Statement by

Mr. Donald Mancuso

Deputy Inspector General
Department of Defense

before the

Senate Committee on Armed Services

on

The National Security Implications of Export Controls and the Export Administration Act of 1999

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to discuss the Federal Government's export licensing processes for militarily sensitive commodities and technology. As you know, in response to a request from the Senate Committee on Governmental Affairs, Inspector General teams from the Departments of Commerce, Defense, Energy, State, Treasury and the Central Intelligence Agency reviewed a series of issues related to export controls for both dual-use items and munitions. The results were contained in an interagency report and six individual agency reports issued in June 1999. Some of those results are pertinent to the ongoing dialogue on renewing the Export Administration Act of 1979 and I will recap the principal findings as a prelude to commenting on S.1712, the Export Administration Act of 1999.

Interagency Inspector General Review

Dual-use commodities are goods and technologies with both military and commercial applications. The current dual-use export licensing process was established by the Export Administration Act of 1979, as amended. Although the Act expired in 1994, its provisions are continued by Executive Orders 12924, "Continuation of Export Control Regulations," and 12981, "Administration of Export Controls," under the authority of the International Emergency Economic Powers Act. Munitions exports are controlled under the provisions of the Arms Export Control Act.

The dual-use export licensing process is managed and enforced by the Department of Commerce, while the Department of State manages munitions export licensing. The Departments of Defense and Energy review the applications and make recommendations to Commerce and State. The Central Intelligence Agency and the U.S. Customs Service provide relevant information to Commerce and State. Customs also enforces licensing requirements for all export shipments except outbound mail, which is handled by the Postal Service. In FY 1998, the Department of Commerce received 10,696 dual-use export license applications and the Department of State received 44,212 munitions export license applications.

The overall objective of the interagency review was to determine whether current practices and procedures were consistent with established national security and foreign policy objectives. To accomplish this objective, we reviewed various random samples of licensing cases to determine if prescribed processing procedures were followed within each agency and in multi-agency groups.

Our June 1999 interagency report included findings in seven areas.

The first area related to the adequacy of export control statutes and executive orders. We concluded that, in general, the Arms Export Control Act and the provisions of the Export Administration Act, as clarified by Executive Order 12981, were consistent and unambiguous. However, the Commerce and Defense IG teams stressed that the dual-use licensing process would be best served if the Export Administration Act were reenacted, rather than to continue to operate under a patchwork of other laws and executive orders. Executive Order 12981 was generally consistent with the Export Administration Act; however, the Order required modification to reflect the merger of the Arms Control and Disarmament Agency with the Department of State and to clarify representation at the Advisory Committee on Export Policy. In addition, policy and regulations regarding the export licensing requirements for items and information "deemed to be exports" needed clarification, and the exporter appeals process should be formalized.

The second area pertained to procedures used in the export license review processes. The Commerce, Defense, Energy and State IG teams concluded that processes for the referral of dual-use license applications and interagency dispute resolution were adequate. Officials from those Departments were generally satisfied with the 30-day time limit for agency reviews under Executive Order 12981; however, not every agency could meet that limit. Several Defense organizations and the CIA indicated they would benefit from additional time to review dual-use license applications. The Defense and State IG teams were satisfied with the referral of munitions license cases for review; however, the Commerce IG team believed that inclusion of the Department of Commerce in the munitions case referral process should be considered. Conversely, the Commerce commodity classification process could benefit from additional input on munitions-related items from the Departments of Defense and State. Also, Energy officials believed a more formal review process for munitions was needed, as the officials were unclear on their role in the current process.

The third area pertained to the cumulative effect of multiple exports to individual foreign countries. The U.S. Government lacks an overall mechanism for conducting cumulative effect analysis. Some of the agencies involved in the export licensing process performed limited cumulative effect analyses, but to varying degrees. The Commerce, Defense, Energy and State IG

teams concluded that additional cumulative effect analysis would benefit the license application review process.

The fourth area was information management. The Commerce, Defense and State IG teams questioned the adequacy of the automated information systems their Departments use to support license application reviews. Specifically, there were shortfalls in data quality, system interfaces, and modernization efforts. The audit trails provided by most of the respective export licensing automated databases were adequate, but Defense procedures did not ensure that final Defense positions were accurately recorded. The CIA IG team reported unsatisfactory documentation of end-user checks on munitions license applications.

The fifth set of issues concerned guidance, training and alleged undue pressure on case analysts by their supervisors. The review indicated that Defense, Energy and State licensing officials had adequate guidance to perform their mission; however, Commerce licensing officers and CIA licensing analysts could benefit from additional guidance. The Commerce, Defense and State IG teams identified a need for standardized training programs in their agencies. With very few exceptions, Commerce and Defense licensing officials reported they were not improperly pressured by their supervisors to change recommendations on license applications. No Energy or State export licensing officials indicated they were pressured regarding their recommendations.

The sixth area concerned monitoring compliance and end-use checks. The Department of Commerce did not adequately monitor reports from exporters on shipments made against licenses, and the Department of State’s end-use checking program could be improved. The Departments of Commerce and State used foreign nationals to conduct an unknown number of end-use checks. The Commerce IG team found that most end-use checks were being conducted by U.S. and Foreign Commercial Service officers or Commerce enforcement agents. The State IG team concluded it may be appropriate to use foreign nationals to do the checks under certain conditions.

The seventh area was export controls enforcement. The Treasury IG team determined that, although Customs Service export enforcement efforts have produced results, the Customs Service was hindered by current statutory and regulatory reporting provisions for exporters and carriers. The Treasury IG team

also identified classified operational weaknesses in Custom's export enforcement efforts.

The IG teams made specific recommendations relevant to their own agencies. Those recommendations and management comments are included in the separate reports issued by each office.

Department of Defense IG Report

Now I would like to change focus from the interagency report to the report issued by my office. Although our report addressed 14 separate issues posed by Chairman Thompson's August 1998 request, for this testimony I will cover only those that relate to the Export Administration Act.

One issue was to examine relevant legislative authority.

The general nature of the Export Administration Act and the Arms Export Control Act creates a broad framework, but we found no inconsistencies or ambiguities in either law. We concluded that the dual-use licensing process would be best served through reenactment of the Export Administration Act.

A second issue was to review Executive Order 12981.

We found that the Executive Order, as implemented, is generally consistent with the objectives of the Export Administration Act. However, the Executive Order decreased from 40 to 30 days the time that the Department has to review license applications. As a result of the shortened review period, there were indications that the Department's ability to locate the information needed for adequate license review may have been diminished.

A third issue was whether Commerce was properly referring export license applications for review by other agencies.

Defense officials expressed general satisfaction with referrals from Commerce, although Defense officials disagreed with Commerce's decision not to refer 5 of 60 sampled dual-use item applications. They also expressed concern that Commerce referred too few commodity classification requests to Defense for review. The commodity classification process matches a prospective export item with an export control classification number. Those numbers indicate whether an export license is required. In FY 1998, exporters submitted 2,723 commodity classification requests containing 6,161 line items to Commerce, which referred a mere 12 requests to Defense for review. I will

discuss our concern regarding the commodity classification process in more detail when I address S.1712.

A fourth issue concerned the interagency dispute resolution process for appealing disputed license applications.

With one possible exception, we found that the interagency escalation process gave Defense a meaningful opportunity to appeal disputed dual-use license applications, although the outcome of the process often favored the Commerce position. Defense elected not to escalate some disputed dual-use applications after weighing such considerations as the substance of the case, the viewpoints expressed by Department principals and the likelihood of prevailing at the Advisory Committee on Export Policy. Disputes over munitions applications were resolved between office chiefs at Defense and State.

Other issues related to whether the current licensing processes adequately took into account the cumulative effect of technology transfers.

We found that the licensing process at the Defense Threat Reduction Agency occasionally took into account cumulative effect, but participants in the licensing process did not routinely analyze the cumulative effect of proposed exports or receive assessments to use during license reviews. In addition, Defense organizations did not conduct required annual assessments that could provide information on the cumulative effect of proposed exports. The Defense Threat Reduction Agency has initiated actions designed to increase the degree to which cumulative effect analysis is incorporated into the licensing process. We recognize that organizing and resourcing a meaningful cumulative effect analysis process poses a significant challenge, but conclude that this is clearly an area warranting more emphasis.

As a result of our review, we made numerous recommendations to the Department to improve the effectiveness and efficiency of export licensing review efforts. In this regard, we recommended that the Department take measures to clarify responsibility for cumulative effect analysis, improve management information systems and revise internal procedures so as to make better data available to licensing officials. Additional recommendations involved such things as improved training and enhanced coordination with State and Commerce.

The Department was generally responsive to our findings and recommendations and a range of agreed-upon actions have been initiated. Meanwhile, however, the Department also has been responding to increasing concerns from allies, U.S. exporters and various officials throughout the Government that the current export licensing review processes are too cumbersome and insufficiently focused. Wide-ranging efforts are currently under way to reengineer those processes. The Office of the Inspector General, DoD, is not yet directly involved in those efforts, but we are monitoring them with interest and tracking progress through our standard audit follow-up process. In addition, we are completing the first of seven annual interagency audits of export control issues mandated by Section 1402 of the National Defense Authorization Act for Fiscal Year 2000. In conjunction with the Inspectors General of Commerce, Energy and State, we plan to issue our reports by March 31, 2000. This year, our reports will focus on "deemed exports" and counterintelligence issues.

Comments on S. 1712

In commenting on S.1712, I emphasize that these views are those of the IG, DoD, and do not necessarily reflect the positions of DoD managers or the managers and IGs of other Federal agencies.

As previously mentioned, we believe there is a clear need to reenact the Export Administration Act. During the two decades since that law was enacted, commercial technologies and products have become vastly more applicable to military systems and capabilities, especially in the information technology arena. It is vital for our national security that the export control regime for dual-use commodities be firmly grounded in a comprehensive, clear and up to date statute. We further believe that S.1712 is a good start toward such a statute; however, it could be improved in a few areas. We respectfully offer the following suggestions.

License Exceptions

Section 101 of S.1712 allows an exporter to file an advanced notification of intent to export in lieu of a license application, in circumstances to be outlined in Department of Commerce regulations. Additionally, this section allows the Secretary of Commerce to grant authority to export an item on the Control List without prior license or notification in lieu of a license--a license exception.

We believe it would best serve the national interest to keep the license exception authority fairly limited. Either the bill or implementing regulations should specify that certain high-risk items, for example encryption technology and jet engines, never should be exported without an export license, regardless of destination. Those items also should not be subject to the foreign availability and mass-market criteria outlined in Section 211 of S.1712, which is discussed later in this statement.

Authority for National Security Export Controls

Section 201(c) of S.1712 states "controls may be imposed, based on the end use or end user, on the export of any item, that could materially contribute to the proliferation of weapons of mass destruction." The addition of the word "materially" weakens the standard and is subject to interpretation. Moreover, the cumulative impact of multiple releases that individually appear immaterial could be significant. We recommend that the term “materially” be deleted.

National Security Control List

The Export Administration Act of 1979 required that a list of militarily critical technologies be integrated into the overall Control List of items requiring an export license. Any disagreement between the Secretary of Commerce and Defense regarding the integration of an item on the list of militarily critical technologies into the control list was to be resolved by the President.

Section 202 of S.1712 prescribes a new National Security Control List. The Secretary of Commerce is authorized to establish and maintain the National Security Control List, although inclusion of items on the list requires the concurrence of the Secretary of Defense. The Secretary of Commerce, in establishing and maintaining the National Security Control List, is required to "balance the national security risks of not controlling the export of an item against the economic costs of controlling the item.” We feel that the Secretary of Defense should have more than just a consultative role in both establishing and maintaining the list and in balancing the risk to national security against economic costs of controlling the item. Additionally, it is important to delineate how disagreements between the Secretary of Commerce and Defense are to be resolved. Similar issues pertain to modifications to the list under Section 205.

Determination of Foreign Availability and Mass-Market Status

Section 211 of S.1712 gives to the Department of Commerce and commercial enterprise (by petition) the authority to determine if an item has foreign availability or mass-market status. If an item is determined to have this status, it is to be removed from the Commerce Control List and National Security Control List, making it no longer subject to export controls. According to the procedures outlined in this section, an interested party can petition the Secretary of Commerce for a determination that an item has a foreign availability or mass-market status. In evaluating the petition, the Secretary of Commerce is required to consult with the Secretary of Defense and other appropriate agencies. However, that is the extent of the Department of Defense role in the process.

The Secretary of Commerce also is given unilateral authority to establish the procedures and criteria to be used in determining whether an item has foreign availability or mass-market status (there is some very vague and subjective criteria outlined in Section 211). Thirty days after a notice of determination is published in the Federal Register, the item would be removed from the National Security Control List. The Secretary of Defense would have no recourse if he or she does not agree with the Secretary of Commerce's determination that the item should no longer be subject to export controls. In our opinion, this section needs to be changed to provide the Secretary of Defense a much stronger role in determining the propriety of removing items from export controls for any reason, including claimed foreign availability or mass-market status.

Export License Procedures

Section 501(b)(2)(A)(ii) of S.1712 could be interpreted to read that a referral of a dual-use license application to the Secretary of Defense for review is discretionary. In Executive Order 12981, “Administration of Export Controls,” the President prescribed additional procedures for export license applications submitted under the Export Administration Act of 1979. Among other things, those procedures required the Department of Commerce to refer all dual-use license applications to the Department of Defense. We believe those procedures should be continued in the proposed Export Administration Act of 1999. Section 501 should be changed to require that all applications, unless otherwise delegated by the Secretary of Defense, be referred to the Secretary of Defense for review.

Section 501(a)(3) of S.1712 indicates that the time period for reviewing applications is based on calendar days. Section 501(c)(4) provides that a department must review matters for which referral is made within 25 days, which translates to approximately 18 working days. In our previous review of the export licensing process, we determined that 30 days was often insufficient for coordination within the Department of Defense and could result in an inadequate review. Recognizing that the Department of Defense is attempting to streamline its internal administrative processes, nevertheless we remain concerned that statutorily mandated timeframes that are too aggressive would result in poor quality reviews and unacceptable risk. Therefore, we believe that the time period for initial review should be at least 30 days, as currently provided for in Executive Order 12981.

S.1712 does not provide for allowance of additional time in noteworthy cases. A provision should be added that, if the Secretary of Defense requests an additional period of time in which to evaluate an application on grounds of national security, the Secretary of Commerce should grant an extension of 25 days.

Commodity Classification Requests

Section 501(h)(1) of S.1712 requires the Secretary of Commerce, upon receiving a written request for the commodity classification of an item on the Control List, to "promptly notify" the Secretary of Defense and other departments and agencies of the request. The section does not further define the role of the Department of Defense. As identified in our 1999 report on the Defense export licensing process, an interagency process is needed in determining the commodity classification of an item on the Control List, so that all perspectives can be considered. S.1712 should be modified to provide for such an interagency process.

Last year, as part of the joint IG review, the Commerce and Defense teams asked officials from those Departments to jointly examine 13 commodity classification decisions previously made by Commerce without Defense input. The officials agreed that Commerce had properly classified 4 items and misclassified one item. There were varying degrees of disagreement on the other 8 decisions. For example, Defense officials questioned a Commerce decision regarding a ruggedized, portable, encrypted radio. Commerce officials stated that the radio had not been built to military standards and therefore was not a munitions

item under the jurisdiction of the International Traffic in Arms Regulations. Defense officials stated that literature described the radio as militarized and that other radios built by the manufacturer were subject to munitions export licenses. The second request was for an antenna. Commerce officials stated that the antenna was not a munitions item, despite company literature describing it as militarized. Defense officials stated that the literature satisfied International Traffic in Arms Regulations criteria for a "defense article" (munitions) and that the manufacturer had a history of exporting products under the munitions export licensing process.

Anecdotal evidence provided to the auditors suggests that Commerce could make incorrect commodity classification decisions if it does not receive Defense advice on those decisions. In 1995 and 1997, Commerce decided that microchannel plates (used in night vision devices) fell under the Export Administration Regulations even though Commerce, Defense and State had decided in 1991 that this type of item fell under the jurisdiction of the International Traffic in Arms Regulations. In 1995, Commerce determined that a U.S. aerospace company's accident report on a failed Chinese rocket launch that contained technical data fell under the Export Administration Regulations rather than the International Traffic in Arms Regulations. In 1996, Commerce determined that a protective suit fell under the Export Administration Regulations, while Defense and State held that it was a chemical and biological defensive suit subject to the International Traffic in Arms Regulations.

I do not have a basis for affirming which position was correct in these cases; however, I believe it is clear that these are difficult decisions and the full range of opinion from various elements of the Government ought to be elicited and considered.

We believe Section 501 should require that the Department of Commerce promptly refer commodity classification requests for Defense review and allow a reasonable time period for Defense to review those referrals. If there is no agreement on the commodity classification, an interagency dispute resolution process should be initiated to determine the final outcome.

Interagency Dispute Resolution Process

Executive Order 12981 establishes dispute resolution procedures to include escalation procedures and timelines for disputed dual-use cases. Included in the Executive Order are provisions for the Secretary of Defense to elevate issues to the President.

This authority is contained in the Section 502 of S.1712, but the provision is somewhat unclear and could be subject to interpretation. Therefore, we recommend an additional separate section to allow the Secretary of Defense to escalate an application dispute to the President for final resolution. Even if this appeal channel is seldom used, its existence would be beneficial as a safeguard for the national interest.

Enforcement

Section 607 of S.1712 appears to enact the same law enforcement authorities that were contained in the Export Administration Act of 1979. However, section 607(a)(2)(A) could be interpreted to allow the head of other departments or agencies the authority to convey the same, more extensive, law enforcement authorities as are enjoyed by Department of the Treasury (Customs) and the Department of Commerce in this area. To avoid confusion, section 607(a)(2)(A) should be modified to reflect that this Act only authorizes officers and employees of departments and agencies other than Customs, or other than those designated by the Secretary of Commerce, to exercise the enforcement authority provided in Section 607(a)(3)(A).

Summary

The Office of Inspector General, DoD, strongly supports the enactment of a new Export Administration Act. This vital area deserves a comprehensive statutory framework that clearly prescribes the roles and responsibilities of all interested Departments and Agencies. We believe that S.1712 should be strengthened by providing an increased role for the Secretary of Defense, in partnership with the Secretary of Commerce, in the ongoing effort to balance national security and economic needs as we move forward in the coming years.