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***BUREAU OF EXPORT
ADMINISTRATION***

*Export Application Screen Process
Could Benefit From Further Changes*

Inspection Report No. IPE-9524/September 1997

Office of Inspections and Program Evaluations



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EXECUTIVE SUMMARY

The Bureau of Export Administration is responsible for controlling the export of dual-use commodities. Within BXA, Export Administration is responsible for reviewing export license applications, and Export Enforcement, specifically the Offices of Export Enforcement (OEE) and Enforcement Support (OES), is responsible for ensuring compliance with the export control provisions of the Export Administration Act (EAA) and the Export Administration Regulations (EAR). These offices also maintain liaison with the defense and intelligence communities on issues dealing with technology transfers and possible diversions.

The National Defense Authorization Act for Fiscal Year 1996, section 1324(b), requires the Inspectors General of the Departments of Commerce and State to each report, in 1996 and 1997, on the effectiveness of their respective agency's export licensing screening process during the preceding year. The act instructed the Inspectors General to (1) assess the extent to which the export licensing watchlist contains all relevant information and parties required by statute or regulation, (2) determine the number of licenses granted to parties on the watchlist, (3) assess the screening process used in granting such licenses, and (4) determine the number of end-use checks performed in connection with these licenses.

We issued our first report on BXA's export license screening process for fiscal year 1995 in September 1996. The report, *Report to the Congress on the Department of Commerce's Export License Application Screening Process (IPE-8647)*, contained several recommendations for improving the screening process. Specifically, we recommended that BXA:

1. Issue a memorandum to enforcement personnel emphasizing the need to properly update the database with unfavorable results from Safeguard visits.
2. Arrange for the electronic receipt of relevant information from the Department of Treasury's Office of Foreign Assets Control (OFAC).
3. Arrange for the electronic receipt of database information from the Department of State or, alternatively, initiate steps to provide for the electronic transfer of all license applications to State's Office of Defense Trade Controls (DTC) for the purpose of screening the applications through State's license screening database.
4. Ask the U.S. Customs Service to provide an on-line Treasury Enforcement Communications System (TECS) terminal or, alternatively, furnish all license application information to Customs to be screened through its TECS database.

BXA generally agreed with our review findings, and has taken steps to implement the first three recommendations. Specifically, the Acting Director for Office of Export Enforcement issued a memorandum on July 20, 1996, to enforcement personnel emphasizing the need to properly update the database with unfavorable results from Safeguard visits. In addition, BXA has recently installed a new stand-alone computer system which enables it to store electronic lists from these agencies. BXA informed us that they recently made an appointment with OFAC officials to request its "Specially Designated Nationals or Blocked Entities" lists on a diskette each time it updates them. BXA also informed us that after the new system has been tested, it will incorporate the updated list of watchlist information it received from DTC on a computer disk in March 1997. These actions, when fully implemented, will meet the intent of our first three recommendations. However, as we discuss in more detail later, we now have concerns about how often DTC provides its watchlist information to BXA (see page 11). Finally, BXA's Office of Enforcement Support conducted an informal study of the TECS issue raised in our fourth recommendation. While the OES study did not agree with our recommendation, the Under Secretary for Export Administration still has not made a decision on the matter of having Customs screen the license application information against the TECS database.

In conjunction with our review of fiscal year 1996 activities, we also conducted a follow-up review on our recommendations from our previous report on fiscal year 1995 activities. We made the following observations:

- ◆ **The Export Licensing Watchlist Generally Contains All Relevant Information.**
EAA and EAR contain no specific requirements regarding which parties are to be included in the watchlist, but establish a number of circumstances in which applications are to be denied. For example, EAA provides for the rejection of export license applications from parties that have previously violated the export control regulations, parties identified by OFAC as "Specially Designated Nationals or Blocked Entities," and parties named in the Department of Justice's report of significant export control violations.

The procedures BXA has established for managing and updating its screening database have generally been effective. All of the names from Justice's report of significant export control violations, Commerce's and State's lists of denial orders, and unfavorable end-use checks were on the watchlist. In addition, BXA has recently contracted with three private organizations to obtain their lists of questionable recipients of U.S. technology in order to expand its available resources for screening license applications (see page 10).

However, some of the names provided by OFAC during fiscal year 1996 were not included in the database. We believe these omissions are due partly to errors in manually inputting the data into the database. A new computer system for storing electronic lists was installed in late June 1997. Once the new system has been tested, BXA will have the

technical capability to meet the intent of two of our previous recommendations dealing with the electronic receipt of database information from DTC and OFAC. However, as pointed out earlier, BXA needs to request this information in an electronic format from OFAC and it still has to incorporate DTC's data into the system once it becomes fully operational (see page 13).

However, we are concerned about the State Department's lack of cooperation in sharing its watchlist information with BXA. We found that State provided BXA with quarterly listings of negative end-use checks for fiscal year 1996, but had not provided an updated overall list of watchlist parties since May 1995. Our September 1996 report recommended that BXA arrange to receive this information in electronic format and in March 1997, during a meeting we had with DTC officials, State finally provided us with an updated list of its watchlist on a diskette to give to BXA. We have referred this matter to State's Office of Inspector General, but we also believe there is a need for the Under Secretary for Export Administration to pursue a Memorandum of Understanding with State's Under Secretary for International Security Affairs to formalize a monthly transfer of DTC's watchlist information in an electronic format (see page 11).

- ◆ **The License Application Screening Process Could Be Enhanced by Screening All Parties Against the Treasury Enforcement Communications System (TECS) Database.** The overall screening process for parties on the watchlist is generally effective in ensuring appropriate levels of review. However, as we reported in our last review, the current screening process is not as comprehensive as it should be for parties not on the watchlist. Specifically, under BXA procedures, parties to pending applications are not checked against the Treasury Enforcement Communication System (TECS) database maintained by the U.S. Customs Service. TECS was created to provide multi-agency 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.

With the recent technological improvement in the direct cable connection between BXA's and Customs' mainframes, we believe the screening of parties to pending license applications is much more feasible. In addition, we believe that with this new access, parties can be screened against TECS and not slow down BXA's normal license process. However, BXA still has not made an official decision whether or not to use this new access to include screening of license applications by Customs.

Based on our comprehensive follow-up work during this review, we are even more

convinced that BXA should take every precautionary measure to ensure that all potential export enforcement concerns within the U.S. government are considered before issuing a license. BXA should meet with Customs in order to amend the current Memorandum of Understanding between the two agencies to provide for the transmission of names, addresses, and telephone numbers from new pending license applications by BXA to Customs for screening against TECS. This additional screening should be tested for at least a one-year trial period to determine if TECS can be a valuable resource in the screening process (see page 16).

- ◆ **The Quality and Utility of End-Use Checks Should Be Improved.** Although the overseas posts were generally in compliance with BXA's guidelines for conducting the checks, there are several areas where the posts need to improve their processes. For example, the posts are not always conducting end-use checks in a timely manner, and, contrary to BXA's guidance, US&FCS's FSNs often conduct the checks. In many cases, BXA was unaware of the posts' noncompliance because they failed to (1) request or receive a waiver from BXA to use FSNs for end-use checks or (2) properly identify who conducted the checks in response cables to BXA. The posts' response cables also do not consistently state whether an on-site visit was conducted, as recommended in BXA directives. In addition, BXA's guidance should be expanded to encourage posts to increase involvement of other embassy agencies in the information gathering process (see page 24).
- ◆ **Sharing of End-Use and Enforcement Information Should Be Improved.** Export Administration and licensing referral agencies want access to more information on end-use checks and enforcement concerns so that they are better informed when processing applications. Licensing officers often do not understand the nature of Export Enforcement's interests in specific applications or whether an end-use check has been initiated, because little information is revealed to them during their review process. Access to a limited amount of additional enforcement information, such as end-use check histories and limited descriptions of enforcement interests, can improve cooperation between Export Enforcement and Export Administration and make the license process more efficient. Making some basic changes to the Export Control Automated Support System screen currently available to licensing officials and information management procedures could improve information sharing within BXA and between BXA and referral agencies (see page 33).

On page 39, we offer a series of recommendations to the Under Secretary for Export Administration that address our concerns.



In responding to a draft of this report, the Under Secretary for Export Administration agreed with all but two of the report recommendations. BXA informed us that it has either taken steps that satisfy the intent of these recommendations or will implement changes or procedures by the end of the first quarter of fiscal year 1998. We are satisfied that these actions meet the intent of our recommendations.

BXA disagreed with our recommendation to screen all parties to new export license applications against Customs' TECS database. According to BXA, our recommendation is inconsistent "with the President's goal to streamline the export licensing process as expressed in [Executive Order 12981]." BXA's argument, however, is not convincing. Our recommendation ensures that BXA has access to all available information in making licensing decisions while not interfering with the strict time requirements outlined in the Executive Order. Hence, we reaffirm our recommendation and will work with BXA to resolve our disagreement.

BXA also disagreed with our recommendation that it electronically receive the Department of Justice's list of significant export control cases. Due to the relatively small number of such cases, we agreed that a paper list may be acceptable as long as BXA ensures adequate quality control over the inputting of this information into its watchlist.

Where necessary, we have made changes to the report and recommendations. BXA's complete response is included as an appendix to this report.

INTRODUCTION

Pursuant to the Inspector General Act of 1978 and the National Defense Authorization Act for Fiscal Year 1996, enacted on February 10, 1996, the Office of Inspector General, U.S. Department of Commerce, evaluated the Bureau of Export Administration's management and use of the export licensing watchlist. Section 1324(a) of the 1996 act required the Secretaries of Commerce and State to jointly report, in 1996 and 1997, on steps taken to improve sharing of information on each agency's watchlist, along with similar information in systems maintained by the Defense Department and the U.S. Customs Service; and to describe any further measures to be taken to strengthen U.S. export control measures. The first joint report was issued in April 1996, and the second was issued in April 1997.

Section 1324(b) of the act requires the Inspectors General of Commerce and State each to report, in 1996 and 1997, on the effectiveness of their respective agency's export licensing screening process during the preceding year. Specifically, the Inspectors General are required to:

- ! assess the extent to which the export licensing watchlist for their respective agencies contains all relevant information and parties required by statute or regulation,
- ! determine the number of licenses granted to parties on the watchlist,
- ! assess the screening process used in granting such licenses, and
- ! determine the number of end-use checks performed in connection with these licenses.

BXA's watchlist is a compilation of three screening databases used to identify license applications that have a greater potential for misuse or diversion of items or technologies than other applications. The watchlist includes parties, types of items and technologies, projects of concern, and other categories that BXA has identified as being potential problems.

PURPOSE AND SCOPE

Evaluations are special reviews that the OIG undertakes to provide agency managers with information about operational issues. By highlighting problems, the OIG hopes to help managers address them quickly and avoid similar problems in the future. As directed by the National Defense Authorization Act, the Office of Inspector General, U.S. Department of Commerce, evaluated BXA's export licensing screening procedures during fiscal year 1996. To assess the extent to which the BXA watchlist contains all relevant information, we reviewed the source documents the agency used to compile its watchlist and verified whether names from those

documents had been entered. Specifically, we compared BXA's watchlist with lists provided by the Treasury Department's Office of Foreign Assets Control (OFAC), the Justice Department's Export Enforcement Control Office, and the State Department's Office of Defense Trade Controls (DTC). We also compared the watchlist with Commerce's list of denial orders and its record of end-use checks for fiscal year 1996. Treasury's U.S. Customs Service did not provide a list of names to BXA during fiscal year 1996. For the individuals whose names BXA failed to include in its database, we checked the records to see if any licenses had been issued to them after they had been listed in the source documents.

To determine whether BXA effectively uses automated systems to screen license applications, we interviewed agency officials to determine how their screening database was compiled and used. To assess how well the screening process worked, we reviewed BXA's procedures and practices used in considering license applications of parties in the database. We also had wide-ranging discussions with officials of the Defense, Justice, State, and Treasury Departments, and the Central Intelligence Agency's Nonproliferation Center (NPC) to obtain their views about the adequacy of BXA's database.

We reviewed the policies, procedures, and methodologies for conducting end-use checks to determine if they are adequate and conform to established guidelines. To determine how many checks have been conducted in connection with applications by parties in the database, we obtained a list of all pre-license checks and post-shipment verifications conducted in fiscal year 1996. We also reviewed copies of all Safeguard trip reports (end-use checks conducted by BXA enforcement agents) for that year. Based on a random sample of all end-use checks, we examined the file records to ascertain if the (1) checks were conducted properly and (2) information obtained was properly considered in making licensing decisions. In addition, as part of inspections of five United States and Foreign Commercial Service (US&FCS) overseas posts conducted by our office in the fall of 1996, we reviewed the posts' performance of end-use checks.¹

This evaluation was conducted by the OIG's inspection staff in accordance with the *Quality Standards for Inspections* issued by the President's Council on Integrity and Efficiency.

¹See *Recent Overseas Inspections Found US&FCS Delivering Services Effectively But Facing Internal Constraints* (IPE-9178, September 1997); *US&FCS Post in Germany* (IPE-9287, August 1997); *US&FCS Post in Indonesia* (IPE-9285, May 1997); *US&FCS Post in Malaysia* (IPE-9284, April 1997); *US&FCS Post in Poland* (IPE-9288, April 1997); and *US&FCS Post in Thailand* (IPE-9286, May 1997).

BACKGROUND

The Bureau of Export Administration is the primary U.S. government licensing agency for the export of dual-use goods and technologies. Dual-use goods and technologies are those determined to have both civilian and military uses and are listed on the Commerce Control List. Exporters of such items are required by the Export Administration Act (EAA) and the Export Administration Regulations (EAR) to either obtain licenses from BXA or determine that the transactions are permitted without specific authorization from BXA before exporting the items outside the United States.

In addition, as authorized by Executive Order 12981, dated December 6, 1995, the Departments of Defense, Energy, and State, and the Arms Control and Disarmament Agency (ACDA) are authorized to review any license application received by Commerce. Defense now receives and reviews all Commerce export license applications with the exception of a few limited categories that it has decided not to review. State, Energy, and ACDA have also delegated to Commerce authority to review certain categories of commodities without referral to those agencies. Applications that are not approved are either denied or returned to the applicant without action.

Within BXA, Export Administration is responsible for reviewing export license applications, and Export Enforcement is responsible for ensuring compliance with the export control provisions of the EAA and the EAR (see Figure 1).

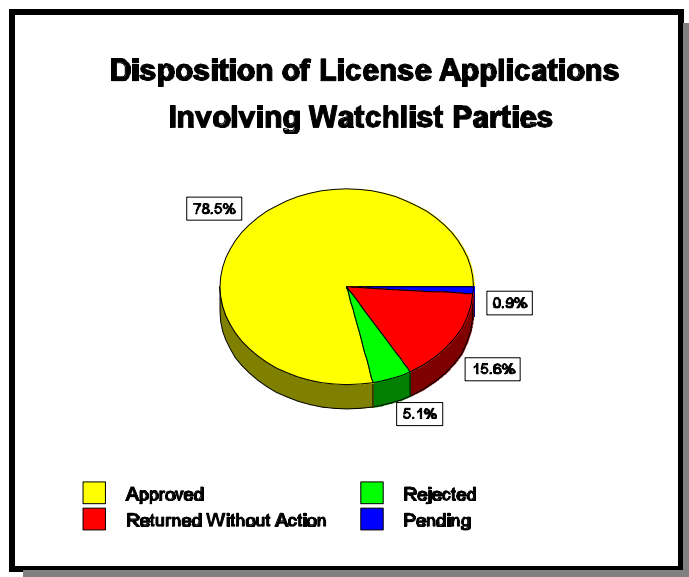
Figure 1: BXA's Organizational Structure



Export Enforcement, through its Offices of Export Enforcement (OEE) and Enforcement Support (OES), investigates possible export violations and assists in the screening of license applications. OEE is responsible for investigating violations of the act and regulations; apprehending violators; and working with BXA's Office of Chief Counsel, U.S. attorneys, and other officials in the prosecution of violators. OES assists OEE's field offices and Export Administration's licensing offices by receiving and disseminating export control information on problem end-users and end-uses. OES also makes recommendations to licensing officers based on intelligence information and input received from special agents in the field and at U.S. posts overseas.

BXA also sends certain applications to NPC for review. The applications are transmitted to NPC electronically and are transferred into its automated export control system. The applications are then reviewed by analysts to identify potential missile, nuclear, chemical, and biological proliferation concerns. NPC analysts discuss applications with BXA licensing officers to resolve any questions about specific licenses. If any of the referral agencies, including NPC, identify potential proliferation concerns, licensing officials are informed of the concerns, and the matter may be referred to the interagency review groups for resolution. These interagency review groups include: the Subgroup on Nuclear Export Coordination (SNEC), involving nuclear-related dual-use cases; the Missile Technology Export Control Group (MTEC), involving missile technology dual-use cases; and the SHIELD, involving chemical-related and biological-related dual-use cases. If issues cannot be resolved within these interagency meetings during the specified time frame, the pending applications are referred to another interagency committee, called the Operating Committee, for resolution.

According to BXA's records, during fiscal year 1996, 8,709 license applications were received, of which 3,839 involved parties on the watchlist. Of the license applications involving parties on the watchlist, 3,013 were approved, 194 were rejected, and 598 were returned without action. The other 34 license applications were still under review at the end of fiscal year 1996. Export Enforcement recommended that about 297 of these license applications be either rejected or returned without action because of diversion risks or other enforcement concerns.

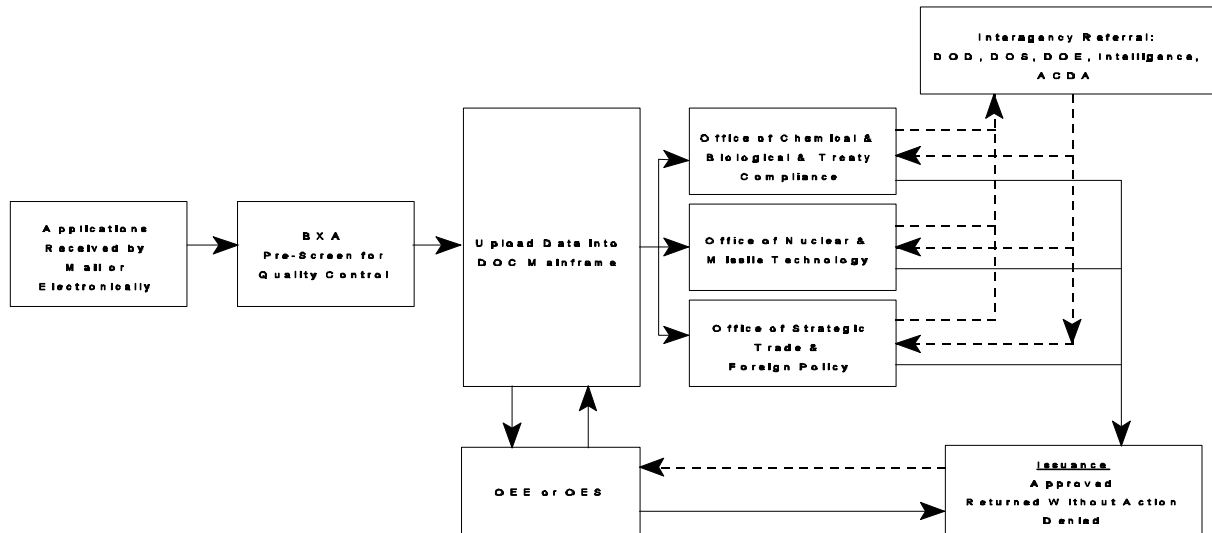


Export License Application Screening Process

ECASS

BXA uses a sophisticated computer system called the Export Control Automated Support System (ECASS) in processing and evaluating export license applications (see Figure 2). The system is intended to ensure that applications are properly reviewed to prevent the issuance of licenses for purposes or items that violate U.S. laws and regulations or are counter to U.S. national security and foreign policy interests. ECASS stores information on license applications and enforcement interests, including end-use checks and investigations. BXA controls access to the enforcement information by storing it in a subsection of ECASS called ENFORCE. Currently, Export Enforcement has access to the entire database, including ENFORCE, while Export Administration can view only information pertaining to license applications. The licensing officers' view of ECASS includes basic information about the application, a real-time referral history, and processing notes.

Figure 2: Flow Chart of BXA's License Application and Screening Process



After a license application is entered into ECASS, either manually or electronically, the system automatically tries to match the parties listed on the application to parties already in the system in order to assign the same identification number. For parties not recognized as already having an identification number, the system refers them to OES. If OES officials are unable to match the parties with existing identification numbers, the parties are assigned new numbers.

On a daily basis, all new applications are automatically screened by ECASS against the watchlist to identify any “flags” on the parties. Applications flagged by the system are automatically referred to OES or OEE for further review and, simultaneously, to licensing officials in Export Administration. Applications that are not flagged are automatically referred to licensing officials for processing. They are not reviewed by OES or OEE unless the case is referred to them during processing. Thus, all applications containing flagged parties or lacking a prior identification number for any party are reviewed to determine if there is any derogatory information in the files concerning the parties involved in the transaction or any other export concerns.

BXA’s watchlist contains the names of more than 38,000 parties that have been identified as warranting increased scrutiny for export licensing purposes. Currently, it includes an unclassified screen, a classified screen, and a signature screen. The watchlist also includes parties for which there is no derogatory information, but that are included for other reasons. For example, firms engaged in the manufacture of sensitive items or technologies are included so that BXA can exercise greater scrutiny over their exports. Similarly, firms that sell items or technologies known to be of interest to foreign parties who potentially may seek to illegally obtain the items are also screened by OES. A party may be included in the screening database for any of a broad range of reasons (see Appendix 1).

Besides reviewing license applications involving parties in the watchlist, OES reviews license applications based on the type of commodity involved and the location of the end-user. For example, licenses for “crime control” commodities, such as tear gas, certain shotguns, handcuffs, and related items, are automatically referred to OES specialists for review. Applications for the export of important technologies of missile or nuclear proliferation concern are also reviewed by OES specialists. License applications for the export of items or technologies to countries of proliferation concern also receive scrutiny by the OES specialists.

The New Stand-Alone Computer System

In response to two of the recommendations from our previous report which essentially stated that BXA needed to arrange for the electronic receipt of database information from DTC and OFAC, BXA acquired a new stand-alone computer system. BXA’s intent is to input the lists received from DTC and OFAC electronically, thereby eliminating errors in the ECASS database that occur during manual data entry that can cause inaccurate or missed matches. BXA’s computer systems personnel explained that the new stand-alone computer system is necessary because the electronic formats DTC and OFAC use have different data fields that are not compatible with ECASS. For example, DTC’s list does not always specify the country of the concerned party, which is a required field in ECASS.

Therefore, in addition to the daily screening of new applications through ECASS, OES also plans to use the new stand-alone computer system to run on a daily basis all parties listed on new license applications against the lists provided by DTC and OFAC, as well as some private sector sources. The stand-alone system will be equipped with privately developed software that will store these databases separately, thereby eliminating the need to reformat the information provided. The software also has advanced search logic that can identify exact matches and typographical and sound variations. OES analysts will then review the search results and judge whether matches are valid. This should improve the quality and the efficiency of the application screening process. Also, the addition of the private sector lists will increase the amount of information reviewed.

The new system was installed in late June 1997. Once the new system has been tested for accuracy, BXA will then have the technical capability to meet the intent of two of our previous recommendations, which essentially stated that BXA needed to arrange for the electronic receipt of database information from DTC and OFAC. However, as discussed in more detail in Section I, BXA still needs to work at obtaining this information from both State and Treasury in an electronic format on a routine basis.

End-Use Checks

End-use checks are an important component of the export licensing process. These 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. The purpose of the check is to determine if the overseas parties are suitable for receiving sensitive U.S. items and technology and will likely comply with appropriate end-use and retransfer restrictions. The result of this check is factored into the licensing recommendation that Export Enforcement makes to the licensing offices. A PSV, conducted after an export has occurred, is used to determine whether the licensed item or technology was received by the party named on the license or shipper's export declaration (SED) or was diverted to an unauthorized end user. The check is also used to verify whether the commodity is being used in accordance with the license provisions.

PLCs and PSVs are generally conducted by Commerce's US&FCS personnel stationed at the post where the check is to take place or by State Department personnel if US&FCS has no office at the post. However, in recent years Export Enforcement has expanded its Safeguards Verification Program, which allows these checks, mostly PSVs, to be conducted by BXA's enforcement officials. 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.

Problems Previously Identified in the Export License Screening Process

In our September 1996 report on BXA's export license screening process, we identified a number of actions needed to improve the license screening process. Specifically, we recommended that BXA:

1. Issue a memorandum to enforcement personnel emphasizing the need to properly update the database with unfavorable results from Safeguard visits.
2. Arrange for the electronic receipt of relevant information from OFAC.
3. Arrange for the electronic receipt of database information from the State Department or, alternatively, initiate steps to provide for the electronic transfer of all license applications to State's Office of Defense Trade Controls for the purpose of screening the applications through State's license screening database.
4. Request U.S. Customs Service to provide an on-line Treasury Enforcement Communications System (TECS) terminal or, alternatively, furnish all license application information to U.S. Customs to be screened through its TECS database.

BXA generally agreed with our review findings, and has taken steps to implement the first three recommendations. Specifically, the Acting Director for Office of Export Enforcement issued a memorandum on July 20, 1996, to enforcement personnel emphasizing the need to properly update the database with unfavorable results from Safeguard visits. In addition, BXA has recently installed a new stand-alone computer system which enables it to store electronic lists from these agencies. BXA informed us that they recently made an appointment with OFAC officials to request its "Specially Designated Nationals or Blocked Entities" list on a diskette each time it is updated. BXA also informed us that after the new system has been tested, it will incorporate the updated list of watchlist information it received on diskette from DTC in March 1997. These actions, when fully implemented, will meet the intent of our first three recommendations. However, as we discuss in more detail later, we now have concerns about how often DTC provides its watchlist information to BXA (see page 11). Finally, BXA agreed to study the fourth recommendation and is still in the process of deciding whether it will implement our recommendation to screen license application information against TECS.

OBSERVATIONS AND CONCLUSIONS

I. Export Licensing Watchlist Generally Contains All Relevant Information

As stated in our September 1996 report, the EAA and the EAR contain no specific requirements regarding which parties should be included in the watchlist. However, the law and regulation establish a number of circumstances in which applications are to be denied. For example, the EAA provides for the denial of export license applications for parties found to have violated the export control regulations administered by the Departments of Commerce (the EAR) and State (the International Traffic in Arms Regulations). The regulations establish additional circumstances that call for the denial of export applications, such as for parties that the Department of Treasury's OFAC has identified as "Specially Designated Nationals or Blocked Entities."

We found that with a few exceptions, the watchlist included the names of appropriate parties. Certain OES staff members have been assigned specific responsibilities for receiving information and adding parties to the watchlist. OES guidance requires these staff members to monitor, research, and analyze all available information sources to ensure that all pertinent export control information is maintained in the database. Key sources include OFAC's list of "Specially Designated Nationals or Blocked Entities," the Commerce and State Departments' denial lists, and the Justice Department's report of significant export control violation cases.

BXA officials also enter the identities of other parties based on the following information or sources:

- ! Unfavorable results of end-use checks conducted for both Commerce- and State-controlled items and technologies.
- ! Reports from the intelligence community identifying diversion, proliferation, misuse, and other relevant concerns.
- ! Dun & Bradstreet reports on firms' export activities.
- ! U.S. Customs Service reports identifying derogatory or adverse information on specific parties (e.g., U.S. Customs "Alert" reports).
- ! Information concerning "targeted" U.S. companies acquired during general research and investigations by BXA.

- ! Possible activities involving Enhanced Proliferation Control Initiative concerns and those affected by multilateral agreements, such as the Missile Technology Control Regime, the Nuclear Suppliers Group, and the Australia Group.

Although we found that BXA's watchlist generally included the names of appropriate parties, we believe the license screening database could be further improved by the addition of information from private sector lists and better information exchange processes between BXA and the Departments of State, Justice, and Treasury.

Private Sector Lists

BXA is expanding its available resources for screening license applications. OES has recently contracted with three private organizations to receive electronic databases of questionable recipients of U.S. technology. Although most of the information on these lists is already known to the U.S. government, BXA stated that these organizations have the advantages of being closer to the business community and having the resources to travel overseas to collect information. The lists are sold to exporters as a resource for identifying questionable parties in order to avoid having an export license denied or committing export violations. Other federal agencies, such as ACDA and NPC, have also used one or more of these lists during their license screening and analysis. Although we encourage BXA to use all available resources to identify unreliable parties for export licenses, BXA needs to draft policies and procedures for using the private source lists.

The first list acquired by BXA is produced by the Nomos Corporation. This list is described as an open-source database on activities related to weapons of mass destruction programs in countries of concern. The list includes several thousand nuclear, biological and chemical warfare, and ballistic missile-related entities, facilities, transactions, and activities. The data is collected from domestic and foreign books, periodicals, academic papers, court records, government and industry reports, electronic news services, and bulletin boards. Each entry identifies the country, entity, activity, relevant dates, and source of the information.

The second source of information is the Monterey Institute of International Studies. The institute's Emerging Nuclear Suppliers database includes information on international trade and developments in nuclear technology, and its International Missile Proliferation database tracks international trade and significant developments in ballistic missiles, cruise missiles, and missile defense systems and components. Each database is compiled from a variety of sources, including periodicals, trade journals, government and defense publications, United Nations and International Atomic Energy Agency releases, international newspapers and news services, and academic journals. Updates will be provided to OES on a diskette three to six times a year or via electronic mail 12 times a year.

The third list, the *Risk Report*, is prepared by the Wisconsin Project on Nuclear Arms Control. This nonprofit research organization identifies foreign companies suspected of building weapons of mass destruction. The database includes the names of suspect parties and analyses of nuclear weapons, chemical and biological weapons, missile programs, and diversion in countries of concern to the United States. Similar to the other two lists, the *Risk Report* is compiled from government reports, manufacturers' brochures, industry databases, trade journals, and media reports. The *Risk Report* is updated six times a year and is available on CD-ROM.

While we encourage BXA to use all available resources to identify unreliable parties for export licenses, the private lists should be used with caution. Some individuals who are involved in the licensing process commented that information on the lists can be unreliable or unverifiable. Others, however, stated that the private lists could provide useful leads or corroborating evidence on suspect parties. We discussed these concerns with OES officials, who explained that BXA will not deny export licenses based on derogatory information found solely from these private sources. To ensure the integrity of licensing decisions and to avoid concerns in the future, we believe that BXA should draft policies and procedures for using the private source lists.



In its response to our draft report, BXA stated that OES “will draft policies and procedures for using private source watch lists in all license review activities by enforcement staff during the first quarter of [fiscal year] 1998.” This action meets the intent of our recommendation.

Department of State

Based on an informal agreement, the Office of Defense Trade Controls sends OES a list of all negative end-use checks for munition items (commonly referred to as Blue Lantern Checks) on a quarterly basis. We verified that all of the designated parties from these lists for fiscal year 1996 were on the watchlist.

Separate from this exchange of information, BXA and DTC agreed, according to their 1996 *Joint State-Commerce Report on Improving Export Watchlists* submitted to the Congress, to “exchange the relevant portion of each agency’s watchlist on a *regular* basis and incorporate the relevant portion into each agency’s watchlist.” [Emphasis added.] Although no specific time frame was established for this exchange, we found during this review that OES was providing this information to DTC on a quarterly basis. However, DTC had not provided BXA an updated version of relevant portions of its list of watchlist parties since May 1995. OES provided us with documentation demonstrating its numerous attempts to get DTC more involved in exchanging information, and we are concerned about DTC’s lack of cooperation.

In addition, our September 1996 report recommended that BXA arrange for this information to be exchanged in an electronic format (e.g., a computer diskette), and both BXA and DTC agreed that this proposal was feasible. In March 1997, during a meeting with our review team, DTC finally provided us with an updated list of its watchlist on a diskette to deliver to OES. During that same meeting, DTC officials again confirmed that putting the names on a diskette would be a much simpler process than sending it by hard copy and could be done on a more frequent basis. DTC officials specifically stated that they could send BXA a monthly update. Based on our meeting with DTC, OES had sent a letter to DTC in April 1997, requesting that they establish a procedure to formalize a monthly transfer of information, but OES received no response. We have referred this matter to the State Department's Office of Inspector General, but we also believe the Under Secretary for Export Administration should pursue a Memorandum of Understanding (MOU) with the State Department's Under Secretary for International Security Affairs to formalize a monthly transfer of DTC's watchlist information on an electronic format.



In responding to our draft report, BXA agreed with our finding and stated that it "will contact the State Department's Office of International Security Affairs and initiate discussions to develop [a Memorandum of Understanding] regarding the monthly transfer of State's watch list information in an electronic format." Although this proposed action meets the intent of our recommendation, we would appreciate BXA keeping us informed of its progress on this matter.

Department of Justice

During fiscal year 1996, the Justice Department reported to BXA 20 significant export control cases with final judgments involving 43 parties to be added to the watchlist. OES added the parties to the watchlist in a reasonable time frame after they received the list and verified that no licenses were issued to any of these parties during fiscal year 1996.

We noted that OES has been receiving the final judgment list from Justice in a paper format. Justice informed us that they could provide the information on a computer diskette if BXA would prefer. To reduce the likelihood of human error associated with manually inputting the names on the watchlist, we believe BXA should request this information in an electronic format. However, due to the relatively small number of parties referred by Justice, a paper list of significant export cases may be acceptable as long as BXA ensures adequate quality control over the inputting of this information into its watchlist.

Although we verified that all of the parties involved in the cases were on the watchlist, and that no licenses were issued to any of the parties, we are concerned about *when* BXA receives the lists of parties. Justice's list is composed of those parties that have been found guilty of export

violations. It can take anywhere from two to five years to complete a criminal investigation, plus additional time to actually reach a conviction or settlement with a guilty plea. We believe BXA should be made aware of these parties much earlier in the investigative process. If the investigating agency were to notify BXA of parties under investigation for export control violations, "when" BXA receives the final judgment list from Justice would be a mute point. The initial investigating agency should notify BXA of these parties *during* the investigation. BXA should not necessarily deny an application to these parties based solely on the fact that they are under investigation for possible export control violations, but this information would allow BXA to make better, more informed decisions regarding such parties. However, the investigating agency involved in these cases, Customs, did not provide any names, including those it solely had under investigation, to BXA during fiscal year 1996. The Customs issue is further discussed below and in Section II.



In responding to our draft report, BXA disagreed with our finding and stated that it would be better to continue to receive the Justice list of significant cases in a paper format and enter these parties into its automated watchlist database. BXA stated that if the information was received in an electronic format and inputted into the new open source database, Export Enforcement personnel in the field would not have access to it because this database is only available to OES employees. Although we still believe that receiving this information in an electronic format would reduce staff time and human error, we recognize the benefit of keeping enforcement agents in the field aware of this information. Therefore, considering the relatively small number of cases and parties received from Justice each year, a paper list of significant cases may be acceptable as long as OES ensures adequate quality control over the inputting of this information. We have made appropriate changes to the report and recommendation.

Department of the Treasury

BXA receives watchlist parties from two Treasury bureaus. OFAC provides information on parties designated as "Specially Designated Nationals or Blocked Entities." The U.S. Customs Service provides reports (e.g. "Alert" reports) that identify derogatory or adverse information on specific parties.

In our September 1996 report, we found that not all of the parties provided by OFAC during fiscal year 1995 were properly added to the watchlist. Part of the problem was due to errors inherent in having the OES staff manually adding the names to the watchlist. During our current review, we found 16 parties missing from the watchlist, a situation we again believe is due, in part, to manual inputting errors. We verified that these names have since been added to the watchlist, and no licenses were issued to the parties during fiscal year 1996. BXA concurred

with our original recommendation to obtain the relevant information from OFAC in electronic format but it still has not fully implemented that recommendation. OFAC's lists of "Specially Designated Nationals or Blocked Entities" have been available electronically for many years. These lists can now also be found on the Internet through OFAC's Home Page. BXA can download the information from the Internet or Commerce's Electronic Bulletin Board, but OES prefers to try and get the information on a diskette directly from OFAC each time the list is updated. As mentioned earlier, BXA's new stand-alone computer system was installed in late June 1997 and OES analysts have received training on it. Once OES has tested the system for accuracy, BXA will have the technical capability of uploading OFAC's lists electronically. We encourage BXA to accelerate its meeting with OFAC and arrange for the electronic receipt of this information.

In addition, a 1993 MOU between BXA and the U.S. Customs Service 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 through its "Alert" reports. Since the signing of the MOU, Customs has provided BXA with only 69 names to add to its watchlist. Of these 69, 42 parties were referred to BXA during fiscal year 1995. However, during fiscal year 1996, Customs did not provide BXA with any "Alert" reports on parties to add to its watchlist. We cannot explain why Customs did not provide BXA with any "Alert" reports during this time. BXA also could not explain why no reports were received and has not made any effort to encourage or remind Customs of its agreement to provide BXA with the names and identifiers of targets under investigation for BXA's use in screening license applications. BXA's senior management contends that the 1993 MOU is sufficient to protect the integrity of the export licensing process and that it is Customs' responsibility to provide all enforcement concern information to BXA.

In our 1996 report, we raised concerns that 42 names may not represent all of Customs export enforcement concerns. We are even more concerned now after learning that no names were provided in fiscal year 1996. Specifically, we are concerned that Customs does not appear to be reporting names of parties to BXA when an investigation is started. Anytime a BXA enforcement agent opens up an investigation on a party, the name is automatically added to the watchlist. This includes joint investigations conducted by BXA and Customs. However, in fiscal year 1996, Customs never reported to BXA parties subject to investigations it conducted solely. As previously stated, we believe that BXA should be made aware of investigations early in the process to ensure that pending license applications are screened against the best information available to the government (we address this issue further in Section II).

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BXA's response to our draft report stated that "[a]s of July 21, 1997, OES does receive weekly updates of OFAC's list of 'Specially Designated Nationals or Blocked Entities' in an electronic format and maintains this data in its new open source database." This action meets the intent of our recommendation.

Department of Commerce

During our earlier review, we found that some of the unfavorable results from Safeguard trips had not been included in the database because special agents failed to follow procedures. As a result, we recommended that BXA issue a memorandum to enforcement officers emphasizing the need to properly update the database. BXA issued the memorandum on July 20, 1996, implementing our recommendation before issuance of our draft report. After reviewing the Safeguard trip reports for fiscal year 1996, we verified that all of the negative results were included in the watchlist. We also verified that all of the names added to the Commerce's Denied Persons List in fiscal year 1996 were included in the watchlist.

II. License Application Screening Process Could Be Enhanced by Screening Parties Against the TECS Database

We conclude that the overall screening process for parties on the watchlist is generally effective in ensuring appropriate levels of review. However, as we reported in our 1996 review, we believe that the current process is not as comprehensive as it could be. Specifically, in accordance with a BXA policy decision, the names of parties to pending applications are not checked against the Treasury Enforcement Communication System (TECS) database maintained by Customs. TECS was created to provide multi-agency access to a common database of enforcement data supplied by the participating agencies, including Customs, the Drug Enforcement Administration, and the Bureau of Alcohol, Tobacco, and Firearms, to satisfy a recognized need to promote the sharing of sensitive information between federal law enforcement agencies. We believe screening every applicant and consignee against TECS during the initial phases of the licensing process would give BXA licensing and enforcement authorities early warning of any potential concerns Customs may have.

With the recent technological improvement in the direct cable connection between BXA's and Customs' mainframes, we believe the screening of pending license applications against TECS is much more feasible. Therefore, the MOU between BXA and Customs should be amended to provide for the transmission of names, addresses, and telephone numbers from new pending license applications by BXA to Customs for screening against TECS as discussed below.

In response to our 1996 report, BXA agreed to study our recommendation to screen all license applications against TECS. However, OES only conducted an informal study of the TECS issue. The OES study, prepared by OES personnel for the Director of OES, essentially concluded that our recommendation was unnecessary given the current BXA-Customs MOU, which already provides a specific process for screening suspect parties at the request of Customs' personnel. While the OES study did not agree with our recommendation, the Under Secretary for Export Administration still has not made a decision on the matter of screening the pending license application information against the TECS database. In addition, during the exit conference on this review, additional concerns were raised by BXA's senior management concerning our recommendation.

We disagree with the informal OES study and continue to believe that screening all parties against TECS during the initial phases of the licensing process would allow BXA licensing and enforcement authorities to know early on of any potential concerns Customs may have. We address BXA's concerns and objections to our recommendation in more detail below.

Customs Involvement in BXA's Current License Application Screening Process

Under a 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 used by Customs' enforcement personnel in the field (for example, an inspector at a U.S. port) to check the validity of certain export shipments. This data is *not* being used by Customs, as some BXA officials told us, to screen the parties against existing information in TECS to see if there are any enforcement concerns with the parties involved.

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 OES place on BXA's screen the name of a party in which the agent has an enforcement interest.
- ! OES 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 the party of concern to the Customs special agent; for example, the party is 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 OES's queue. The license is held in this queue until the enforcement concern is resolved. The license cannot be approved until OES lifts the "flag."
- ! OES notifies the Customs headquarters contact of the screen hit. OES provides this contact a copy of the relevant license application. Customs provides to OES any derogatory information Customs may have on the license application in question.
- ! If Customs does not respond to the OES notification within four working days, OES 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 EAR, Customs provides the information to OES.

However, we believe the screening process can now be easily expanded to incorporate the screening of parties to pending license applications against TECS.

Enhancing the Current License Application Screening Process

Recent technological improvements in BXA's access to TECS should facilitate screening all parties against TECS. Customs has granted BXA use of an existing cable connection between Customs' and Commerce's main frame computers. This connection will enable BXA to have direct access to TECS, thereby replacing the current modem access that users found unreliable. According to Commerce's systems personnel, the connection can accommodate a daily transfer of application information from BXA to Customs if sent during off-peak hours, such as at night. With the new access, we believe that BXA can readily screen TECS and not slow its normal license process. 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 new hard-line access to TECS and then automatically screened against the database, or those portions of the database that BXA and Customs have already 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 EAR, Customs would provide the relevant information to OES 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.

BXA Concerns on TECS Screening Are Not Warranted

BXA's senior management contends that the 1993 MOU is sufficient to protect the integrity of the export licensing process and that it is Customs' responsibility to provide its enforcement concerns to BXA—not BXA's responsibility to provide all pending license applications to Customs. We believe that BXA has the ultimate responsibility for issuing U.S. dual-use export license applications and, therefore, should take every precautionary measure to ensure that all potential export enforcement concerns within the U.S. government are considered before issuing a license.

The need to adopt an acceptable method of checking license application information against the TECS database can be illustrated by the fact that BXA did not have the names of 43 parties to add to its watchlist until *after* they had already been found guilty of export violations by Justice. If BXA were to run all parties against TECS, these parties would be identified *during* the investigation process since the Justice convictions involve cases resulting from Customs' investigations. 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 Customs concerns (all parties under investigation by Customs are automatically put in TECS). This is far more desirable than finding out about export control violators years later upon conviction.

In addition, numerous officials we spoke to, including those within the defense and intelligence communities, agreed that BXA could enhance its export license screening process by screening parties against *all* available sources within the federal government. For example, NPC officials told us that because they are unable to collect information on U.S. citizens or companies, they are also unable to collect information on U.S. subsidiaries overseas, including those in countries of concern. However, Customs *is* able to collect such information and store it in TECS, thereby giving BXA another valuable source of information to check export application parties against.

OES Study of Previous OIG Recommendation

After the issuance of our 1996 report, OES conducted an informal study to determine the usefulness of BXA's checking of all applications against TECS. The OES study, prepared by OES personnel for the Director of OES, essentially concluded that our recommendation was unnecessary given the current BXA-Customs MOU, which already provides a specific process for

screening suspect parties at the request of Customs personnel. We disagree. Again, under the current process, no information from investigations conducted solely by Customs during fiscal year 1996 was provided to BXA. However, we believe that if all parties to pending license applications were run against the TECS database, the issue of Customs not providing BXA the names of parties Customs has an enforcement concern with is a mute 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 their concerns with that particular license application.

In conjunction with its study, OES surveyed all of OEE's special agents-in-charge to determine whether they found TECS to be a valuable enforcement tool. The overall response from the field was that TECS was a useful system. We asked numerous law enforcement personnel if, in their opinion, BXA should routinely screen applications against all available sources of information within the U.S. law enforcement community, including TECS. The unanimous response was "yes."

Section 12(c) of the Export Administration Act

Although Customs currently receives ECASS data once a license has been issued or denied, BXA officials have expressed concerns about sending ECASS data to Customs on pending license applications. The OES study points out that under our proposal, "BXA would be passing large amounts of sensitive data to an agency without license review functions," and that, "Such an action would increase BXA's liability in the event of inappropriate handling or a malicious public exposure of sensitive trade data." Specifically, some BXA officials told us that they are concerned that Customs may inadvertently leak proprietary information regarding a potential export transaction if they were to have access to pending license application data.

During the course of this review, BXA licensing officials repeatedly cited section 12(c) of the Export Administration Act as a reason why BXA should not send pending license application data to Customs. Section 12(c) of the EAA requires that export license information be withheld from public disclosure unless the release of such information is determined by appropriate authority to be in the national interest.

However, according to section 12(c)(3) of the 1985 amendments to the Export Administration Act:²

“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.]

In our opinion, the law calls for cooperation among export control agencies—including the U.S. Customs Service. The above provision clearly provides the authority for BXA to exchange pending license application information with Customs. Nonetheless, some BXA officials still believe that sharing this information creates the potential for mishandling of the information by Customs personnel. However, as shown by the statement above, section 12(c) should not be construed as restricting the flow of information between government agencies. In addition, any concerns regarding the inappropriate handling of license data should have been alleviated considering Customs, as a part of the 1993 MOU, has agreed to abide strictly by the confidentiality provisions of section 12(c) of the EAA.

Due to BXA’s persistent concerns over the 12(c) issue, we asked Export Administration officials if Customs had ever violated this provision and, if so, to provide us specific examples of violations. They could not. Unless Customs has violated this agreement, we do not believe that the “fear” of Customs misusing this information is a valid argument for not screening all parties to new pending applications against TECS.

In addition, the 1993 MOU clearly states that all access to the ECASS data in TECS will be recorded to provide a comprehensive audit trail. This audit trail can be used to provide periodic reports to BXA on use of the data as well as to enable Customs’ Office of Internal Affairs to investigate improper use or disclosure of the information.

Conclusion

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. As BXA has already established the four-day turnaround time under the current procedures, we believe that this is a reasonable amount of time

²Although the EAA has lapsed, Executive Order 12924, dated August 12, 1994, specifically continues provisions of the EAA as amended, under the President’s authority in the International Emergency Economic Powers Act. This executive order stays in effect until terminated.

to allow Customs to inform BXA of a potential problem. In addition, the four-day time frame is compatible with application processing times established by Executive Order 12981.³

We discussed our proposal with a Customs' official, who agrees that this additional screening could enhance the license review process. We suggest BXA and Customs amend the current MOU to provide for the transmission of names, addresses, and telephone numbers from new pending license applications by BXA to Customs for screening against TECS for at least a one-year trial period. This will enable the agencies to determine if TECS can add valuable information to the screening process.



In responding to our draft report, BXA agreed that it is important for policy makers to have all information available to them in order to reach a licensing decision. However, BXA disagreed with our recommendation to screen all parties to export license applications against TECS. Specifically, their 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].”

First, we are not suggesting that Customs make licensing recommendations as do the existing referral agencies. However, we do believe that BXA should send all *parties* to pending license applications to Customs for screening against TECS. The information going to Customs would only include the names, addresses, and phone numbers of the parties—not specific details on the license application, such as the commodity to be exported. 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. We do not believe that additional screening of parties against TECS is inconsistent with Executive Order 12981. In fact, the Executive Order clearly states in several places that “the Secretary may refer license applications to other United States Government departments or agencies for review as appropriate.” If BXA does not screen its parties against all available resources—such as TECS—it is leaving itself and the Secretary of Commerce vulnerable to criticisms of licensing decisions based on incomplete information.

Second, BXA argues 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

³The Executive Order mandates that license applications requiring referral will be acted upon by Commerce within nine days of receipt and that all referral agencies will respond to Commerce within 30 days of receipt.

escalation of cases.” We agree. Our proposal gives Customs a four-day time period (the established time frame under the MOU) in which to notify BXA of any enforcement concerns. The four-day time frame is 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, it is possible that the processing time for that application may be extended to address the enforcement concerns. This is the current practice for applications in which Customs and/or Export Enforcement agents have concerns. We believe that this 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.

BXA’s response also states that “this important issue should be discussed within the Memorandum of Understanding between Customs and BXA. The MOU currently provides for quarterly meetings. At these meetings, we will remind Customs of its obligation to provide BXA with the relevant information that Customs holds which can be used to screen license applications.” Yet, BXA has not taken full advantage of these meetings to discuss Customs’ obligations to share investigative information under the MOU since we issued our first report in September 1996. Although we acknowledge that the MOU has proven to be a useful tool for building better working relationships between BXA enforcement agents and Customs enforcement agents in the field, we believe that the current MOU is insufficient for screening parties to pending license applications. Even if Customs began sending BXA a listing of future parties with which it has enforcement concerns, it will not capture the many parties previously included in TECS. In addition, by sending the parties to Customs electronically, BXA will reduce the likelihood of human error associated with manually inputting names.

We agree with BXA that Customs agents have a responsibility to identify those firms and individuals about whom they have developed investigative information that would be relevant to the licensing process. However, the Under Secretary for Export Administration has the ultimate responsibility for issuing U.S. dual-use export licenses and should ensure that BXA takes every precautionary measure to consider all potential export enforcement concerns within the U.S. government before issuing a license. We therefore reaffirm our recommendation that the current MOU between BXA and Customs be amended to provide for the transmission of names, addresses, and telephone numbers from new pending license applications by BXA to Customs for screening against TECS for at least a one-year trial period. BXA and Customs should use their established quarterly meetings to discuss the value of this additional information sharing.

We request to be informed of BXA and Customs’ progress towards expanding information sharing between the two agencies.

III. Quality and Utility of End-Use Checks Should Be Improved

BXA relies on the American embassies overseas to assist it in fulfilling its export control activities by performing end-use checks to verify the legitimacy of export transactions. BXA licensing officers and export enforcement special agents or analysts, as well as other federal agencies involved in the licensing process, can request that an overseas post conduct an end-use check on a foreign company or organization. Pre-license checks determine if an overseas person or firm is a suitable party to a future transaction involving controlled U.S.-origin goods or technical data. Post-shipment verifications confirm whether goods exported from the United States were received and are being used in accordance with the terms of an export license.

In March 1996, BXA distributed guidance, *How to Conduct Pre-License Checks and Post-Shipment Verifications* (March 1996), to the posts overseas. Overall, the new guidance is comprehensive and easy-to-use, and has been well-received by those who conduct end-use checks. As the guidance describes, when an export application warrants an end-use check, OES prepares a cable to the appropriate post overseas, requesting that a PLC or PSV be conducted. The cable transmits all relevant information about the application and its parties and any specific questions to be answered. US&FCS officials are responsible for conducting the checks in countries where it has operations; otherwise, State Department or other U.S. government employees conduct the checks. If the post's response is late, OES follows up with a cable reminding the post of its obligation to complete the check.

Through BXA's Safeguard program, export enforcement agents also conduct end-use checks overseas. OEE headquarters, in consultation with other Export Enforcement managers, select target countries and parties based on enforcement concerns. While overseas, export enforcement agents may also train U.S. and foreign government officials and local business representatives on U.S. export controls.

In fiscal year 1996, overseas personnel or BXA export enforcement agents on travel duty completed 469 end-use checks. The following table summarizes the end-use checks conducted during this period:

**Table 1:
Summary of Final Status
of End-use Checks**

| | Favorable | Unfavorable | Canceled | Total |
|--|------------|-------------|------------|------------|
| Pre-License Checks | 259 | 41 | 85 | 385 |
| Post-Shipment Verifications ^a | 88 | 4 | 35 | 127 |
| Safeguard Checks ^b | 69 | 8 | 1 | 78 |
| Total | 416 | 53 | 121 | 590 |

^a Fifty PSVs conducted by overseas posts were for goods or technology exported without a license, but identified by an SED at the time of shipment.

^b In addition to some informational interviews, all of the end-use checks conducted during Safeguard visits were PSVs. Six of these PSVs were identified by an SED and not a license.

As shown in Table 1, 259 of 385 PLCs (67 percent) and 157 of 205 PSVs (76 percent) concluded that the foreign parties were suitable recipients of U.S. technology. As required by BXA's internal procedures, all of the questionable parties identified in the 41 unfavorable PLCs, four unfavorable PSVs, and eight unfavorable Safeguard checks were included in BXA's watchlist.

In addition to the 469 completed end-use checks, 121 were canceled or not completed after first being requested. Reasons for canceling end-use checks varied. As we discussed in our previous report, BXA has had difficulty completing end-use checks in China. In fiscal year 1996, 17 PLCs in China were canceled—seven because the Chinese government would not permit the post to conduct the check, five were returned to the exporter without a final BXA determination, three cases were rejected, and two cases were determined to not require a license. Of the canceled PLCs in countries other than China, the following reasons were given for their cancellation:

- ! The post failed to respond in a timely manner (19 cases).
- ! Applications were returned to the exporter without a final BXA licensing decision or rejected before completion of the PLC (eight cases).

- ! The exporter did not require a license to export the technology (seven cases).
- ! The controlled items were within State's licensing jurisdiction (two cases).
- ! Other reasons—including the federal furlough, a decision to conduct a PSV instead, errors on the application, and checks conducted by export enforcement agents during a Safeguard visit (32 cases).

We found that the overseas posts were generally complying with BXA's guidance for conducting end-use checks. However, the posts need to improve their end-use check processes in several areas. For instance, we found that the posts are not always conducting end-use checks in a timely manner. Also, contrary to BXA's guidance, US&FCS's foreign service nationals (FSNs) often conduct end-use checks without prior BXA approval. In many cases, BXA was unaware of the posts' noncompliance because the posts failed to (1) request or receive a waiver from BXA to use FSNs for end-use checks or (2) properly identify who conducted the checks in response cables to BXA. The posts' response cables also do not consistently state whether an on-site visit was conducted, as required for PSVs and suggested for PLCs. Finally, some posts need to increase the involvement of other embassy agencies in the information gathering process. 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.

A. Timeliness should be improved

Based on our review of a random sample of 152 PLCs completed in fiscal year 1996, only 41 percent of the posts' responses were within BXA's 28-day time frame.⁴ The average PLC response time was 49 days, which is significant because PLCs suspend a decision on an export application until the check is completed. In comparison, of a random sample of 191 PSVs completed in fiscal year 1996, 167 (87 percent) were completed within BXA's 60-day response period. Timeliness of PSVs is important because the threat of diversion increases as time passes, and the results are often used in making future licensing decisions.

Presidential Executive Order No. 12981 governs the processing times for dual-use export applications. The Executive Order requires BXA to make a license determination or refer applications to other federal agencies within nine days of registration of any application. Referral agencies then have 30 days to make a recommendation. All license applications must be resolved

⁴During our review of end-use checks, we conducted two random samples. To determine whether the checks were conducted in a timely manner, we sampled 152 PLCs and 191 PSVs. To evaluate the substantive results of end-use checks, we sampled 39 PLCs and 34 PSVs.

or referred to the President within 90 days of receipt. One of five exceptions to these strict time frames is PLCs. The processing time for a PLC does not count against the Executive Order's time requirements.

In its fiscal year 1996 annual report to Congress, BXA reported that the average processing time for cases that did not require referral was nine days and, for applications that were referred, 30 days. The overall average processing time was 33 days.⁵ Yet these statistics do not take into account the amount of time involved if a PLC was conducted. We believe that applications involving a PLC likely took much longer to complete (on average an additional 49 days), thereby further delaying export of the subject items. Licensing officers claimed that longer processing times often frustrate exporters, who are eager to make a sale, by increasing the possibility that sales will be lost due to failure to deliver when expected.

Some PLC files revealed valid reasons why some of the checks took longer. For example, one post experienced consistent problems with the embassy's communications office not forwarding copies of incoming cables, including end-use check request cables from BXA. In another case, the post reported in an interim cable that they were having problems contacting the subject company or organization. In most of these cases, BXA sent one or more cables reminding the post that a PLC request was outstanding.

To ensure that posts are held accountable for responding to end-use check requests in a timely manner, BXA should send an information copy of all outgoing cables that relate to end-use checks to US&FCS's Office of International Operations. The regional directors, located in this headquarters office, are responsible for overseeing the US&FCS posts overseas, including preparing performance evaluations for the senior commercial officers. US&FCS would then have direct knowledge of which posts are delinquent and can take action to correct their performance.



According to BXA's response to our draft report, "[e]ffective May 1, 1997, procedures were implemented to ensure that all outgoing cables relating to end-use checks are copied to the US&FCS Office of International Operations Regional Directors responsible for the overseas post involved in the check." This action meets the intent of our recommendation.

⁵BXA attributed the increase of average processing times from 30 days in fiscal year 1995 to the backlog of cases that developed during the federal furlough and the increased percentage of cases referred to other agencies.

B. US&FCS usage of foreign service nationals and personal service contractors to conduct end-use checks should be addressed

Several overseas posts are not following BXA's guidance for conducting end-use checks by allowing FSNs to perform the checks. Six of 39 PLC response cables sampled stated that a FSN alone performed the check, but in only one of those cases did the post seek advance approval from BXA. All PSVs within our sample were conducted by American officers or BXA agents on temporary duty or travel. However, during our recent overseas inspections, we found that three of five posts visited used FSNs to conduct PLCs and PSVs. In addition, one of the other posts allowed an American personal service contractor to conduct a check.

The BXA guidance states that it is "BXA's strong policy preference that pre-license checks and post-shipment verifications be performed by [U.S. government] employees who are U.S. citizens unless *extraordinary circumstances* require the use of FSNs." [Emphasis added.] The guidance also lists three disadvantages to having FSNs conduct the checks: (1) the credibility of the check; (2) the possible reluctance of a foreign national to testify against a fellow citizen in a U.S. court; and (3) foreign nationals' lack of access to classified material. Only BXA has the authority to determine whether special circumstances outweigh these concerns.

However, most of the noncompliant posts have neither requested nor received a waiver from BXA to allow FSNs to conduct the checks. If necessary, posts could seek such a waiver from BXA. At the time of this report, BXA had officially permitted only a few posts to use FSNs, but until recently, BXA still accepted end-use checks conducted by FSNs as completed (i.e., favorable or unfavorable). This de facto BXA policy, however, sends noncompliant posts mixed signals. Although one part of the guidance does specifically state that "BXA normally will not consider such checks performed solely by FSNs to be completed checks," other parts of the guidance are a bit more ambiguous. For example, the guidance states that unless BXA approves on a case-by-case exception, FSNs are not to be used (except with a U.S. government employee who is a U.S. citizen) to conduct PLCs and PSVs for nuclear nonproliferation controls, chemical and biological warfare controls, and missile technology controls. However, the guidance does not specifically address this issue for PLCs and PSVs conducted for national security controls, foreign policy controls, and short supply controls—leaving room for some posts to interpret the guidance to allow for FSNs to perform these checks. BXA needs to clarify its policy on the use of FSNs for all end-use checks and reemphasize the need for posts to seek a waiver if they must use FSNs.

In addition, after completing our on-site inspections overseas, we discovered that the US&FCS post in Poland allowed an American personal service contractor to conduct an end-use check. Because this American contractor uses the title "commercial attaché," BXA officials assumed that this individual was a commercial officer and approved the end-use check results. Due to their lack of understanding of US&FCS usage of personal service contractors, BXA officials informed

us that, at this time, personal service contractors, regardless of their citizenship or security clearance, should not perform end-use checks. US&FCS has been relying on personal service contractors to perform an increasing share of core US&FCS functions, such as market research, specialized client services, and business counseling. BXA needs to discuss this matter with US&FCS, especially if US&FCS posts are considering using American contractors in the place of American officers to carry out this work. BXA should establish a formal policy on when, if ever, posts may use contractors to conduct end-use checks. As in the case of FSNs, BXA should consider requiring posts to seek a waiver *before* allowing a contractor to conduct a check.

Despite some posts' noncompliance with this portion of BXA's guidance, our review of the posts' files discovered that an adequate amount of appropriate information-gathering, such as correspondence with the subject company or organization and copies of documentation of the transaction at issue, was conducted during the end-use checks.

BXA's response to our draft report stated that "[i]nitial discussions between BXA and US&FCS Office of International Operations regarding the use of FSNs and personal service contractors to conduct checks took place on July 24, 1997. A worldwide cable providing additional guidance in this area is being drafted and will be cleared by both [US&FCS] and BXA. This cable will be sent by October 31, 1997." This action meets the intent of our recommendation. We would appreciate being informed of BXA and US&FCS's final decision on this matter.

C. Thoroughness of posts' response cables should be improved

Most end-use check responses from the posts include all of the information needed for BXA to make a determination about the outcome of the checks. However, it is also important for BXA to know whether the end-use checks were conducted by an American officer or not and whether an on-site visit was performed in order for OES to determine the reliability of the information gathered. However, as shown in the Table 2, 13 percent of the sampled PLCs did not clearly state whether an on-site visit was performed, while 31 percent of the PLCs and 3 percent of the PSVs did not clearly state whether an American officer or an FSN conducted the check. In addition, during our inspections of the posts in Indonesia and Malaysia, we found that they were not fully identifying the name and position of the individual conducting the checks in the response cables.

**Table 2:
Summary of Information Contained in a
Random Sample of End-use Check Response Cables**

| | Total files reviewed | On-Site review conducted? | | | | | | End-use check conducted by? | | | | | | Canceled before conducted | |
|------------------------|----------------------|---------------------------|------|-----------------|-----|---------|-----|-----------------------------|-----|-----|-----|---------|-----|---------------------------|-----|
| | | Yes | | No ^a | | Unclear | | Officer | | FSN | | Unclear | | | |
| PLC | 39 | 20 | 51% | 7 | 18% | 5 | 13% | 13 | 33% | 7 | 18% | 12 | 31% | 7 | 18% |
| PSV^b | 34 | 34 | 100% | 0 | 0% | 0 | 0% | 30 | 88% | 0 | 0% | 1 | 3% | 3 | 9% |
| Total | 73 | 54 | 74% | 7 | 10% | 5 | 7% | 43 | 59% | 7 | 10% | 13 | 18% | 10 | 14% |

^a Reasons why an on-site was not conducted included: Customs recommended denial based on other policy reasons; the subject company could not be contacted or located; a Blue Lantern on-site check was recently conducted; and the subject party was a prestigious public research institute. In one case, OES approved the end-use check results after further communication with the post.

^b Nineteen of the PSVs during fiscal year 1996 were conducted by export enforcement agents during Safeguard trips and three other PSVs were conducted by agents on temporary duty at the post overseas.

BXA will not normally consider checks conducted solely by FSNs to be complete. Also, on-site visits are mandatory for PSVs and strongly recommended for PLCs. BXA cannot properly determine whether an end-use check was compliant without a clear statement in the response cable indicating who conducted the check and whether an on-site was performed. In our recent overseas inspections reports, we recommended that US&FCS require the posts to specifically state (1) whether an on-site visit was conducted and (2) the name, title, and employment status (e.g., either American officer, FSN, or personal service contractor) of the official who conducted the check, as shown in the sample response cable in the BXA guidance. BXA can also encourage more complete responses from the posts. Currently, OES sends an electronic mail message to posts confirming that a response was received. OES could also use electronic mail to ask posts to clarify incomplete or unclear responses.



BXA stated in its response to our draft report that “[e]ffective September 30, 1997, when a PLC or PSV response does not provide the necessary information to determine whether an on-site visit was conducted or who conducted the check at post, BXA will contact the post to gain complete information on the check.” This action meets the intent of our recommendation.

D. US&FCS posts should involve other embassy agencies

During our recent overseas inspections, we determined that some posts' processes for conducting the checks might be improved by involving other parts of the embassy that may have information about how certain items could be inappropriately used or diverted or about the subject company or organization. While the Germany, Indonesia, and Poland posts routinely coordinated their BXA checks with other agencies at the embassies, the Malaysia and Thailand posts did so irregularly. We recommended to US&FCS that all of the posts review the embassy's Blue Lantern implementation plan, which defines how checks of Department of State controlled items are conducted and which sections of the embassy participate. The Blue Lantern plan may provide additional sources of information for the US&FCS posts to access during end-use checks. Depending on the number of end-use checks conducted each year, we recommended that US&FCS balance on a country-by-country basis the benefit of greater access to information, which could improve the depth of analysis for these checks, with the likely burden on the post or the other sections. We believe that BXA should include a reference to the blue lantern plan or using other embassy agencies in its end-use check guidance to posts.



According to BXA's response to our draft report, "BXA will update its March, 1996 guide, *How to Conduct Pre-License Checks and Post-Shipment Verifications*, to expand the internal resources used in conducting checks to include a check of other embassy agencies prior to initiating the PLC or PSV. The revised guide will be produced and distributed during [fiscal year] 1998." This action meets the intent of our recommendation.

E. Memorandum of Understanding between BXA and US&FCS is needed

As mentioned earlier, our recent draft inspection report to US&FCS entitled, *Recent Overseas Inspections Found US&FCS Delivering Services Effectively But Facing Internal Constraints*, discussed some of our concerns about how end-use checks are conducted overseas. Although we recommended that US&FCS take several actions to correct deficiencies found in its end-use check process, we believe it would benefit both agencies, particularly BXA, to enter into an MOU which would outline specific procedures and responsibilities for end-use checks.

According to Commerce's Department Organization Order 40-1: International Trade Administration, dated March 15, 1996, the Assistant Secretary and Director General of the US&FCS is supposed to coordinate with the Under Secretary for Export Administration for export administration matters through its Office of International Operations. In addition, section 7(b)(5) of the order states that the Deputy Assistant Secretary for International Operations (through US&FCS's overseas posts):

“Conducts pre-license checks and post-shipment verifications for the Under Secretary for Export Administration and provides U.S. firms with counseling on U.S. export control laws and the Export Administration Regulations at US&FCS posts overseas through a memorandum of agreement.”

Despite assurances from several key BXA and US&FCS officials that they were currently operating under an agreement, neither agency could produce an agreement for us. We believe that BXA should meet with US&FCS and develop an MOU or revise the dormant one if it does exist. The MOU should address the concerns raised in this report regarding the conduct of end-use checks by US&FCS personnel. The MOU should also provide a mechanism for BXA to inform US&FCS of problems in order to hold senior commercial officers at posts accountable for following BXA’s guidance in conducting end-use checks. This could be accomplished by notifying the Regional Directors in charge of US&FCS overseas posts when problems arise



Responding to our draft report, BXA stated that it “will initiate discussions with [US&FCS Office of International Operations] and propose the development of an MOU based on the concerns raised in IG report IPE-9524. These discussions will begin by October 31, 1997.” We would appreciate being kept informed of BXA and US&FCS’s progress towards an MOU.

IV. Sharing of End-Use and Enforcement Information Should Be Improved

We found that Export Administration and licensing referral agencies want access to more information on end-use checks and enforcement concerns in order to be better informed when processing applications. Licensing officers often do not understand the nature of Export Enforcement's interests in specific applications or whether a PLC has been initiated, because little information is revealed to them during their review process. Access to a limited amount of additional enforcement information, such as end-use check histories and generic descriptions of enforcement interests, can improve cooperation between Export Enforcement and Export Administration and make the license process more efficient. Some basic changes to the ECASS screen currently available to licensing officials and information management procedures would improve information sharing within BXA and with referral agencies.

ECASS is programmed to inform enforcement agents or analysts when a party of interest to them is included on a new license application. As soon as the application is received and logged into the system, a warning that Export Enforcement has an enforcement interest in one or more parties, called a "screen flag", is placed on the main ECASS screen of the application. A brief reason for the screen flag is also included. For example, OES or OEE may want a PLC the next time a party is involved in an application. The system can be programmed to automatically flag new applications so that the analyst or agent can decide whether to request a PLC. OES can also add a screen flag to a pending case later in the licensing review process if a referral agency or Export Administration requests a PLC or some other enforcement interest arises. As stated previously, a license application is suspended until a PLC is completed.

The system was originally designed to inform Export Enforcement of new applications to allow for their input into licensing decisions, to assist in enforcement actions, and to provide Export Administration and referral agencies with the minimum information necessary about Export Enforcement's interest in applications. We understand that BXA controls access to the enforcement information to protect current and future enforcement actions from unauthorized access, which could lead to use of the information in a way that could jeopardize an investigation. Yet, we believe that minor changes to the system, such as those outlined below, could expand the information available to Export Administration and referral agencies without jeopardizing investigations. Increased access to this information could facilitate the processing of license applications and improve licensing decisions by giving the decision-makers the information they need.

A. OEE and OES should be identified in the application's referral history

ECASS tracks the referral history on each license application by showing the agencies, offices, or personnel who have reviewed the application electronically. The specificity of the identification depends on the office or agency that has reviewed the application and whether there is more than one office within the agency with licensing responsibilities. For internal referrals, the specific Export Administration licensing office and the name of the official is identified, but referral to anyone within Export Enforcement is indicated simply by "OEE." BXA purposely designed ECASS to generically identify all Export Enforcement referrals as "OEE" to prevent the disclosure of any information that would indicate an investigation is in process or planned. Licensing officials expressed concern that this anonymity makes it difficult to locate a knowledgeable Export Enforcement official who can explain why an application is being held.

Although Export Enforcement has a valid concern about unauthorized disclosure of investigative information, the system could be more precise by at least identifying either OEE or OES as the Export Enforcement office that is reviewing an application. This would give Export Administration a more direct point of contact, while protecting the anonymity of the enforcement official who has interest in an application. The main OEE or OES offices can then judge how much information about the enforcement interests should be revealed to the licensing officials.

However, the utility of this action would be limited by how ECASS's referral history is designed. ECASS is programmed to identify a referral to Export Enforcement as having occurred at the end of the process, regardless of when the application was electronically referred to OEE or OES. Therefore, during their review process, licensing officials' only indication that OEE or OES is reviewing an application is the screen flag that appears on the main screen of the application. As discussed below, the screen flag may not provide enough information to the licensing officers. There are additional changes to ECASS that could improve understanding of Export Enforcement's interests in applications throughout the review process.

B. ECASS should show all reasons for screen flags

Currently, ECASS is programmed to show a screen flag and a brief reason for the flag, such as "PLC review" or "routine investigative observation." If there are two or more reasons for the flag, which is common, ECASS only indicates that there is more than one reason (showing the reason "multiple flags"), but does not list the specific reasons.

According to BXA's computer system officials, ECASS can be programmed to list all reasons for screen flags by stringing the comments together on one or more lines or in a smaller field that allows the viewer to scroll through the comments. Alternatively, BXA could program ECASS to show just the reason codes and provide all relevant offices and agencies with a list of the codes

and the associated descriptions of the screen flag reasons (see Appendix 1). Because these descriptions are already shown to Export Administration when there is only one reason for a screen flag, there should be no concern that showing all reasons for a screen flag would jeopardize an investigation. Instead, licensing officers would have a better understanding of the Export Enforcement's concerns that may delay approval of an application or result in a rejection. Licensing officers also can process applications more efficiently since they would no longer have to contact Export Enforcement to determine the reasons for multiple screen flags. We believe that the main ECASS screen should provide *all* reasons why applications are screened.

C. ECASS should identify when PLCs are initiated

We believe that the reason code for "PLC review" should be more explicit. Specifically, this screen flag reason does not necessarily mean that a PLC has been requested; it means that an agent or analyst might request one. We found that licensing officers are often unaware that a PLC has been requested—either because the "multiple flags" reason provides no information about the screen flag or the "PLC review" reason is ambiguous. Licensing officers are interested in knowing if a PLC has been requested so they know that an application will remain pending longer. We understand that ECASS can be programmed to change automatically a "PLC review" reason code to another code, such as "PLC pending," when OES has actually initiated a PLC. Again, a more precise description of the screen flag will improve licensing officers' understanding of Export Enforcement's interests in license applications.

D. Licensing officers should be able to query end-use check histories

The fourth change, which relates to what information is available electronically, would allow Export Administration to search for information on previous end-use checks.⁶ Currently, users with access to ENFORCE can query records to list all previous end-use checks by name, country, date, and other key fields. Enforcement agents and analysts use this information to determine whether another end-use check is needed or as background information for investigations. This information could be useful to others involved in the licensing process as well.

⁶End-use checks are identified as favorable, unfavorable, or canceled. In January 1997, BXA implemented two additional categories for end-use checks—"limited" and "not conclusive." "Limited" refers to checks that were not completed in compliance with BXA's end-use check procedures, such as if an on-site check was not performed or if a FSN completed the check. "Not conclusive" refers to checks that were not completed, but based on other policy considerations, the post included a recommendation for the license application. Because these categories were implemented in fiscal year 1997, we did not review their effect on the end-use check process or BXA's compliance with applicable procedures.

Licensing officers expressed interest in having the ability to do similar searches. They claim that knowing the end-use history on application parties would improve application processing by making them and the referral agencies better informed. For example, for certain commodities and destinations, referral agencies often recommend approval of an application conditional on a favorable PLC. If the licensing officer could inform the referral agencies up-front of the parties' end-use history, BXA could avoid having to go back to referral agencies who recommend approval conditional on a favorable PLC to determine whether another PLC must be performed. In addition, Export Administration could anticipate how long certain applications might take to process by querying end-use check histories to analyze which commodities and destinations are more likely to result in an end-use check.

We understand that BXA can program ENFORCE to allow Export Administration access to end-use check histories. Access to this information should not jeopardize investigations, would expand the knowledge of those making license determinations, and could improve efficiency of application processing.

E. Copies of end-use check response cables should be provided to Export Administration and referral agencies

During interviews with licensing officers and officials of referral agencies, we learned that BXA does not routinely give parties copies of end-use check response cables, even when they request that an end-use check be conducted. OES informs licensing officials that the cables are available for review, but faxes response cables to enforcement personnel when they request end-use checks. We recognize that it is OES's responsibility to analyze end-use check results and recommend license determinations based on that information. However, information revealed during end-use checks can be useful to licensing officers and referral agencies as background for future licensing decisions. Therefore, we believe that OES should fax or mail copies of response cables to those agencies, offices, or members of interagency committees that request end-use checks. Limiting distribution to cases when a check is requested by a licensing officer, referral agency, or interagency committee minimizes the burden on OES, while ensuring that those officials with particular interest in a foreign party have access to this important information.

F. Safeguard trip reports should be more accessible

Licensing officers were unaware that they could review the Safeguard trip reports prepared by Export Enforcement. In fiscal year 1996, Export Enforcement conducted Safeguard visits in eight countries, performing a total of 78 PSVs and no PLCs. Whereas posts report their end-use check results in cables filed with OES, Safeguard trip findings and end-use check recommendations are summarized in comprehensive reports on each country visited. The Safeguard trip reports are filed with OEE's Intelligence Division, but the program is being temporarily managed out of

Export Enforcement's headquarters office. Although access to these reports may be restricted "For Official Use Only" in some cases, Export Enforcement informed us that licensing officers and other Export Administration officials with a need to know can review the reports at any time.

Similar to providing Export Administration with the ability to query end-use check histories, access to Safeguard trip reports can improve the quality of the license application review process by providing the licensing officials with valuable information on parties, commodities, and destinations. Our recommendation to program ECASS to allow licensing officers the ability to query end-use check historical data will give licensing officials access to information on which end-use checks have been performed during Safeguard visits. However, considering the current misunderstanding about whether Safeguard trip reports are accessible by Export Administration, the Director of Export Enforcement should notify all BXA employees with direct responsibilities for licensing decisions that Safeguard trip reports are available for their review. Also, until programming changes are made to ECASS and as the trip reports are completed, Export Enforcement should notify cognizant employees by memorandum or electronic mail that the reports are available and how they can be accessed.

The NPC receives an information copy of all end-use check cables, but it is also interested in reviewing Safeguard trip reports. By reviewing the trip reports, NPC would then have a more complete understanding of the results of end-use checks. We believe that the Director of Export Enforcement should send a copy of all future Safeguard trip reports to NPC.



In its response to our draft report, BXA agreed to implement each of the recommendations relating to sharing end-use and enforcement information through changes in its ECASS database. During the first quarter of fiscal year 1998, BXA agreed to reprogram ECASS to (1) identify whether an application flag is associated with OEE, OES, or both; (2) provide a brief statement of all reasons why an application is flagged; (3) automatically change any flag message in ECASS to "PLC pending" once a PLC has been initiated; and (4) allow licensing officers to query end-use check historical data. In addition, effective October 1, 1997, BXA will implement procedures to ensure a copy of the PLC/PSV response cable is sent to the requesting office in BXA or the requesting agency. Also by that date, OEE will ensure that NPC receives copies of all OEE Safeguard trip reports on a regular basis. Each of these actions are consistent with the intent of our recommendations.

In responding to our recommendation to notify Export Administration on a quarterly basis of recent Safeguard trips and where the trip reports can be reviewed, BXA stated that the programming changes it plans to make will satisfy this recommendation. We agree with this conclusion. However, until programming changes are made to ECASS to allow licensing officers

the ability to query end-use check historical data, the Director of Export Enforcement should notify Export Administration on a quarterly basis of recent Safeguard trips and where the trip reports can be reviewed. We have made appropriate changes to the report and recommendation.

RECOMMENDATIONS

We recommend that the Under Secretary for Export Administration:

1. Draft policies and procedures for using private source watchlists in licensing and enforcement activities.
2. Pursue the development of an MOU with the State Department's Under Secretary for International Security Affairs to formalize a monthly transfer of DTC's watchlist information in an electronic format. The OIG should be kept informed of the progress towards reaching an agreement.
3. Request the Department of Justice to send its list of significant export control cases in an appropriate electronic format, or if BXA decides to continue receiving paper copies of the list, ensure adequate quality control over the inputting of this information into its main application screening database.
4. Accelerate BXA's efforts in obtaining OFAC's list of "Specially Designated Nationals or Blocked Entities" in an electronic format as soon as the new computer system for storing electronic lists has been tested.
5. Amend the 1993 MOU between BXA and Customs to provide for the transmission of names, addresses, and telephone numbers from new pending license applications by BXA to Customs for screening against TECS for at least a one-year trial period. BXA and Customs should discuss the value of this additional information sharing during their established quarterly meetings.
6. Send an information copy of all outgoing cables that relate to end-use checks to US&FCS's Office of International Operations to notify the Regional Directors responsible for the overseas posts of the status of all end-use checks.
7. In consultation with the Assistant Secretary and Director General for US&FCS, develop policy guidance for the overseas posts' use of FSNs to conduct end-use checks. The policy should also address whether and how posts can use American personal service contractors with appropriate clearances to conduct these checks.
8. Communicate more with posts about the clarity and adequacy of end-use check response cables through electronic mail or other appropriate media (e.g., clarify whether an on-site visit was conducted or who at the post conducted the check).

9. Amend current end-use check guidance to recommend that overseas posts use the embassy's blue lantern implementation plan or work with other embassy agencies to expand the internal resources used during end-use checks, when appropriate.
10. Develop an MOU with the Assistant Secretary and Director General for US&FCS to address the concerns raised in this report regarding the conduct of end-use checks by US&FCS personnel. The MOU should also provide a mechanism for BXA to inform US&FCS of problems in order to hold senior commercial officers at posts accountable for following BXA's end-use check guidance.
11. Program ECASS to designate whether Export Enforcement's OEE or OES has a "flag" on an application.
12. Program ECASS to provide a brief statement of *all* reasons why an application is flagged (e.g., PLC review, routine investigation, etc.).
13. Program ECASS to automatically change a "PLC review" code to "PLC pending" once a PLC has been initiated.
14. Program ECASS to provide licensing officers the ability to query end-use check historical data.
15. Provide a copy of posts' end-use check response cables to the requesting office or agency (e.g., the Departments of Defense, State, or Energy).
16. Until programming changes are made to ECASS to allow licensing officers the ability to query end-use check historical data, notify Export Administration on a quarterly basis of recent Safeguard trips and where the trip reports can be reviewed.
17. Send future copies of Safeguard trip reports to the NPC.

APPENDIX 1

**EXPORT ENFORCEMENT'S
AUTOMATED SCREENING CATEGORIES**

| <i>Code</i> | <i>Category</i> | <i>Description</i> |
|-------------|---|--|
| 1 | <i>Routine Investigative Observation</i> | <i>Parties that OEE determines warrant monitoring based on information learned in its investigative activities.</i> |
| 2 | <i>Pre-license Check</i> | <i>Parties added to the list when a pre-license check is requested. Name is removed if the check is satisfactory.</i> |
| 3 | <i>Economic Defense List</i> | <i>Parties believed to divert or misuse U.S. exports.</i> |
| 4 | <i>U.S. Customs</i> | <i>Foreign or domestic parties of concern to U.S. Customs.</i> |
| 5 | <i>Enforcement Concern or Interest</i> | <i>Parties that OES determines warrant monitoring based on information derived from all sources.</i> |
| 6 | <i>Denied Party</i> | <i>Foreign or domestic parties denied U.S. export privileges for violating U.S. export control regulations.</i> |
| 7 | <i>Controlled in Fact Firm</i> | <i>Party that is controlled by sanctioned or embargoed country, such as Libya.</i> |
| 8 | <i>U.S. Treasury-Designated Nationals</i> | <i>Parties identified by the Treasury Department's Office of Foreign Asset Control as nationals of embargoed countries.</i> |
| 9 | <i>Bankrupt, Insolvent, or Out of Business</i> | <i>Firms identified through overseas reporting as no longer doing business or out of business.</i> |
| 10 | <i>International Terrorist Organization</i> | <i>Parties or organizations identified through various sources as possibly supporting international terrorism.</i> |
| 11 | <i>Apartheid Supporting Party</i> | <i>Parties believed to have violated the then South Africa trade embargo.</i> |
| 12 | <i>Targeted U.S. Firm</i> | <i>U.S. parties or firms engaged in the manufacture of especially sensitive items and technologies known to be sought by foreign entities.</i> |
| 13 | <i>South African Foreign Investment</i> | <i>Parties believed to have violated the ban on investment in South Africa.</i> |
| 14 | <i>Past Export Control Violation</i> | <i>Parties in which previous export restrictions have expired or were lifted for other reasons, but that BXA continues to monitor.</i> |
| 15 | <i>Soviet Bloc Trade or Business Representative</i> | <i>Parties identified as being representatives or having close ties with members of the former Soviet Bloc.</i> |
| 16 | <i>Unfavorable Pre-license Check</i> | <i>Parties receiving unfavorable results from Commerce Department pre-license checks.</i> |
| 17 | <i>Unfavorable Post-shipment Verification</i> | <i>Parties receiving unfavorable results from Commerce Department post-shipment checks</i> |
| 18 | <i>Missile Technology Control Regime</i> | <i>Consignees identified as being possibly connected with missile programs of concern.</i> |
| 19 | <i>Nuclear Proliferation</i> | <i>Consignees identified as possibly being connected with nuclear programs of concern.</i> |
| 20 | <i>Space Defense Initiative Technology</i> | <i>Parties engaged in research, design, and development of critical technologies associated with the former Star Wars program.</i> |
| 21 | <i>State/DTC Debarred Parties</i> | <i>Parties prohibited from obtaining export licenses by the Department of State. Names are published in the Federal Register.</i> |
| 22 | <i>Chemical or Biological Warfare Concern</i> | <i>Consignees identified as possibly being connected to chemical or biological warfare programs.</i> |
| 23 | <i>PRC Controlled or Owned</i> | <i>Parties identified as being owned or controlled by the People's Republic of China.</i> |
| 24 | <i>International Drug Trafficking Concern</i> | <i>Parties identified in cable traffic and other sources as possibly being involved in drug trafficking.</i> |
| 25 | <i>Subject of Enhanced Proliferation Control Initiative</i> | <i>U.S. parties that have been informed that a proposed foreign customer is an EPCI Informed Letter concern and that a license is required for the export of certain items.</i> |
| 26 | <i>Subject of Multilateral Control Group Denial</i> | <i>Parties that have been denied licenses by members of multilateral control groups, such as the Australia Group or the Nuclear Suppliers Group, for certain items. Generally referred to as the "no undercut provisions" of the group agreements.</i> |

APPENDIX 2

GLOSSARY OF ACRONYMS

| | |
|--------|---|
| ACDA | Arms Control and Disarmament Agency |
| BXA | Bureau of Export Administration |
| EAA | Export Administration Act |
| EAR | Export Administration Regulations |
| ECASS | Export Control Automated Support System |
| DTC | Defense Trade Controls |
| FSN | Foreign Service National |
| NPC | Nonproliferation Center |
| OEE | Office of Export Enforcement |
| OES | Office of Enforcement Support |
| OFAC | Office of Foreign Asset Control |
| PLC | Pre-license Check |
| PSV | Post-shipment Verification |
| SED | Shipper's Export Declaration |
| TECS | Treasury Enforcement Communication System |
| US&FCS | U.S. and Foreign Commercial Service |


APPENDIX 3



UNITED STATES DEPARTMENT OF COMMERCE
The Under Secretary for Export Administration
Washington, D.C. 20230

September 12, 1997

MEMORANDUM FOR FRANK DEGEORGE

FROM: William A. Reinsch 

SUBJECT: Draft Inspection Report
Export Application Screening Process Could Benefit from Further
Changes (IPE-9524)

Thank you for the opportunity to review this draft report. We believe this to be an excellent report and generally agree with its findings. Attached are our comments and implementation plans for each of your recommendations. Please feel free to give me a call if you have any questions.



Draft Inspection Report
Export Application Screening Process Could Benefit from Further Changes (IPE-9524)
BXA Comments on Recommendations

1. The Office of Enforcement Support (OES) will draft policies and procedures for using private source watch lists in all license review activities by enforcement staff during the first quarter of FY 1998.
2. BXA will contact the State Department's Office of International Security Affairs and initiate discussions to develop an MOU regarding the monthly transfer of State's watch list information in an electronic format.
3. BXA believes that it would be better to continue to receive the Justice list of significant cases in a paper format and enter these parties into its automated watch list database. Since the number of these cases is small (20 cases involving 43 parties in 1996), it requires only a few hours for OES to enter this data into its watch list database. With these parties related to significant export control cases available in BXA's watch list database, all Export Enforcement personnel in headquarters and the field can query the ENFORCE database and be aware of this information. If the information is received electronically and loaded into OES's new open source database, it is only available to OES employees.
4. As of July 21, 1997, OES does receive weekly updates of OFAC's list of "Specially Designated Nationals or Blocked Entities" in an electronic format and maintains this data in its new open source database.
5. While we agree that it is important for policy makers to have all information available to them in order to reach a decision, information exchange must be consistent with established mandates. We believe that the IG recommendation here is not consistent with Executive Order 12981 which reformed the system to process export license applications submitted to the Department of Commerce. EO 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. The effect of the EO changes was to inject accountability, transparency, and timeliness into the export licensing system.

The recommendation of the IG 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 the EO. Referral of license applications to Customs is not the best way to ensure that BXA receives information on parties that is relevant to an export transaction.

We do agree that this important issue should be discussed within the Memorandum of Understanding between Customs and BXA. The MOU currently provides for quarterly meetings. At these meetings, we will remind Customs of its obligation to provide BXA with the relevant information that Customs holds which can be used to screen license applications. This will

accomplish the same end as the IG's recommendation and be consistent with both the EO and the MOU.

Customs agents have the same responsibility as Office of Export Enforcement agents. They must identify those firms and individuals about whom they have developed investigative information that would be relevant to the licensing process. They should give the names of these entities to the Office of Enforcement Support for screening. This is what OEE agents do and this is what Customs agents should do. It is also what the MOU calls for.

6. Effective May 1, 1997, procedures were implemented to ensure that all outgoing cables relating to end-use checks are copied to the US&FCS Office of International Operations Regional Directors responsible for the overseas post involved in the check.

7. Initial discussions between BXA and US&FCS Office of International Operations regarding the use of FSNs and personal service contractors to conduct checks took place on July 24, 1997. A worldwide cable providing additional guidance in this area is being drafted and will be cleared by both FCS/OIO and BXA. This cable will be sent by October 31, 1997.

8. Effective September 30, 1997, when a PLC or PSV response does not provide the necessary information to determine whether an on-site visit was conducted or who conducted the check at post, BXA will contact the post to gain complete information on the check.

9. BXA will update its March, 1996 guide, *How to Conduct Pre-License Checks and Post-Shipment Verifications*, to expand the internal resources used in conducting checks to include a check of other embassy agencies prior to initiating the PLC or PSV. The revised guide will be produced and distributed during FY 1998.

10. BXA will initiate discussions with FCS/OIO and propose the development of an MOU based on the concerns raised in IG report IPE-9524. These discussions will begin by October 31, 1997.

11. During the first quarter of FY 1998, BXA will initiate the programming changes necessary within ECASS to identify whether an application "flag" is associated with OEE, OES, or both.

12. During the first quarter of FY 1998, BXA will initiate the programming changes necessary to provide a brief statement of all reasons why an application is "flagged."

13. During the first quarter of FY 1998, BXA will initiate the programming changes necessary to automatically change any "flag" message in ECASS to "PLC pending" once a PLC has been initiated.

14. During the first quarter of FY 1998, BXA will initiate the programming necessary to allow licensing officers to query end-use check historical data.

15. Effective October 1, 1997, procedures will be put in place by OES to ensure a copy of the PLC/PSV response cable is sent to the requesting office in BXA or the requesting agency (DOD, DOS, DOE).

16. This recommendation is resolved with BXA's proposed action for item 14 above. All safeguard trip information is maintained in the section of ECASS that also contains end-use check historic information. Thus, all Export Administration employees will be able to access this safeguard trip information at any time they want.

17. Effective October 1, 1997, the Office of Export Enforcement will ensure that NPC receives copies of all OEE Safeguard trip reports on a regular basis.