End Use Checks Are a Valuable Tool, but Some Improvements Are Needed

End use checks are an important part of the license evaluation process and are used to verify the legitimacy of export transactions controlled by BXA. A pre-license check (PLC) is used to validate information on export license applications by determining if an overseas person or firm is a suitable party to a transaction involving controlled U.S.-origin goods or technical data. In contrast, post shipment verifications (PSV) strengthen assurances that exporters, shippers, consignees, and end users comply with the terms of export licenses and licensing conditions by determining whether or not goods exported from the U.S. actually were received by the party named on the license and if those goods are being used in accordance with the provisions of that license.

Although we found some need for improvement in the conduct of end use checks, we believe they are still a valuable tool in preventing proliferation and detecting problems. These checks are important for the protection of controlled U.S. goods and technology by helping to prevent and detect illegal technology transfer. However, as we mentioned in Section I, we believe that conducting post shipment verifications for every high performance computer, as required by the National Defense Authorization Act of 1998, may not be the most effective use of resources.

These checks can be requested by licensing officers, Export Enforcement special agents and analysts, and officials from other federal agencies involved in the license review process. Most PLCs and some PSVs are conducted by Commerce's U.S. and Foreign Commercial Service (US&FCS) officers stationed at overseas diplomatic posts who have knowledge of the geography, bilateral relations, cultural norms, and local business practices and can provide valuable insight into the end use check process.<sup>60</sup> In addition, most PSVs and some PLCs are conducted by Export Enforcement's export enforcement agents under the Safeguard Verification program.

According to ECASS reports generated in October 1998, there were 275 PLCs and 109 PSVs completed in fiscal year 1998.<sup>61</sup> In addition to these completed end use checks, there were 56 PLCs canceled. Reasons for canceling the pre-license checks varied including:

- The post was unable to conduct the PLC within the time limit or the post did not reply in a timely manner (13).
- License applications were going to be returned to the exporter without action (12).

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<sup>60</sup>While the US&FCS's primary role is to promote U.S. exports, it also has an ancillary role in helping to control the illegal diversion of sensitive U.S. products and technologies.

<sup>61</sup>As discussed in Section B, 8 PLCs and 237 PSVs conducted by Safeguard Verification teams were not shown in the October 1998 ECASS printout.

- Enforcement agents or analysts changed their minds (11).
- Recent end use checks had been done on the end user (5).
- Change in export control policy towards India (4).
- Difficulty in conducting end use checks in China (4).
- License applications ended up being rejected (3).
- Items would be under the control of US/UK citizens (2).
- Cost of conducting PLC was prohibitive (1).
- Operating Committee had already approved the license (1).

The 1993 special interagency OIG review of the export licensing process found a number of problems with end use checks, including (1) BXA lacked a strategic plan for checks and verifications, (2) some US&FCS posts failed to follow guidelines for end use checks, and (3) BXA needed to provide more guidance and product information to the posts.

In our 1997 Commerce OIG report on BXA's watchlist screening process,<sup>62</sup> we found the following to be issues in the area of end use checks: timeliness of end use checks, US&FCS use of foreign service nationals (FSNs) and personal service contractors (PSCs) to conduct end use checks, need for improvement in posts' response cables, accessibility of Safeguard trip reports, and better coordination by posts with other parts of the embassy in conducting end use checks.

During our current review, we conducted an analysis of 124 PLCs and 18 PSVs selected from the October 1998 ECASS report. We also participated in end use checks conducted by US&FCS Israel and a Safeguard verification team in Malaysia. In addition, we conducted a survey of 27 US&FCS posts identified by BXA's 1998 strategic plan as priority areas for PLC/PSV selections.

Based on this work, we found that BXA had made improvements in its end use checks process, e.g., in September 1998, BXA issued an updated handbook for the posts, "How to Conduct Pre-License Checks and Post Shipment Verifications." However, we again found some of the same areas of concern identified in our earlier reports with respect to end use checks conducted by US&FCS. We also found that BXA's Office of Export Enforcement needs to provide clearer

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<sup>62</sup>*Bureau of Export Administration: Export Application Screening Process Could Benefit From Further Changes*, Inspection Report No. IPE-9524, September 1997.

guidance for the report process and information accessibility of Safeguard trip reports. We also highlight some specific conditions regarding end use checks in China, Hong Kong, and Israel.

**A. *More interaction between BXA and US&FCS posts is needed***

According to a 1988 Memorandum of Understanding between BXA and the International Trade Administration, in each country in which it has an office, US&FCS will conduct pre-license and post shipment checks, within the statutory or regulatory time limits, where applicable, in accordance with the BXA pre-license and post shipment guide and host country regulations. Overall, we believe that US&FCS is generally complying with BXA's guidance for conducting end use checks. In addition, most of the end use check responses from the posts included all of the information needed by BXA to make a determination about the outcome of the check. However, we did identify weaknesses in the process that need to be corrected including:

- Timeliness is still an issue with PLCs.
- Post cable reports on completed end use checks do not always indicate who conducted the check.
- On-site visits are not always conducted.
- Record-keeping at some posts needs improvement.
- Coordination among agencies at some embassies could be improved.

We also believe that BXA needs to make its guidelines clearer regarding who exactly is allowed to conduct end use checks. In addition, more training is needed for US&FCS personnel to enable them to effectively conduct these checks. We discuss these problems in detail below and recommend a number of actions that BXA can take to encourage posts to improve end use checks.

Timeliness is still an issue with PLCs but not PSVs

We found that timeliness is still an issue with PLCs, resulting in over 20 percent of PLCs canceled in fiscal year 1998 due to the posts not responding in a timely manner. According to BXA's 1998 Handbook, PLCs must be completed within 28 calendar days. However, according to an October 1998 ECASS printout of PLCs, we determined that the average processing time for the 331 PLCs completed or canceled in fiscal year 1998 was 50 days. Timely PLCs are important because PLCs suspend a decision on an export application until the check is completed. As a result, the longer an application is "on hold" waiting for a PLC, the greater the risk for a U.S. exporter to lose a sale based on its inability to deliver the product in a timely manner.

On the other hand, PSVs are generally conducted within BXA's established time frames. Specifically, BXA's 1998 Handbook provided for 60 calendar days for completion of PSVs. We determined that the average processing time for the 109 PSVs completed in fiscal year 1998 as reported on an October 1998 ECASS printout was 42 days.

In our survey of US&FCS officers in 27 foreign posts, we asked them whether BXA's requested response times were reasonable. In response to this specific question, four posts indicated that the 28-day turnaround period for PLCs was not enough at times. One specifically stated that meeting response time deadlines can be problematic due to limited staffing and other demands at post such as high-level visitors from headquarters that require special attention, local difficulties in travel, and arranging appointments at restricted facilities. Another said that they encountered problems with deadlines when travel had to be arranged while a third commented that the 28-day limit did not take the many and varied priorities of the post into consideration.

Based on survey responses, the most common reason given by posts for untimely end use checks was that their primary responsibility of export promotion took precedence over PLCs and PSVs, particularly if (1) there was a trade mission or high level visitor in country, (2) it was a busy time of year, or (3) the check involved an extended trip.

To ensure that posts were held accountable for responding to end use check requests in a timely manner, we recommended in our 1997 report that BXA send an information copy of all outgoing cables that relate to end use checks to the regional directors in US&FCS Headquarters' Office of International Operations. The regional directors, who are responsible for overseeing the US&FCS posts overseas, would then have direct knowledge of which posts are delinquent and can take action to correct their performance. BXA agreed with our recommendation and is now including the regional directors on the outgoing cables. However, this does not appear to have improved the timeliness of PLCs conducted by US&FCS posts. We encourage BXA senior level management to discuss this issue with the US&FCS Director General and other senior level US&FCS managers and work with them to improve the timeliness of PLCs.



In its written response to our draft report, BXA agreed to continue to work with US&FCS on this issue. BXA also noted that it implemented the 1997 OIG recommendation to include an information copy of every outgoing PLC request cable and follow-up cable to ensure that US&FCS management was aware of delays in the completion of PLCs at overseas posts. In addition, BXA stated that it always highlights the importance of timeliness on PLCs in briefings to all post personnel prior to their placement overseas and that it is specifically highlighted in BXA's PLC-PSV guide sent to all posts.



Majority of PLCs are performed by American Officers but clearer guidance is needed

According to our survey of 27 US&FCS posts, American officers reportedly conduct PLCs and PSVs at six posts, combination teams of commercial officers and FSN/PSCs conduct checks at 15 posts, and FSNs have conducted or are allowed to conduct checks at five posts. The remaining post has a special arrangement under which the host government performs these checks.

In addition, based on our review of completed checks conducted by US&FCS personnel—90 PLCs from our sample of 124 PLCs and 15 PSVs from our sample of 18 PSVs in fiscal year 1998—it appears that the majority of PLCs and PSVs are being conducted by appropriate personnel such as an American officer or a combination team that includes an American officer as well as either a foreign service national or personal service contractor. (See Table 8.)

**Table 8: US&FCS Personnel Conducting End use Checks**

	US&FCS Checks Reviewed	End use check conducted by?			
		Officer	FSN/PSC	Combination	Unclear
PLC	90	22	5	36	27
PSV	15	10	0	0	5
<b>Total</b>	105	32	5	36	32

Source: Office of Enforcement Analysis, Bureau of Export Administration.

However, it was not always clear from the posts’ reporting cable who conducted some of these PLCs and PSVs. As discussed in our 1997 review, it is important for BXA to know whether the end use checks were conducted by an American officer or not in order for them to weigh the information accordingly. Although 10 of the response cables indicated that the “Commercial Attaché” had performed the PLC, it was not clear whether that person was an American Officer or a PSC because the latter personnel often use this title. Post responses in two PLCs referred to “embassy officers,” but again it was not clear whether they were *American* officers. The remaining 15 response cables did not provide any indication as to who had performed the PLC. Furthermore, post responses were not always clear about who conducted PSVs. Of 15 PSVs completed by US&FCS in our sample of fiscal year 1998 PSVs, it was not clear who had conducted 5 PSVs, while American officers had conducted the remaining 10 PSVs. The outcomes of the 15 PSVs were 14 favorable and one unfavorable. US&FCS posts clearly need to provide unambiguous information in their reporting cables regarding who conducted the end use check.

Our review also identified four PLCs that were conducted by FSNs in Austria, Hong Kong, and the Ukraine. None of these posts had either requested or received a waiver from BXA authorizing the FSNs to conduct these checks. Table 9 summarizes the circumstances of these PLCs.

**Table 9: PLCs Conducted by FSNs**

Country	Conducted by	PLC Result	License Outcome	Comments
Austria	FSN	Favorable	Approved	Item controlled for nuclear nonproliferation.
Hong Kong	FSN	Unfavorable	Returned Without Action	Results indicated China was to be country of final destination.
Hong Kong	FSN	Limited	Approved with Conditions	On-site PSV done a month earlier by American officer and FSN. Limited PLC due to FSN conducting PLC over phone.
Ukraine	FSN	Unfavorable	Rejected	Crime control items.

**Source:** Office of Enforcement Analysis, Bureau of Export Administration.

We believe that BXA’s new guidelines for “How to Conduct Pre-License Checks and Post shipment Verifications” dated September 1998 is unclear on the use of FSNs and PSCs for end use checks. Specifically, the guidance in the Handbook itself states:

“PLCs must be conducted by an FCS Officer when one is stationed at post. If one is not stationed at post, PLCs must be conducted by other U.S. Government personnel who are U.S. citizens. In rare circumstances, BXA might allow an FSN or PSC to conduct a check. Any post considering using an FSN or PSC must cable the individual’s credentials to the Office of Enforcement Analysis along with a justification of why an exception to this policy should be granted. The Office of Enforcement Analysis will consider the facts and circumstances and respond to the request. Do not proceed with the check until the Office of Enforcement Analysis has responded.”

However, while Appendix I reiterates “BXA’s strong policy preference that PLCs and PSVs be performed by U.S. government employees who are U.S. citizens unless extraordinary circumstances require the use of FSNs or PSCs,” it also states that if the country is not listed under a particular control (e.g., nuclear, missile, chemical/biological), then anyone can conduct the checks. We believe this type of instruction is very ambiguous and needs to be clarified. If BXA’s new policy is to allow FSNs and PSCs to conduct end use checks in those countries not specified in the Appendix, then it should clearly reflect this in both portions of the guidance. Either way, BXA must provide clear and concise guidance on this issue; in addition, BXA should remind posts to clearly identify who conducted an end use check in its reporting cable.

Based on BXA’s own argument on this issue, we believe that it would be in the best interests of the U.S. government for these checks to be conducted by a U.S. citizen who is a U.S. government employee. Specifically, as stated in Appendix I of BXA’s Handbook, there are three disadvantages of using FSNs to conduct PLCs including credibility, possible reluctance to testify against a fellow citizen in a U.S. court, and lack of access to classified material. Some or all of these disadvantages may also apply if a PSC is used to complete end use checks. Even for those PSCs that are U.S. citizens, their credibility as a temporary employee without any specific training in conducting checks could be called into question. In addition, many PSCs may not have appropriate security clearances to give them access to relevant files and data sources within other agency files at post, a necessary research tool before conducting a check according to BXA’s Handbook.



In its written response to our draft report, BXA stated that it would reiterate to US&FCS its policy preference for having a U.S. citizen/U.S. government employee present at all end use checks. Specifically, it stated that it will redraft the PLC/PSV Handbook to make it clear when use of an unaccompanied non-USG employee, non-U.S. citizen is merely undesirable and when it is unacceptable. However, we believe that BXA’s use of the word “undesirable” implies that it may be acceptable to use an unaccompanied non-U.S. government employee or a non-U.S. citizen. In our opinion, this still sends an ambiguous message to US&FCS personnel. If BXA is willing to accept end use check results from non-U.S. government employees and/or non-U.S. citizens on a case-by-case basis, then it should state just that and explain when and under what specific conditions use of foreign nationals or personal services contractors is acceptable for the conduct of end use checks.

#### On-site visits still not always conducted

Our survey questionnaire to the 27 posts asked whether they conducted on-site visits for PLCs and PSVs. In their responses, one post stated it did not conduct on-site visits, and one post stated it would conduct on-site visits “as appropriate.” A third post reported that it conducted on-site visits in the capital city, but it did not conduct on-site visits outside of the capital city because of a

lack of funds. However, BXA’s 1998 Handbook provides the following guidance for on-site visits for PLCs:

“It is the visit to the company, however, that is by far the most important. This is why an on-site visit is considered to be a requirement except under unusual circumstances, which must be stated clearly in the reporting cable.”

However, we found in our PLC sample that some posts do not conduct on-site visits, as shown in Table 10 below:

**Table 10: On-Site Reviews for US&FCS End Use Checks**

	US&FCS Checks Reviewed	On-Site review conducted?		
		Yes	No	Unclear
PLC	90	61	14	15
PSV	15	15	0	0
<b>Total</b>	105	76	14	15

Source: Office of Enforcement Analysis, Bureau of Export Administration.

In 1992 US&FCS sent several worldwide cables to US&FCS posts that explained funding procedures for BXA PLCs and PSVs. Upon receiving a PLC or PSV request from BXA, the post is to estimate the marginal costs anticipated for that specific check, cable BXA with the estimate, and request for authorization of funds within five working days. If BXA informs post that the check is canceled, no further action from post is required. If BXA cables back to post with funding authorization, the 28-day time limit for completion begins on the day that cable is sent. A January 1993 cable modified the funding procedure by allowing posts to spend up to \$50 for a single PLC or PSV with no advance approval by BXA. A standard paragraph included in BXA cables to posts requesting PLCs states:

“The deadline for this PLC is 28 calendar days from the date of the BXA cable providing funding. However, if the associated costs are less than 50 U.S. dollars, the deadline is 28 calendar days from the date of this cable.”

We believe that BXA should stress the importance of on-site visits in its cables requesting PLCs and as part of periodic regional training seminars and workshops for US&FCS staff.



In its written response to our draft report, BXA agreed with our recommendation to stress the importance of on-site visits in its end use request cables and when meeting with US&FCS personnel prior to their departure for a new post or when visiting BXA in Washington. In addition, BXA stated that it has prepared a cable on this subject and, after US&FCS clearance, will send it to all US&FCS posts.

#### Record-keeping at most posts needs improvement

BXA's 1998 Handbook recommends that each PLC or PSV file at post be retained for five years, the statute of limitations for the Office of Export Enforcement investigations. The Handbook also recommends that posts maintain specific types of records from the end use check including date and location of the on-site visit, names and titles of all company officials contacted, copies of all commercial reference materials used, copies of any documents provided by the company, copies of all applicable cables, and any notes made by the officer conducting the check. However, based on our survey results, only eight of the 27 posts indicated that they retained records for five years or more. In addition, the types of records retained by these posts varied, but generally did not include all the record types recommended by the BXA. We believe that BXA should remind US&FCS staff of this record-keeping requirement for end use checks.



In its written response to our draft report, BXA stated that it agreed with our recommendation to remind US&FCS staff of its record-keeping requirement to retain proper end use check records for five years. In addition, it stated that it will send a cable to all US&FCS posts reminding them of this requirement after US&FCS management has cleared it. It also informed us that it will reiterate this point when meeting with US&FCS staff prior to their departure for a new post or when they visit BXA in Washington.

#### Most posts surveyed consult with other embassy agencies on end use checks

In our 1997 watchlist review, we recommended that posts' processes for conducting end use checks be improved by consulting with other agency sections at the embassy that may have information about how certain items could be inappropriately used or diverted or about the subject company or organization. In our recent survey of 27 foreign posts, 20 posts responded that they had some involvement with other agencies of the embassy when conducting the checks.

Specifically, 12 of the posts reported that they coordinated or consulted with the State Department's political or economic officer while one post responded that it was State's Economic officer who conducts the end use checks for BXA and coordinates with US&FCS. Ten posts also

reported that they coordinate or consult with Defense offices at the embassy with one reporting that it had to rely on the Defense attaché for appointments with the local military. Four posts reported that they coordinate with the Customs attaché stationed at the embassy, and three posts reported that they coordinate their end use checks with the Regional Security Officer at the embassy. We believe that BXA's guidelines for conducting PLCs and PSVs should specifically list other embassy sections by name that US&FCS should confer with on PLCs and PSVs and include suggested questions for each section.



In its response to our draft report, BXA disagreed with our recommendation to specifically list in the PLC/PSV Handbook the other embassy sections by name that US&FCS should confer with on PLCs and PSVs. It stated that it will continue to recommend that US&FCS check with all appropriate sections at post, but it believes US&FCS staff stationed at a post are in a better position than BXA personnel in Washington to be aware of which sections of a particular post are likely to have useful information about an end user in that country. While we agree that all posts are different and they may have different U.S. government sections present, we have found during our recent inspections of US&FCS posts, as well as our recent visits to two US&FCS posts in conjunction with this review, that US&FCS officials did not always know who they should consult with on an end use check. Therefore, we still contend that BXA should provide in its handbook a general list of U.S. government agencies that US&FCS should consult with when conducting end use checks.

#### Additional training and guidance needed by US&FCS

Of the US&FCS posts surveyed during the current review, 13 of the 27 posts indicated a need for better information in the form of training or other guidance by BXA in order to effectively carry out BXA's end use program. Five felt additional training was not needed, and nine had no opinion. While two posts stated they had received some formal training either from a BXA seminar or a briefing at US&FCS headquarters, the other 25 posts stated that they had received no formal training in how to conduct BXA end use checks.

The posts offered a number of suggestions for what they felt would enable them to conduct more productive and efficient end use checks. One post suggested that the BXA Handbook provide more examples of procedures which proved to be useful with different commodities and in different countries. Another suggested that "best practices" information and samples of informative reports be sent periodically to the posts. Another suggestion was for BXA to provide more background on the history of the need for the checks and exactly how the process should work in the best circumstances. The posts would also like to have training cover up-to-date information on Congressional mandates for export controls, changes to regulations, more background on BXA activities, and case studies or successful and difficult end use checks in workshops. Twelve of the 13 posts visited in recent years by Safeguard teams indicated that accompanying the teams on their checks either provided valuable training or would provide

valuable training if they were invited to accompany the teams. One Commercial Officer summarized the comments of many of his colleagues at other posts when he said, "more direct interaction is needed between BXA and the posts."

We believe that BXA should speak at US&FCS regional conferences, training seminars, or workshops to keep US&FCS staff abreast of current developments in export controls and BXA regulatory procedures. In addition, we believe that BXA should take the opportunity to use its Safeguard Verification program to train US&FCS staff by having the staff accompany enforcement agents on their visits to foreign entities and/or providing other training while at post.



In its written response to our draft report, BXA generally agreed with our recommendation to periodically train US&FCS staff and keep them abreast of current developments in export controls and BXA regulatory procedures. However, it noted that while periodic training is always an excellent idea, neither Export Enforcement nor BXA as a whole is currently in a position to fund the travel of US&FCS officers to the proposed seminars. It was not our intent for BXA to fund the travel of US&FCS officers to proposed seminars but rather that BXA speak at the annual regional seminars that US&FCS holds for its officers, or at other appropriate US&FCS conferences. Nevertheless, BXA also agreed that its Safeguard teams will provide training at posts they visit to the extent possible.

***B. Safeguard Verification Program enhances end use check process, but some improvements are necessary***

BXA's Export Enforcement conducts numerous on-site end use checks under its Safeguard Verification Program. The Safeguard program was originally developed in 1990 to ensure the legitimate use of strategic U.S. goods and technology by the newly emerging democracies of Central Europe, which could serve as diversion points to the former Soviet Union. Since then, the program has been significantly expanded, and export enforcement agents conduct PLCs and PSVs in countries worldwide. In cases where Export Enforcement's Safeguard Verification Teams discover items are being inappropriately used or in a manner that is inconsistent with an export license, they initiate appropriate enforcement actions. Due to the time-sensitive nature of PLCs, almost all Safeguard visits are PSVs.

In addition to conducting pre-license and post shipment checks, Safeguard teams also conduct educational or "outreach" visits to foreign firms and provide guidance and support on preventive enforcement matters to the American Embassy personnel and/or host government export control officials. In fiscal year 1998, Export Enforcement conducted Safeguard Verification trips to the following countries: Jordan, the United Arab Emirates, Russia, Saudi Arabia, Oman, Qatar, Slovenia, Romania, Bulgaria, South Africa, Hong Kong, Israel, Egypt, India, Turkey, Mexico, and Singapore.

From March 8 through March 11, 1999, we participated in 10 post shipment verifications and one outreach visit as an observer on Export Enforcement's Safeguard Verification trip to Malaysia. We also took this opportunity to meet with U.S. Embassy personnel in Malaysia (including the Ambassador, Deputy Chief of Mission, US&FCS Officers, the State Economic Officer, and other appropriate embassy officials) to discuss their views on the Safeguard Verification Program and U.S. end use checks in general. Our participation in that trip greatly enhanced our understanding of how export enforcement agents conduct end use checks.

Based on this trip and our review of Safeguard Verification Trip reports from fiscal year 1998, we believe this program is a valuable tool because of the "enforcement" element it brings to the end use check process. However, we have identified several areas where we believe improvements could make this program more effective, including the initial planning of trips, performing the verifications, reporting the results, and disseminating the final results. We believe all of these areas can be addressed with proper guidance. As noted previously, we also believe that BXA should use Safeguard visits as an opportunity to better train US&FCS staff on conducting end use checks.

#### Selection of verifications should be consistent

BXA has not prepared any written procedures for its export enforcement agents to use in conducting Safeguard visits. Essentially, it is up to the individual Safeguard team to plan and conduct its Safeguard visit however it sees fit without any feedback from headquarters. For example, the team which conducted the verifications in Malaysia informed us that it is left up to the individual team members to decide which PSVs they will perform based on no specific selection criteria.

The agent who selected the checks for this trip used his previous experience in conducting Safeguard visits as a guide to select targets. Specifically, he stated that he pulled all of the licenses approved for Malaysia since the last Safeguard team had been there and then selected a number of shipments based in large part on his familiarity with the commodity itself such as filament winding machines, oscilloscopes, and a chemical known as botulinum toxin. While these commodities appeared to be appropriate, it was not clear from our discussions if either agent knew which types of commodities or end users were "more of a concern" from either a proliferation or diversion perspective in Malaysia.

Since BXA's Office of Enforcement Analysis issues a Strategic Plan for Targeting PLC/PSVs annually which lists countries of concern by a regime office, we believe it might be helpful to incorporate this information into a handbook for conducting Safeguard Verifications.



In-country consultations would be helpful

Also, the teams have not been given instructions as to whom they should meet with in the U.S. mission at post to get a broad picture of the country's economic, political, and security policies. As a result, the Safeguard team we observed in Malaysia did not meet with any of these embassy officials with the exception of the US&FCS. We believe the teams should also meet with host government officials involved in local export control or enforcement areas as well as U.S. embassy personnel (e.g., the Defense attaché, State's Economic or Political Officer, the Customs attaché, Federal Bureau of Investigation attaché, and other appropriate embassy officials) who might be knowledgeable of proliferation threats or diversion activities associated with the individual country, what export control programs the country has and how effective they are, as well as the country's relationships with countries of concern.

Safeguard reports are not consistent in content and format

In addition, we found that the quality and format of Safeguard trip reports varied. Some reports we reviewed provided an initial description of critical details about the specific checks performed, including whether it was a PLC or PSV; results of check; license number, if applicable; date of shipment; commodity control number; exporter name and location; ultimate consignee name and location; end user name and location; end user statement; and list of conditions placed on the license. Other reports we reviewed had some of this information, but it was buried in the descriptive summary of the particular check. However, one report never clearly identified the actual commodities being verified. In addition, the method used to count the number of National Defense Authorization Act checks appeared to vary from one report to another. We believe that any guidelines created for conducting Safeguard Verifications should include a template or standard format for agents to follow when preparing these reports.

In addition, Export Enforcement may want to encourage Safeguard teams to take photographs during the course of their verifications. During the checks we observed in Malaysia, the agents took photographs of various sites and commodities they checked out. We believe this could be a useful tool for Export Enforcement with regard to educating other agents or licensing officials of how certain generic commodities can actually have a variety of appearances (e.g., filament winding machines). We believe that Safeguard teams should be encouraged to add such details to their reports whenever possible.

Timeliness of reporting results is an issue

We believe that Safeguard Verification trips are an important source of information for both the licensing officers and Export Enforcement analysts at headquarters. However, we found that enforcement agents took an average of over three months to submit a written report to Export Enforcement headquarters after each trip. Thus, the results of the Safeguard checks, mostly post shipment verifications, were not entered into ECASS in a timely manner.

Based on the 12 Safeguard visits conducted from October 1, 1997 thru September 30, 1998, Export Enforcement reported it conducted 25 PLCs and 286 PSVs. However, according to an October 1998 ECASS printout for all PLCs and PSVs conducted during fiscal year 1998, only 66 of these were listed.<sup>63</sup> Five of the missing PSVs conducted resulted in unfavorable findings. Licensing officers who are not aware of the unfavorable checks may approve export licenses for exports to consignees with unfavorable end use checks. Thus, we believe it is critical for unfavorable or questionable findings to be included in ECASS, as soon as possible, so that licensing officers and export enforcement analysts can have that information when making licensing and enforcement case decisions. As a part of any handbook created for conducting Safeguard Visits we believe that Export Enforcement should provide guidelines for the prompt reporting of unfavorable Safeguard results.

Wider dissemination of Safeguard trip reports is needed

While BXA has forwarded some hard copy Safeguard trip reports to the Nonproliferation Center in the past, we found during our review that this has not been a routine practice. While the Nonproliferation Center has found the reports it has seen to be informative, it indicated that hard copy reports are difficult to use in its analysis because the reports are categorized by country and it conducts its searches by end user. Therefore, the Nonproliferation Center suggested that these reports be sent in an electronic format so that the data can more easily be uploaded into its database of end users. Export Enforcement officials informed us that this should not be a problem since the agents usually send the reports to headquarters in an electronic format. Therefore, we encourage BXA to ensure that the Nonproliferation Center is on its distribution list for all of these reports and that these reports are forwarded to the Nonproliferation Center in an electronic format.

In addition, US&FCS has also expressed an interest in receiving Safeguard trip reports. They believe that the results would be informative because of US&FCS's role in working with local businesses in the host country. The reports could also be a guide for commercial officers to follow when they prepare their end use check reports for BXA. We believe that this could be helpful and suggest that BXA include the appropriate US&FCS post on its distribution list.



In its written response to our draft report, BXA agreed with our overall recommendation to develop guidance for EE agents for Safeguard Verifications, including (1) criteria to help guide agents in selecting which PLC/PSVs to do, targeting countries and shipments of greatest concern, (2) a template or standard format for agents to follow when preparing Safeguard trip reports,

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<sup>63</sup>BXA later provided us with an updated ECASS printout dated April 1998 and we determined that most of the data related to Safeguard end use checks had been entered into ECASS.

(3) a suggestion that photographs be taken of the sites and commodities inspected, when appropriate, during their verifications to be included in their reports, and (4) procedures for the prompt reporting of unfavorable Safeguard results.

In addition, while BXA disagreed with our recommendation that there be a requirement for the Safeguard Verification teams to meet with host government officials involved in local export control or enforcement areas, as well as U.S. embassy personnel who might be knowledgeable of proliferation threats or diversion activities associated with the specific country, it agreed that this is a valuable suggestion and BXA will implement it where feasible. Specifically, BXA stated that the feasibility of meeting these officials varies from country to country and will depend on the interests of the host government and U.S. Embassy or Consulate officials.

Finally, BXA generally agreed with our recommendation to distribute its Safeguard trip reports to the CIA's NPC and US&FCS posts. Specifically, it reported that the Office of Export Enforcement is currently working with the Office of Executive Support to make the Safeguard trip reports available to the Nonproliferation Center in an electronic format. However, it stated that its ability to distribute these reports to US&FCS posts is contingent upon US&FCS agreeing to appropriate procedures to prevent their improper dissemination. We believe that BXA should work out the details of such dissemination with US&FCS as soon as possible so that US&FCS officials can benefit from the use of the Safeguard reports.

***C. End use checks in three countries of concern were reviewed by OIG teams***

As a part of our inspections of US&FCS operations in the People's Republic of China and Hong Kong during August 1998, we reviewed these posts' end use check activities. While the reluctance of the Chinese government to allow end use checks has precluded the United States government from performing many of these checks, BXA reports a slight improvement in this area since the U.S. China summit in June 1998. In addition, we found that Hong Kong—even after its reversion to Chinese sovereignty on July 1, 1997—has continued its willingness to work with the United States to ensure that exported technologies are protected from diversion or misuse. During the course of this review, we also visited Israel and observed how US&FCS conducted end use checks there by participating in five post shipment verifications.

**End use checks are an ongoing struggle in China**

With a population of 1.3 billion, China is a market with enormous potential for U.S. exporters. While the United States wants to help its high-tech industries remain competitive in China, it cannot ignore China's military modernization or its role in weapons proliferation. In April 1998, the Justice Department began investigating two aerospace companies for possibly providing sensitive information to China which could help it improve its ballistic-missile launch capabilities. It is not yet known whether the recent allegations in the U.S. Congress and press over U.S. sensitive technology trade with China will change the prospects for continuing growth in general U.S.-China trade. To complicate matters, the controversy over U.S. strategic trade with China

has escalated considerably since our August 1998 visit to China with the recent accusations of espionage by the Chinese at Energy’s laboratories.

The U.S. government’s ability to distinguish between a civilian and military end use is critical when determining whether to issue an export license for sensitive technologies. Due to these concerns, US&FCS and BXA reached an agreement in which BXA relinquished one of its full-time equivalent positions to US&FCS China in exchange for placing one of BXA’s employees in FCS Beijing.<sup>64</sup>

End use checks have always been an issue in China. For instance, the Chinese began denying requests for PLCs from late 1996 to May 1998. Of the 10 PLCs requested in 1996, five were completed and five were canceled. Of the five completed, four were considered favorable, and one unfavorable. Of the four PLCs requested in 1998, two were completed and determined to be favorable while two were canceled. Of the two that were canceled, one was due to the Chinese refusal to allow the check and one was due to the fact that BXA determined that the item in question did not require an export license. (See Table 11.)

While the Chinese allowed the United States to conduct some PLCs, no PSVs had ever been conducted until September 1998. According to BXA officials, one of the accomplishments of the U.S.-China Summit in June 1998 was that the Chinese agreed to a framework allowing PSVs of U.S. exports. However, under this framework, the Chinese government still reserves the right to arrange these visits on a case-by-case basis. If the Chinese government refuses the request for an end use visit, the U.S. maintains the ability to take appropriate action—which can include denying future licenses to the Chinese end user.

**Table 11**

<b>Pre-License Check History in China Fiscal Years 1996-98</b>				
<b>Fiscal Year</b>	<b>Requested</b>	<b>Completed</b>	<b>Canceled</b>	<b>Pending</b>
1996	10	5	5	0
1997	10	0	10	0
1998	4	1	2	1

Source: US&FCS Beijing

At the time of our inspection, there were three pending PSVs (two of which had been pending for more than 30 days and a third that was new). We have since learned that the Chinese allowed

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<sup>64</sup> The employee, who speaks Mandarin Chinese, arrived in Beijing in August 1995 under a limited appointee status. His responsibilities include both export controls and other US&FCS-related activities.

these checks to be conducted as well as an additional three. The results of these checks, which were conducted jointly by Chinese and U.S. officials, were favorable.

End use checks in Hong Kong are being conducted with local government consent

There has been no change in the U.S. export licensing policy for dual-use goods and technologies to Hong Kong since its reversion to Chinese sovereignty on July 1, 1997. Current U.S. policy is to continue the preferential treatment of Hong Kong—a Special Administrative Region of the Peoples Republic of China—for dual-use licensing despite more stringent export controls on China itself. This is due in part to the Hong Kong Government's own restrictions on the export of high-technology products to countries proscribed under the current nonproliferation regimes, including China.

In October 1997, the Secretary of Commerce and the Hong Kong Secretary for Trade and Industry signed an "agreed minute" on ways to enhance export control cooperation, including semi-annual interagency meetings to exchange information and provide updates. Officials at BXA believe these semiannual meetings are an important component of its monitoring of Hong Kong's export control program to determine whether Hong Kong's system continues to be effective and autonomous, rather than influenced by the Chinese government.

Based on our discussions with BXA officials and various U.S. officials at the U.S. Consulate in Hong Kong, it appears as though the U.S. has close and beneficial relations with the Hong Kong Customs Authorities and the Hong Kong Trade Department which provides the basis for Hong Kong's continued access to exports of controlled U.S. technologies. However, it is still important for the U.S. to continue its monitoring of trade to Hong Kong to ensure that exported technologies are protected from diversion or misuse.

One significant way in which the Hong Kong government's approach to export controls continues to be different from that of China is its policy regarding U.S. officials' preventive enforcement activities. Specifically, the U.S. is not precluded from conducting these checks on its own as the U.S. is in China.

During our inspection of US&FCS Hong Kong in August 1998, we found that the US&FCS routinely coordinated its end use checks with other consulate agencies such as State's economic/political section and the U.S. Customs Service. Although we did not find that US&FCS was coordinating these checks with the Defense section, both agencies agreed that such coordination could prove useful. US&FCS Hong Kong subsequently agreed to notify the Defense attaché's office of any future end use check requests.

A review of the available records and interviews at the time of our on-site visit indicated that the checks were generally conducted on-site by a commercial officer and a Foreign Service

National.<sup>65</sup> During fiscal year 1997, US&FCS Hong Kong conducted 12 PLCs and one PSV. From October 1997 to May 1998, US&FCS conducted 12 PLCs and four PSVs. We found the response cables for these checks to be detailed and thorough. In addition to the normal “cable” channels used by posts to officially report these results, US&FCS Hong Kong and BXA routinely communicated with each other via e-mail which enabled US&FCS to ask additional questions of BXA concerning the requested checks and for BXA to provide additional information to the post in a more timely fashion. BXA officials informed us that they were satisfied with the information US&FCS Hong Kong provided them on end use checks.

As mentioned previously in this section, BXA also sent two Safeguard Verification teams to Hong Kong during fiscal year 1998 and one in March 1999. Both U.S. consulate officials and the US&FCS Hong Kong consider BXA’s safeguards program to be an important part of U.S. efforts to maintain vigilance of Hong Kong’s export control system and both are fully supportive of this effort. The team that went to Hong Kong in June 1998 was able to conduct 13 PLCs and PSVs (including one end use check that had been assigned to US&FCS). Eight of these checks resulted in favorable and three in favorable ratings with reservations. The team that went in September 1998 were able to conduct 13 PSVs, two of which had unfavorable ratings. In addition, this team noted that while they saw few signs of Chinese governmental presence, nearly every corporation visited had a facility in China and many employees of Hong Kong companies live in China. At the time of this writing, the results of the Safeguard trip in March 1999, had not been released.

This gradual blending of China and Hong Kong will undoubtedly create new challenges for U.S. export control policy to Hong Kong. It is our understanding that the Secretary of Commerce’s fiscal year 2000 budget submission to the Office of Management and Budget included a request for an export enforcement agent to be stationed in Hong Kong. We believe such action is warranted considering Hong Kong’s willingness to work with the United States to prevent and detect illegal diversions of critical dual-use commodities and technologies to China.

#### US&FCS Tel Aviv generally follows BXA guidelines for end use checks

The United States is Israel’s major source of economic and military aid. According to U.S. embassy officials in Tel Aviv, Israel has a technologically advanced market economy with

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<sup>65</sup> As discussed previously in part A of this section, one PLC consisted of an FSN calling the entity to set up an appointment but learning that the entity intended to sell the commodities to factories in China. Based on this information, BXA gave the PLC an unfavorable rating. In a second PLC, US&FCS personnel (CO and FSN) had conducted an on-site PSV of the ultimate consignee one month prior and decided to call instead of revisiting the entity. The ultimate consignee advised that one of the end users (also subject to this check) had not placed an order yet and emphasized that the end users listed were potential customers. The FSN subsequently called one of the end users to set up an on-site visit but the company verbally confirmed it had not placed an order yet. US&FCS did not have any reason to question the legitimacy of the ultimate consignee and recommended approval. BXA rated this check as “limited” because of the sole FSN involvement in the later conversation.

substantial government participation. However, as discussed in the 1999 Country Commercial Guide prepared by the U.S. Embassy in Tel Aviv, Israel maintains very few export controls. Those that do exist are primarily targeted against internationally controlled substances and/or designed to protect national security. Israel adheres to the Missile Technology Control Regime and maintains export controls on a variety of military and sensitive technologies destined for certain proscribed countries. U.S. export licenses are required for exports to Israel of certain high-technology, defense equipment/technologies and weapons for chemical/biological warfare. Israel is considered by BXA to be a country of concern for nuclear control, chemical or biological warfare control, and missile technology control.

As a part of our current review of export licensing, we visited Israel in January 1999 to accompany US&FCS Tel Aviv personnel on five post shipment verifications to observe how they conduct end use checks. In addition, we examined post records for fiscal year 1998 end use checks. Overall, we found that US&FCS Tel Aviv generally performed the end use checks in accordance with BXA guidelines. In fact, the Senior Commercial Officer informed us that he likes to participate in these checks because not only do they emphasize the continued oversight of exports by the United States Government, but they also afford US&FCS the opportunity to establish or reestablish positive contacts with Israel's commercial companies and military organizations.

#### ***End use checks observed by OIG***

During our on-site visit, we discovered that US&FCS Tel Aviv was using BXA's 1992 guidance to conduct end use checks. US&FCS personnel stated that they were unaware that BXA had issued subsequent guidance in 1996 and 1998 so we provided post personnel with BXA's 1998 guidance.<sup>66</sup>

The five post shipment verifications conducted by US&FCS Tel Aviv during our visit all dealt with high performance computers going to two commercial and three military end users in Israel.<sup>67</sup> US&FCS personnel classified all five checks as favorable. During our visits at one of the military installations, we did not observe three of six systems. The military entity informed us that the three systems had been installed at two other military installations located elsewhere in Israel. US&FCS Tel Aviv's response cable to BXA stated that despite only identifying three of the six systems during the one visit, they had no reason to suspect that the other three systems

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<sup>66</sup>Upon our return, we asked BXA about its distribution method for its guidance and it informed us that the guidance is given to US&FCS headquarters to send to post.

<sup>67</sup>These post shipment verifications were performed pursuant to the requirements in the National Defense Authorization Act for Fiscal Year 1998 as previously discussed in Section I of this report.

were not being used in accordance with the terms of the export licenses.<sup>68</sup> The cable further stated that if BXA believed US&FCS Tel Aviv's report was incomplete, BXA should cable the post with a new PSV request for on-site visits verifying the three remaining systems.

### ***End use checks conducted by post and Safeguard Verification Program***

During fiscal year 1998, US&FCS Tel Aviv performed 13 PLCs and 13 PSVs. An additional PSV was canceled because the equipment was allegedly incorporated into two flight simulators at an Israeli air force base and US&FCS was unable to physically inspect the goods. Twenty five out of the 26 checks were conducted by a US&FCS officer or a representative from the Department's International Trade Administration who was on temporary assignment at US&FCS Tel Aviv. One PLC was performed solely by a senior FSN, however, the post had not requested a waiver from BXA to do so as its guidelines require. Specifically, since the commodity subject to the check was controlled for missile technology concerns and Israel is one of the countries that BXA has identified as of concern for missile technology controls, FSNs may not be used (except to accompany a permanent U.S. government employee who is a U.S. citizen) for PLCs or PSVs for such checks. In the future, US&FCS Tel Aviv must request waivers from BXA before using FSNs to conduct end use checks for nuclear, chemical or biological warfare, and missile technology controls.

We also found that post personnel maintained fairly extensive records of current and prior end use checks. Post personnel have maintained a log of every check for the last 12 years and file records for all checks for the last three years. However, BXA's current guidelines recommend that file records be kept on all checks for five years. After we pointed this out to the SCO, he assured us that the post will extend their file records for five years.

While there are other sections in the embassy that either perform end use checks (e.g., State's Economic Officer) or potentially could provide technical expertise or information (e.g., Defense Attaché), US&FCS Tel Aviv does not exchange its end use check information or discuss end use check issues with these other groups. US&FCS personnel stated that because each group at the post is burdened with its own workload, structured coordination has not taken place. However, it agreed that they could improve information exchange with the other groups.

We also discussed this issue with the embassy's Deputy Chief of Mission and we suggested that the various embassy sections attend quarterly meetings to discuss prior and current check cases, issues, and problems. The Deputy Chief of Mission agreed that quarterly meetings would benefit all personnel involved in end use checks. US&FCS personnel also believed that quarterly meetings would be beneficial and plan to initiate meetings very shortly.

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<sup>68</sup>USDOC Tel Aviv 01544, dated February 2, 1999, and USDOC Tel Aviv 01817, dated February 8, 1999.



We also noted that a Safeguard Verification team visited Israel during June and July 1998 and conducted 40 post shipment verifications—32 of them were for high performance computers as required by the National Defense Authorization Act. However, other than one senior FSN participating in this Safeguard Trip with BXA enforcement personnel, US&FCS Israel's commercial officers have not received any end use check training from BXA. As we pointed out in Part A of this section, BXA needs to conduct periodic training seminars and workshops to keep US&FCS staff abreast of current developments in export controls.



## IX. Other OIG Concerns Are Related to the Export Licensing Process

During our review, we identified two areas in the export licensing process that have raised enforcement concerns. One area is BXA's practice of "returning without action" export license applications for which unfavorable PLCs were received. A second area is the untimely processing by Export Administration of license determination requests from Export Enforcement and the U.S. Customs Service.

### A. *Applications were returned without action after receiving unfavorable PLCs*

A decision to return a license application to the exporter without action means that the license application has been neither approved nor denied. If a license is required for the commodity and/or destination, such a decision blocks the export. The exporters can still reapply for a license in the future. In fiscal year 1998, BXA processed 11,015 license applications, 2,130 of which were returned without action.

According to the Export Administration Regulations,<sup>69</sup> an application may be "returned without action" for one of the following reasons:

- The applicant has requested the application be returned.
- A License Exception applies.
- The items are not under Department of Commerce jurisdiction.
- Required documentation has not been submitted with the application.
- The applicant cannot be reached after several attempts to request additional information necessary for processing of the application.

Based on our sample of fiscal year 1998 PLCs, we identified three export license applications that were returned without action although they received unfavorable PLCs. We asked BXA and Defense about these three cases, and their comments are discussed below. In the first case, the application listed four end users located in Hong Kong. However, based on the PLC initiated by Export Enforcement, all four end users reportedly planned to have the commodities shipped directly to their factories in China. Although the application failed to mention that the ultimate destination was China, the licensing officer requested that the application be returned without action due to the age of the application (the application was received in early October 1997 and returned without action in mid-March 1998). Ultimately, Export Enforcement concurred with this recommendation.

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<sup>69</sup>15 CFR 772.

The Deputy Assistant Secretary for Export Administration informed us that all referral agencies reviewed the case and recommended approval with standard conditions. However, according to the Defense OIG, the Defense Threat Reduction Agency (DTRA) believes that BXA should have notified them of the unfavorable PLC even though it did not condition its approval on a favorable check. DTRA said that if it had known about the unfavorable PLC, its recommendation would have been different.

In the second case, comments by the licensing officer in the case history indicate that the licensing officer wanted to return without action the case after Export Enforcement had recommended rejection, but was prevented from doing so as long as Export Enforcement maintained its rejection. Per the case history, one reason Export Enforcement was recommending rejection was due to a guilty plea by a U.S. representative of the foreign entity in a 1995 U.S. Customs case involving a similar export. In addition, there was an ongoing Customs investigation of the company.

In his comments on this case, the Deputy Assistant Secretary wrote that when the investigation was closed with no derogatory results for the foreign company, the licensing officer was advised to call the exporter to see if he still wanted the license. The applicant asked that the application be returned without action since the order had been canceled. Because the applicant requested that this case be returned, the Office of Export Enforcement changed its rejection recommendation to return without action. However, a non-derogatory pre-license check was a requirement for a conditional approval by Defense. According to Defense OIG, DTRA was not informed of the unfavorable PLC conducted by the post.

In a third case, a license application was returned without action after an unfavorable PLC by the post reported that the equipment in question had already been delivered to the consignee in Malaysia and reexported six weeks earlier. According to the regulations, an exporter may not submit a license application for a shipment that has already been exported or reexported.<sup>70</sup> If such an export or reexport should not have been made without first securing a license authorizing the shipment, the exporter should send a letter of explanation to BXA's Office of Export Enforcement. The Office of Export Enforcement headquarters referred this case to one of its field offices for an investigation.

In his comments, the Deputy Assistant Secretary wrote that there is no indication in the file that Export Enforcement recommended a rejection to this application. According to the Defense OIG, Defense Threat Reduction Agency was again not informed of the unfavorable PLC. Although it did not condition its approval on a favorable check, Defense stated that if it had known about the unfavorable PLC, its recommendation would have been different.

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<sup>70</sup>15 CFR 748 and 15 CFR 748.4.

In the opinion of a senior Export Enforcement official, if information is known that would cause an application to be denied, that application should be denied, not returned per the applicant's request. If the application is not denied, the applicant is not officially informed as to why BXA had a problem with the end user. In addition, if the commodity is one controlled by an international regime with a "no undercut" policy, returning the application without action prohibits the U.S. from notifying the group. The purpose behind the "no undercut" rule was to discourage a country from licensing a commodity to a particular end user who has been denied a shipment by another member of the group. This prevents the companies in one country from profiting as a result of export controls in another country.

We believe that returning license applications without action, which have already received unfavorable PLCs, sends an unclear message about the legitimacy of the export transaction to the exporter. A denial of an application sends an unambiguous message that some part of a transaction involving controlled U.S.-origin goods or technical data was not suitable. We also believe that BXA should inform referral agencies of all derogatory PLC results.



In its written response to our draft report, BXA stated that it agreed with our recommendation to inform the advisory agencies when it receives a negative result on a PLC involving a case that had been referred to them, understanding that this additional information may affect the agencies' original position on the application. However, it disagreed with the three examples we highlighted. While we agree with BXA that returning a license application without action is not a license to export, it does not change the fact that BXA should have consulted with the advisory agencies on these three cases before doing so—especially since the PLCs were unfavorable. In addition, the first case involved commodities controlled by the Australia Group and the United States could have applied the "no undercut" rule if it had denied the application. Finally, we want to point out that while our report does mention that there were 2,130 return without actions in FY 1998, we did not state that we found only 3 cases of BXA returning a license without action when a negative PLC existed from this number. The examples we found were identified from our selected sample of 166 PLCs conducted in FY 1998.

***B. License determination process is untimely***

BXA's Export Enforcement implements the enforcement provisions of the Export Administration Regulations, such as investigating allegations of violations of the Export Administration Regulations. The U.S. Customs Service is also authorized to seize and detain any item whenever they know or have probable cause to believe that the items are intended to be, are being, or have been exported in violation of the Export Administration Regulations.<sup>71</sup> In both circumstances, it is often necessary for BXA's export enforcement agents and Customs inspectors to request

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<sup>71</sup>22 U.S.C. Section 401, et seq.

license determinations from BXA licensing officials in Export Administration. The license determination—similar to a commodity classification request from an exporter—includes an assessment of (1) whether or not the item is “subject to the Export Administration Regulations,” (2) the reason for control, and (3) the licensing policy for export of the item to the specified destination. During fiscal year 1998, BXA completed 393 Export Enforcement and Customs license determinations.

We examined Export Enforcement’s manual records for 212 license determinations referred to Export Administration during the period January 1, to June 30, 1998, finding that the average response took 36 days.<sup>72</sup> Included in this 36-day average, are 12 license determinations that took more than 100 days to be returned to Export Enforcement. Export Administration officials informed us that six of the 12 license determinations took longer than 100 days to process because of delays in obtaining additional information from the agents (such as additional technical specifications and possible end uses for the item). However, Export Administration could not justify why the remaining six took so long. As a result of the lengthy processing times, Export Enforcement officials informed us that agents are sometimes forced to delay opening an official investigation on an exporter.

In addition, we worked with the Department of Treasury’s OIG who examined 120 license determination referral records from Customs to Export Administration during the period January 1, to June 30, 1998. While the average processing time was somewhat better than that for Export Enforcement license determinations—the average processing time being 24 days—we still found two license determinations which took more than 100 days. Treasury’s OIG sampled 10 of the license determinations that were beyond the 20-day response time, finding that three license determinations were agent inquiries involving no detention, three were referred to State, and the remaining four were ultimately released because it was determined no license was required.

According to the Export Administration Act, Customs is only allowed to detain a shipment for up to 20 days before it must either formally seize or release the goods.<sup>73</sup> Thus, Customs essentially has three options with regard to holding shipments up as a result of license determinations more than 20 days old. It can either (1) continue to detain the shipment in violation of the Export Administration Regulations, (2) formally seize the shipment, or (3) let the shipment go. Depending on the view—law enforcement community or U.S. exporters—none of these three options are optimal if the agent does not have a license determination. In options one and two, Customs could hold up legitimate trade if it is determined that the item did not require a license (as indicated in four of the cases above). On the other hand, by letting shipments go after 20 days

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<sup>72</sup>To Export Administration’s credit, Export Enforcement officials stated that Export Administration is usually very responsive to emergency license determination requests.

<sup>73</sup>Section 12 (2)(a) of the Export Administration Act.

due to untimely license determinations, controlled goods could leave the United States without a valid license decision.

Some of the reasons for untimely processing of license determinations are similar to those which cause delays in the CCATS process. They include a (1) lack of a front-end technical review in Export Administration to pre-screen license determinations before assigning them to the appropriate licensing division for review, (2) lack of incentives to process license determinations in a timely manner, and (3) lack of written procedures for assigning license determinations that are reviewed by LOs in multiple divisions. We believe our recommendations to correct these deficiencies in the CCATS process should also be implemented for license determinations. Namely, Export Administration needs to ensure that the quality control mechanism put in place in February 1999 is not affected in the future by absences of key staff persons currently assigned this function. Secondly, Export Administration managers must communicate to LOs the importance of processing license determinations in a timely manner and hold them accountable for doing so. To help managers with this task, BXA should program ECASS to allow for the "hold without action" feature for limited circumstances, e.g., during a request for additional information necessary related to the license determination request. Finally, Export Administration should issue written procedures for assigning license determinations reviewed by multiple divisions as soon as possible.

However, we also identified some additional reasons why license determinations may not be processed in a timely manner including (1) Export Administration's lack of established time frames for processing license determinations and (2) BXA's and Custom's license determination referral processes are not automated.

#### Lack of established time frames to process license determinations

Unlike the 14-day time requirement allocated to process CCATS requests for exporters, there is no established time requirement for processing license determinations for the law enforcement community.<sup>74</sup> In October 1998, BXA's Deputy Assistant Secretary for Export Administration drafted guidance recommending that license determinations should be completed within the same 14-day time period as required for CCATS, as long as the license determination consists of six items or less and all information necessary to complete the license determination has been submitted. However, this guidance has not been officially approved or circulated to LOs. We encourage Export Administration management to do so immediately.

In addition, we believe that some type of written agreement may be needed to outline the responsibilities of each party involved in this process (i.e., Export Administration and Export Enforcement, and Export Administration and Customs). Specifically, each agreement should set forth standard procedures for (1) submitting license determination requests (e.g., required

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<sup>74</sup> 15 CFR 750.2.

information needed by Export Administration to make a determination), (2) processing license determination requests in a timely manner, and (3) the escalation process for late license determinations.

BXA and Customs license determination referral process not automated

When custom agents or inspectors in the field need a license determination from BXA, they must first submit the request, by FAX or phone call, to the EXODUS Command Center at Customs Headquarters. An individual in this unit then actually hand carries the request over to BXA's Headquarters. Once BXA has completed the license determination, someone from EXODUS must physically come back over to BXA and pick it up. Then, EXODUS must feed the license determination back to the original requester in the field, by FAX or phone call. We believe this is an inefficient process which causes unnecessary delays for Customs in obtaining license determinations. Both BXA and Customs officials have stated that this process should be automated to make it more efficient. We agree and we would encourage BXA to work with Customs to find a way to automate this process.



In its written response to our draft report, BXA agreed with our overall recommendation to process license determinations in a timely manner. Specifically, it agreed to (1) institute a front-end review process, (2) implement guidance requiring that license determinations be made within 14 days, and (3) develop a written agreement between Export Administration and Export Enforcement and Export Administration and the Customs Service outlining the responsibilities of each party involved in the LD process. With respect to the front-end review process and the written agreement between Export Administration and Export Enforcement, BXA informed us that these actions have already been completed. However, BXA did not indicate how it plans to ensure that the front-end review of LDs will not be affected by absences of key staff persons who are currently assigned this responsibility. Therefore, we reaffirm this recommendation.

In addition, BXA's response stated that similar to our CCATS recommendation of instituting a "hold without action" feature in ECASS for LOs to use in limited circumstances, it will investigate the costs and benefits of this recommendation further. However, we still contend that BXA managers are unable to tell why an LD has been delayed which makes it harder for them to hold licensing officers accountable for their inactions. Therefore, we reaffirm our recommendation.

BXA also indicated it was reviewing our recommendation to issue written procedures for assigning LDs reviewed by multiple divisions. It went on to say that based on the experience gained from its front-end assignment effort, it will develop written procedures as appropriate. We agree.



Finally, BXA concurred with our recommendation to automate the referral of LD requests from Customs to Export Administration, resources permitting. We believe that automating this process will greatly enhance the efficiency of processing LDs for Customs. Therefore, we reaffirm this recommendation.

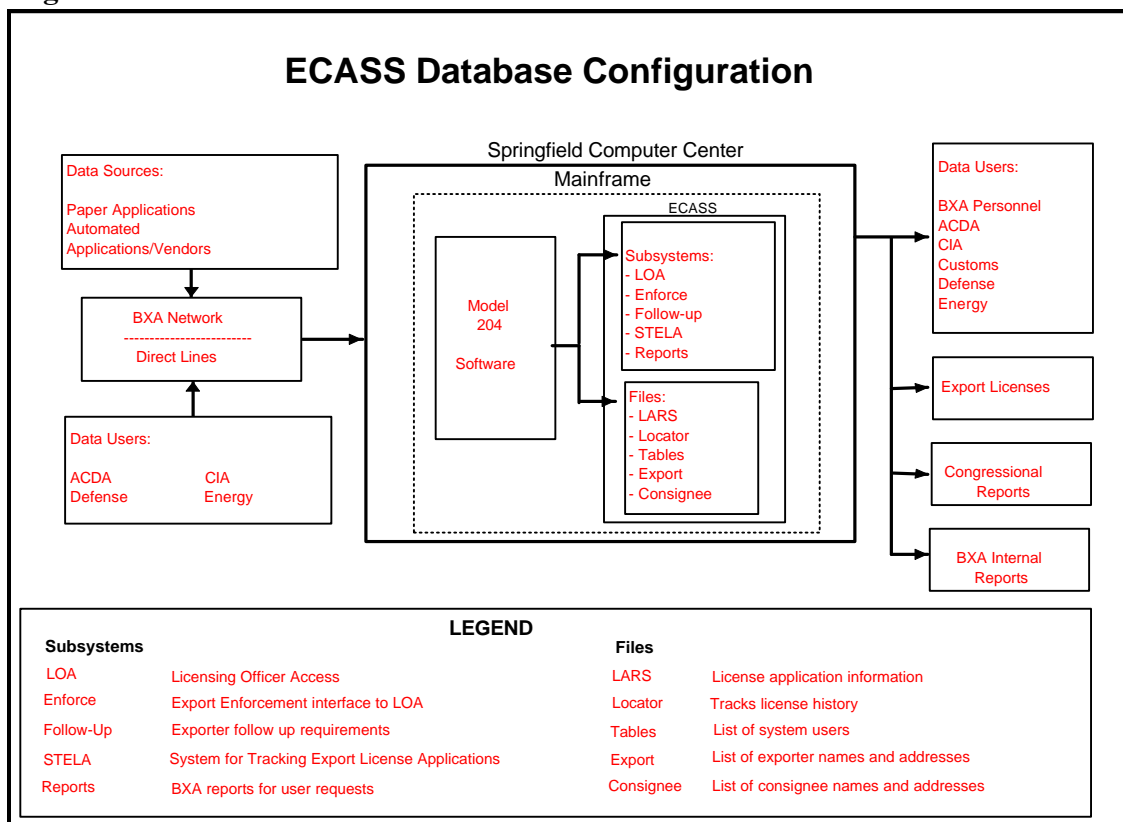


## X. BXA Needs a New Automated Export Licensing System

BXA developed the Export Control Automated Support System (ECASS) in 1984 to expedite the license approval process and better serve the U.S. exporter. ECASS is a large database designed to process, store, and transmit dual-use export licensing information. It runs on a mainframe at the departmental computer center in Springfield, Virginia. ECASS is an unclassified system and it supports over 600 users including BXA headquarters and field offices; the Arms Control and Disarmament Agency (now part of the State Department); the Central Intelligence Agency; and the Departments of Defense, Energy, State, and Treasury. (See Figure 12.) During its life cycle, ECASS has been upgraded to permit manual, electronic, and optical character recognition data entry of license applications and commodity classification requests.

To complete our review of the export licensing process we (1) evaluated BXA's plans to upgrade ECASS, (2) determined whether current system coordination by the export licensing agencies has been adequate, and (3) conducted an internal control review of ECASS general and application controls. While we determined that ECASS internal controls are adequate, we concluded that a new system is needed to process export license applications more efficiently and effectively, and better interagency coordination is needed to coordinate system issues.

Figure 12



Source: Office of Administration, Bureau of Export Administration.

**A. ECASS has major limitations and needs to be replaced**

ECASS was designed to be an “assembly-line” database that would process many applications with minimal analysis and text input from the licensing officers and supervisors. By 1990, ECASS was processing about 65,000 applications a year. While the number of license applications has significantly fallen throughout the 1990s, the analysis required for each application has significantly grown. ECASS is not suited for the current era of license processing. Today’s licensing systems need good query capabilities, expanded text capabilities, modern interfaces, online access to exporter technical specifications, and access to outside commercial databases. ECASS lacks all of these functions.

- **ECASS has limited query capability.** As such, it is difficult for licensing officers to obtain historical information on a commodity, consignee, or end user necessary to make the most informed licensing decision.
- **ECASS has limited text capability.** Specifically, it does not allow licensing officers to incorporate detailed text into the license record.
- **ECASS has no modern interfaces.** Licensing officers must exit the database every time they want to use any office automation applications such as word processing.
- **ECASS lacks online access to exporter technical specifications.** Licensing officers at both BXA and referral agencies cannot review exporter technical specifications online through ECASS. Therefore, BXA must make copies and distribute the paper technical specifications to the applicable referral agencies, a task that is time consuming.
- **ECASS has limited access to outside databases.** ECASS does not allow its users to obtain information from outside databases, such as Dun and Bradstreet, and directly input the information into a license application file. Licensing officers and supervisors must obtain information outside of ECASS and then “cut and paste” information into the system.

**B. Future export licensing automation needs interagency commitment and coordination**

BXA’s licensing officers have maintained for some time that the above problems severely limit their processing capabilities. BXA management, recognizing these problems with ECASS, has spent over two years and approximately \$500,000 on a contractor’s analysis for a new automated licensing system. The contractor’s final product included (1) a business case study of BXA’s export licensing process, (2) a business process re-engineering study, and (3) an information

architecture study.<sup>75</sup> The contractor concluded that “ECASS is no longer mission capable” because it was not designed to meet the current licensing and enforcement requirements, and that BXA should re-engineer its automated licensing, enforcement, policy, and administrative processes. Specifically, the contractor recommended that BXA implement an integrated relational/document oriented system with a centralized architecture located at Commerce headquarters. A relational database would store structured data, including the names, consignees, and end users from license applications, and a document-oriented system would store unstructured data, including licensing officer notes, supervisory comments, and enforcement reports.

BXA personnel stated that the contractor’s three studies provided valuable information, including technical architecture requirements, information architecture principles, and information architecture standards. We agree. Overall, the three reports provide BXA with excellent guidelines, requirements, and standards for future system development and, we believe, support BXA’s justification for a new system. However, after reviewing the three studies, we found that the contractor was not tasked with evaluating all reasonable alternatives. Specifically, the contractor did not (1) determine whether developing a classified system made sense, (2) evaluate how the current interfaces with the referral agencies could be improved, and (3) determine if a joint interagency system was feasible. Nor did the contractor fully justify the proposed move of BXA’s licensing operations to Commerce headquarters.

#### Other Alternatives Not Explored

In the 1993 special interagency IG review report, we recommended that the various export licensing agencies develop improved access to ECASS to enhance the effectiveness of the licensing review process. However, BXA’s contractor did not evaluate the current or future interfaces with the other licensing agencies, including whether a classified or joint interagency system would be desirable or feasible, in its re-engineering effort.

#### ***Classified system may be warranted***

Currently, three of the five referral agencies—Defense, Energy, and the CIA’s Nonproliferation Center—have classified export licensing systems. Because ECASS is an unclassified database, there are no direct connections between it and the three agency databases. BXA exchanges

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<sup>75</sup>Process Reengineering and Implementation Plan, Booz Allen & Hamilton, June 22, 1998; Information Architecture and Implementation Plan, Booz Allen & Hamilton, October 1998.

licensing data with these agencies through electronic data interchange.<sup>76</sup> As such, these agencies receive license applications daily when the data is uploaded to terminals connected to their respective classified databases. BXA personnel stated that this interchange has been a reliable interface with a reconciliation program to ensure that data is received. However, if BXA had a classified system, licensing data could be sent directly to these agency databases in a real-time basis without going to an unclassified terminal (State and ACDA already work off of ECASS terminals located at their sites).

A classified system would not only enable BXA to interface more easily with the other referral agencies, but also enable BXA licensing officers on-line access to classified data needed to process applications. Currently, when the Nonproliferation Center sends its electronic response to BXA on a particular export license application, it references a report number in the system and then manually faxes the reports over to a centralized secure location. Then the licensing officers have to physically go to that location to read the report. However, if ECASS was classified, the intelligence reports themselves could be attached to the actual license record, and all licensing officials who review that case would have ready access to the data.

In addition, BXA export enforcement managers stated that they would like to develop an online database of end user profiles that its agents and licensing personnel could use when analyzing applications. Because such profiles may contain classified information, this database would have to be on a separate stand-alone computer, making it inefficient to use during the everyday licensing evaluation process when this information would be most important. Based on these reasons, we believe a classified system would be a more efficient and effective tool in processing export license applications.

BXA's Information Technology Steering Committee, which is chaired by the Deputy Under Secretary for Export Administration, agreed that a classified system would be more beneficial in processing export licenses through better interfaces and information exchanges with the referral agencies. BXA's Under Secretary agrees that a classified system has benefits. However, he is concerned that BXA's new initiative, to allow exporters to submit export license applications over the Internet, will be affected by having a classified system. We disagree. Exporters' submission of licenses should not be affected by a classified or unclassified system. BXA's current plan is to have these applications stored on a network site physically separated from ECASS. After applications are received, BXA will download them into ECASS. Nor do we think that a classified BXA system would pose a problem for the other federal agency users that would

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<sup>76</sup>Electronic data interchange is commonly defined as the application-to-application transfer of business documents between computers. Many businesses choose electronic data interchange as a fast, inexpensive, and safe method for sending purchase orders, invoices, shipping notices, and other frequently used business documents. Since the transfer of information from computer-to-computer is automatic, there is no need to rekey information. Electronic data interface standards are internationally adopted and are effective in the electronic exchange of information in commerce. With no data entry, the chance for error drops to near zero.

interface with BXA's system. There should be adequate firewall protection that would preclude any public access to the other classified systems or data.

***Export licensing agencies need to coordinate***

BXA staff informed us that they discuss the routine exchange of data with other agency personnel, but admitted that the agencies have had little discussion about improving system coordination or addressing problems related to multiple systems and interfaces. In fact, we found that both the BXA and Defense export licensing systems were independently undergoing re-engineering efforts. By not coordinating these efforts, Commerce and Defense will both be pumping in millions of dollars to upgrade two separate automated licensing systems without also trying to improve the multiagency license processing capabilities. In addition, the State Department has been developing software called "Tracker" that is being used by foreign countries to track commodities and process licenses. This new software could potentially be adapted for the dual-use export licensing system in the United States.

We understand that both BXA and Defense desperately need improved licensing systems. However, for these two agencies, there may not be another opportunity for many years to implement common requirements. We believe that BXA and Defense need to coordinate and implement common system architecture requirements, such as a database management system and text management system. If common requirements are implemented, three of the six agencies involved in licensing—BXA, Defense, and State—would have the same system.<sup>77</sup>

We believe that BXA and the other export licensing agencies can effectively use one database management system to provide user access to licensing subsystems and other support tools, while allowing agencies to maintain control of their respective databases. By working together, the export licensing agencies can improve license processing while reducing their operating costs.<sup>78</sup> Although we understand that developing one database management system is not easy, there is no technical or operational need for multiple redundant licensing database management systems to exist. Therefore, we strongly recommend that BXA coordinate its systems development efforts with the other export licensing agencies and encourage them to consider implementation of common system architecture requirements. If the agencies can agree to common requirements, we believe this would create a de facto integrated system providing better systems transparency while still allowing agencies to maintain control of their databases.

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<sup>77</sup>Because the Department of State uses ECASS in an on-line real-time mode, State personnel would use BXA's new system.

<sup>78</sup>There are a number of savings from a consolidated system, such as consolidating computer facilities, standardizing hardware and software, reducing systems support staff, and reducing the image processing of hard-copy documents and storage from many locations to one location.

### Alternative computer centers not explored

BXA's contractor recommended that the new BXA system comprise a centralized architecture located at Commerce headquarters to restrict the number of entry points into the system. However, both departmental and BXA personnel stated that security at the Department's Computer Center in Springfield, Virginia, where the BXA system currently operates, has been excellent. Nonetheless, BXA wants to move its license processing to its existing telecommunications room in Commerce headquarters because of the reportedly high cost of using the Springfield center.

While the contractor prepared a cost-benefit analysis documenting BXA's move to Commerce headquarters, the analysis did not take into account all costs and other options, including the costs of moving the operation to another Commerce computer center, other federal computer centers (such as a combined computer facility with Defense), or outsourcing. In addition, although BXA has operated its own telecommunications center for many years, we question its ability to run a full-service computer center. We discussed this issue with Commerce's Chief Information Officer, who said he does not see a need for any departmental agency to develop a new computer service center since the Department already has 10 in place.

### *Summary and funding issues*

In February 1999, BXA's Information Technology Steering Committee requested that BXA information technology personnel analyze other potential information system architecture alternatives. They are currently looking at different relational databases and text processing packages. The information technology personnel have told us that no matter what information architecture alternative is chosen, the licensing component needs to be implemented first. The enforcement, policy, and administrative components are important, but they believe that the licensing component has the most weaknesses that need correction. BXA's planned time frame to fully implement the licensing component is October 2002.<sup>79</sup>

BXA's contractor estimated that BXA would need about \$6.4 million over five years—fiscal years 1998-2002—to fund its proposed unclassified system.<sup>80</sup> To date, BXA has not received *any* funding for its new system. The President's fiscal year 2000 budget submission to the Congress requested \$2.1 million for a new system. However, for BXA to implement a classified system, BXA may need more than the \$6.4 million for an unclassified system as estimated by its contractor.

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<sup>79</sup>BXA's *IT Strategic Plan for FY 1999-2004*, January 1999.

<sup>80</sup>*Information Architecture and Implementation Plan*, Booz Allen & Hamilton, October 1998.



Building on the results of its cost-benefit analysis of the best alternatives for a new system, BXA needs to revise the budget and funding plan for its system development effort and obtain departmental, Office of Management and Budget, and congressional commitment to fund it. With approval of the \$2.1 million in its fiscal year 2000 budget request, BXA can immediately start on its licensing system development while exploring the feasibility of a classified system and greater interagency cooperation on systems development.

As the export licensing referral process has become increasingly transparent over the past five years, the agency automation systems are lagging way behind. Without improved coordination between the licensing agencies, multiple and distinct automation efforts will continue. Throughout our review, BXA personnel expressed tremendous dissatisfaction and impatience with the outdated capabilities of ECASS and with hearing promises for many years that a new system would be developed. While an ECASS replacement is urgently needed, we believe it makes sense to ensure that the best available options (e.g., classified system) are considered and the most cost-effective one is selected and funded. Therefore, we would encourage BXA to work with the Department, OMB, and the Congress to obtain a commitment to fully fund the chosen option to replace ECASS. As part of its new system development effort, BXA needs to take the following actions:

1. Establish (and charter) a project management “team,” including a full-time project director as soon as possible.
2. Prepare a cost-benefit analysis for developing a classified database system with software upgrades that could be made to allow better interface capabilities with other U.S. Government licensing systems at a later date. This would include:
  - Performing a network analysis to determine future network requirements.
  - Performing one or more prototype tests of proposed systems before a final system alternative is chosen.
  - Obtaining approval from the departmental Information Technology Steering Committee for the chosen alternative.
3. Evaluate the most viable options for the location of BXA’s computer operations. Specifically, it should look at the possibility of service by another Commerce center, another federal center, and outsourcing, as well as the creation of an in-house BXA center. BXA must obtain departmental approval if it decides to leave the Springfield Computer Center and move to another location.

However, as part of the above system development efforts, we believe that BXA should coordinate with the Defense and State Departments to maximize efficiencies and savings as well as acquire a better, integrated licensing data system. BXA should encourage not only the Defense

and State Departments, but the other export licensing agencies as well, to establish an interagency steering committee to review the automation portion of the export licensing process and take the necessary actions to:

1. Coordinate and implement common system architecture requirements.
2. Coordinate and implement a common set of licensing database elements.
3. Determine minimal security requirements for current and future joint processing.
4. Determine where a common licensing database management system will reside.
5. Determine how to incorporate or “bridge” all agencies into a future system.
6. Evaluate Tracker software and other viable options for future licensing software.
7. Determine how interagency resources can be used to fund and implement a fully integrated system.



In its written response to our draft report, BXA agreed with our recommendation to work with the Department, OMB, and the Congress to obtain a commitment to fully fund its new export licensing system to replace ECASS. In addition, it agreed to establish a project management team, including a full-time project director to oversee the development and implementation of BXA’s new system. Specifically, BXA reported that it has formed an interim team with a project manager and when ECASS funding becomes available, a full time manager and team will be hired.

BXA also agreed with our recommendation to coordinate its system development efforts with the other export licensing agencies. It indicated that it has already had initial discussions with its counterparts and it will continue to do so to ensure full interoperability and compatibility of the systems. Furthermore, BXA agreed to evaluate the most viable option regarding the location of its computer operation and gain departmental approval for the selected option.

With regard to our recommendation that BXA prepare a cost benefit analysis for developing a classified database system, BXA indicated that it has already conducted such an analysis as part of its work with its contractor. The response also indicated that BXA should be able to encrypt its new automated system at a reasonable cost which will enable them to deal with sensitive materials. However, we disagree with BXA that it has already conducted such an analysis and believe that its statement is misleading. BXA’s contractor conducted a cost benefit analysis for an

unclassified replacement system for ECASS—the analysis did *not* include a classified system alternative.

Both BXA systems personnel and BXA's contractor have confirmed this. Furthermore, we do not believe that BXA's plans to encrypt its new system will address our recommendation for BXA to review the costs and benefits of a classified system. As a result, we strongly reaffirm our recommendation that BXA prepare a cost benefit analysis of implementing a classified database as a part of its new system development effort.

***C. ECASS internal controls are generally satisfactory, but some improvements are needed***

According to General Accounting Office guidelines, when computer-processed data is an important or integral part of a review and the data's reliability is key to accomplishing the review objectives, reviewers need to satisfy themselves that the data is relevant and reliable.<sup>81</sup> To determine data reliability, the reviewers may either conduct a review of the general and application controls in the computer-based systems, including tests as warranted, or conduct other tests and procedures if the general and application controls are not reviewed or are determined to be unreliable.<sup>82</sup> Since database controls are organized by database operational activity, such as data management, database management, database integrity, database operations, and database security, we identified and tested ECASS general and application controls in those areas. Overall, we determined that ECASS general and application controls are generally adequate and that ECASS data are sufficiently reliable but some controls need strengthening or further implementation.

BXA has adequate data management controls in place

Data management addresses how data is defined, input, and controlled usually through an active data dictionary and database administrator.<sup>83</sup> Without adequate data management, data elements are not controlled, incorrect data may be placed into production, and standard data definitions are not enforced. We found that the ECASS data elements are well defined and controlled. We also found that the data management function has sufficient organizational authority and is properly divided between administrative and technical functions, and the data audit trail is fairly complete. However, we determined that the audit trail can be improved, documenting changes to

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<sup>81</sup>*Assessing the Reliability of Computer-Processed Data*, General Accounting Office, April 1991.

<sup>82</sup>**General controls:** The structure, methods, and procedures that apply to all computer operations in an agency, including organization and management controls, security controls, and system software and hardware controls. **Application controls:** Methods and procedures designed for each application to ensure the authority of data origination, accuracy of data input, integrity of processing, and verification and distribution of output.

<sup>83</sup>An active data dictionary provides an online list of standardized file names and ensures that database and data dictionary file names are consistent. Users cannot define or access data unless those data definitions are processed through the data dictionary system.

recommendations in open and closed licenses can be improved, and the ECASS data element responsibility can be assigned to the individuals who use the individual data elements.

***Data audit trail complete but needs improvement***

Office of Management and Budget Circular A-123 (Revised) states that government agencies must maintain documentation to justify decisions and operations. An audit trail in a database environment comprises data input, processing, and output to substantiate transaction processing, support financial or other critical totals, and provide a means to reconstruct the database in the event of a system crash or major processing problem. The nature of BXA operations, whereby hundreds of users share the same database from on-line terminals through local and wide area networks, magnifies the importance of an adequate system audit trail.

We found that BXA's licensing process provides a fairly complete audit trail to reliably assess licensing performance. This audit trail comprises 11 major elements: (1) paper and automated license applications;<sup>84</sup> (2) automated license applications containing licensing decisions by licensing officers, supervisors, and referral agencies; (3) paper files maintained by licensing officers; (4) paper Operating Committee licensing decisions disseminated to licensing officers and the referral agencies; (5) scanned exporter technical specifications;<sup>85</sup> (6) current and archived licenses in ECASS; (7) backup tapes of current and archived licenses; (8) the ECASS file that documents reopened cases; (9) the ECASS logs that record database and security activities; (10) system documentation for each program change; and (11) ECASS verification of data transmitted to the referral agencies.

Even with these 11 major elements, BXA's system audit trail is systemically limited. ECASS cannot combine key license elements into one automated file; for example, the license application, database updates and modifications, and applicable exporter technical specifications are in separate systems.<sup>86</sup> ECASS has no central repository where a user can go to directly view all database updates and modifications. However, this limitation has not precluded BXA from having an adequate audit trail because the 11 major elements of BXA's audit trail complement one another.

In addition to the above limitation, we identified four areas relating to the audit trail that need correction. First, ECASS does not record what change has been made to each field. The ECASS

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<sup>84</sup>Exporter paper applications become automated license applications after they are scanned in and verified.

<sup>85</sup>Exporter technical specifications include brochures and design drawings.

<sup>86</sup>The Multipurpose Archival and Records Retrieval System electronically archives all export license documents and forms by scanning paper documents and storing them as images on a server in BXA's network room. The system became operational in fiscal year 1997 to replace BXA's old microfiche system.

electronic record only records when and by whom a change to a data field was made. If, for example, licensing officers make changes to data fields in pending licenses, the current data in that field is “written over,” or eliminated. The database management system (or Model 204) cannot “audit” each field in the database to show what specific changes are made. As a result, licensing officers are supposed to “document” changes in licensing officer notes, but that is not consistently done. To determine what fields have been changed, BXA personnel would have to painstakingly compare different versions of backup tapes. To correct this problem, BXA’s Acting Chief Information Officer stated that a separate record with the old value will be coded to show the old and new value. We agree that this change will improve the ECASS audit trail. For issued cases, BXA’s audit trail comprises an electronic record documenting who, when, and what was changed.

Second, BXA does not ensure that all license conditions agreed to by the Operating Committee are correctly inputted into ECASS. If conditions are not properly input, the audit trail changes, data integrity is affected, and quality control is reduced.

Third, we found that the departmental computer center in Springfield is adequately maintaining automated applications by backing up the ECASS database on a daily, weekly, and monthly basis, and copies are stored at the center and at the Department of Commerce headquarters. However, there is the possibility that these tapes could be modified by BXA personnel, invalidating the audit trail. In 1993 we recommended that BXA provide a duplicate read-only tape to the Under Secretary for Export Administration every day, highlighting any changes that might be made by lower ranking BXA personnel. BXA personnel stated that getting the tape to the Under Secretary’s office and finding enough space to store it would be a difficult daily task. As a result, this has not happened. Since we still maintain that the audit trail would be strengthened by having the stored databases owned by BXA’s Under Secretary with read-only access to produce historical reports as required, we recommend that a duplicate read-only tape be provided to the Under Secretary every 90 days, highlighting any changes that might be made by lower ranking BXA personnel.

Fourth, we also recommended in the 1993 report that paper applications and technical specifications be retained for five years. Currently, BXA physically retains hard-copy information for only 90 days except memorandums from BXA personnel or exporters requesting system changes, which are maintained for one year. BXA personnel stated that maintaining paper applications for five years is too long. We are satisfied that maintaining paper applications for 90 days is adequate.

***Improvements are needed to better document changes to recommendations of open and closed cases in ECASS***

We examined ECASS to determine whether recommendations entered into the database were later changed without the consent or knowledge of licensing officials. We found two key controls to preclude this from happening.

The first control is that supervisors cannot make changes to pending or closed licenses without the licensing officers' knowledge.<sup>87</sup> For pending licenses, supervisors can only verbally suggest changes to LOs or insert changes into the licensing officer notes section of the automated license application. For example, supervisors can request that LOs reject licenses based on current intelligence that the LOs are not privy to. If the LOs are verbally instructed to make changes, they are supposed to document the request in the LO notes section. However, we have found that the LOs do not consistently document their changes or changes requested by a supervisor in LO notes. If a supervisor goes into the file and electronically requests that an LO make changes to a pending license, ECASS automatically documents the request. Supervisors can move cases from one LO to another to balance an LO's workload, but again, the supervisors cannot physically make changes in the system. Even cases decided by the Operating Committee and the Advisory Committee on Export Policy are returned to the LOs for inclusion of new conditions and/or deletion of conditions. Our survey confirmed that the LOs believe that their recommendations are not changed without their consent or knowledge.

For closed licenses, supervisors, LOs, and exporters must submit a written request to BXA's operations staff to reopen a case and make the appropriate change. Changes to cases closed and archived are rare, with only 120 cases reopened in fiscal year 1998 (out of approximately 11,000 license applications). After the operations staff reopens a case and makes the appropriate change, the case is then sent to the applicable LO for review. Reasons for reopened cases included: correcting data input errors; changing case decisions from denied to approved or approved with conditions, and adding or deleting conditions as a result of the escalation or appeals processes.

However, we identified two areas where corrections are needed. First, BXA lacks written criteria for when a case can be reopened. Second, although the operations staff receive written justifications for reopening a case, no one periodically reviews the reopened case report to ensure that valid reasons for reopening cases are received and that the electronic audit trail describing why the case was reopened is complete. We found that the electronic audit trail ranged from very complete descriptions of why a case was reopened and who requested the case be reopened, to very minimal descriptions of why a case was reopened (e.g., "modify conditions") and no description of who made the request. This is an important audit trail issue because when the paper document requesting a case be reopened is eliminated, the electronic audit trail is the only source for why a case was reopened. BXA needs to ensure that the electronic audit trail is more complete.

The second control to prevent unauthorized changes to ECASS involved the interagency referral process. We found that Defense, Energy, and the Nonproliferation Center could not make changes either directly to ECASS from their ECASS terminals or to the ECASS files they

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<sup>87</sup>Countersigners or supervisors review and sign off on license cases from the licensing officers before the licenses are issued, returned without action, or denied.

download to their systems. We also found that State and ACDA could not make changes directly to ECASS from their ECASS terminals.

***ECASS data element responsibility has not been assigned to the individuals who own the individual data elements***

Although BXA's operations staff scans and verifies application data before it goes into ECASS, they do not "own" the data. BXA has identified 18 "principles" that its future system will incorporate, the 7<sup>th</sup> of which states that "The managers of the organizations entering and capturing the data will be accountable for its accuracy and content."<sup>88</sup> Under the proposed new system, BXA senior management must indicate their desire to manage data and, through a database administrator, assign data element responsibilities to individuals throughout the organization. Thus, an individual or individuals would have the responsibility for authorizing access to the data element, and assuring the integrity of the data element.

**Database management controls have ensured that ECASS has run properly for many years**

Adequate database management requires an appropriate organizational structure and resources needed to effectively use database technology and recognize and prevent risks. ECASS has been well managed for many years by the same individual who ensures that data elements are well defined, analyzes database performance statistics, and corrects problems that occur. However, this individual is a contractor who has never been officially designated as the database administrator. BXA needs to officially designate a database administrator, designate an official database review board, perform ongoing internal control reviews, and reorganize ECASS.

***BXA has not officially designated a data base administrator***

In 1991, we recommended and BXA agreed to develop a charter that clearly identifies the duties and responsibilities of a database administrator and ensure that a database administrator performs these duties.<sup>89</sup> While BXA had a database administrator for about three years after our review, when he left, BXA did not fill the position. Since then, BXA's de facto database administrator has been a contractor. BXA has not prepared a charter for the de facto database administrator. BXA's Acting Chief Information Officer plans to designate himself the official administrator and prepare a charter. We believe this action will satisfy this requirement.

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<sup>88</sup>Task 5: Information Architecture, Booz Allen & Hamilton, October 1998.

<sup>89</sup>Inspection of ECASS Internal Controls, Final Report, Office of Inspector General, June 1991.

### ***BXA lacks an official database review board***

BXA needs a review board that is independent of the database administrator and software team to ensure that ECASS database standards and procedures are being followed and that ECASS is meeting user needs. In some organizations, these boards are called quality assurance boards or systems assurance groups and have their own charter. While BXA has an IT Steering Committee, it lacks a charter. In addition, this committee has focused solely on BXA's system re-engineering project and not on database standards and procedures. BXA's contractor recommended that a standards development group be "constituted to establish the appropriate database standards," including data definition, data documentation, passwords, and writing and testing programs.<sup>90</sup> In order for an organization to achieve promised performance, specific standards must be established and plans developed to achieve the standards. This process requires the continual monitoring of results versus standards. Database leaders should work with users to develop performance standards which are then measured against results.

### ***BXA does not perform ongoing internal control reviews***

Internal controls must be periodically reviewed to determine whether they are functioning as planned. Although BXA personnel have performed prior internal control reviews of ECASS, the last documented review was performed in 1991. However, ECASS has undergone numerous changes since then. BXA's standards team could perform ongoing internal control reviews, or BXA could establish a team to periodically (about once a year or when conditions materially change) review the internal controls and risks associated with its system. The team could comprise the database administrator, security officer, users, database analysts, and operations personnel.

### ***BXA has not reorganized ECASS in two years***

In 1991, we recommended that BXA reorganize and verify the database, using appropriate software, and maintain a record of results. BXA personnel informed us during our current review that the database has been reorganized a few times since 1991, but not since 1997. After normal usage, data becomes physically unorganized, logically unlinked, and possibly lost. The physical and logical database needs to be restructured periodically to meet the changing needs of users. A database verifier is a software package that reviews the integrity of the database to ascertain that all the designated paths through the database are complete. Reorganizing ECASS will arrange files more efficiently and ensure data linkage. BXA's database administrator should reorganize the database every year.

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<sup>90</sup>Task 5: Information Architecture, Booz Allen & Hamilton, October 1998.



### Database integrity controls need improvement

Database integrity controls help the database administrator ensure the accuracy, completeness, and authorization of database data. Without adequate database integrity controls, inaccurate or incomplete data can be entered into ECASS, data may not be entered on a timely basis, and integrity errors may not be detected. We evaluated ECASS data input and processing controls to determine data and system integrity, finding that changes to pending, issued, and archived licenses are adequately controlled. However, the overall process of inputting and verifying paper licenses is an ineffective process prone to errors. Data processing controls have allowed some licenses to be issued without exporter codes and export control classification numbers.

### ***Data input controls need improvement***

While it is unlikely that any computer system contains error-free data, we found that (1) paper applications take too long to get scanned, verified, and inputted into ECASS, (2) paper applications get scanned, verified, and inputted into ECASS with errors, and (3) some exporters, consignees, and end users have more than one identification number. As mentioned previously, BXA and its system contractor prepared 18 principles for its new information system architecture to ensure data consistency, accuracy, quality, and system integrity.<sup>91</sup> However, until BXA's new system is developed and its 18 principles implemented, the three problems described above need to be addressed and corrected.

First, BXA's License Application Scanning System was implemented in 1994 to process paper license applications using a PC-based forms processing and image management system. We found that, before being loaded into ECASS, scanned applications take too long to process. BXA receives approximately 200 license applications a week. In fiscal year 1998, it took an average of 5.4 days to input each application. BXA personnel stated that scanning and verification have been inadequate because of (1) poor work and low motivation of the employees, (2) poor staff management, (3) increased applications, and (4) the habitual illnesses of some staff members. BXA is currently testing a new system, called SNAP, whereby exporters will submit license applications over the Internet. BXA personnel hope that the electronic submission of licenses will significantly reduce the number of paper applications. If the new system does not successfully reduce paper applications, BXA would like to mandate that all paper applications be replaced by the new system. Although we agree, this might be difficult to enforce. When asked if some type of outreach effort would influence exporters to use the new system, BXA personnel stated that they have been performing outreach efforts.

Second, the licensing officers have complained that the poor quality of some inputted applications causes them to have to make changes or submit changes to the operations staff. Input controls are critical in a database environment because many programs use the same data for processing.

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<sup>91</sup>Task 5: *Information Architecture*, Booz Allen & Hamilton, October 1998.

Thus, there must be increased reliability. From February 1, 1998, to February 1, 1999, BXA received 7,333 applications and the operations staff made changes to 3,766 of these applications (51 percent). From November 1998 through January 1999, about 45 percent of the applications had at least one change, such as an address change or inputting a missing sentence. BXA personnel cited little quality control of verified applications before they are entered into ECASS as the reason for the number of changes being made by the operations staff and LOs. The operations staff director stated that she believes her staff finds most errors because there were only 120 cases reopened in fiscal year 1998 for various reasons—not just data input errors. However, these changes should be corrected before the applications are inputted into ECASS, because some errors may not be detected by the operations staff, LOs, and outside parties, and remain in the database.

We suggested that BXA consider the feasibility of one clerk's work being reviewed by another before it goes into the database or contract this function out. The operations staff director stated that her staff does not have time for such reviews, nor does BXA have the funding to contract out this function. However, if BXA's new system greatly reduces the number of paper applications, the operations staff should have time for this quality control measure. In addition, BXA personnel suggested that the old "User Meetings" between the operations staff, LOs, and Information Technology staff should be reestablished so that issues are discussed and problems quickly identified and resolved. We concur with that suggestion.

Third, the Office of Export Enforcement uses a computer name-matching program to assign unique identification numbers to all exporters, consignees, and end users on an application, so that its agents can flag and review any party to a case. However, some exporters, consignees, and end users in the ECASS database have more than one identification number, resulting in a long watchlist, lengthy searches for the LOs, and some identification numbers that may not get flagged by the Office of Export Enforcement.

Although data integrity means that the same company does not have more than one identification number, this was not an initial business rule of BXA. For many years, Export Enforcement assigned a different code to an exporter, consignee, or end user even if their name and address was only slightly different. More importantly, Export Enforcement assigned different codes to a company even if that company, with the same name and address, already had an identification number. Export Enforcement did this to ensure that all parties to a case were added to or screened against its watchlist. However, the General Accounting Office stated that BXA has not ensured that each party is given only one identification number and has in some cases assigned multiple identification numbers to the same party.<sup>92</sup> Some of these identification numbers have watchlist flags, while others do not. As a result, license applications involving parties on the watchlist may not be caught because the parties may be assigned identification numbers that do

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<sup>92</sup>*Export Controls: License Screening and Compliance Procedures Need Strengthening*, General Accounting Office, NSIAD-94-178, May 1994.

not carry watchlist flags. BXA personnel stated that multiple identification numbers provide the LOs and export enforcement agents with different results when they query ECASS. As a result, both LOs and agents must submit queries many different ways to ensure that they find all relevant information.

By evaluating just one page of BXA's January 1997 Watchlist printout, we found several company entries that were spelled the same and had the same addresses (e.g., OIG Corporation) and companies that were spelled differently (e.g., OIG Corp. or Office of Inspector General Corporation) that had the same and different addresses. All of these entries had different identification numbers. We asked BXA if they could determine how many companies are in the database (i.e., OIG Corporation) but are spelled differently (i.e., Office of Inspector General Corporation, or OIG Corp.). To answer our question, BXA personnel stated that they would have to use many hours of system processing time, which would affect the processing of licenses. BXA's new system is expected to have an improved identification numbering process. In the meantime, BXA personnel stated that companies with duplicate identification numbers remain in the database, which makes reviewing all companies provided by a licensing officer query a very time consuming task.

BXA has taken steps to reduce the number of duplicate codes in its database, including an extensive archiving effort to retire a large number of duplicate company entries. For example, in 1993, BXA evaluated two states and two countries to determine what duplicate companies existed, finding and archiving many of them. However, BXA has not performed a similar review since 1993. This needs to be done.

### ***Coding and case numbering controls need improvement***

Although we found that most data processing controls were adequate, a few cases were issued without a code and/or export control classification numbers. We identified five cases that were issued without being properly coded. Specifically, three cases were issued without the end users being coded, and two were issued without the system being set to "Y" (yes) indicating the parties had been coded. We also found that 35 cases were issued without export control classification numbers. According to the General Accounting Office, each computer system should have steps aimed at ensuring the accuracy of computer processing, and these steps are designed to verify that all relevant records were completely processed and, more importantly, that computer processing met the intended objectives of the system.<sup>93</sup>

Although the number of cases issued without codes and numbers is small compared to all the cases in the database, this is still a serious breach of internal controls. BXA personnel could only speculate on why cases had been issued without codes or numbers. At our request, they have agreed to determine what caused this breakdown in data processing controls. Without a code for

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<sup>93</sup> *Assessing the Reliability of Computer-Processed Data*, April 1991.

an exporter, consignee, or end user, Export Enforcement cannot perform a match against its watchlist.

***Operating Committee Chair does not verify that conditions agreed upon on each case are placed on the final license***

According to the Executive Order 12981, the conditions agreed to by the Operating Committee should be the official record. However, as discussed in Section V of this report, we found some issued cases where conditions that exporters must comply with, and agreed to by the Operating Committee, have been changed, which seriously undermines data integrity.

Database operations have been significantly improved

Database operations comprise the day-to-day maintenance and recovery procedures of the database. Since ECASS runs on a mainframe computer at the departmental computer center in Springfield, a large part of database operations is handled by that staff. In February 1998, the Office of Inspector General reviewed the general controls pertaining to the center's management, operations, and security. At that time, we recommended improvements in the center's security program, access control, segregation of duties, system software, and service continuity.<sup>94</sup> During our current review, we found that the center had made significant improvements to access controls, security, and service continuity. Both the center and BXA maintain adequate copies of database information. However, we found that BXA lacks a current contingency plan and risk analysis, and BXA personnel do not know where to report database problems.

***BXA lacks a system contingency plan***

In 1991, we recommended that BXA revise and test its ECASS disaster plan and train appropriate personnel in its use to comply with Federal Information Processing Standards Publication 87 guidelines.<sup>95</sup> Federal Publication 87 states that unless contingency plans are continually reviewed and tested, they may fail when needed. Personnel should test contingency plans at the designated backup site by taking copies of all needed data and other information. The test should show that the backup site remains unharmed in a simulated catastrophe or disruption or service.

BXA personnel stated that they had taken an old disaster plan and converted it into a current continuity-of-operations plan but the new plan needs improvement. BXA's contractor, as part of a Year 2000 Business Continuity and Contingency Plan for BXA mission critical systems and high

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<sup>94</sup>Office of Computer Services General Controls, Office of Inspector General, Audit Report No. FSD-10021-8-0001, February 18, 1998.

<sup>95</sup>ECASS Internal Controls, June 1991.

priority non-mission critical systems, plans to upgrade its current continuity-of-operations plan to include BXA policy and procedures regarding security of BXA systems, prevention, incident handling, and planned response to catastrophic emergency events.<sup>96</sup> BXA plans to disseminate its plan to all employees.

Although BXA has historically relied on the Springfield Computer Center in the event of a system catastrophe, there are other issues that BXA needs to document including how its network and users would operate after a catastrophe. BXA does not believe that its network warrants a complete backup facility, due to the small probability of a catastrophic network failure. BXA will include its local area network facility in its plan. BXA plans to do export licensing outside of its network via dial-up from LO and special agent workstations. However, we found that BXA lacks written procedures for its LOs and agents to use. Because BXA's core mission of processing licenses depends on the Springfield Computer Center's hot-site contingency plan, if there is a problem at the center, BXA's licensing operation is in jeopardy. The contractor who prepared a draft 2000 Business Continuity and Contingency Plan for BXA recommended that BXA develop, where possible, manual licensing and enforcement contingency processes. We agree that BXA should update its plan to include all appropriate manual and system contingency processes as soon as possible.

#### ***BXA lacks a risk analysis/vulnerability assessment***

BXA has not updated its risk analysis in five years. Federal Publication 65 states that risk analyses should be conducted at least every three years and when significant changes are made to the equipment, system, or physical environment. A risk analysis should document system vulnerabilities, threats, and safeguards. In addition to having exceeded the three-year standard, BXA is planning to significantly change its system, equipment, and physical environment. Before this is done, BXA needs to update its risk analysis to outline the potential unfavorable events and the corresponding safeguards. For example, moving to a new system at Commerce headquarters could be very disruptive unless BXA has outlined potentially unfavorable events and the corresponding safeguards.

BXA plans to complete a vulnerability assessment of ECASS during fiscal year 1999.<sup>97</sup> To address this issue, BXA should either establish a risk management team to identify and assess the severity of risk in its database environment or have a contractor perform the assessment. A risk management team comprised of users, database analysts, security personnel, and data processing personnel would have detailed knowledge of the system. Although more costly, a contractor would provide an outsider's independent view of the system.

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<sup>96</sup>BXA IT Strategic Plan for FY 1999-2004, January 1999.

<sup>97</sup>BXA IT Strategic Plan for FY 1999-2004, January 1999.

### ***BXA personnel do not know where to report database malfunctions***

Although BXA's Acting Chief Information Officer stated that BXA personnel are suppose to call the BXA hotline with all problems, we told him that some personnel were unaware of where to call with a database problem. BXA personnel stated that they would only call the hotline with a problem that directly affected them, such as their computer breaking down. If a larger problem occurred, BXA personnel stated that they would call BXA's main database analyst and lead programmer. Malfunction reporting provides a formal process that normally involves a form and procedures to identify the malfunction, its potential cause, and potential course of action. BXA's database administrator receives daily database error reports, but he has not designed a form for users of the database to complete and return when suspected problems have been detected. A database malfunction reporting process could encourage users to present any condition that may not be a database problem, such as a personal computer not working, as a database problem. However, with BXA planning to implement a new database environment, a malfunction reporting process is needed. BXA needs to send out a "network message" to emphasize that all database problems should be reported via the hotline.

### **Database security controls have improved, but additional improvements are needed**

Database security comprises the overall methods, procedures, and techniques used to prevent, detect, and correct intentional, unintentional, and unauthorized access to the database. By reviewing the general controls, including security controls, of the departmental computer center, we found that access to and use of the ECASS have greatly improved. However, we found that BXA's security controls could be improved by improving database access controls, preparing a security plan, performing periodic security reviews, officially assigning the security duties to its security officer, providing all users with current security training, and restricting the number of BXA employees with file manager access.

### ***BXA lacks a security plan***

We found that BXA had no strategic security plan addressing its licensing process. It had no overall strategy to minimize risk and thereby safeguard sensitive license information. According to the Commerce *ADP Security Manual*, effective security planning is the basic prerequisite for implementing any cost-effective system of security controls. It requires (1) the application of risk analysis techniques to improve the security planning process, (2) a continuing evaluation of security measures, and (3) the safeguarding of data processed by a system. BXA's security officer is aware of BXA's need for an overall security plan. She found an old BXA security plan and plans to prepare a new plan. We would like to review BXA's new security plan before it is issued in final.

***BXA does not perform periodic security reviews or tests***

BXA's security officer could not remember when the last security review of ECASS was conducted. Without routine, repeated reviews, security weaknesses may not be promptly identified or corrected. The Department's *ADP Security Manual* requires continuing security evaluations be performed. We recommend that BXA conduct yearly security reviews to update and improve ECASS security, improve user security awareness, and improve security training. BXA's security officer agrees with our recommendation, stating that she plans to set up a security program including periodic security tests.

***BXA has not officially assigned its security responsibilities***

BXA's Information Technology Strategic Plan for fiscal years 1999-2004 states that BXA appointed an IT security officer in the latter half of 1998. However, the appointed individual stated that she had not been officially designated the security officer. Specifically, she has not received an official designation in writing or had her performance plan updated to reflect her new duties. We found that some LOs were uninformed of who the BXA security officer was and where to report security incidents. BXA's Security Standards Operating Procedures state that employees should report all suspected or actual security incidents to their supervisor and the ECASS Security Administrator.<sup>98</sup> However, if the LOs do not know who the security administrator is, reporting security incidents is difficult. BXA needs to designate its current security officer as the official security officer and distribute a network message stating who is the security officer and where to report incidents. BXA should also provide the security administrator's telephone number in its security manual.

***BXA users, including BXA's security officer, have not received complete security training***

BXA's security officer stated that she plans to provide security awareness training to everyone with network access. Some BXA personnel stated that they had not received any security training over the last few years. As a first step, BXA's security officer plans to issue and have all BXA employees sign for BXA's updated security manual. BXA's security officer would also like to attend a training session on ACF-2, which is the security package used by the Springfield Computer Center. She has little knowledge of the capabilities of the package, and what security improvements, if any, could be made.

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<sup>98</sup>Security Standard Operating Procedures, *Export Control Automated Support System*, Bureau of Export Administration, March 1999.

### *Database access controls need to be improved*

In February 1998, the OIG issued a report documenting the Office of Computer Services general controls.<sup>99</sup> The report stated that the office controls needed improvement in access control. During our current review, we found three problems with access controls identified in our prior report that had not been addressed: (1) the Springfield Computer Center is not regularly analyzing security violations, (2) the center is not analyzing user access privileges, and (3) BXA and the center lack an electronic mechanism where terminated/transferred employees are immediately removed from center access.

Database access controls assure that only authorized individuals gain access to database resources. Feedback information should indicate both the number of times the access rules prevent an unauthorized access, and the number of detected access violations. During our inspection, we found that the center was still not regularly monitoring its security log for security violations. The individual responsible for this activity at the center stated that the center lacked adequate resources to perform this function. We recommended that the Acting Director consider hiring a third individual to assist in performing log-on account administration, to provide existing personnel with more time for such duties as monitoring violation reports. The Acting Director agreed to consider hiring a third individual depending on any reorganization or job function changes. The office needs to start regularly monitoring its security log as soon as possible.

During our inspection, we found that neither BXA nor the center was regularly analyzing the population of inactive log-on accounts and multiple and generic log-on IDs. In our prior report, we recommended that the center analyze the population of inactive log-on accounts in the ACF-2 database and delete and suspend accounts no longer needed, and analyze the population of multiple and generic log-on IDs and delete all unnecessary duplicates.<sup>100</sup> The center's Acting Director stated that the center analyzed the database in November 1997 and suspended all identification numbers that had been inactive for 60 days. He further stated that the center's security team would review the ID database on a quarterly basis, and take appropriate action. However, from November 1997 to March 1999, only one review had been performed. The center needs to perform these analyses every quarter.

BXA is not immediately notifying the center when users move or are terminated. During our prior review, we found that there was no reliable mechanism for informing the center of employee transfers or terminations. Formal procedures and direct communication lines between center personnel and security departments would increase the effectiveness of controlling user access to the production environment. We recommended that the center develop communication links to client personnel departments for immediate notification of terminated or transferring employees in order for system access to be promptly revoked or modified. Center personnel stated that center

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<sup>99</sup>Office of Computer Services General Controls, February 1998.

<sup>100</sup>Office of Computer Services General Controls.



procedures require each client to have a security administrator who is responsible for notifying the center security when an employee is terminated or transferred. However, we recently determined that BXA's security officer had not notified the center of some terminated or transferring employees. Center security will institute a procedure whereby client personnel departments will be queried to ascertain terminated or transferred employees.

We reaffirm our recommendation that a communication link be developed to immediately notify the center of terminated or transferring employees in order for system access to be promptly revoked or modified (by the end of each working day).

***Too many BXA IT employees have file manager access***

Five BXA employees have file manager access to ECASS. This is too many, since this level of access can override all system controls. File manager access needs to be restricted to only the database administrator and a backup.



In its written response to our draft report, BXA generally agreed with all of our recommendations to implement or strengthen the internal controls for ECASS. With regard to our recommendation to have the database administrator assign data element responsibilities to individuals throughout the organization, BXA stated it plans to assign ownership of data elements to BXA organizations and subunits. We concur with this suggestion. In addition, we recommended that BXA designate an official database review board that is independent of the database administrator, but it responded that these functions should be handled by its Chief Information Officer. We concur with this suggestion.

With regard to our recommendation that BXA determine why some cases were issued without codes or Export Control Classification Numbers, BXA indicated that it has researched this issue and found that it occurred in only a minimal number of cases and it has not occurred at all since 1996. BXA does not believe further attempts will be successful. However, if this happens again, BXA has implemented procedures to quickly determine why such cases have been issued. This action satisfies our recommendation.



## RECOMMENDATIONS

We recommend that the Under Secretary for Export Administration take the following actions:

### Legislative Authority, Executive Orders, and Regulations

1. Continue to work closely with the Congress and the Administration to renew legislative authority for export controls (see page 27).
2. Work with the Congress to revise the current NDAA requirement to conduct a post shipment verification for every high performance computer shipped to Tier 3 countries. Seek legislation that (a) requires checks on only those high performance computers that are of greatest concern to national security, and (b) provides resources to conduct these checks so that BXA agents can also target other critical commodities and technologies for end use checks (see page 33).
3. Request the National Security Council to clarify the issue of the appropriate level of representation at the Advisory Committee on Export Policy meetings (see page 34).
4. In conjunction with the National Security Council, seek a viable alternative for ACEP decisions that may result in a tie vote (see page 34).
5. Coordinate with the National Security Council to clarify what the United States' goal is with regard to requiring deemed export licenses and to revise the policy and regulations for deemed exports as necessary to make it clear who needs to get deemed export licenses and then enforce those regulations (see page 37).
6. Develop and implement an outreach program to explain and seek compliance with the requirements for export licenses for deemed exports. Outreach target audiences should include high tech companies, industry associations, and federal, university, and other private research laboratories (see page 37).

### Commodity Classification

7. Make the commodity classification process more timely and transparent by taking the following actions:
  - (a) Ensure that there is a front-end technical review of commodity classifications, and that this responsibility is not dropped in the future because of absences of key staff persons (see page 40).

- (b) Reemphasize the importance of processing commodity classification requests from exporters in a timely manner and hold licensing officers accountable for doing so (see page 40).
- (c) Program ECASS to allow licensing officers to use the “hold without action” feature, when processing CCATS (see page 41).
- (d) Develop policy and procedures for the intra-agency review of commodity classifications, as BXA did for the intra-agency review of export license applications (see page 41).
- (e) Work with the Departments of Defense and State to make the CCATS process more transparent with regard to items or technologies specifically designed, developed, configured, adapted, and modified for a military application, or derived from such items as called for in the NSC guidance. As a part of this effort, work with the NSC to develop specific criteria and procedures on how to implement its 1996 guidance for the referral of munitions-related commodity classifications to Defense and State. In addition, consult with Defense to determine if it wants to continue or withdraw its delegation to BXA on munitions-related CCATS (see page 45).

#### **Policies, Procedures, Guidance, and Training for Licensing Officers**

- 8. Expand the new licensing officer case analysis guidance by providing licensing officers with a specific list of questions that they should address when processing export license applications to specific countries (e.g., China), and require that the licensing officers include the dates of the most recent approvals or denials in the license history (see page 50).
- 9. Ensure that export licensing policies and procedures are updated on a regular basis to reflect current issues and new regulations. Fully implement BXA’s electronic library to maintain these policies and procedures and develop a long-term plan for maintaining the library, including designating who will be responsible for updating it and what procedures will be followed for updates (see page 51).
- 10. Develop and implement a training program for BXA licensing officers and designate either a training team or training coordinator to manage and implement this program (see page 53). In addition to classroom, seminar, manual, and on-line training, consider including the following alternative training options in the LO training program:
  - (a) Regular briefings by the various other licensing and referral agencies.

- (b) Brief exchanges of licensing personnel among the referral agencies, or even short-term assignments of BXA's LOs to another licensing office or the Central Intelligence Agency's Nonproliferation Center.
- (c) Temporary internships for new LOs to work on the Operating Committee staff to observe the types of questions and issues that will be raised by the referral agencies.

### **License Referral Process**

11. Instruct LOs to follow BXA's referral procedures to ensure that all applicable export license applications are referred to the reviewing agencies, including seeking concurrence from the referral agencies when processing amendments to existing licenses that they reviewed (see page 62).
12. Engage in discussions with the Director of the Central Intelligence Agency to seek ways to strengthen the role of the intelligence community in the export licensing review process. Topics to be addressed should include:
  - (a) Referral of all license applications to the CIA (see page 64).
  - (b) Performance of risk assessments on end users (see page 65).
  - (c) Need for more detailed intelligence information (see page 65).
  - (d) Establishment of a more realistic time frame for its review of end users, especially in countries of concern like China (see page 66).
  - (e) Feasibility of developing a mechanism to track and assess the cumulative effect of dual-use exports to a specific country or region (see page 67).
13. Instruct licensing officers to indicate in the referral history the reason they believe the CIA's Nonproliferation Center should review an end user when it is contrary to the MOU between the two agencies regarding the export licensing application referral policy (see page 67).
14. Periodically look at the State Department's timeliness in reviewing export license referrals. If there is an increase in the number of "pullback" cases, work with State to identify additional resources or other solutions to improve that agency's ability to handle referrals within the 30-day deadline (see page 70).
15. Update the 1993 MOU between BXA and Customs to provide for BXA's transmission of names, addresses, and telephone numbers from new pending license applications to

Customs for screening against the Treasury Enforcement Communication System (TECS) for at least a two-year trial period (see page 71).

16. Notify all referral agencies that stipulated a favorable pre-license check for approving a license when a PLC is canceled and obtain the agencies' concurrence to proceed with closing out the license (see page 76).

### **Dispute Resolution Process**

17. Avoid any action that would interfere with the OC Chair's ability to render an independent licensing decision and use BXA's right to escalate cases to the ACEP when BXA disagrees with the OC Chair's decision on a case (see page 81).
18. Work with referral agencies that have delegated back to Commerce some of their initial license review authority to find a solution to expediting late reviews by these agencies (see page 82).
19. Provide the OC with the responsibility and adequate resources to become a "one-stop shop" for processing all licensing decisions made by the OC, ACEP, and EARB to ensure quality control (see page 85).

### **Exporter Appeals Process**

20. Coordinate with the National Security Council to amend Executive Order 12981 to establish formal procedures to include the referral agencies in the appeals process (see page 92).

### **Monitoring of License Conditions**

21. Improve BXA's monitoring of license conditions by taking the following actions:
  - (a) Direct officials in the Office of Exporter Services to regularly purge its follow-up subsystem of expired licenses and, in doing so, contact the exporters to determine whether or not shipments were made against the licenses. In addition, direct personnel to periodically perform a random spot-check on licenses in the subsystem that have not expired in an effort to remind exporters that BXA is serious about monitoring exporter compliance with conditions placed on export licenses (see page 97).
  - (b) Notify licensing officers and supervisors of the importance of not flagging licenses with "Write Your Own" conditions for follow-up if they have no reporting requirement (see page 97).

- (c) Routinely spot-check companies related to deemed exports, to verify that security procedures are indeed in place and meet the established criteria (see page 99).
- (d) Utilize the steps taken by licensing officers involved in monitoring exporter compliance with license conditions for encryption and deemed exports as a best practice by the other licensing divisions (see page 99).
- (e) Provide licensing officers with “read-only” access to the compliance subsystem so that they can verify an exporter’s compliance history and deny a license based on noncompliance, if necessary (see page 99).
- (f) Ensure that licensing officers review all compliance reports submitted by the exporter and be involved with contacting exporters who do not comply with the reporting conditions (see page 99).
- (g) Direct the Office of Export Analysis to perform timely follow-up work on licenses with condition “14” to verify compliance among exporters and uncover any noncompliance. Incorporate this responsibility into the supervisory export compliance specialist’s performance plan to ensure accountability (see page 102).

### **End Use Checks**

- 22. Seek to improve the timeliness and quality of end use checks performed by the US&FCS overseas posts by taking the following actions:
  - (a) Work with the Assistant Secretary and Director General for US&FCS to improve the timeliness of pre-license checks conducted by US&FCS posts (see page 106).
  - (b) Provide clear and concise guidance to US&FCS and its overseas posts regarding the use of foreign service nationals and personal service contractors to conduct end use checks. Revise the PLC/PSV Handbook accordingly and make sure that it is sent to all US&FCS posts (see page 109).
  - (c) Communicate more with US&FCS posts about the importance of (1) identifying who conducted an end use check in their reporting cables (see page 109); (2) conducting on-site visits for each end use check (see page 110); and (3) retaining proper end use check records for five years, the statute of limitations for Office of Export Enforcement investigations (see page 111).
  - (d) In the PLC/PSV Handbook, specifically list embassy sections by name that US&FCS should confer with on end use checks and include suggested questions for each section (see page 112).

- (e) Provide periodic regional training seminars and workshops to keep US&FCS staff abreast of current developments in export controls and BXA regulatory procedures. Also consider using the Safeguard Verification program as a mechanism to train US&FCS staff (see page 113).
23. Develop guidance for export enforcement agents to use in conducting Safeguard Verifications. This guidance should include:
- (a) Criteria to help guide agents in selecting which PLCs/PSVs to do, targeting countries and shipments of greatest concern (see page 114).
  - (b) A template or standard format for agents to follow when preparing Safeguard trip reports (see page 115).
  - (c) A requirement that the Safeguard verification teams meet with host government officials involved in local export control or enforcement areas, as well as U.S. embassy personnel who might be knowledgeable of proliferation threats or diversion activities associated with the specific country, to determine what export control programs the country has, how effective they are, and the country's relationships with countries of concern (see page 115).
  - (d) A suggestion that photographs be taken of the sites and commodities inspected, when appropriate, during their verifications to be included in their reports (see page 115).
  - (e) Procedures for the prompt reporting of unfavorable Safeguard results (see page 116).
24. Ensure that the CIA's Nonproliferation Center and the appropriate US&FCS posts are on BXA's distribution list for all Safeguard trip reports. These reports should be forwarded to the CIA's Nonproliferation Center in an electronic format (see page 116).

### **Other OIG Concerns**

25. Notify referral agencies of all negative pre-license checks (see page 127).
26. Take the following actions necessary to ensure license determinations prepared for Export Enforcement and Customs are conducted and communicated in a timely manner. Such actions should include:
- (a) Institute a front-end technical review of license determinations and make sure that they are not affected by absences of key staff persons currently assigned this function (see page 129).



- (b) Ensure that licensing officers process license determinations in a timely manner and hold them accountable for doing so (see page 129).
- (c) Program ECASS to allow LOs to use the “hold without action” feature while processing license determinations under limited circumstances, e.g., during a request for additional information necessary to complete the request (see page 129).
- (d) Issue written procedures for assigning license determinations reviewed by multiple divisions (see page 129).
- (e) Approve and implement Export Administration’s draft guidance recommending that license determinations should be completed within the same 14-day time period as required for CCATS, as long as the license determination consists of six items or less and all information necessary to complete the license determination has been submitted (see page 129).
- (f) Develop written agreements between Export Administration and Export Enforcement, and Export Administration and U.S. Customs Service, to outline the responsibilities of each party involved in the license determination process. Specifically, the agreements should set forth standard procedures for (1) submitting license determination requests (e.g., required information needed by Export Administration to make a determination), (2) processing license determination requests in a timely manner, and (3) the escalation process for late license determinations (see page 129).
- (g) Work with Customs to find a way to automate the referral of license determinations between Customs and Export Administration (see page 130).

### ECASS

27. Work with the Department, OMB, and the Congress to obtain a commitment to fully fund the chosen option to replace ECASS (see page 139). As part of its new system development effort, BXA needs to:
- (a) Establish a project management team, including a full-time project director, as soon as possible, to oversee development and implementation of BXA’s new information database system (see page 139).
  - (b) Conduct a cost-benefit analysis for developing a classified database system with software upgrades that could be made to allow better interface capabilities with the referral agencies’ licensing systems at a later date, including (1) performing a network analysis to determine future network requirements; (2) performing one or

more prototype tests of proposed systems before a final system alternative is chosen; and (3) obtaining approval of the departmental Information Technology Steering Committee for the chosen alternative (see page 139).

- (c) Coordinate BXA's system development efforts with the other export licensing agencies. Encourage these agencies to establish an interagency steering committee to review the automation portion of the export licensing process from coordinating common system architecture requirements to determining how interagency resources can be used to fund and implement a new system (see page 139).
  - (d) Evaluate the most viable options for the location of BXA's computer operations. Specifically, look at the possibility of continuing at its current facility, or service by another Commerce center, another federal center, outsourcing, as well as creation of an in-house BXA center. BXA must obtain departmental approval if it decides to leave the Springfield Computer Center and move to another location (see page 139).
28. Take the following actions necessary to implement or strengthen the internal controls for ECASS, including:
- (a) Provide a duplicate read-only tape to the Under Secretary for Export Administration every 90 days, highlighting any changes that might be made by lower ranking BXA personnel (see page 143).
  - (b) Establish criteria for reopening closed cases in the system (see page 144).
  - (c) Ensure that the electronic audit trail is more complete (see page 144).
  - (d) Have the database administrator assign data element responsibilities to individuals throughout the organization (see page 145).
  - (e) Establish an official database review board (see page 146).
  - (f) Establish a standards development group to develop appropriate database standards, including data definition, data documentation, passwords, and writing and testing programs (see page 146).
  - (g) Designate a team to periodically review the internal controls and risks associated with BXA's system, about once a year or when conditions materially change (see page 146).

- (h) Require the database administrator to reorganize the database every year (see page 146).
- (i) Consider the feasibility of one data entry clerk's work being reviewed by another before it goes into the database, or contract this function out (see page 148).
- (j) Reestablish the old "User Meetings" between the operations staff, licensing officers, and information technology staff to discuss issues and identify and resolve problems quickly (see page 148).
- (k) Take steps to reduce the number of duplicate codes in the database, including an extensive archiving effort to retire a large number of duplicate identification numbers (see page 149).
- (l) Update the current continuity of operations plan to include all appropriate manual and system contingency processes as soon as possible (see page 151).
- (m) Establish a risk management team to identify and assess the severity of risk in BXA's database environment, or have a contractor perform the risk analysis (see page 151).
- (n) Send a "network message" to emphasize that all database problems should be reported via the hotline (see page 152).
- (o) Prepare a BXA system security plan (see page 152).
- (p) Perform periodic security reviews (see page 153).
- (q) Officially assign the security duties of BXA's computer system to BXA's security officer (see page 153).
- (r) Provide all ECASS users with current security training (see page 153).
- (s) Develop a communication link to immediately notify the Springfield Computer Center of terminated or transferring employees so that system access can be promptly revoked or modified, by the end of each working day (see page 155).
- (t) Restrict the number of BXA employees with file manager access (see page 155).



## APPENDIX A

### Answers to the Chairman of the Senate Committee on Governmental Affairs' Questions of August 26, 1998

In a letter dated August 26, 1998, Senator Fred Thompson, Chairman of the Senate Committee on Governmental Affairs, requested that the Inspectors General from the Departments of Commerce, Defense, Energy, State, and the Treasury and the Central Intelligence Agency conduct an interagency review of the export licensing process for dual-use commodities and munitions. The Chairman specifically asked the six Inspector General offices to update a 1993 interdepartmental OIG review of the export licensing process<sup>101</sup> and, at a minimum, answer 14 specific questions. Our report, in its entirety, fulfills this request. However, Appendix A (1) presents the 14 specific questions raised and (2) summarizes our responses as follows:

**1. Please examine whether the current, relevant legislative authority contains inconsistencies or ambiguities regarding the licensing of dual-use and munitions commodities, and the effect of any such inconsistencies and ambiguities.**

The Export Administration Act of 1979, as amended, is the primary legislative authority for controlling the export of dual-use commodities. As first reported in the 1993 special interagency OIG review, the act does contain ambiguous language concerning the extent to which the Commerce Department must refer license applications to other federal agencies. Specifically, the act gives decision-making authority for dual-use license applications to Commerce and encourages Commerce to carry out its authority with limited referral to other agencies. On the other hand, the act also states that the Secretary of Commerce will seek recommendations from government agencies concerned with aspects of U.S. policies and operations that have an important bearing on exports. This ambiguity led to many conflicts or misunderstandings between the various export control agencies as to which licenses Commerce should refer for review by other agencies.

However, in December 1995, Executive Order 12981 more clearly defined the export licensing referral process by authorizing the Departments of Defense, Energy, and State, and the U.S. Arms Control and Disarmament Agency (ACDA)<sup>102</sup> to review any license application received by Commerce. As a result, each agency has an opportunity to provide its individual perspective (e.g., national security or foreign policy) about a potential dual-use export transaction, thus making the licensing process more transparent.

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<sup>101</sup>*The Federal Government's Export Licensing Processes for Munitions and Dual-Use Commodities*, conducted by the OIGs at the Departments of Commerce, Defense, Energy, and State, September 1993.

<sup>102</sup>Since April 1, 1999, ACDA has been part of the State Department, as mandated by the Foreign Affairs Agencies Consolidation Act of 1998.

Nonetheless, the fact that it has been 10 years since the expiration of the act<sup>103</sup> could send an ambiguous message to other countries (including our allies) that the United States is not truly committed to export controls. Thus, we believe that it is imperative that the Congress renew legislative authority for export controls. In the new legislation, the Congress should maintain the transparency provided for in the executive order and continue to give all licensing agencies the authority to review all export license applications.

In addition, the Congress should maintain the dispute resolution process outlined by Executive Order 12981. Under the current process, any dissenting agency can escalate its concerns about any license application to various ascending levels of review all the way to the President. As we discuss in Question number 4 below, we found the interagency dispute resolution process to be working well.

Furthermore, the Congress should discuss the benefits of opening up the munitions licensing process to the Commerce Department's Bureau of Export Administration (BXA). Although the other export licensing agencies have the opportunity to participate in the dual-use export licensing process, BXA lacks the same opportunity to participate in the munitions licensing process. The Arms Export Control Act of 1976 authorizes the President to control the commercial export of goods and technologies that are on the U.S. Munitions List. The authority for administering the export control functions of this act was delegated to the Secretary of State. State's Office of Defense Trade Controls (DTC) administers the International Traffic in Arms Regulations, which govern the export of munitions. DTC refers license applications to other agencies or bureaus for review because of concerns about technical or policy issues related to the applications, but it does not refer any applications to BXA.

However, since there are a limited number of items that may be subject to both the International Traffic in Arms Regulations and the Export Administration Regulations, we believe both Commerce and State could benefit from having a complete picture of what each agency is approving or denying for consistency's sake. Although we are not suggesting that BXA be consulted on export licenses for "arms," we do believe that the Congress and the Administration should evaluate the benefits of making the munitions licensing process more transparent with regard to those items that may be "dual-use" but fall under the U.S. Munitions List. (See Section I of our report,<sup>104</sup> page 23, for further discussion of export control legislation.)

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<sup>103</sup>The Export Administration Act has been expired since September 1990, except for a brief time in 1994 when it was reinstated. During periods in the past when one version of the act has expired and a new version has not been enacted, the authority for imposing export controls is derived from the International Emergency Economic Powers Act (IEEPA). Most recently, IEEPA has enabled BXA to control exports for the period from August 1994 to the present while the Congress continues to debate enactment of a new export control act.

<sup>104</sup>*Improvements Are Needed to Meet the Export Licensing Requirements of the 21<sup>st</sup> Century*, Draft Inspection Report IPE-11488, May 1999.

**2. Please examine whether Executive Order 12981 (1995) as implemented is consistent with the objectives of the Export Administration Act and other relevant legislative authority.**

We determined that Executive Order 12981 is generally consistent with the objectives of the Export Administration Act. As we stated in our response to Question number 1, the executive order more clearly defines the export licensing referral process by giving the Departments of Defense, Energy, and State, and ACDA the right to review *any* license application received by Commerce. As a result, each agency has an opportunity to provide its individual perspective about a potential dual-use export transaction.

However, unlike the Export Administration Act, the executive order fails to mention the exporter appeals process. Specifically, once an export license application has been formally denied, the exporter has the right to appeal to Commerce's Under Secretary for Export Administration, whose decision is considered final. Although BXA informally confers with the referral agencies on appeals, there is no requirement that this decision be made in consultation with these agencies.

Officials at the Department of Defense have questioned the authority for the exporter appeals process now that the Export Administration Act has expired and the executive order makes no mention of the process. However, we believe that there is ample authority for the appeals process and we do not share the view that because the executive order fails to mention the exporter appeals process that somehow this process is invalid. On the other hand, we recognize that the question arises as to whether an exporter could use the appeals process to circumvent the interagency referral process; i.e., a case denied during the interagency license review could be approved during the appeals process, with no formal interagency review.

While we found no evidence indicating that BXA does not consult with the referral agencies before overturning a denial, we believe that for the sake of transparency in the export licensing process, the referral agencies should be formally included in the appeals process. Therefore, we are recommending that BXA work with the National Security Council to establish formal procedures to include the referral agencies in the appeals process. We would also encourage the Congress to address this issue in drafting new export control legislation. (See Section VI of our report, page 87, for further discussion of the exporter appeals process.)

We also determined that minor changes are needed to Executive Order 12981 with regard to the impact of ACDA's merger with State, as well as clarification on agency representatives at the assistant secretary-level Advisory Committee on Export Policy (ACEP). Specifically, the merging of ACDA into State leaves the ACEP, an important part of the dispute resolution process, with only four standing voting members. Since ACEP decisions are based on a majority vote, the committee faces a potential problem if a vote comes down to a tie. We recommend that BXA request that the National Security Council review this issue and provide a procedure to follow in

the event of a tie vote. In addition, the Congress should consider this issue when drafting new export control legislation.

During our review, BXA managers expressed their frustration regarding the failure of referral agencies to send the appropriate representation level to the ACEP meetings. Upon examination of the executive order, we found that its language gives referral agencies the flexibility to decide who should attend these meetings. BXA officials disagree with this interpretation and insist that it was the intent of the drafters of the executive order for ACEP representatives to be at the assistant secretary-level or its equivalent. To settle this dispute, we recommend that BXA request the National Security Council to clarify this issue in an amendment to the executive order. In addition, the Congress should consider this issue when drafting new export control legislation. (See Section I of our report, page 23, for further discussion of Executive Order 12981.)

**3. Please determine if there is a continued lack of interagency accord, as stated in your 1993 interagency report, regarding whether the Commerce Department is properly referring export license applications (including supporting documentation) out for review by the other agencies.**

In the 1993 special interagency report, the OIGs pointed out that there was not complete accord between Commerce and most of the other federal licensing agencies regarding which license applications should be referred for comments to the other agencies. During our recent review, we determined that the dual-use export licensing process is clearly more transparent today than it was in 1993. Specifically, in fiscal year 1998, 85 percent of all export license applications submitted to Commerce were referred to other export licensing agencies as compared to only 53 percent in 1993.

As we stated in our response to Question number 1, in 1995 the President issued Executive Order 12981, which authorized the Departments of Defense, Energy, and State, and ACDA to each have the authority to review any export license application submitted to the Department of Commerce. While the four referral agencies can now see all applications, they have provided Commerce with delegations of authority for certain types of applications, based on the level of technology, the appropriateness of the items for the stated end use, and the country of destination. Even with the delegations, most export license applications are still referred to Defense. In addition, since the transfer of jurisdiction of commercial encryption products from State to Commerce in 1996, the Justice Department has been given a role in the license review process for encryption license applications.<sup>105</sup> Furthermore as we discuss in our response to Question number

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<sup>105</sup>Executive Order 13026, *Administration of Export Controls on Encryption Products*, November 15, 1996, authorizes the Department of Justice to review any export license applications pertaining to encryption items. In addition, the National Security Agency was delegated authority by the Defense Threat Reduction Agency to review most encryption item exports referred to the Defense Department.



4 below, when the reviewing agencies cannot agree on a final disposition of an export license application, the case is automatically escalated to the dispute resolution process.

However, although the referral of export license applications has improved due to increased transparency, the commodity classification process is vulnerable to incorrect classifications due to a lack of transparency. Specifically, BXA holds the exporter responsible for classifying an export item, but it will advise an exporter whether an item is subject to the Export Administration Regulations and, if applicable, identify the appropriate Export Control Classification Number. Exporters may verbally inquire about a commodity classification (e.g., telephone call), but only written inquiries result in binding determinations.

Both Defense and State indicated to us a need for this process to be completely opened for interagency review similar to the export licensing process. To illustrate the need for this, the agencies point to the 1995 investigative report on the crash of a Chinese rocket carrying a satellite for which BXA mistakenly determined no license was required. BXA allowed the release of the investigative report without consulting the referral agencies. BXA has since admitted that this decision was incorrect because the accident occurred in part of the rocket, not in the satellite being carried, and thus was a munitions item that fell under State's jurisdiction.

As part of our review, we sought to determine whether past commodity classification determinations by BXA did, in fact, support the concerns of Defense and State. We invited analysts from State and Defense to review a sample of commodity classification line items and second-guess the original determinations made by BXA.<sup>106</sup> Of the 103 selected for our sample, Defense identified 13 it found to be the most troublesome, and after discussing these cases with Commerce, Defense ultimately disagreed with BXA's decision in 5 of them.

In two of the five cases, Defense argued that the items were not under the Commerce Control List, and the commodity classifications should have been referred to State as commodity jurisdiction requests. BXA disagreed. According to 1996 NSC guidance, BXA is required to share with State and Defense all commodity classification requests for items or technologies specifically designed, developed, configured, adapted and modified for a *military application*, or derived from such items or technologies.<sup>107</sup> Therefore, regardless of whether these items fall under the Commerce Control List or the U.S. Munitions List, we believe that BXA should have at least referred these two commodity classifications to State—especially since the manufacturers' own literature describes them as "militarized." In the remaining three cases, Defense agreed that

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<sup>106</sup>Officials from State's Defense Trade Controls chose not to participate in the review.

<sup>107</sup>Subsequent to the NSC guidance on this subject, Defense informed BXA in 1996 that it did not want the opportunity for an initial review of munitions-related commodity classifications and instead requested that Commerce provide, on a weekly basis, a copy of such completed commodity classifications requests and decisions to Defense. Defense's current position on this matter is significantly different than it was in 1996.

the items fell under the Commerce Control List but disagreed with BXA's export control classification number. BXA ultimately agreed with Defense's classification for one of the three commodity classifications but maintained its original position on the other two.

Nonetheless, as our sample demonstrates, BXA appears to not have fully complied with NSC's 1996 guidance to refer all munitions-related commodity classification requests to State. Furthermore, per Defense's request, BXA has not referred all of the completed commodity classifications for such items to Defense. At this time, we are not convinced that BXA should refer all CCATS to both Defense and State given the fact that these agencies may not have adequate resources to review all CCATS in a timely manner. However, we strongly believe that BXA needs to work with both Defense and State to ensure that the CCATS process is more transparent with regard to items or technologies specifically designed, developed, configured, adapted and modified for a military application, or derived from such items as called for in the NSC guidance. Therefore, we recommend that BXA, in conjunction with the Defense and State Departments, work with the NSC to develop specific criteria and procedures on how to implement its 1996 guidance for the referral of munitions-related commodity classifications to Defense and State. In addition, we believe BXA should consult with Defense to determine if it wants to continue its delegation to BXA on munitions-related CCATS or withdraw it. (See Section II of our report, page 39, for further discussion of the commodity classification process.)

**4. Please determine if the interagency dispute resolution (or "escalation") process for appealing disputed license applications allows officials from dissenting agencies a meaningful opportunity to seek review of such applications, and assess why this process is so seldom used.**

Overall, we found that the interagency escalation process for disputed license applications allows officials from dissenting agencies a meaningful opportunity to seek additional review of such cases. Of the 9,405 export license applications referred to other agencies in fiscal year 1998, only 8 percent were escalated to the dispute resolution process. The other 92 percent were resolved by consensus among the agencies without escalation. In many cases, individual agency concerns are addressed during the referral process by adding or modifying license conditions. If any of the reviewing agencies does not agree on a final disposition of a license application, the case is automatically escalated to a higher level of review as mandated by Executive Order 12981.

There are four levels of escalation for dual-use cases: Operating Committee (OC) at the senior civil service level, Advisory Committee on Export Policy at the assistant secretary-level, the Export Administration Review Board (EARB) at the Cabinet level, and the President. Each level of the escalation process is required to consider all matters referred to it, giving consideration to foreign policy, national security, and domestic economy concerns as well as concerns about the proliferation of weapons of mass destruction.

From fiscal years 1991 to 1998, the number of cases escalated to the OC increased by 353 percent, while the number of cases escalated to the ACEP decreased by 62 percent. In addition, only 21 license applications have been escalated to the EARB during this time period, and only one since 1991. The fact that there has been a significant increase in the cases escalated to the OC, and a decrease in cases escalated to the ACEP and EARB, as well as a small percentage of OC cases overturned at the ACEP, indicates that this process is working well.

At the first level of escalation, the Department of Commerce serves as the Chair of the Operating Committee and its voting members also include Commerce, Defense, Energy, Justice (for encryption cases), State, and ACDA. Representatives of the Director of the Central Intelligence Agency and the Chairman, Joints Chief of Staff, are nonvoting members. The OC meetings are held weekly. A notice of the OC license decision is sent to the designated person in each participating agency. Any decision not escalated to the ACEP by a dissenting agency within five days of the notification of the OC decision becomes final.

Based on the three OC meetings we observed, we found that the OC Chair affords each agency—including BXA—the opportunity to present its recommendation on every application. We generally found that the meetings build consensus through healthy exchanges and debates. While the OC Chair has been given the authority to decide all cases at this level without having to reflect the recommendations of the majority of the participating agencies, the decisions of the Chair are usually based on interagency consensus. Typically, agencies who maintain a denial but do not wish to escalate to the ACEP, often play a key role in crafting the conditions placed on the approved licenses. Only about five percent of the OC decisions decided by the Chair are contrary to the majority decision, and virtually all of these cases were escalated to the ACEP for a final decision. BXA records indicate that of the 70 cases escalated to the ACEP between February 1997 and February 1999, in only 6 cases did the ACEP decisions overturn the OC Chair's determination.

The Assistant Secretary for Export Administration serves as the Chair of the ACEP. The ACEP, which meets monthly, also includes assistant secretary-level representatives from the Departments of Defense, Energy, State, and ACDA. Appropriate representatives of the CIA's Nonproliferation Center and the Joint Chiefs of Staff are non-voting members of the committee. ACEP decisions are based on recommendations of the majority of the agencies voting at the meeting. One of the primary reasons agencies escalate a case to the ACEP is because they want the case to be decided at higher levels because of policy implications raised by the proposed transaction.

Any dissenting department or agency may appeal an ACEP decision to the Export Administration Review Board within five days. The EARB is chaired by the Secretary of Commerce, and its members include the Secretaries of Defense, Energy, and State and the Director of ACDA. The Chairman of the Joint Chiefs of Staff and the Director of the Central Intelligence Agency are nonvoting members of the EARB. The EARB's decision is based on a majority vote. Again,

within five days of this decision, any dissenting agency may make a final appeal to the President. No cases have been escalated to the President since the implementation of Executive Order 12981 in December 1995. We would conclude that the upper three levels of the resolution process are seldom used because both the regular referral process and the Operating Committee are working well and disputes over specific licenses are effectively resolved at those levels. (See Section V of our report, page 77, for further discussion of the dispute resolution process.)

**5. Please review whether the current dual-use licensing process adequately takes into account the cumulative effect of technology transfers resulting from the export of munitions and dual-use items, and the decontrol of munitions commodities.**

The current dual-use licensing process does not take into account the cumulative effect of technology transfers. While individual technology sales may appear benign, combining technology sales over a long period of time may allow U.S. adversaries to build weapons of mass destruction or other capabilities that could threaten our national security.

We found that BXA licensing officers have some institutional knowledge about what goods and technologies specific end users or countries are receiving because they tend to process similar export license applications dealing with the same commodities, exporters, and end users over time. However, according to the responses from licensing officers to our survey, they do not routinely analyze the cumulative effect of proposed exports or receive such assessments to use during license reviews. During our review, many licensing officials noted that to fully analyze the cumulative effect would be very difficult because, in addition to knowing what U.S. exports have been received, one would have to know what internal capabilities a specific country has and what technology it has acquired from other countries. We believe that this type of cumulative effect analysis, while difficult, would be valuable during the export license application decision-making process.

We understand that the Department of Energy's seven laboratories conduct a limited cumulative effect assessment review for nuclear dual-use exports, but there is no coordinated effort to conduct such an assessment for all commodities. In addition, we learned that Defense has a requirement to perform annual assessments of the total effect of transfers of goods, munitions, services, and technology on U.S. security, but it had not yet performed such reviews. We believe that BXA should work with the intelligence community, including the CIA, Defense, and Energy, to determine the feasibility of developing a mechanism to better track and assess the cumulative effect of dual-use exports to a specific country or region and to make that information available for the licensing process.

- 6. Please review whether the current munitions licensing process adequately takes into account the cumulative effect of technology transfers resulting from the export of munitions and dual-use items, and the decontrol of munitions commodities.**

This question is not applicable to the Department of Commerce because it does not participate in the munitions licensing process.

- 7. Please determine whether license applications are being properly referred for comment (with sufficient time for responsible review) to the military services, the intelligence community, and other relevant groups (the “recipient groups”) by the Defense Department and other agencies. Please consider in particular numerical trends in the frequency of such referrals, trends in the types of applications referred, trends in the nature of the taskings made in connection with the referrals, and the perceptions of officials at the recipient groups.**

While we believe the overall referral process is generally effective, we did identify some areas that need management attention. Specifically, as part of our review, we looked at a randomly selected sample of 60 non-referred cases to determine whether BXA had sufficient justification for not referring those applications. The most common reasons export license applications in the sample were not referred were because they (1) lacked sufficient information to allow BXA to evaluate the application and were returned to the exporter; (2) were automatic denials, e.g., they involved certain items going to India due to its detonation of nuclear explosive devices; and (3) were routine cases that the other agencies have elected to delegate to Commerce. However, 6 of the 60 non-referred export license applications should have been referred to Defense (5 cases) and Energy (1 case). Two of these cases involved amendments to previous licenses, and the other four raised procedural concerns. We recommended that BXA remind its licensing officers to reread BXA’s referral procedures and to follow them in the future to address these concerns.

Furthermore, we identified two weaknesses in the export licensing referral process itself. First, while the intelligence community plays a critical role in license review and threat analysis, we found that the CIA and its Nonproliferation Center are not fully engaged in the export licensing process. Specifically, the CIA, at its own request, does not review all dual-use export license applications or always conduct a comprehensive analysis of export license applications it does receive. In addition, we believe that the CIA may not have adequate review time for its end user checks, especially in countries of concern like China.

Second, as we have reported in the past, another key element missing from the export licensing referral process is the screening of all parties to pending license applications against the Treasury Enforcement Communication System (TECS) database maintained by the Treasury Department’s U.S. Customs Service. TECS was created to provide multi-agency access to a common database of enforcement data to satisfy a recognized need to promote the sharing of sensitive information between federal law enforcement agencies. Screening every export license applicant and

consignee against TECS during the initial phases of the licensing process would give licensing and enforcement authorities early warning of any potential concerns Customs may have. (See Section IV of our report, page 57, for further discussion of the export licensing referral process.)

**8. Please determine whether license review officials at each of the agencies are provided sufficient training and guidance relevant for reviewing license applications, and whether more formal training and guidance is warranted. Dr. Leitner noted a paucity of such training and guidance in his Committee testimony.**

Our review disclosed that the policy and procedures used by licensing officers varied. Many of our survey respondents, as well as those we interviewed throughout the review, identified the lack of up-to-date guidelines as one of BXA's major weaknesses. However, in an effort to improve licensing officer guidance, on March 31, 1999, BXA officials implemented new procedures that emphasize the importance of obtaining sufficient information before processing a case and documenting all relevant facts and details pertaining to it. While the new guidance is clearly more thorough than the previous guidance, we believe it would also be beneficial to provide licensing officers with specific questions they should consider when processing export license applications to dynamic markets, such as China and Russia.

We also note that BXA is developing an electronic library to store its policies and procedures. We believe that this on-line licensing officer manual will be a valuable reference tool for licensing officers to access while preparing their case analyses. We have recommended that BXA develop a long-term plan for maintaining the library, including designating an individual to be responsible for updating the procedures, and determining when they will be updated and what procedures will be followed for updates.

During our review, we also found training provided to licensing officers to be inconsistent and often unresponsive to their needs. The export licensing function requires a continuous structured training program to ensure that the licensing officers' critical thinking and knowledge of export control issues and concerns are as strong as possible.

We were particularly concerned about the adequacy of training for new licensing officers. Such training is left up to the individual divisions and generally consists of reading the Export Administration Regulations and learning on-the-job by directing questions to experienced staff. However, we found that the Encryption Policy Division provides a comprehensive training program for all of its new analysts. Specifically, new analysts (1) spend three weeks answering phones and sitting in on other calls in the Exporter Counseling Division, (2) observe the division director's telephone responses to exporter questions, (3) attend regulations and technology seminars sponsored by BXA for exporters, and (4) observe interagency working group and industry meetings. While we recognize that training needs to be flexible to allow for a variety of learning methods in a variety of disciplines, we recommend that Export Administration consider using this kind of training program for all new licensing officers.

BXA needs to identify and prioritize the current and future learning needs of its licensing officers and then establish a formal training program to meet those needs. In addition, BXA should designate either a training team or training coordinator and provide the necessary resources to manage and implement an export administration training program. We provide a number of suggestions for in-house and outside training, as well as interagency exchanges, that we believe could improve licensing officers' performance. (See Section III of our report, page 47, for further discussion of policies and procedures and training provided to licensing officers.)

**9. Please review the adequacy of the databases used in the licensing process, such as the Defense Department's FORDTIS, paying particular attention to whether such databases contain complete, accurate, consistent, and secure information about dual-use and munitions export applications.**

Overall, we determined that ECASS, BXA's Export Control Automated Support System, contains complete, accurate, consistent, and secure information about dual-use license applications.<sup>108</sup> ECASS, developed by BXA in 1984, is an unclassified database system that provides license processing and historical license information to BXA and the referral agencies. We determined that the system's internal controls are generally adequate and that its data is sufficiently reliable. However, we have identified some controls that need strengthening or further implementation.

Furthermore, although the export licensing referral process has been working reasonably well and become increasingly transparent over the past five years, the agency automation systems are lagging way behind. We strongly agree with BXA that it needs a new system to process export license applications efficiently and effectively. While we encourage BXA and the Congress to move ahead with the development and funding of a new system as soon as possible, we believe that BXA should concurrently ensure that it considers the best available options, including a classified system. We urge BXA to coordinate its system development efforts with the other export licensing agencies to ensure that all of the systems are compatible and, at a minimum, are able to interact with one another. (See Section X of our report, page 133, for further discussion of ECASS.)

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<sup>108</sup>We identified and tested the controls in five major areas: (1) data management, (2) database management, (3) database integrity, (4) database operations, and (5) database security. General controls apply to all computer operations in an agency, including organization and management controls, security controls, and system software and hardware controls. Application controls ensure the authority of data origination, accuracy of data input, integrity of processing, and verification and distribution of output.

**10. In his testimony, Dr. Leitner described instances where licensing recommendations he entered on FORDTIS were later changed without his consent or knowledge. Please examine those charges, and assess whether such problems exist at your agencies.**

We examined ECASS to determine whether recommendations entered into the database were later changed without the consent or knowledge of licensing officers. We found two key controls to preclude this from happening.

The first control is that supervisors cannot make changes to pending or closed licenses, without the licensing officers' knowledge.<sup>109</sup> For pending licenses, supervisors can only orally suggest changes to licensing officers or insert changes into the licensing officer notes section of the automated license application. For example, supervisors may request licensing officers to reject a license based on current intelligence that the licensing officers are not privy to. Nevertheless, if the licensing officers are orally instructed to make changes, they are supposed to document the request in the licensing officer notes section. However, we have found that licensing officers do not consistently document their changes or supervisor-suggested changes in licensing officer notes.

If a supervisor goes into the case file and electronically requests that a licensing officer make changes to a pending license, ECASS automatically documents the request. Supervisors can move cases from one licensing officer's queue to another queue to balance a licensing officer's workload, but again, the supervisors cannot physically make changes to the electronic record. Our survey confirmed that the licensing officers believe that their recommendations are not changed without their consent or knowledge.

With regard to closed licenses, both supervisors and licensing officers must submit a written request to BXA's operations staff to reopen a case. Reopening a case is rare; for example only 120 out of approximately 11,000 export license applications were reopened in fiscal year 1998. After the operations staff reopens a case and makes the appropriate change, the case is then sent to the applicable licensing officer for review. Reasons for reopening a case include: correcting data input errors, changing case decisions from denial to approved or approved with conditions, and adding or deleting conditions and riders as a result of the escalation or appeals processes. However, while there is a paper audit trail of who requested the case be opened, we found a few examples where the electronic audit trail did not have this information. BXA must ensure that the electronic audit trail is complete because when the paper document requesting a case be reopened is eliminated, the electronic audit trail will be the only source to determine why and at whose request a case was reopened.

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<sup>109</sup>Countersigners or supervisors review and sign off on license cases submitted to them by licensing officers before the licenses are issued, denied, or returned without action.



The second control to prevent unauthorized changes to ECASS involves the referral agencies. Specifically, we determined that Defense, Energy, and the CIA's Nonproliferation Center could not make changes either directly to ECASS from their terminals or to the files they download to their systems. We also found that State and ACDA could not make changes directly to ECASS from their ECASS terminals. (See Section X of our report, page 133, for further discussion of ECASS.)

**11. Please determine whether license review officials are being pressured improperly by their superiors to issue or change specific recommendations on license applications. Dr. Leitner testified about one such incident that happened to him at DTSA.**

While BXA managers provide their opinions on many cases, our survey confirmed that most licensing officers believe that their recommendations entered are not changed without their consent or knowledge, and more importantly, they are not improperly pressured into changing specific positions on license recommendations. Specifically, out of the 36 licensing officials' responses to this survey question, only 3 indicated that they had received pressure to change positions on recommendations.

One of the three respondents indicated that he had been pressured to change his recommendations, but "not very often." However, after we met with this individual to get more details on the cases on which he was allegedly pressured, the licensing officer could not remember the license numbers or provide us any more details on the cases.

The second respondent stated that,

"There have been numerous instances of management at all levels putting pressure on licensing officers to approve applications over the years. Even when the event becomes known, no action is taken to remove or chastise the manager. This is well known to be the case throughout the organization."

We attempted to substantiate this statement even though the survey response was sent anonymously. However, the remaining licensing officer responses to the survey, as well as our interviews with BXA personnel, do not support this individual's position.

The third respondent, who also is the Chair of the Operating Committee, indicated that upper management sometimes conveys instructions about the decision she should make on a specific OC case. Both National Security Agency and Justice officials informed us that the OC Chair has also indicated to them that any OC decisions written in the passive voice (e.g., "It has been decided..." versus "The Chair determines...") can be interpreted to mean that BXA management told her how to decide a case and, therefore, it was not "her" decision.

When we questioned the OC Chair about these allegations, she confirmed that she writes in the passive voice when she believes management has told her how to decide a case. However, she

also indicated that this is a rare occurrence and generally it involves a situation where she believes more information is needed about the transaction before a final decision can be made, and not necessarily a decision that she would ultimately disagree with if she had more time to consider the case.

We discussed this issue with both the Assistant Secretary for Export Administration and his deputy, who informed us that they have never “told” the OC Chair how to vote on a particular case. However, since the OC Chair reports to both of them, they did state that they have a responsibility to ensure that the OC Chair carries out her responsibilities efficiently and in concert with U.S. regulations and policy. As a result, they indicated that they may have from time to time instructed the OC Chair on the provisions of the regulations or on changes in U.S. licensing policy to ensure that her actions are consistent with U.S. regulations and policies or to bring a case review to closure by making a decision (e.g., where the loss of a sale is imminent or a case has exceeded the time frames of the Executive Order).

The OC plays a pivotal role in the export licensing process. Overall, we heard only positive feedback about both the committee and its Chair. While we recognize that the OC Chair is a BXA employee and that the Executive Order recognizes that an OC decision is a Commerce decision that can be escalated by a dissenting member agency, we also believe that one could interpret the role of the OC Chair as outlined in the Executive Order to be “independent” since the procedures call for the OC Chair to preside over the OC meeting and listen to all of the reviewing agency arguments—including BXA’s—before rendering a decision on a case.

Our review indicated that the main reason the OC review process is so successful is because of the current OC Chair’s willingness to be objective in her decisions and not necessarily just vote the “Commerce” position. As noted above, the OC Chair works very hard to involve all agency representatives in a very interactive and dynamic decision-making process on each case, and most decisions are based on interagency consensus. In addition, we were impressed with the Chair’s willingness to stand firm on the licensing decisions she makes. For instance, in one recent case, the Chair approved a license with conditions over the objections of all of the participating agencies—including BXA. While the case was escalated to the ACEP, it illustrates that the OC Chair does not give in easily if she firmly believes in her decision.

Nonetheless, no matter what the rationale is, we believe that the OC Chair should be free to independently decide a case. BXA management should definitely not give the impression that it is instructing the Chair on what licensing decisions to make. If the Chair makes a decision that BXA disagrees with, BXA should use the avenue afforded it under the executive order to escalate cases to the ACEP in order to avoid any misconceptions that this part of the process is not transparent. (See Section V of our report, page 77, for further discussion of the Operating Committee.)

**12. Please determine whether our government still uses foreign nationals to conduct either pre-license or post-shipment licensing activities and whether such a practice is advisable.**

Based on our sample of end use checks completed in fiscal year 1998 by Commerce’s United States and Foreign Commercial Service (US&FCS) personnel and a survey of 27 US&FCS overseas posts, most end use checks are being conducted by American officers or BXA enforcement agents.<sup>110</sup> However, foreign service nationals (FSN) are still occasionally used, and it was not always clear from the posts’ reporting cables who conducted some of these pre-license checks (PLCs) and post shipment verifications (PSVs).

There were a total of 283 PLCs and 346 PSVs conducted in fiscal year 1998. Of 283 PLCs, approximately 91 percent were conducted by US&FCS post personnel, and the other 9 percent by Export Enforcement Safeguard Verification teams. Of 346 PSVs, approximately 17 percent were conducted by US&FCS post personnel, and approximately 83 percent by Safeguard Verification teams.

In addition, based on our review of completed checks conducted by US&FCS personnel—90 PLCs from our sample of 124 PLCs and 15 PSVs from our sample of 18 PSVs in fiscal year 1998—it appears that the majority of PLCs and PSVs are being conducted by appropriate personnel, such as an American officer or a team that includes an American officer as well as either an FSN or a personal services contractor (PSC). (See Table 1.)

**Table 1**

	US&FCS Checks Reviewed	US&FCS Personnel Conducting End Use Checks			
		Officer	FSN/PSC	Combination	Unclear
PLC	90	22	5	36	27
PSV	15	10	0	0	5
<b>Total</b>	105	32	5	36	32

Notes: PLC= pre-license check, PSV= post shipment verification, FSN= foreign service national, and PSC= personal services contractor

Source: Office of Enforcement Analysis, Bureau of Export Administration.

<sup>110</sup>End use checks are conducted by BXA’s export enforcement agents under the Safeguard Verification program.

However, it was not always clear from the posts' reporting cables who conducted some of these PLCs and PSVs. Although 10 of the response cables indicated that the "Commercial Attache" had performed the PLC, it was not clear whether that person was an American officer or a PSC because the latter personnel often use this title. Post responses on two PLCs referred to "embassy officers," but again it was not clear whether they were *American* officers. The remaining 15 response cables did not provide any indication as to who had performed the PLC.

Furthermore, post responses were not always clear about who conducted PSVs. Of 15 PSVs completed by US&FCS in our sample of fiscal year 1998 PSVs, it was not clear who had conducted 5 PSVs, while American officers had conducted the remaining 10. US&FCS posts clearly need to provide unambiguous information in their reporting cables regarding who conducted the end use check.

According to a survey of 27 US&FCS posts conducted during our review, American officers reportedly conduct PLCs and PSVs at six posts, combination teams of commercial officers accompanied by FSNs or PSCs conduct checks at 15 posts, and FSNs have conducted or are allowed to conduct checks at five posts. The remaining post has a special arrangement under which the host government performs these checks.

Based on BXA's own argument on this issue, we believe that it would be in the best interests of the United States for these checks to be conducted by U.S. citizens who are also U.S. government employees. Specifically, as stated in Appendix I of BXA's Handbook, there are three disadvantages of using FSNs to conduct PLCs: the credibility of the check, the possible reluctance of an FSN to testify against a fellow citizen in a U.S. court, and lack of access to classified material. Some or all of these disadvantages may also apply if a PSC is used to complete end use checks. Even for those PSCs who are U.S. citizens, their credibility as a temporary employee without any specific training in conducting checks could be called into question. In addition, many PSCs may not have appropriate security clearances to give them access to relevant files and data sources within other agency files at post, a necessary research tool before conducting end use checks. (See Section VIII of our report, page 103, for further discussion of end use checks.)

**13. Please determine whether the agency licensing process leaves a reliable audit trail for assessing licensing performance.**

We found that BXA's licensing process provides a fairly complete audit trail to reliably assess the licensing process and decision-making on any specified license. BXA's audit trail comprises 11 major elements: (1) paper and automated license applications;<sup>111</sup> (2) automated license applications containing licensing decisions by licensing officers, supervisors, and referral agencies;

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<sup>111</sup>Exporter paper applications become automated license applications after they are scanned in and verified.

(3) paper files maintained by licensing officers; (4) paper copies of the Operating Committee licensing decisions that were disseminated to licensing officers and the referral agencies; (5) scanned exporter technical specifications;<sup>112</sup> (6) current and archived licenses in ECASS; (7) backup tapes of current and archived licenses; (8) the ECASS file that documents reopened cases; (9) the ECASS logs that record database and security activities; (10) system documentation for each program change; and (11) ECASS verification of data transmitted to the referral agencies.

Nonetheless, we identified several areas that still need correction. First, the ECASS electronic record records only when and by whom a change to a data field was made in a pending case, not what change was made. If, for example, licensing officers make changes to data fields in pending licenses, the current data in that field is “written over” or eliminated. The database management system cannot “audit” each field in the database to show what specific changes are made. As a result, licensing officers are supposed to “document” changes in licensing officer notes, but that is not consistently done. To determine what fields have been changed, BXA personnel would have to painstakingly compare different versions of backup tapes. To correct this problem, BXA’s Acting Chief Information Officer stated that a separate record with the old value will be coded to show the old and new value. We agree that this change will improve the ECASS audit trail.

Second, BXA does not ensure that all license conditions agreed to by the OC, ACEP, or EARB, are correctly inputted into ECASS. If conditions are not properly input, the audit trail changes, data integrity is affected, and quality control is reduced. We have recommended that the OC be given the authority and resources to process all licensing decisions made during the escalation process to better ensure quality control. (See Section V of our report, page 77, for further discussion of the quality control of OC decisions.)

Third, we found that the departmental computer center in Springfield, Virginia, is adequately maintaining automated applications by backing up the ECASS database on a daily, weekly, and monthly basis, and copies are stored at the Springfield Computer Center and the Department of Commerce headquarters. However, there is the possibility that these tapes could be modified by BXA personnel, invalidating the audit trail. In 1993 we recommended that BXA provide a duplicate read-only tape to the Under Secretary for Export Administration every day, highlighting any changes that might be made by lower ranking BXA personnel. BXA personnel stated that getting the tape to the Under Secretary’s office and finding a place to store the tapes would be difficult to do on a daily basis. As a result, this has not happened. Since we still maintain that the audit trail would be strengthened by having the stored databases owned by BXA’s Under Secretary with read-only access to produce historical reports as required, we recommend that a duplicate read-only tape be provided to the Under Secretary every 90 days, highlighting any changes that might be made by lower ranking BXA personnel.

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<sup>112</sup>Exporter technical specifications include brochures and design drawings.

Fourth, we also recommended in the 1993 report that paper applications and technical specifications be retained for five years. Currently, BXA only physically retains hard-copy information for 90 days except memorandums from BXA personnel or exporters requesting system changes, and these are maintained for one year. BXA personnel stated that maintaining paper applications for five years is too long. BXA believes that reliance on electronic records is appropriate. We agree. Therefore, we have modified our recommendation based on BXA's concerns to reflect its current practice. (See Section X of our report, page 133, for further discussion of ECASS.)

**14. Please describe the procedures used by agencies to ensure compliance with conditions placed on export licenses (e.g. no retransfers without U.S. consent, no replications, and peaceful use assurances), and assess the adequacy and effectiveness of such procedures.**

BXA has several tools to monitor conditions placed on export licenses, including (1) a computer tickler system to identify conditions that require follow-up reporting, (2) post shipment verifications, and (3) outreach visits. The ability to place conditions on a license is an important part of the license referral and resolution processes, as well as an additional means to monitor certain shipments. Frequently, the conditions are the result of lengthy negotiations among the referral agencies.

While there are 28 standard conditions that could be placed on an export license, only 7 actually require the exporter to submit documentation back to BXA concerning any shipment made against the license. BXA's Export Administration is responsible for monitoring six of these conditions, and BXA's Export Enforcement monitors the other one. However, BXA is still not adequately monitoring these license conditions, as first reported in the 1993 special interagency OIG review.

Specifically, we found that BXA's Export Administration follow-up subsystem was out of date due to (1) the low priority placed on this function, (2) the improper flagging of licenses requiring reports from exporters, and (3) the subsystem not tracking two major reporting conditions. As a result, exporters may continue to receive licenses even though they were non-compliant on prior licenses. In addition, most licensing officers (except for those responsible for deemed exports and encryption) are not involved in monitoring conditions placed on the licenses, and they did not have access to exporters' compliance history in order to make the most informed decision about an export license application. By not having an adequate monitoring system, BXA cannot assure itself that the goods were not diverted to an unauthorized end user, and exporters may receive new licenses even though they did not comply with previous ones.

We believe that the steps taken by licensing officers involved in monitoring exporter compliance with encryption and deemed exports license conditions should be used as a best practice by the other licensing divisions. Specifically, both licensing divisions were closely monitoring conditions they place on licenses. The encryption licensing staff monitor conditions by making follow-up

telephone calls to exporters, reminding them of their reporting requirements. They also use this opportunity to keep the exporters informed about pending policy changes and to find out how new regulations are affecting their businesses.

In addition, the program director for deemed exports informed us that besides calling U.S. companies, he was able to perform one on-site visit with a company who had received the most deemed export licenses over the past several years. Since deemed export licenses usually involve foreign nationals working for entities in the United States, we believe it should be easy for BXA to routinely spot-check these companies to physically verify that security procedures are in place and meet the established criteria to protect controlled technology, and we encourage BXA to do so.

We also found that BXA's Office of Export Enforcement was not closing out licenses from its subsystem after they had expired. After we pointed out the problem, Export Enforcement took immediate action and began contacting the exporters who held these licenses. However, we discovered that at least three of the exporters who were noncompliant on old license conditions from Export Enforcement's follow-up subsystem continue to receive licenses. Thus, it is imperative that Export Enforcement perform timely follow-up work to verify compliance among exporters and uncover any noncompliance. In July 1998, Export Enforcement hired a supervisory export compliance specialist to, among other things, monitor exporter compliance with regard to this reporting condition. However, we found no mention of the compliance monitoring follow-up task in the employee's performance plan. We recommended that BXA incorporate this responsibility into the supervisor's performance plan to ensure accountability. (See Section VII of our report, page 93, for further discussion of exporter compliance with reporting conditions.)

The remaining 21 license conditions do not require the exporter to submit any documentation or information to BXA but may require the exporter to perform certain actions or to ensure that certain rules are followed. For example, one condition stipulates "No reexport of the items listed on this license is authorized without prior authorization by the U.S. Government," while another one stipulates "The items authorized for export by this license/authorization are not to be used by nuclear end users or for nuclear end uses." These types of conditions are only monitored when export enforcement agents perform Safeguard visits overseas or when US&FCS personnel perform post shipment verifications.

As we mentioned in Question number 12, PSVs give BXA a reading as to whether exporters, shippers, consignees, and end users are complying with the terms of export licenses and licensing conditions. PSVs help BXA determine whether goods exported from the United States were actually received by the party named on the license and are being used in accordance with the license provisions. BXA focuses its PSVs on shipments that have special conditions attached to the license to make certain those conditions are being met. In fiscal year 1998, 346 PSVs were conducted.

Our review found some of the same concerns identified in previous OIG reports with respect to end use checks conducted by US&FCS. Among these concerns are (1) US&FCS's use of foreign service nationals and personal services contractors to conduct some checks, (2) failure to perform on-site checks, (3) inadequate record-keeping at posts, and (4) insufficient US&FCS coordination with other parts of the embassy and host governments in conducting checks.

Furthermore, we participated in 10 PSVs and one outreach visit as an observer on Export Enforcement's Safeguard Verification trip to Malaysia. Our participation in that trip greatly enhanced our understanding of how export enforcement agents conduct end use checks. Based on this trip and our review of Safeguard Verification Trip reports from fiscal year 1998, we believe this program is a valuable tool because of the "enforcement" element it brings to the end use check process. However, we have a number of suggestions that could make this program more effective: (1) better initial trip planning, (2) better in-country consultations, (3) clearer guidance or a standard format for trip reports, and (4) faster and wider dissemination of Safeguard check results, especially negative findings. We also believe that BXA should use the Safeguard visits as an opportunity to better train US&FCS staff on conducting end use checks. (See Section VIII of our report, page 103, for further discussion of end use checks.)

Finally, we found that BXA's export enforcement agents conduct outreach visits to selected exporters in high concern categories to determine how the exporter has complied with license conditions. Although we did not assess this program, we believe that educating exporters of the importance of complying with license conditions can be a valuable exercise.



## APPENDIX B

### Tier 3 Countries

Afghanistan	Laos
Albania	Latvia
Algeria	Lebanon
Andorra	Lithuania
Angola	Macedonia
Armenia	Mauritania
Azerbaijan	Moldova
Bahrain	Mongolia
Belarus	Morocco
Bosnia & Herzegovina	Oman
Bulgaria	Pakistan
Cambodia	Qatar
China (People's Republic of)	Romania
Comoros	Russia
Croatia	Saudi Arabia
Djibouti	Serbia and Montenegro
Egypt	Tajikistan
Estonia	Tunisia
Georgia	Turkmenistan
India	Ukraine
Israel	United Arab Emirates
Jordan	Uzbekistan
Kazakhstan	Vanuatu
Kuwait	Vietnam
Kyrgyzstan	Yemen



## APPENDIX C

### List of Acronyms

ACDA	Arms Control and Disarmament Agency
ACEP	Advisory Committee on Export Policy
AG	Australia Group
BXA	Bureau of Export Administration
CBCTC	Office of Chemical and Biological Controls & Treaty Compliance
CCL	Commerce Control List
CFR	Code of Federal Regulations
CJ	Commodity Jurisdiction
CWC	Chemical Weapons Convention
DTC	Office of Defense Trade Control
DTRA	Defense Threat Reduction Agency
EAA	Export Administration Act
EAR	Export Administration Regulations
EARB	Export Administration Review Board
ECASS	Export Control Automated Support System
EPCI	Enhanced Proliferation Control Initiative
IEEPA	International Emergency Economic Powers Act
LE	License Exception
MTCR	Missile Technology Control Regime
MTEC	Missile Technology Export Control Group
NLR	"no license required"
NMT	Office of Nuclear & Missile Technology Controls
NSG	Nuclear Suppliers Group
OC	Operating Committee
OEA	Office of Export Analysis
OEE	Office of Export Enforcement
OEXS	Office of Exporter Services
OIG	Office of Inspector General
SED	Shipper's Export Declaration
SIES	Office of Strategic Industries & Economic Security
SNEC	Subgroup on Nuclear Export Coordination
STFPC	Office of Strategic Trade & Foreign Policy Controls
WA	Wassenaar Arrangement



APPENDIX D



UNITED STATES DEPARTMENT OF COMMERCE  
The Under Secretary for Export Administration  
Washington, D.C. 20230

June 3, 1999

MEMORANDUM FOR JOHNNIE E. FRAZIER  
Acting Inspector General

FROM: William A. Reinsch

A handwritten signature in black ink, appearing to read "W. A. Reinsch".

SUBJECT: Draft Report: Improvements Are Needed to Meet the Export Licensing Requirements of the 21st Century (IPE-11488)

Thank you for the opportunity to review and comment on your Draft Report: Improvements Are Needed to Meet the Export Licensing Requirements of the 21st Century (IPE-11488). We are pleased that you found the export licensing process to be greatly improved since your last review in 1993. The Clinton Administration has worked hard to ensure that the export control system for dual-use items is one characterized by transparency, inclusion, predictability, and efficiency. We believe that we have achieved a system that provides for a balanced, multi-agency review process in which referral and escalation procedures work smoothly. It is rewarding to note that you have reached this same conclusion.

As with any complex, bureaucratic system, there is always room for improvement, and your report recommends a number of modifications. BXA is already pursuing many of your suggestions, including seeking new legislative authority and developing a modern computer system. For others, you have provided new recommendations that bear serious consideration, such as those for streamlining the procedures of the Operating Committee and those for improving our automated support system. For a few, the benefits of changing our current practice are not readily apparent or may be difficult to implement, such as those relating to "deemed exports," or providing for TECS screening of pending license applications. I am attaching a summary of our reactions to each of your recommendations at Tab A.

There are a few points raised in your report that I want to highlight specifically. First, a significant compliance initiative we have developed over the past several months, the License Enforcement Action Program (LEAP), addresses a number of your compliance-related recommendations. Since it was being developed at the same time as your office was undertaking its review, I understand that it was difficult for you to take it into account in your report. Because it does address a number of your concerns, I am attaching a summary of the program at Tab B, so that it can be included in your final report as part of our agency comments.

Second, we largely concur with your recommendations regarding ECASS, and they are compatible with our proposed ECASS replacement plan which is part of our FY 2000 budget request. We will look forward to working with your staff in FY 2000 as we begin to develop our



new interagency export control system. I have no doubt your support will be helpful in obtaining funds for this project from the Appropriations Committees.

Third, the question of cumulative effect analysis deserves further study. We believe that it properly belongs as part of our regular list review exercise rather than something that should be undertaken with respect to individual license application. Either way would require new resources for BXA, but the requirements would be far larger if we undertook such analysis as a part of each licenses application.

Fourth, we have some concern that your answers to Senator Thompson's questions do not precisely track the body of the report. Obviously, the report will be a more detailed and more nuanced document than answers to questions, but since the Senator is likely to use your answers as points of departure for his further work, it is particularly important that they accurately reflect the full substance of your report. We provide some specific suggestions for the answers at Tab C.

Fifth, I am concerned that virtually none of your recommendations, whether we agree with them or not, include any assessment of their budgetary impact. None are cost free, and many would require substantial increases in our budget. Without an appreciation of the cost of neither the Congress not the Department can endorse them. To be fully responsive to the Congress and to be a document with the most impact, we believe that this is a critical shortcoming that needs correction. We would be pleased to work with your staff in developing cost estimates.

Finally, your report notes that you found BXA's managers, licensing officers, and systems personnel to be cooperative. I am not surprised as our policy is one of full support to the activities of the I.G. Your report goes on to note the terrific strain that the agency has been under in the past year in trying to respond to the literally hundreds of requests for information that we have received from outside organizations. You correctly point out that BXA personnel felt under siege during this period. However, I am disappointed that you go on to state that BXA personnel "were somewhat defensive in responding to our request for information." I am sure that there were cases where you did not get information as quickly as you would have liked, but I can assure you that, even with all the conflicting claims for time and resources placed on the staff, nothing we did took a higher priority than being responsive to your analysts.

Again, thank you for the opportunity to review your draft. I hope that our comments will be useful as you prepare your final report.

Attachments

Tab A

BXA COMMENTS ON THE RECOMMENDATIONS OF THE DRAFT REPORT  
OF THE OFFICE OF THE INSPECTOR GENERAL:  
*IMPROVEMENTS ARE NEEDED TO MEET THE EXPORT LICENSING REQUIREMENTS  
OF THE 21ST CENTURY (IPE-11488)*

LEGISLATIVE AUTHORITY, EXECUTIVE ORDERS, AND REGULATIONS

1. Continue to work closely with the Congress and the Administration to renew legislative authority.

Agree. We are actively working with the Congress and have testified several times on the importance of renewing the Export Administration Act.

2. Work with Congress to revise the current NDAA requirement to conduct PSV for every computer in Tier III.

Agree. We concur that this requirement is a waste of enforcement resources and are seeking correction by the Congress that will permit us to focus checks on transfers of concern.

Conducting a post shipment verification for every computer with a composite theoretical performance exceeding 2,000 millions of theoretical operations per second (MTOPS) diverts enforcement resources from other activities that contribute more to our non-proliferation goals. In the first year of NDAA implementation, end users in the communications, utilities and financial industries received a majority of the high performance computers exported. A U.S. government employee has to visit all of these end users no matter how well known, and no matter how many times they have been visited in the past, to judge whether their computers are being used for weapons development. As a result, the burden of these visits becomes disproportionate to the benefits derived from them. When NDAA was passed, the PSV requirement affected some mainframes, high end workstations and powerful servers. As of May 1999, several manufacturers have introduced dual processor desktop workstations that exceed 2,000 MTOPS and top-of-the-line personal computers that exceed 1,200 MTOPS. At the rate computer performance is growing, export enforcement will soon be expected to verify the end use of personal computers that are sold by the millions.

3. Request the NSC to clarify the appropriate level of Representation at the ACEP.

We agree that our advisory agencies need to improve the level of representation at the ACEP and are working with them toward that end. We do not believe that this issue needs to be referred to the NSC. Additionally, we believe that the cited language that Energy relies upon to send less than assistant-secretary representation is taken out of context. The EO intended to provide for the absence of the correct person by making it clear that someone with the full



authority of the assistant secretary may attend and vote. This ability to send an “acting” official in the absence of the correct official is far different from routinely sending a “designee” when the right one is at work and in town. The report should address the validity of the BXA position on this point.

4. In conjunction with the NSC, seek a modification to ACEP procedures to deal with decisions that may result in a tie vote.

Agree. This review is already underway in the NSC.

5. Coordinate with the NSC in clarifying the goals of the deemed export licensing requirement and modify the policy and regulations accordingly.

While your draft report points out some of the ambiguity surrounding this provision and possible uneven compliance by U.S. companies and other federal agencies, it ignores the most serious aspect of the issue which is the current standard being employed for triggering “deemed export” license applications. The current standard requires an export license for hiring a foreign national when he or she will be exposed to technology in the United States that would require export authorization if it were to be transferred to his or her home country. U.S. industry has suggested an alternative that relies on the exporter's knowledge of a potential export, i.e., knowledge that the foreign national being hired will return to his or her home country. There are also concerns with Constitutional issues involved in the application of the current standard dealing with prior restraint of free speech. We believe that modifications to our present requirements should appropriately await the resolution of these issues.

6. Develop outreach programs on “deemed exports.”

We regularly include the “deemed export” provisions of the EAR in our seminar and outreach activities and will ensure that this subject is covered fully in our programs with the DOE labs. We are prepared to expand these efforts once the issues noted above are resolved.

#### COMMODITY CLASSIFICATIONS

7. Make the commodity classification process more timely and transparent by:

a. Ensuring that the front end review process is continued.

Agree. We have the front end review process in place to improve the timeliness and consistency of commodity classifications.

- b. Reemphasizing the importance of processing commodity classifications in a timely manner and hold licensing officers accountable.

Agree. Our goal is to complete all commodity classifications within the fourteen days stipulated in the EAA. This has been difficult in recent months due to the demands placed on the agency by external interests. We are hopeful that the requests for information from the Congress and other agencies and the public will return to traditional levels, allowing us to reallocate our resources to our normal functions.

- c. Program ECASS to allow commodity classifications to be put on "hold without action."

This is an interesting suggestion that we will review as we balance the interest in timely completion of commodity classifications with the need for accurate time accounting.

- d. Improve intra-BXA referral of commodity classifications between divisions.

Agree. As part of the front-end review, we have developed guidelines to ensure that commodities covered by more than one division are properly referred to all interested parties.

- e. Commodity classification referral criteria needs to be clarified.

Agree. We concur with your recommendation that the NSC 1996 memorandum should be revisited to clarify the guidance on the referral of commodity classifications and munitions licenses. While we are prepared to continue to refer commodity classifications requests to Defense and State "for items/technologies specifically designed, developed, configured, adapted and modified for a military application..." we disagree with some of your analysis.

- First it is important to note the fundamental difference between CCATS and license applications. The former are technical determinations that can and should be divorced from policy or politics. Basically, a CCATS determines what a product is and where it appears on the CCL. Whether or how an item appears on the CCL is an empirical judgment well within the expertise of a BXA licensing officer and should not be the subject of interagency negotiation. On the other hand, licensing determinations are policy decisions on whether a certain export should be approved or not. These are fittingly interagency decisions, as the perspectives of different agencies are important in these policy decisions.
- With respect to commodity classifications, the extensive review of these by DOD and BXA resulted in DOD acknowledging that it had no disagreement with the Commerce decisions in 98 of the 103 classifications reviewed. For the remaining five, BXA contends that only one case was improperly classified, though the net practical result

would have been to require a license application in any case. For the four with which DOD took issue, BXA continues to stand by its classifications. Regardless of whether one accepts BXA's or DOD's conclusions about the analysis, in either case the high level of accuracy argues strongly for leaving the system as it is. (We were surprised that in your review, the IG did not reach an independent assessment of the accuracy of BXA's referral, but, rather, simply reported the dissent by DOD.)

- Nevertheless, under the NSC guidance of 1996, we referred 27 cases to DTC. You report that DTC claims to have only received 21 cases. Under separate cover, we have provided your office with the complete list of all 27 classification requests provided to DTC, and we stand by that number.
- As you point out in your report, part of the 1996 NSC decision directed the State Department to refer to BXA any munitions license applications that might more properly be controlled under the CCL. To date we have received no such referrals. You point out the additional issue of the items controlled as dual-use commodities by our allies and the multilateral export control regimes being controlled as munitions in the United States. Certainly these are areas where greater transparency would serve both the public and our foreign policy interests well. As the Department of Defense becomes increasingly dependent on commercial-of-the-shelf procurement, the viability of the commercial sector (whose growth has been export driven) becomes a national security issue. Commerce's involvement in those dual-use licenses currently under State's jurisdiction is appropriate.
- Finally, you make mention of the investigative report on the crash of a Chinese rocket carrying a commercial communication satellite under Commerce's jurisdiction. You use this as an example of an incorrect commodity classification. Of course this was not a true commodity classification at all but part an export license which had been referred to the other agencies. The licensing officer's error was to inform the exporter that the information it wished to convey was covered by the license, when in fact it probably needed a separate authorization from State. The fact that the licensing officer used a CCAT form to convey this information does not change the fact that it related to an export license and was guidance on the scope of the specific validated license. We suggest you drop this example of a licensing effort from your discussion of commodity classifications.

#### GUIDANCE AND TRAINING FOR LICENSING OFFICERS

8. Provide a check list for licensing officers and require them to include the dates of the most recent approval or denials in the licensing history.

Pursue. We are willing to explore the implementation of these suggestions. As each case is unique, it is not clear that any specific check list or list of questions will fit every contingency.

Nevertheless, as part of our training of licensing officers on case analysis, we will pursue the development of such a list with them. Licensing officers are encouraged to provide full support of their licensing recommendations/decisions. In most cases, past licensing history will be relevant and should be included in the analysis. Recent guidance issued to the LOs on Case Analysis requires that past licensing history be considered.

9. Update policies and procedures regularly and fully implement the BXA electronic library.

Agree. As your report notes, we have recently augmented our policy and procedural guidance to the licensing officers and will continue to do so. The electronic library is nearing completion and will go far in improving the consistent and timely provision of guidance to licensing officers.

10. Develop and implement a training program for BXA licensing officers.

Agree. Though we disagree with your finding that BXA “has not emphasized the need to develop and maintain a corps of highly qualified LOs.....” we do recognize that the current diversion of resources to respond to the extraordinary requests for information placed on the agency has impacted our ability to conduct formal training programs. Accordingly, the Licensing Officer Task Force is organizing an extended formal training program for all licensing officers that will include briefings by other agencies, including the NPC. One such session was already conducted with other agency representatives last fall. Though mentioned in your report, we do not think your report makes clear that the primary method for training licensing officers (especially new ones) is On-The-Job in concert with a senior licensing officer. This is central to our commitment to “a corp of highly trained LOs.” We will continue this approach, as well.

In part, your analysts may have reached their conclusions about LO training as a result of comparing the training programs of EE and EA. EE, with two-thirds of its staff in the field, has standard job requirements among its special agents and intelligence analysts, which enables it to conduct extensive, formal, systematic, centralized training. EA, with its widely different areas of expertise and responsibilities, must tailor its training on a more individual basis. Nevertheless, more training is desirable, and we do not argue with the basic thrust of your recommendation. It is ironic that this recommendation comes at a time when budgetary constraints on the agency not only limit our ability to expand training but will force us to cancel certain planned activities.

#### LICENSING REFERRAL PROCESS

11. Instruct LOs to follow BXA's referral procedures, including amendments.

Agree that amendments to referred cases should be referred themselves. However, as mentioned above, we believe that the review conducted by your office demonstrated conclusively that BXA refers cases with an exceptionally high degree of accuracy. And shows that in every case BXA made the correct decision with respect to agency referrals and nonreferrals. While you

have contended that we did not refer three India cases to DOD that we should have, our review shows that these were items destined for end users on the Entities List and that we appropriately denied them without referral. We had informed DOD of our intention to deny such cases. While we never received a response to our letter, we contend that we acted appropriately and have not received any objection to our proposal from DOD. Though many amendments are inconsequential and do not affect the what is to be exported or to whom, we will consider issuing new guidance requiring that they be routinely referred regardless of the insignificant nature of the amendment.

12. Strengthen the role of the Intelligence Community to include: a) referring all cases, b) assessing the risk of end users, c) obtaining more detailed information, and d) providing more review time.

We can agree with all of your suggestions in items (a)-(d), with the possible exception of providing for additional review time. However, we note that all of your recommendations are resource intensive, and we defer to the intelligence community on the costs and feasibility of implementing your suggestions. With respect to additional time, this too is really a resource issue, as increased resources at the NPC would permit a more timely review of license applications. Obviously, additional time for review must be reconciled with the competitive realities that U.S. exporters face and their need for prompt decisions from the government.

“e) Track and assess the cumulative effect of dual-use exports.”

We concur that this is desirable; though, difficult. We believe that the assessment of cumulative effect should be made in the list review process, not on each individual license application. Cumulative effects result not only from the transfer of items under approved licenses but also occur as the result of the provision of items not requiring a license. Perhaps most importantly, cumulative effects also occur as the result of shipments from foreign suppliers that would not be caught by our licensing system. Nevertheless, we agree with your position and have included as part of our 2001 budget request the resources that we would need to conduct such assessments.

13. Require LOs to document why an NPC referral is necessary when it is outside the MOU.

Of course, if we adopted your recommendation to refer all applications to the CIA, this suggestion would become moot. We encourage LOs to refer cases to the NPC whenever they have doubts about the parties to the transaction. Current guidance, which we will reiterate, calls for documenting the reasons why such referrals are made when the established guidance would normally preclude referral.

14. Review State's “pullback” profile.

Agree. However, as State has requested to review certain cases under the E.O., it is incumbent on that agency to determine how to meet its own responsibilities. Obviously the solution lies in a

combination of giving licensing review greater priority and more resources, improving internal efficiency, and/or cutting back on its work load through greater delegation back to Commerce.

15. Update the 1993 MOU between BXA and Customs to provide for TECS screening of pending license applications.

Disagree. Since the IG's last recommendation to BXA on this issue, Customs has provided BXA with data to add to its watch list, and OEA has provided that data (on disk) to the Office of Administration to load into Enforce for daily screening. As of April 1999, Administration has had this data and is working to ensure that all of this data is uploaded properly into Enforce to perform exactly the screening function that the IG has recommended. Therefore, we do not believe the alternative solution recommended by the IG is necessary.

16. Notify Referral Agencies when pre-licensing checks (which were licensing conditions) are canceled.

Agree.

#### DISPUTE RESOLUTION PROCESS

17. Ensure the independent licensing decision-making authority of the OC Chair.

We do not read your report as finding significant problems with management influence over the vote of the OC Chair. Thus, we are a bit surprised that it results in so much discussion in your report. The Chair of the OC is a Commerce employee and as the E.O. itself indicates is not intended to be entirely impartial. (See Section 5(b) of the E.O. which states, "If any department or agency disagrees with a licensing determination of the *Department of Commerce made through the OC*, it may appeal the matter to the ACEP for resolution." (Emphasis added.)

Of course, the OC Chair reports to the DAS and AS of EA, and both have a responsibility to ensure that the OC Chair carries out her responsibilities efficiently and in concert with U.S. law. In this regard, both have from-time-to-time instructed the OC Chair to bring a case review to closure by making a decision (e.g., where the loss of a sale is imminent or a case has exceeded the time frames of the E.O.) In addition, both have instructed the OC Chair on the provisions of the regulations or on changes in U.S. licensing policy to ensure that her actions are consistent with USG rules and policies. We saw nothing in your report that would recommend or lead to a change in this oversight.

Both the DAS and AS have encouraged the OC Chair to make decisions consistent with the EAR and U.S. licensing policy, even if that means voting against the position of the BXA representative or the majority of agencies in attendance. Your own analysis appears to support this contention. You may wish to revisit this section.

18. Work with advisory agencies who have delegated decisions to BXA to deal with their representation at the OC so that cases are not unnecessarily delayed.

Agree.

19. Let the OC become, a "one-stop shop" for licensing decisions brought before that body.

This is a complex issue that is currently under review by the Licensing Officer Task Force. BXA needs to carefully balance the desire for efficient processing with quality and vulnerability controls. By foregoing review and countersigning by the technical licensing offices, BXA may compromise its ability to ensure the accuracy and consistency of licensing decisions and their regulatory sufficiency. In addition, by foregoing meaningful countersigning, BXA exposes itself to possible improper licensing actions. However, we continue to review this matter toward overall improvement of our processes.

#### EXPORTER APPEALS PROCESS

20. Include Referral Agencies in the Appeal Process

We do not in principle object to your major recommendation that the other agencies be brought into the appeals process in a more formal way, and we are prepared to work with the NSC on this matter.

The concern you expressed about deciding cases informally in lieu of action by the Under Secretary is not well taken. In the single case that you cited, the exporter was clearly told that if action by the OC did not produce a favorable result, the Under Secretary would address the issue, favorably or unfavorably, in the appeals process. Additionally, the appeal was not closed until after the interagency decision to grant the license was completed. The Under Secretary was prepared to address this appeal at his level, but that became unnecessary as the case was settled without his action. The exporter did not lose his appeal right. To follow your recommendation in situations like this one would only delay a case's resolution and prolong the exporters uncertainty.

#### MONITORING OF LICENSE CONDITIONS

21. Improve BXA's monitoring of license conditions.

Agree. BXA has recently implemented a new Licensing and Enforcement Action Program designed to deal with the vast majority of the problems with assigning conditions and their follow-up. We are proposing additional resources to fully implement the program. In the meantime, we will take steps to improve our implementation of conditions, including their monitoring, consistent with budgetary realities.

With respect to the recommendation to perform timely follow-up work on licenses with condition "14." We disagree with the recommendation to incorporate this responsibility as a specific function of a supervisory export compliance specialist's performance plan. OEA has specific written instructions in place for the individual to perform this function. BXA believes the written instructions are sufficient without making them part of the performance plan.

#### END USE CHECKS

#### 22. Improve timeliness and quality of EUCs performed by US&FCS

- a. Work with the Assistant Secretary and Director General for US&FCS to improve the timeliness of pre-licensed checks conducted by US&FCS posts.

Agree. We will continue to work with the US&FCS on this issue as we have in the past. BXA implemented the 1997 IG recommendation to include an information copy of every outgoing PLC request cable and follow-up cable to ensure FCS management was aware of delays on the completion of PLCs at overseas posts. In addition, BXA always highlights the importance of timeliness on PLCs in briefings to all overseas post personnel prior to their placement overseas. Also, this point is specifically highlighted in BXA's PLC-PSV guide sent to all posts.

- b. Provide clearer and concise guidance to the US&FCS and its overseas posts regarding the use of foreign service nationals and personal service contractors to conduct end use checks. Revise the PLC/PSV Handbook accordingly and make sure that it is sent to all US&FCS posts.

Agree. We will redraft the PLC/PSV Handbook to eliminate the perceived ambiguities. We will make clear when use of an unaccompanied non-USG employee, non-U.S. Citizen is merely undesirable and when it is unacceptable. We will reiterate our clear policy preference for having a U.S. citizen/U.S. government employee present at all checks.

- c. Communicate more with US&FCS posts about the importance of (1) identifying who conducted an end use check in their reporting cables (see page 96); (2) conducting onsite visits for each end use check (see page 97); and (3) retaining proper end use check records for five years, the statute of limitations for Office of Export Enforcement investigations.

Agree. After US&FCS clearance, we will send a cable to all US&FCS Posts reminding them of these points. In addition, we will reiterate these points when meeting with FCS personnel prior to their departure for a new post or when visiting BXA while on home leave.



- d. In the PLC/PSV Handbook, specifically list embassy sections by name that US&FCS should confer with on end use checks and include suggested questions for each sections.

Disagree. We will continue to recommend that FCS check with all appropriate sections at post. However, US&FCS personnel stationed at a post are in a better position than BXA personnel in Washington to be aware of which sections of a particular post are likely to have useful information about an end user in that country.

- e. Provide periodic regional training seminars and workshops to keep US&FCS staff abreast of current developments in export controls and BXA regulatory procedures. Also consider using the Safeguard Verification program as a mechanism to train US&FCS staff.

Agree. One issue that will have to be decided is how this proposal will be funded. While periodic training is always an excellent idea, neither Export Enforcement nor BXA as a whole are currently in a position to fund the travel of FCS officers to the proposed seminars. In the meantime, EE Safeguards teams will provide training at posts they visit to the extent possible.

23. Develop guidance for EE agents for Safeguard Verifications

- a. Criteria to help guide agents in selecting which PLC/PSVs to do, targeting countries and shipments and greatest concern.

Agree.

- b. A template or standard format for agents to follow when preparing Safeguard trip reports.

Agree.

- c. A requirement that the Safeguard verification teams meet with host government officials involved in local export control or enforcement areas as well as U.S. embassy personnel who might be knowledgeable of proliferation threats or diversion activities associated with the specific country, to determine what export control programs the country has, how effective they are, and the country's relationship with countries of concern.

We disagree that this should be a requirement but agree that it is valuable where feasible. The feasibility of meeting varies from country to country and will depend on the interests of the host government and U.S. Embassy or Consulate officials.

- d. A suggestion that photographs be taken of the sites and commodities inspected, when appropriate, during the course of their verifications to be included in their reports.

Agree. While we do not believe that this should be a requirement, we agree that it is valuable where appropriate.

- e. Procedures for the prompt reporting of unfavorable Safeguard results (see page 101).

Agree.

24. Distribute list of safeguard trip reports to NPC and US&FCS

Ensure that the CIA's Nonproliferation Center and the appropriate US&FCS posts are on BXA's distribution list for all Safeguard trip reports. These reports should be forwarded to the CIA's Nonproliferation Center in an electronic format (see page 102).

Agree. The Office of Export Enforcement is currently working with the Office of Executive Support to make the Safeguard trip reports available to the Nonproliferation Center in an electronic format. Our ability to distribute these reports to the posts, however, is contingent upon the US&FCS agreeing to appropriate procedures to prevent their improper dissemination.

OTHER OIG CONCERNS

25. Notify referral agencies of all negative PLCs

We agree with the thrust of your recommendation and will inform our advisory agencies when we get a negative result to a PLC on a case that had been referred to them, understanding that this additional information may affect their position on the application.

Your report also discusses 2,130 RWAs in FY 1998, in which you found only three instances when a case was RWA'd when a negative PLC existed. Each of these is an exceptional case and appears to have been appropriately RWA'd. An RWA is not permission to export for items requiring a license.

In the first case, due to the delay in completing the PLC and the age of the case (six months), the LO recommended that the case be RWA'd when the PLC determined that the ultimate country of destination appeared to be different than that specified on the license. EE concurred.

In the second case, the transaction involved EE and Customs concerns about a U.S. representative of the foreign party involved in the transaction. The case was closed with no derogatory information about the consignee. However, by the time the investigation was completed, the order had been lost and the applicant asked for the case to be RWA'd. Again, EE concurred.

In the third case, the PLC determined that the goods had already been shipped. Consistent with BXA policy not to take a licensing action on a shipment that has already been made, the application was RWA'd and the matter turned over to EE for investigation of a violation of the EAR.

26. Ensure the timely completion of license determinations

a. Institute a front-end review

Agree. Done.

b. Process in a timely manner

Agree. Your report points out that LDs take an average of 36 days for EE and 24 for Customs. (It is interesting to note that CCATS take a comparable length of time (37 days), which is not surprising as they involve similar kinds of analysis.) The reasons for delay are also similar as those for CCATS--lack of necessary technical information which EE agents must obtain from the manufacturer, the press of other activities (FOIAs, Congressional requests, licenses, etc.), and inadequate resources. Nevertheless, EA is committed to improving its responsiveness (both for CCATS and LDs). As you noted yourself in your report, many of the process modifications described above for CCATS will also benefit the timely processing of LDs.

c. Program ECASS to allow LDs to be put on HWA

As with CCATS, we will investigate the costs and benefits of this recommendation further. Putting cases on HWA does permit the time tracking system to reflect when the work on Lds has stopped due to the need to get additional information from the exporter or special agent, but it can also affect the time disciplines imposed on the agency.

d. Issue written procedure for assigning LDs to be reviewed by multiple divisions.

Reviewing. The assignment of LDs is currently being managed by the new front-end process. Based on the experience gained from this effort, we will develop written instructions as appropriate.

- e. Implement draft guidance.

Agree. Done.

- f. Develop written agreements between EA and EE and Customs

Agree. Done with EE. Will undertake with Customs.

- h. [sic--should be "g"] Automate referral of LDs between Customs and EA

Agree. We started this two years ago but had to curtail due to budgetary constraints. Budget permitting, we will recommence this effort.

#### ECASS

28. Work with the Department, OMB, and Congress to obtain a commitment to fully fund the chosen option to replace ECASS (see page 122). As part of its new system development effort, BXA needs to:

- a. Establish a project management "team," including a full-time project director, as soon as possible to oversee development and implementation of BXA's new information database system.

Agree. We have formed an interim team with a project manager. In the absence of funding, the team is limiting activities to developing a project plan and risk mitigation strategies. If and when ECASS funding becomes available, a full time project manager and team staff will be hired.

29. Prepare a cost benefit analysis for developing a classified database system with software upgrades that could be made to allow better interface capabilities with the referral agencies' licensing systems at a later date.

We have already conducted a cost benefit analysis as part of our work with Booz Allen and Hamilton. While we do not believe that a further, formal analysis is necessary, system security is of the utmost importance to us and will be a major component of the new system architecture. With the advancements that have been made in commercially available encryption in the past couple of years, we should be able to encrypt our system at reasonable cost in a fashion that will enable us to deal with sensitive materials in our redesigned system, and we will be exploring this option fully. Our plan for hiring a full-time project team, if we receive full funding for ECASS, includes a position for a security expert for this system. This person will assist us in working through the myriad of security issues that we must consider, including the cost-benefit analysis.

- c. Coordinate BXA's system development efforts with the other export licensing agencies. Encourage these agencies to establish an interagency steering committee to review the automation portion of the export licensing process from coordinating common system architecture requirements to determine how interagency resources can be used to fund and implement a new system.

Agree. Our ITSC has already recognized the importance of this and has had initial discussions with our counterparts. We will continue this process to ensure the full interoperability and compatibility of our systems.

- d. Evaluate the most viable options for the location of BXA's computer operations. Specifically, BXA should look at the possibility of continuing at its current facility, or service by another Commerce center, another federal center, outsourcing, as well as creation of an in-house BXA center. No matter which option BXA selects, it must obtain departmental approval to leave the Springfield Computer Center and move to the selected option.

Agree. BXA is choosing Oracle as the new database management system and, in so doing, we gain the flexibility to run anywhere and on any hardware platform. We will evaluate the most viable option regarding the location of the computer operation and gain Departmental approval for the selected option.

30. Take the following actions necessary to implement or strengthen the internal controls for ECASS, including:

- a. Provide a duplicate read-only tape to the Undersecretary for Export Administration every 90 days, highlighting any changes that might be made by lower ranking BXA personnel.

Agree.

- b. Maintain paper license applications for at least 90 days.

Agree. This is current practice.

- c. Establish criteria for reopening closed cases in the system.

Agree. We will establish written criteria in this area.

- d. Ensure that the electronic audit trail is more complete.

Agree. If funding is approved for the new system then this improvement will be a requirement of the new system. If funding is not received we will incorporate it into ECASS. Incorporating this feature into the present ECASS will require a major modification and considerable resources. For this reason we are delaying action until we know status of funding for a new system.

- e. Have the database administrator assign data element responsibilities to individuals throughout the organization.

Data accuracy is certainly a priority and concern for BXA. However, it may not be practical to assign ownership of every field to an individual. For example, the field containing the final recommendation can be assigned to EA but it cannot be assigned to just one person unless that person is the Assistant Secretary or Deputy Assistant Secretary for EA. We primarily assign ownership of data elements to organizations or subunits.

- f. Designate an official database review board.

We are unclear how this would work or what problem it is designed to rectify. We are not sure what this board would do in addition to those functions assigned to the BXA Chief Information Officer.

- g. Establish a standards development group to develop appropriate database standards including data definition, data documentation, passwords, and writing and testing programs.

Agree. This will be part of the system design effort, if funded, and will be headed by BXA's OIC.

- h. Designate a team to periodically review the internal controls and risks associated with BXA's system, about once a year or when conditions materially change.

Agree.

- i. Require the database administrator to reorganize the database every year.

Agree.

- j. Consider the feasibility of one data entry clerk's work being reviewed by another before it goes into the database, or contract this function out.

While we are willing to consider this, we are hopeful that data entry automation innovations, such as SNAP, will preclude the necessity of implementing this procedure. We will monitor this closely.

- k. Reestablish the old "User Meetings" between the operations staff, licensing officers, and information technology staff to discuss issues and identify and resolve problems quickly.

Agree.

- l. Take steps to reduce the number of duplicate codes in the database including an extensive archiving effort to retire a large number of duplicate identification numbers.

Agree. This will be part of our next archiving process. If the new system is funded, exhaustive efforts will be made to preclude duplicates from migrating to the new system.

- m. Determine why some cases were issued without codes or Exporter Commodity Classification Numbers and make sure that all cases have such numbers in the future.

We have researched this issue and found that it occurred in only a minimal amount of cases and has not occurred at all since 1996. We have tried, without success, to determine how these cases were issues without codes or ECCNs. We are not hopeful that more attempts will meet with success. However, we have taken steps to give us a quick alert if it ever does.

- n. Update the current continuity of operations plan to include all appropriate manual and system contingency processes as soon as possible.

Agree. We are currently working on the update of the COOP.

- o. Establish a risk management team to identify and assess the severity of risk in BXA's database environment, or have a contractor perform the risk analysis.

Agree. A vulnerability assessment team will be formed and this team will perform this assessment in FY 2000.

- p. Send a "network message" to emphasize that all database problems should be reported via the hotline.

Agree. Done.

q. Prepare a BXA system security plan.

Agree.

r. Perform periodic security reviews.

Agree.

s. Officially assign the security duties of BXA's computer system to BXA's security officer.

Agree. Done.

t. Provide all ECASS users with current security training.

Agree.

u. Develop a communication link to immediately notify the Springfield Computer Center of terminated or transferring employees so that system access can be promptly revoked or modified, by the end of each working day.

Agree. We will continue to communicate with Springfield in writing, by phone and email to provide this information.

v. Restrict the number of BXA employees with file manager access.

Agree. File manager access will be restricted to only the database administrator and a backup administrator as recommended.

#### ADDITIONAL COMMENTS

##### Page #

6 In the Background section (page 6), you refer to the establishment of BXA in 1987, caused in part because of the concern that the export control function should not be part of the export promotion agency--ITA. You go on to say, "Despite the separation, there is still much debate about whether the Commerce Department and BXA maintain the appropriate balance between promoting U.S. trade and exports and controlling the export of goods and technology that could be detrimental to our national security interests." While we concede that periodically this issue is raised by those unhappy with U.S. export control policy, in fact there has been little debate about this issue since 1987. As you provide no data to support your contention and do nothing



more with it in your report (i.e., provide any analysis or recommendations), we suggest you delete this reference from your report.

- 29 Para 2. The argument here misses the forest for the trees. Rather, than highlighting a problem with the inefficiency of end use checks, the real point here relates to the futility of certain export controls in the area of networked computers.
- 32 Para 1. The IG should make clear that this is not an inadequacy of the export control system. Academic freedom, protected by the First Amendment, is beyond the scope of export controls.
- 32 Para 4. That DOE considers the deemed export rules difficult to interpret is not surprising or relevant. The IG should not give credence to DOE's contention that federal funding equals "publicly available" treatment under the EAR.
- 34 Para 1. First sentence. Your report should note industry's responsibilities for classifying their own products and, thus, for determining their responsibilities under the EAR. This is not solely a BXA role.
- 36 First full para., beginning "Second..." Penultimate sentence says that the IG has been told misunderstandings have occurred resulting in processing delays. Did you identify any? It is inappropriate to make allegations like this without disposing of them by determining whether or not there was any evidence for them.
- 39 2nd para. last line. somehow "disagreements" have become BXA "mistakes". This is unfair. If we made a mistake, the IG should say so and say why. Otherwise, it should continue to be a disagreement.
- 44 Second full para. Reference to our March 31 updated guidance should be made earlier. Otherwise, the reader will assume we have done nothing for several pages until he gets to this point.
- 46 Para 1. To state that we have a new LO with *no training* is misleading. On-the-job training conducted by working under the guidance of an experienced LO is relevant and should be considered as training. The comment, as is, implies that someone fresh off the street is making uninformed decisions. This is not true
- 55 Second para. under B. should make clear that this is at the insistence of the NPC not BXA. BXA is more than willing to send them more requests. This is implied later on but should be explicit here.

- 57 Para 2. NPC statement that BXA does not understand “intelligence” information should be removed. This most likely represents the opinion of a particular CIA employee and does not represent the position of the agency. It is self-serving for the IG to include this. It is also inconsistent with what the CIA considers its primary objective (as stated on p 55, para 1, last sentence).
- 61 Second para. from bottom. As a presentational matter it would be more balanced if the IG would state the reasons for BXA's objection to this recommendation up front rather than solely in the context of refuting them in later pages.
- 62 First paragraph under “Customs involvement....” Last sentence says, “... we learned during our current review that this has not happened.” Why not? Your report should discuss what you found out about why Customs hasn't delivered on its promises.
- 71 Para 3. Last sentence. “...voting at the meeting” implies agencies abstain at the ACEP. In fact, they do not.
- 83 1st para. A. (1) The Office of Exporter Services does not place a low priority on maintenance of the follow-up subsystem; however, full support is resource dependent.
- 84 1st para. The IG reported that the employee told them that she had not received any written procedures or guidelines for maintaining the subsystem. The employee either misspoke or was incorrectly quoted. When the employee assumed the follow-up functions, the employee received written and verbal instructions and formal training from the employee who developed the subsystem.
- 104 first paragraph. BXA's policy is pursuant to law--Hong Kong Policy Act of 1992 and not just a matter of Presidential discretion. This should be pointed out.
- 130 Top of Page. Data base reorganization. This is one of several places where the IG recommends a lot of work without providing any evidence that there is a problem and without estimating the cost that goes along with implementing the recommended reorganization.
- 130 Last para. Here, as in other places in the report, the IG states as facts the opinions of certain staff members without doing any independent verification. There have been periodic delays in entering applications into the data base, due primarily to the diversion of employees to respond to Congressional inquiries, GAO investigations, FOIA requests, and the IG study itself. Undoubtedly, there have been other factors at work, as well, but simply repeating employee gossip without independent verification does not contribute to meaningful solutions.

- 134 First full para. This has been taken care of in the new Continuity of Operations Plan. The IG should examine it.
- 137-8 BXA has no comment to make on the Springfield operations. However, the IG should properly check with the Office of the Secretary on these observations.
- 150 First line. This is not technically correct. The EAA was last reenacted 11 years ago, but it last expired in August 1994, 5 years ago.

Tab B

## LICENSE AND ENFORCEMENT ACTION PROGRAM (LEAP)

### A. CLARIFYING EXPORTER AND END-USER RESPONSIBILITY

#### **Standardize license conditions**

BXA will review its standard license conditions, revise as appropriate, and communicate them to the other licensing agencies. The Office of Chief Counsel will review standard conditions to assess enforceability.

#### **Organize and clarify license conditions**

BXA will organize license conditions according to who is bound by them. Certain conditions may apply to the exporter, while other conditions may apply only to the consignee, and still other conditions to the end-user. BXA will specify explicitly in the license to whom conditions apply.

#### **Require exporter to notify consignee(s) of all license conditions**

Exporters are currently required to convey licensing conditions to their customers by regulation and direction. BXA will place a rider on each export license stating that the exporter is required to convey to consignee(s), and end-users, freight forwarders and banks as appropriate, all conditions that affect them. BXA will also revise its regulations as necessary to ensure that they make this exporter obligation clear.

#### **Require end-user and intermediary acknowledgment of license conditions**

BXA will amend the regulations to require that all such parties to the transaction acknowledge in writing to the exporter the receipt of the conditions conveyed by the exporter. Exporters will be required to retain such acknowledgments consistent with their other record keeping obligations and to report to BXA if they fail to receive them. This will require OMB approval since it will increase the paperwork burden on the exporter.

#### **Contact exporters after license approval but before shipment to confirm that they understand the conditions and have not shipped prior to receipt of a license**

For sensitive exports identified by licensing or enforcement officers or other agencies, Export Administration (EA) will contact the exporter after the issuance of the license but prior to actual shipment to stress the importance of adhering to all licensing conditions and being vigilant during the course of the export to ensure that the equipment or technology goes to the proper end-user, and that it is appropriately used. This contact may be in writing, by telephone or in person.

**Contact companies failing to file required reports**

BXA uses a computer tickler system to identify conditions that require follow-up reporting. Delinquent companies will be contacted by phone and in writing within 30 days after a report's due date to remind them of their obligations. BXA will document all attempts to obtain required information. Failure to respond to BXA's written request will generally result in suspension of the license and referral to Export Enforcement (EE) for enforcement action.

**Include US government access to end-user and intermediary facilities as a license condition**

For defined transactions of concern, BXA will include a license condition requiring access to the end-users' and intermediaries' facilities by U.S. government officials to ensure that the conditions imposed are being implemented.

**B. RECORDKEEPING TO SUPPORT LICENSING AND ENFORCEMENT**

**Maintain a comprehensive and readily accessible system of records pertaining to its licensing and enforcement activities**

BXA will fund, staff, and routinely audit its recordkeeping system to ensure strict compliance with its policy and all applicable statutes.

Specifically, BXA will ensure that it keeps records pertaining to commodity classifications, license determinations, license conditions, communications with license applicants and other parties, and investigations.

**Ensure all license conditions are properly documented**

BXA will redesign its computer data system (ECASS) to ensure that conditions can be entered more easily and comprehensively.

**C. EXPANDED ENFORCEMENT ACTIVITIES**

**Notify enforcement agencies of all approved, denied, and RWA'd cases**

BXA will continue its system of keeping enforcement agencies notified of licensing actions. BXA's EE has on-line access to all pending, approved, denied, and returned without action (RWA) licenses. U.S. Customs receives a daily data transfer of all completed licensing actions. EE maintains the ECASS screening and flag system to ensure that all cases are reviewed in concert with existing enforcement concerns and cannot be approved without EE's concurrence.

**Expand Pre-License Check (PLC) and Post-Shipment Visit (PSV) Focus on License Conditions**

EE, with input from EA, will identify more appropriate candidates for PLCs and PSVs that focus on license conditions. Enforcement's Office of Enforcement Analysis will set PLC and PSV priorities and manage the process with our embassies consistent with its Performance Plan.

EA and EE will identify more candidates for PSVs and identify product categories and end-users warranting more frequent visits. Enforcement's Office of Enforcement Analysis will initiate the visit requests, and the Office of Export Enforcement will conduct more PSVs through the Foreign Commercial Service's officers or its own agents' Safeguards Verification Trips and manage the PSVs consistent with its Performance Plan.

**D. REVIEWS AND SPOT CHECKS**

**Select one license exception category each year for comprehensive review**

BXA will conduct an annual analysis of one commonly used license exception (LE) to determine its ease of use, adherence to conditions, affect on legitimate trade, potential opportunities for abuse, and recommend corrective action and modification of LE terms, as needed. While there are thirteen different LEs, BXA will focus on the six that are based on destination or value (CTP-Computers, GBS-Group B Shipments, CIV -Civil End-users, TMP-Temporary Exports, LVS-Limited Values Shipments, and KMI-Key Management Infrastructure).

**Conduct reviews of all Special Comprehensive License (SCL) holders**

BXA will conduct thorough systems reviews of all SCL holders at least once every two years. BXA also will conduct reviews on all SCL consignees at least once during the validity period of the license. EA will make the results of systems reviews available to EE upon request. Any evidence of violations of the Export Administration Regulations (EAR) will be referred immediately to EE.

**Enhance spot-checks of use of license exceptions**

BXA will intensify its identification of exporters of sensitive items to countries of concern and identify those exporters' use of license exceptions. It will contact exporters and review documents justifying the application of the license exception or visit the company to verify the correct use of license exceptions.

**Conduct periodic reviews of select companies' internal compliance plans/export management systems, including procedures for ensuring license condition compliance**

BXA will identify companies that sell large volumes of controlled products to destinations of concern and conduct reviews of their internal control and export management procedures, prepare a report of findings and make appropriate recommendations.

If evidence of violations of the EAR is discovered during the course of the review, it will be forwarded to EE for action.

**E. INFORMATION SHARING WITH THE INTELLIGENCE COMMUNITY**

**Obtain broader information sharing with the intelligence community**

BXA will work with the intelligence community for better information exchange, especially on potential parties of concern.

**F. EXPANDED OUTREACH EFFORTS**

**Enhance visits to exporters that focus on compliance with license conditions**

EE will enhance outreach visits to selected exporters in high concern categories. These visits, generally conducted in person, will focus on how the exporter has complied with license conditions.

**Educate exporters on license conditions**

BXA will emphasize the importance of complying with license conditions in seminars and other outreach activities.

**Develop a special training initiative for freight forwarders, trading companies, and distributors**

BXA will establish specialized training opportunities for freight forwarders, trading companies, and distributors.

**Revise the EAR and work with Census to revise the Foreign Trade Statistics Regulations (FSTR), in order to clarify the responsibilities of seller, buyer, and freight forwarder**



**G. MULTILATERAL COOPERATION**

**Work with other agencies to seek support from international partners in developing common practices with respect to:**

- Imposition of conditions
- Control of reexports/retransfers
- Sharing of information, especially with respect to denials
- Obtaining end-use assurances
- Enforcement cooperation
- Sharing of investigative information
- Sharing of intelligence information
- Export Management Systems/Internal Control Programs

**Seek to develop a shared vision with our major partners of security concerns for the next century and common approaches to combating proliferation through enhanced export controls**

A major part of this effort will be the development of case studies and presentations for our closest trading partners on our export licensing and enforcement concerns in order to enlist their cooperation in implementing similar policies and practices.

Tab C

BXA'S COMMENTS'  
ON  
THE INSPECTOR GENERAL'S PROPOSED ANSWERS  
TO  
SENATOR THOMPSON'S QUESTIONS ON THE EXPORT LICENSING PROCESS

1. Please examine whether the current, relevant legislative authority contains inconsistencies or ambiguities regarding the licensing of dual-use and munitions commodities, and the effect of any such inconsistencies and ambiguities.

Agree.

2. Please examine whether Executive Order 12981 (1995) as implemented is consistent with the objectives of the Export Administration Act and other relevant legislative authority.

As mentioned in our comments on your report, we do not concur with your reading of E.O. 12981 regarding attendance at ACEP meetings. We do not believe the E.O. gives other agencies "the flexibility to decide who should attend these meetings." Rather, the E.O. states that "Representatives of the departments or agencies shall be the appropriate Assistant Secretary or equivalent (or appropriate acting Assistant Secretary or equivalent in lieu of the Assistant Secretary or equivalent) of the concerned department or agency, or appropriate Deputy Assistant Secretary or equivalent (or the appropriate acting Deputy Assistant Secretary or equivalent in lieu of the Deputy Assistant Secretary or equivalent) of the concerned agency." In other words, representation is to be by an Assistant Secretary, Deputy Assistant Secretary, or someone officially acting for them.

As we mentioned in the comments on the I.G. report (Recommendation 20), the Export Administration Act itself provides for the right of appeal to the Department by exporters. It does not include a provision for referring this decision to (or even consultation with) other agencies.

Nevertheless, as a practical matter, the Under Secretary has routinely consulted with his colleagues in other agencies before taking any action on an appeal. Consistent with your recommendation in your report, we are prepared to work with the NSC in bringing the other agencies into this process in a more formal manner.

While your proposed answer raises a theoretical possibility that an exporter might attempt to use the appeals process to somehow circumvent the interagency licensing process, nothing in your analysis indicates that this has been done or that any of the decisions taken by the Under Secretary have been inconsistent with the goals and objectives of the EAA. Your report provides no evidence that there is a problem here needing fixing. Accordingly, we would recommend that your answer be revised to stress the lack of any indication of problems in this area.

3. Please determine if there is a continued lack of interagency accord, as stated in your 1993 interagency report, regarding whether the Commerce Department is properly referring export license applications (including supporting documentation) out for review by the other agencies.

We have significant problems with your proposed response to this question, as we did for your analysis in the body of your report.

- In the initial paragraph of your response, where you state that 85 percent of applications are referred, it would be useful to mention here (as you do in the next paragraph) that the other agencies have a right to see 100 percent but have decided, through delegations, to forego that right in 15 percent of the cases due to the low level of the technology or the country of destination.
- The laborious review conducted by the Inspector General on the referral/nonreferral of applications, which took a great deal BXA resources, demonstrated conclusively that BXA operates with an exceptionally high degree of accuracy. For example the review of the nonreferral of applications resulted in a finding that in every case BXA made the correct decision. Though your report identifies six instances where other agencies (primarily DOD) felt that the licenses should have been referred, referral policy at the time did not require such referral. (We continue to contend that cases for end users on the Indian Entities list which we denied did not require referral to DOD based on our letter informing them of our intentions to deny these types of cases and to which they offered no objection.) With respect to amendments, we will issue new guidance requiring that they be referred to the agencies to whom the original case was referred.
- With respect to commodity classifications themselves, the extensive review of these by DOD and BXA resulted in even DOD admitting that they had no disagreement with the Commerce decisions in 98 of the 103 classifications reviewed. For the remaining five, BXA contends that only one case was improperly classified, though the net practical result would have been to require a license application in any case. For the four with which DOD took issue, BXA continues to stand by its classifications. Regardless of whether one accepts BXA's or DOD's conclusions about the analysis, in either case the high level of accuracy argues strongly for leaving the system as it is. (We were surprised that in your review the IG did not reach an independent assessment of the accuracy of BXA's referral, but, rather, simply reported the dissension by DOD.)
- We agree with your recommendation to have the NSC clarify its 1996 guidance on the referral of certain munitions-related commodity classifications to DOD and State and for State to refer to BXA certain dual-use munitions license applications.
- Finally, here as you did in your report, you make mention of the investigative report on the crash of a Chinese rocket carrying a commercial communication satellite under Commerce's

jurisdiction. You use this as an example of an incorrect commodity classification. As we stated in our comment on your report, we do not consider this to be a commodity classification at all but part of an export license which had been referred to the other agencies. The licensing officer's error was to inform the exporter that the information it wished to convey was covered by the license, when in fact it probably needed a separate authorization from State. While the licensing officer used a CCATS form to convey his guidance to the exporter, that doesn't change the fact that this was advice concurrent with the review of an export license. We suggest you drop this example of a licensing error from your discussion of commodity classification.

4. Please determine if the interagency dispute resolution (or "escalation") process for appealing disputed license applications allows officials from dissenting agencies a meaningful opportunity to seek review of such applications, and assess why this process is seldom used.

Agree.

5. Please review whether the current dual-use licensing process adequately takes into account the cumulative effect of technology transfer resulting from the export of munitions and dual-use items, and the decontrol of munitions commodities.

As you state in your response, assessing the cumulative effect of transfers would be desirable. However, though your response admits it would be difficult, you go no further in assessing what would be a major budget increase to develop this capability. As you point out in your response, cumulative effects also occur as the result of the contributions from indigenous capabilities and shipments from foreign suppliers that would not be caught by our licensing system. In addition, cumulative effects can result from the transfer of items not requiring a license. This suggests to us that the appropriate place to conduct such analyses is during our regular list review process rather than in the context of individual license applications. That would permit a more comprehensive approach, the information from which could then be used in reviewing individual licenses. That approach too, however, also requires significant additional resources, a need we believe you should stress in your report.

6. Please review whether the current munitions licensing process adequately takes into account the cumulative effect of technology transfers resulting from the export of munitions and dual-use items, and the decontrol of munitions commodities.

No comment.

7. Please determine whether license applications are being properly referred for comment (with sufficient time for responsible review) to the military services, the intelligence community, and other relevant groups (the "recipient groups") by the Defense Department and other agencies. Please consider in particular numerical trends in the

frequency of such referrals, trends in the types of applications referred, trends in the nature of the taskings made in connection with the referrals, and the perceptions of officials at the recipient groups.

Your answer here is at odds with your findings in the body of your report. Here, you state categorically that BXA failed to refer 6 of 60 cases or ten percent. However, the body of your report points out that this was the assessment of DOD and DOE and not your independent conclusions. As you know, BXA disagrees with the opinions of DOD and DOE in this matter and believes that our conclusion not to refer the applications was correct in every instance. We request you delete the conclusion about our error rate (10%) or at least attribute this view to the other agencies while noting our dissent.

In pointing out that the NPC does not review all cases, it would be useful to note that this is due to the NPC declining to review certain categories of cases. You should also point out that to review more case will require more resources. In addition, it would be useful to note that an alternative to simply giving the NPC more time would be to give it more resources.

Although the IG recommended furnishing licensing data to the Customs Service to be used for screening parties against the Treasury Enforcement Communication System database, we believe that this is not a desirable policy. The TECS system contains a variety of data, much of it irrelevant to export licensing decisions. We believe that screening will be more effective if Customs provides Commerce with a list of names that are appropriate for screening as is provided for in the memorandum of understanding between Commerce and Customs. Since the IG's last recommendation to BXA on this issue, Customs has provided BXA with data to add to its watch list and OEA has provided that data (provided on disk) to the BXA's Office of Administration to load into our computer data base for daily screening. As of April 1999, Administration has had this data and is working to ensure that all of this data is uploaded properly into Enforce to perform exactly the screening function that the IG has recommended. Therefore, we do not believe the alternative solution recommended by the IG is necessary.

8. Please determine whether license review officials at each of the agencies are provided sufficient training and guidance relevant for reviewing license applications, and whether more formal training and guidance is warranted. Dr. Lietner noted a paucity of such training and guidance in his Committee testimony.

We generally agree with your response; though, we think you might wish to point out, as you did in the body of your report that the current diversion of resources to respond to the extraordinary requests for information placed on the agency has impacted our ability to conduct formal training programs. In passing, you state that training is "left up to the individual divisions and generally consists of ... *learning on the job*....."(emphasis added), as if that were an undesirable approach.

As we mentioned in our response to your report, the primary method for training licensing officers (especially new ones) is On-The-Job in concert with a senior licensing officer. Due to the idiosyncracies of each licensing division's technical areas, this is highly desirable. EA, with its widely different areas of expertise and responsibilities, must tailor its training on a more individual basis. Nevertheless, more training is desirable, and we do not argue with the basic thrust of your recommendation. As mentioned in our response to your report, an expanded training program is not resource-neutral. If you are going to recommend more training in your answer to Senator Thompson, you might point out that more budgetary resources for this effort will have to be appropriated by the Congress.

You might want to point out that you are unable to assess the accuracy of Dr. Leitner's statement as he was referring to DOD where he is employed.

9. Please review the adequacy of the data bases used in the licensing process, such as the Defense Department's FORDTIS, paying particular attention to whether such data bases contain complete, accurate, consistent, and secure information about dual-use and munitions export applications.

Agree. We have already conducted a cost benefit analysis as part of our work with Booz Allen and Hamilton. While we do not believe that a further, formal analysis is necessary, system security is of the utmost importance to us and will be a major component of the new system architecture. With the advancements that have been made in commercially available encryption in the past couple of years, we should be able to encrypt our system at reasonable cost in a fashion that will enable us to deal with sensitive materials in our redesigned system, and we will be exploring this option fully. Our plan for hiring a full-time project team, if we receive full funding for ECASS, includes a position for a security expert for this system. This person will assist us in working through the myriad of security issues that we must consider, including the cost-benefit analysis.

10. In his testimony, Dr. Leitner described instances where licensing recommendations he entered on FORDTIS were later changed without his consent or knowledge. Please examine those charges, and assess whether such problems exist at your agencies.

While we generally agree with this answer, we are surprised that you do not categorically state, "We found no instances where any licensing officers' recommendations were later changed without his or her knowledge in Commerce's ECASS system."

11. Please determine whether license review officials are being pressured improperly by their supervisors to issue or change specific recommendations on license applications. Dr. Leitner testified about one such incident that happened to him at DTSA.

Senator Thompson's question concerns the "improper" direction of subordinates by their supervisors. As mentioned in our response to your report, we disagree with the way in which you

have dealt with this issue and responded to this question. We believe that based on your own analysis you should state categorically, "We found no evidence of license review officials being pressured improperly to issue or change specific recommendations on license applications."

We do not read your report as finding significant problems with management influence over the vote of the OC Chair. Thus, we are a bit surprised that it results in so much discussion in your report. The Chair of the OC is a Commerce employee and as the E.O. itself indicates is not intended to be entirely impartial. (See Section 5(b) of the E.O. which states, "If any department or agency disagrees with a licensing determination of the *Department of Commerce made through the OC*, it may appeal the matter to the ACEP for resolution." (Emphasis added.)

Of course, the OC Chair reports to the DAS and AS of EA, and both have a responsibility to ensure that the OC Chair carries out her responsibilities efficiently and in concert with U.S. law. In this regard, both have from-time-to-time instructed the OC Chair to bring a case review to closure by making a decision (e.g., where the loss of a sale is imminent or a case has exceeded the time frames of the E.O.) In addition, both have instructed the OC Chair on the provisions of the regulations or on changes in U.S. licensing policy to ensure that her actions are consistent with USG rules and policies. We saw nothing in your report that would recommend or lead to a change in this oversight.

Both the DAS and AS have encouraged the OC Chair to make decisions consistent with the EAR and U.S. licensing policy, even if that means voting against the position of the BXA representative or the majority of agencies in attendance. Your own analysis appears to support this contention. You may wish to revisit this section.

12. Please determine whether our government still uses nationals to conduct either prelicense or post-shipment licensing activities and whether such a practice is advisable.

BXA has and will continue to express its clear policy preference for having checks done by U.S. Government employees who are U.S. citizens. Its handbook for the conduct of pre-license checks and post shipment verifications makes this point and, in addition, sets forth the circumstances when the risks engendered by allowing unaccompanied foreign nationals to conduct a check are so grave that BXA will not consider such a check to be complete. As a result of this study, BXA will revise the handbook to reiterate this preference and to eliminate any perceived ambiguities as to when a check by a foreign national is merely undesirable and when it is unacceptable.

13. Please determine whether the agency licensing process leaves a reliable audit trail for assessing licensing performance.

With respect to your answer that you recommend that the OC Chair be given additional responsibility for taking the final action on cases, we mentioned in the response to your report



that we are reviewing this matter. While there may be benefits to this approach, we feel that you could better balance your answer by pointing out that there are down sides, too. BXA needs to carefully balance the desire for efficient processing with quality and vulnerability controls. By foregoing review and countersigning by the technical licensing offices, BXA may compromise its ability to ensure the accuracy and consistency of licensing decisions and their regulatory sufficiency. In addition, by foregoing meaningful countersigning, BXA exposes itself to possible improper licensing actions. However, we continue to review this matter toward overall improvement of our processes.

With respect to modification of Springfield controlled tapes by BXA personnel, you fail to explain how this "possibility" could occur, and you provide no support for the need to have the Under Secretary store duplicate, read-only tapes in response to this theoretical problem. You also make no budgetary recommendations to cover the duplication and storage costs. With respect to the maintenance of paper files, we continue to support retaining such documents for 90 days. As you did not in your original suggestion to save these files for five years, you again do not offer a compelling rationale for saving these files for one year or provide evidence that any additional benefit would outweigh the costs to the agency. In this day and age, we believe that reliance on electronic records is appropriate as evidenced by our current retention of information for both paper applications and technical specifications in digitized image format in our MARRs system.

With respect to the first of the 11 major elements to the BXA audit trail, the item should read paper and "electronically submitted" license applications rather than "automated". Paper applications become "electronic" applications after they are scanned and uploaded into the ECASS automated system where they are processed in electronic format.

14. Please describe the procedure used by agencies to ensure compliance with conditions placed on export license (e.g. no retransfers without U.S. consent, no replications, and peaceful use assurances), and assess the adequacy and effectiveness of such procedures.

Since your answer comments in some detail on post-shipment visits, it would also be appropriate to include here the comments in your report to the effect that NDAA visits are a questionable use of resources. The National Defense Authorization Act of 1998 (NDAA), which requires post shipment verifications for every computer with a composite theoretical performance exceeding 2,000 millions of theoretical operations per second (MTOPS) to a Tier 3 country, diverts enforcement resources from other activities that contribute more to our non-proliferation goals. In the first year of NDAA implementation, end users in the communications, utilities and financial industries received a majority of the high performance computers exported. A U.S. government employee has to visit all of these end-users no matter how well known, and no matter how many times they have been visited in the past, to judge whether their computers are being used for weapons development. As a result, the burden of these visits becomes disproportionate to the benefits derived.

As mentioned in the response to your report, BXA has recently implemented a new Licensing and Enforcement Action Program designed to deal with the vast majority of the problems with assigning conditions and their follow-up. We have proposed additional resource for FY 2001 to fully implement the program. In the meantime, we will take steps to improve our implementation of conditions, including their monitoring, consistent with budgetary realities. We would hope that you would mention this important initiative in your answer to Senator Thompson, as well as point out the additional resources that will be needed to carry out your recommendations in this area.





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