United States Government Accountability Office

GAO

Report to the Chairman, Committee on International Relations, House of Representatives

February 2005

DEFENSE TRADE

Arms Export Control System in the Post-9/11 Environment

GAO-05-234

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Arms Export Control System in the Post-9/11 Environment

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Highlights

Highlights of GAO-05-234, a report to the Chairman, Committee on International Relations, House of Representatives

Why GAO Did This Study

The U.S. government controls arms exports by U.S. companies to ensure that such exports are consistent with national security and foreign policy interests. There have been various efforts to change the arms export control system, which is overseen by the State Department. One effort was the Defense Trade Security Initiative of 2000, which was intended to facilitate defense trade with allies in the post-Cold War environment. Given the September 2001 terror attacks, the U.S. government has had to reevaluate whether existing policies support national security and foreign policy goals.

In light of the September 2001 attacks, GAO was asked to review several aspects of the arms export control system. Specifically, GAO is providing information on (1) changes in the arms export control system since September 2001 and overall trends in arms export licensing, (2) extent of implementation of or revision to initiatives designed to streamline arms export licensing, and (3) extent of coordination on these initiatives between State and arms export enforcement agencies, as well as enforcement efforts.

What GAO Recommends

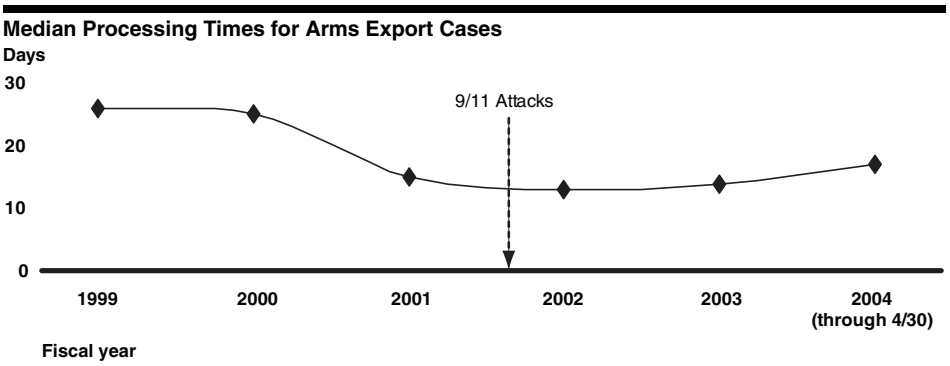
GAO is not making recommendations in this report. State disagreed with information contained in the report, while the Departments of Defense and Homeland Security generally agreed with the report.

www.gao.gov/cgi-bin/getrpt?GAO-05-234.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Katherine Schinasi at (202) 512-4841 or schinasik@gao.gov.

What GAO Found

Since the September 2001 terror attacks, the arms export control system has not undergone fundamental changes. While the system essentially remains unchanged, new trends have emerged in the processing of arms export cases. The median processing time for export license applications and related cases began increasing in fiscal year 2003.



Source: GAO analysis of State data.

State and Defense, which reviews export licenses, have continued to implement through regulations and guidance several initiatives primarily designed to streamline the processing of arms export licenses. According to State officials, they have not evaluated the effects of these initiatives on the export control system or revised the initiatives. However, applications processed under these initiatives have generally not been processed within the time frames established by State and Defense. For example, applications for Operation Iraqi Freedom are to be processed in 4 days if they require interagency review, but the median processing time for these applications in the first 7 months of fiscal year 2004 was 22 days. Also, exporters have not widely used several of these initiatives.

State has sought limited coordination with the agencies responsible for enforcing U.S. arms export laws—the Departments of Homeland Security and Justice—regarding the initiatives designed to streamline arms export licensing. The only exceptions have been regarding proposed export licensing exemptions. Enforcement officials have raised concerns regarding licensing exemptions, including difficulties in enforcing the proper use of exemptions and the increased risk of diversion. According to enforcement officials, they face a number of challenges associated with arms export enforcement efforts, such as limited resources to conduct inspections and investigations and other difficulties in obtaining a criminal conviction for export violations.

Contents

Abbreviations

AECA	Arms Export Control Act
AES	Automated Export System
BIS	Bureau of Industry and Security
CBP	U.S. Customs and Border Protection
CIA	Central Intelligence Agency
DCI	Defense Capabilities Initiative
DDTC	Directorate of Defense Trade Controls
DTSA	Defense Technology Security Administration
DTSI	Defense Trade Security Initiative
FTE	full-time equivalent
GPA	Global Project Authorization
ICE	U.S. Immigration and Customs Enforcement
JSF	Joint Strike Fighter
NATO	North Atlantic Treaty Organization
OEF	Operation Enduring Freedom
OIF	Operation Iraqi Freedom

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United States Government Accountability Office
Washington, DC 20548

February 16, 2005

The Honorable Henry J. Hyde
Chairman
Committee on International Relations
House of Representatives

Dear Mr. Chairman:

Exports of arms[1] by U.S. companies are controlled by the U.S. government to help ensure that such exports are consistent with U.S. national security and foreign policy interests. The Department of State oversees arms export controls and has responsibility for licensing arms exports. Over the years, there have been various efforts to change the arms export control system. One such effort was the Defense Trade Security Initiative (DTSI) of 2000,[2] which was characterized as the first major post-Cold War adjustment to the arms export control system and an effort to facilitate defense trade with our allies. Given the terror attacks of September 11, 2001, the U.S. government has had to reevaluate whether existing policies support national security and foreign policy goals.

In light of the events of September 11, 2001, you requested that we assess several aspects of the arms export control system. In November 2004, we briefed your staff on the results of our work to date. This report provides that briefing with updates and expanded explanations (see app. I). Specifically, we are furnishing information on (1) changes in the arms export control system since the September 2001 terror attacks and overall trends in arms export licensing, (2) extent of implementation of or revision to initiatives designed to streamline arms export licensing, and (3) extent of coordination regarding these initiatives between State and arms export enforcement agencies, as well as enforcement efforts.

To determine changes in the export control system and the status of initiatives, we interviewed State and Department of Defense officials, as

[1] For the purposes of this report, "arms" refers to defense articles and services as specified in 22 U.S.C. 2778.

[2] For additional information on DTSI, see GAO, *Defense Trade: Analysis of Support for Recent Initiatives*, GAO/NSIAD-00-191 (Washington, D.C.: Aug. 31, 2000).

well as reviewed applicable laws, regulations, and other guidance. We also analyzed State export license application data covering October 1, 1998, through April 30, 2004, to identify trends in licensing and evaluate the implementation of initiatives. To assess the reliability of the data, we compared randomly selected license application files to the information in State's licensing database. While we identified inaccuracies in the database, we determined that the data are sufficiently reliable for the purposes of this report. To determine the extent of coordination between State and enforcement agencies, we interviewed officials and obtained supporting documents from the Department of Justice, the Department of Homeland Security's U.S. Customs and Border Protection and U.S. Immigration and Customs Enforcement, State, and Defense. We also obtained and analyzed data from Homeland Security and State regarding enforcement actions. See appendix II for a more detailed discussion of our scope and methodology. We conducted our work from April 2004 through January 2005 in accordance with generally accepted government auditing standards.

Summary

The arms export control system has not undergone fundamental changes since the September 2001 terror attacks. State has not made significant changes to its arms export control regulations or proposed statutory changes in response to the terror attacks. According to a senior State official, such changes were not needed because the system was already designed to counter the threats that emerged after September 2001. While the system itself remains basically unchanged, new trends have emerged in the processing of arms export cases.[3] Median processing times[4] for all arms export cases declined between fiscal years 1999 and 2002, but began increasing in fiscal year 2003 with this upward trend continuing into the first 7 months of fiscal year 2004. A senior State official informed us that median processing times increased in fiscal year 2004 when State licensing officers resumed fulfilling the requirement to screen all parties listed on export license applications against the department's watchlist of entities

[3] Cases include applications for the permanent export of arms, the temporary export and import of arms, and agreements between U.S. industry and foreign entities to provide technical assistance or manufacturing capability, as well as requests for amendments to existing licenses and jurisdiction determinations.

[4] The median processing time is the point at which 50 percent of the cases took more time and 50 percent less time. We are reporting the median processing time because the average or mean processing time can be significantly affected by a small number of cases that had much longer review times than the majority of cases.

of concern. While the resources State devoted to arms export controls have generally increased since fiscal year 2000, the department has transferred some of its licensing resources to other functions. For example, between fiscal years 2003 and 2005, five licensing officer positions were transferred to policy and management functions.

State and Defense[5] have continued to implement, through regulation and guidance, initiatives primarily designed to streamline and expedite the processing of arms export license applications. According to State officials, they have not evaluated the effects of the initiatives on the export control system or revised these initiatives, stating that DTSI and related initiatives remain relevant in the aftermath of September 2001. However, license applications processed under the various initiatives have generally not been processed within the time frames established by State and Defense. For example, the departments established an expedited process for reviewing license applications in support of Operation Iraqi Freedom with the goals of processing nonstaffed applications within 2 days or, if they are staffed for interagency review, within 4 days. However, in the first 7 months of fiscal year 2004, the median processing times were 7 days for nonstaffed Operation Iraqi Freedom applications and 22 days for staffed applications. Further, several initiatives have not been widely used by exporters. For example, exporters have only submitted three applications for the comprehensive export authorizations to provide advance approval for a range of exports associated with transnational defense efforts.

State has sought limited coordination with the agencies responsible for enforcing U.S. arms export laws—Homeland Security and Justice—regarding initiatives designed to streamline arms export licensing. According to Homeland Security and Justice officials, they have only been consulted on how proposed export licensing exemptions might affect enforcement efforts. These officials told us that export licensing exemptions increase the risk of diversion and complicate enforcement efforts. According to enforcement officials, they face a number of challenges associated with arms export enforcement including limited resources to conduct inspections and investigations and other difficulties in obtaining a criminal conviction for export violations.

[5] State refers, or staffs, a portion of the cases it processes to Defense for technical and national security reviews.

Agency Comments and Our Evaluation

In written comments on a draft of this report, State criticized the report for not reflecting various arms export control-related initiatives that the department, in its words, has "successfully undertaken." State acknowledged increased license application processing times, but cited several activities that it has taken to ensure that defense exports further foreign policy and national security objectives. Additionally, State characterized statements in our report as inaccurate or misleading. Specifically, State contends that our report implies significant changes to the arms export control regulations should have been made following the September 2001 terror attacks and that the department has been indifferent to those attacks. Further, State questioned the need for coordination with law enforcement agencies beyond the coordination that occurred regarding the proposed exemptions. Finally, the department concluded that our evaluation of the initiative to expedite Operation Enduring Freedom applications included cases not identified as such by State and, therefore, did not receive expedited processing. State's comments are reprinted in appendix III, along with our evaluation of them.

We disagree with State's characterization of our report. We identified numerous arms export control initiatives, including those cited by State as being ignored, and evaluated those initiatives for which data were available. As we reported, license applications processed under the various initiatives have generally not been processed within the time frames established by State, and several initiatives have not been widely used by exporters. We are, therefore, uncertain of the basis for State's assertion that it has successfully undertaken initiatives, particularly since State has not evaluated the initiatives' effects on the arms export control system and has not provided data supporting its contention. Our report does not imply that changes should have been made following the September 11, 2001, terror attacks. Rather, it clearly states what has or has not occurred in terms of changes to the arms export control system since those attacks. During the course of the audit, senior State officials confirmed that State has not offered legislative proposals to change the arms export control system or made major revisions to its export control regulations in response to September 2001 attacks. Further, our report cites a senior State official's explanation as to why State did not think such changes were needed. Regarding State's coordination with law enforcement agencies, our report accurately describes the extent of coordination and provides State's explanation as to why it limited coordination to the exemption-related initiatives. Finally, State's conclusion about our analyses of Operation Enduring Freedom applications is inaccurate. As explained in our scope and methodology, we used unique identifiers entered into State's licensing database to identify

applications processed under various initiatives, including the Operation Enduring Freedom initiative. Thus, information in this report regarding the number of Operation Enduring Freedom applications and their associated processing times is based on our analyses of applications identified by State as Operation Enduring Freedom.

In its written comments on a draft of this report, Defense stated it generally agreed with the report. Based on an analysis of its own licensing data, Defense stated that its median processing times were lower than those presented in our report. Defense explained that the differences between its median processing times and ours can be attributed, in part, to a lag between when State decides to refer cases and when Defense begins its review. Additionally, Defense noted discrepancies with how State identified cases related to Operations Enduring Freedom and Iraqi Freedom for special processing when staffed to Defense. According to Defense, in some instances, State staffed cases to Defense for special processing, but those cases were not coded as Operations Enduring Freedom or Iraqi Freedom in State's database. In other instances, cases were coded in State's database as Operations Enduring Freedom or Iraqi Freedom, but were not processed in an expedited manner by either State or Defense. Finally, Defense indicated that State did not rigorously screen cases before staffing them to Defense for special processing under the Operations Enduring Freedom and Iraqi Freedom initiatives. According to Defense, State identified cases for special processing even though they did not involve material for U.S. forces and coalition partners engaged in operations. Defense's comments are reprinted in appendix IV, along with our evaluation of them.

Processing times presented in our report are based on our analyses of State's licensing data for both staffed and nonstaffed cases—as acknowledged by Defense. Because we did not analyze Defense's data nor assess its reliability, we cannot verify the accuracy of the data presented in Defense's comments. We already acknowledged Defense's explanation regarding a lag between when State decided to staff cases and when Defense began its review. However, regardless of the reasons for delays, transit times add to the overall time it takes for an exporter to be provided with a final determination. Additionally, information contained in the report regarding the number of applications related to Operations Enduring Freedom and Iraqi Freedom staffed to Defense and their associated processing times is based on our analyses of applications identified by State as related to the two operations. We cannot validate the discrepancies Defense identified regarding these applications as we did not review Defense's files or assess their accuracy or completeness.

However, based on comments from both State and Defense, it appears that there is a lack of agreement and consistency as to which applications should be processed under the initiatives for Operations Enduring Freedom and Iraqi Freedom.

In written comments on a draft of this report, Homeland Security expressed appreciation for GAO's work related to enforcement challenges. Homeland Security also clarified information previously provided to GAO and made technical comments, which we have incorporated into our report. Additionally, the department elaborated on U.S. Customs and Border Protection's participation in the arms export control system. Homeland Security's comments are reprinted in appendix V.

Justice also reviewed a draft of this report and had no comments.

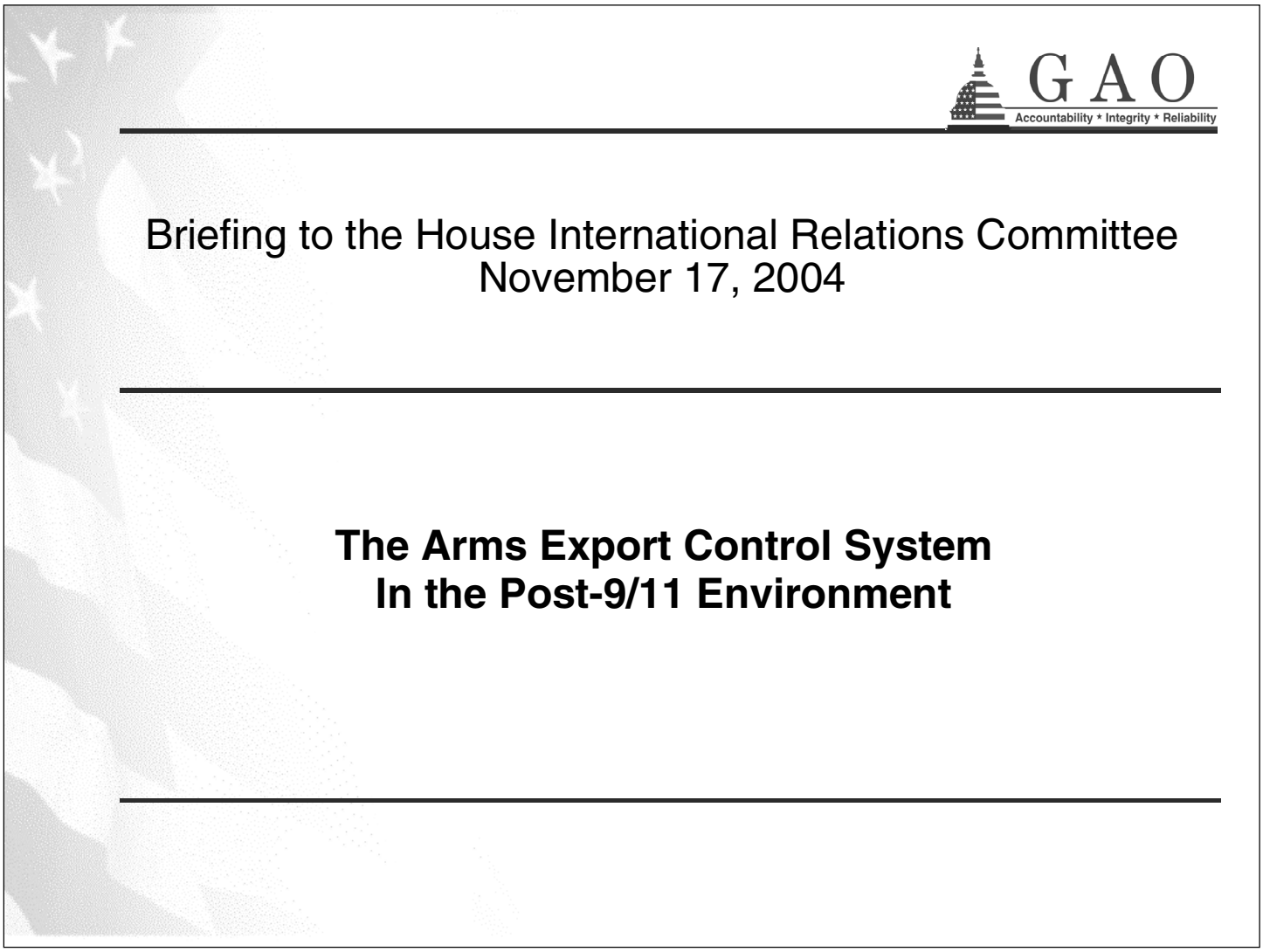
As we agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution of it until 30 days from the date of this letter. We will then provide copies of this report to the Ranking Member of the House International Relations Committee; the House Armed Services Committee; the House Committee on Government Reform; the Senate Armed Services Committee; the Senate Foreign Relations Committee; and the Senate Governmental Affairs Committee. We also will provide copies to the Secretaries of Commerce, Defense, Homeland Security, and State; the Attorney General; the Director, Office of Management and Budget; and the Assistant to the President for National Security Affairs. In addition, this report will be made available at no charge on the GAO Web site at http://www.gao.gov.

If you or your staff have questions concerning this report, please contact me at (202) 512-4841. Others making key contributions to this report are listed in appendix VI.

Sincerely yours,

Katherine V. Schinasi
Managing Director
Acquisition and Sourcing Management

Appendix I: GAO Briefing Slides



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Briefing Objectives

- Provide an overview of
  - Changes in the arms export control system since the September 11, 2001 terror attacks (9/11) and overall trends in arms export licensing.
  - Extent of implementation of or revision to initiatives designed to streamline and expedite arms export licensing.
  - Extent of coordination regarding these initiatives between State and arms export enforcement agencies, as well as enforcement efforts.

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Background

- Arms Export Control Act (AECA) (22 U.S.C. 2751 *et. seq.*) provides statutory authority for the control of defense articles and services (arms).

- State Department Directorate of Defense Trade Controls (DDTC)
  - Has been delegated the authority to regulate arms exports.
  - Administers the arms export licensing system.
  - Established in January 2003 as the successor organization to the Office of Defense Trade Controls.

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Background (cont.)

- Defense Department Defense Technology Security Administration (DTSA)
  - Represents Defense on export control issues.
  - Provides technical and national security reviews of and coordinates Defense's position on export license applications referred (staffed) by DDTC.
- Homeland Security Department U.S. Customs and Border Protection (CBP) and U.S. Immigration and Customs Enforcement (ICE) enforce the AECA and related regulations through inspections at ports and investigations.
- Justice Department U.S. Attorneys' Offices prosecute suspected violators of the AECA with headquarters support from the Criminal Division's Counterespionage Section.

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Status of the Arms Export Control System Since 9/11

- A year after the 9/11 terror attacks, the White House announced the initiation of a "comprehensive assessment of the effectiveness of U.S. defense trade policies, to identify changes necessary to ensure that those policies continue to support U.S. national security and foreign policy goals."

- The assessment was to include a review of the arms export control system, as well as an evaluation of the Defense Trade Security Initiative (DTSI), which was announced in 2000 and consisted of 17 measures intended to streamline processing of arms export license applications and increase mutual security with our allies.

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Status of the Arms Export Control System Since 9/11 (cont.)

- Since the 9/11 attacks, DDTC has not
  - offered legislative proposals to change the arms export system in response to the events of 9/11 or
  - made major revisions to its export control regulations.
- Per a senior State official, DDTC did not need to change its objectives after 9/11 because it was already concerned with safeguarding U.S. technology. Instead, it rededicated itself to the pre-9/11 objectives of
  - preventing U.S. technologies from falling into dangerous hands and
  - ensuring that allies have the arms needed to fight alongside U.S. forces.
- Since 9/11, DDTC along with DTSA have continued to implement DTSI and introduce other initiatives generally designed to streamline the export control system. While DDTC officials said they reviewed the status of implementation, they have not evaluated DTSI's effect on the export control system or made changes to the DTSI measures. They stated that DTSI and its objectives remain relevant in the post-9/11 environment.

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Table 1: State, Commerce, and Defense - Workload, Staffing, and Budget for Fiscal Year 2003

	State's DDTC	Commerce's BIS	Defense's DTSA
Number of cases reviewed	54,736	12,443	17,122 State cases 12,585 Commerce cases 29,707 total cases[b]
Number of personnel	65	367	163 civilian and military
Expenditures (in millions)	$14.04[a]	$66.29	$26.99

Sources: GAO analysis of State data and State, Defense, and Commerce budget documents and reports; Defense officials.

[a] Of the $14.04 million, $2.86 million came from registration fees paid by arms manufacturers and exporters. Under the AECA, manufacturers and exporters of items controlled by State must register with State and pay the associated registration fee, which, as of December 8, 2004, is $1,750 per year (69 FR 70888, Dec. 8, 2004).
[b] Cases reviewed by DTSA include cases that were referred by either DDTC or BIS more than once for additional consideration.

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State, Commerce, and Defense: Workload, Staffing, and Budget for Fiscal Year 2003

The U.S. export control system for defense-related items and technologies is primarily divided between two regulatory regimes. One, managed by State's DDTC, controls the export of arms. The other, managed by the Commerce Department's Bureau of Industry and Security (BIS), controls exports of dual-use items that have military and commercial applications. DTSA, which represents Defense on export control issues, provides support to both regulatory regimes. This support includes assisting State and Commerce in determining which items will be controlled and reviewing export license applications submitted to either department.

In fiscal year 2003, DDTC reviewed almost 55,000 cases. These cases included applications for the permanent export of arms, the temporary export and import of arms, and agreements between U.S. industry and foreign entities to provide technical assistance or manufacturing capability, as well as requests for amendments to existing licenses and jurisdiction determinations.[6] By comparison, BIS reported[7] that it reviewed almost 12,500 dual-use applications in fiscal year 2003—less than a quarter of the cases reviewed by DDTC. Most of the cases reviewed by DTSA were referred by DDTC.

DDTC, which is overseen by the Deputy Assistant Secretary of State for Defense Trade, was authorized 71 staff positions in fiscal year 2003 to carry out its arms export licensing, compliance, and other functions. Of these positions, 65 were filled. Under the direction of the Under Secretary of Commerce for Industry and Security, BIS had almost 300 more employees carrying out its principal activities, including dual-use licensing and enforcement efforts.[8] DTSA, which is overseen by the Deputy Under Secretary of Defense for Technology Security Policy and Counter-proliferation, had a staff of 163, most of whom supported DDTC and BIS's efforts. Thirty-one DTSA personnel monitored space launch and space systems and were not involved in the review of license applications.

[6] Exporters can request a jurisdiction determination when they are uncertain which department controls exports of an item or want an item transferred from State to Commerce jurisdiction. For additional information on the commodity jurisdiction process, see GAO, *Export Controls: Processes for Determining Proper Control of Defense-Related Items Need Improvement*, GAO-02-996 (Washington, D.C.: Sep. 20, 2002).

[7] Department of Commerce, Bureau of Industry and Security, *Annual Report Fiscal Year 2003* (Washington, D.C.: 2004).

[8] BIS's other principal activities include monitoring the viability of the defense industrial base, ensuring industry compliance with arms control treaties, enforcing antiboycott laws, and assisting other countries in developing effective export control systems.

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DDTC Funding and Staffing

- The Foreign Relations Authorization Act, Fiscal Year 2003 (P.L. 107-228) authorized $10 million to be available in fiscal year 2003 for DDTC salaries and expenses, with an additional $4 million to be available in fiscal year 2003 for modernizing DDTC's information management systems.
  - When asked, DDTC officials and DDTC's budget director indicated that they were not familiar with this authorization language.
- P.L. 107-228 also directed the Secretary of State to assign a sufficient number of license review officers to ensure that the average weekly caseload for each officer does not routinely exceed 40 cases.
  - DDTC officials stated that they do not track the average weekly caseload and, therefore, do not know if they are in compliance with the act. Nevertheless, the officials stated they regard the 40 cases per week average as a target.

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Table 2: DDTC Staffing Levels

	Fiscal year					
	2000	2001	2002	2003	2004	2005
Total FTEs authorized	65	71	71	71	71	71
Total positions filled	40	47	59	65	65	66
Licensing officer FTEs authorized	33	36	35	37	34	32
Licensing officer positions filled	16	21	30	35	31	31
Compliance officer FTEs authorized	14	16	16	16	17	16
Compliance officer positions filled	8	10	12	13	15	14

Source: State officials.

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DDTC Staffing Levels

DDTC's 71 authorized full-time equivalents (FTE)[9] are divided between licensing officers, compliance officers, and other staff, including policy, management, and support staff. DDTC's licensing officers are responsible for reviewing license applications and making determinations as to whether those applications should be approved. The number of authorized licensing officers increased from fiscal year 2000 through 2003, but then decreased in fiscal years 2004 and 2005. Similarly, the number of licensing officers positions filled at the start of each fiscal year increased through fiscal year 2003, but has since decreased. Compliance officers carry out a range of functions to help ensure exporter compliance, including addressing disclosures of possible violations, assisting Justice in prosecuting criminal violations, and managing DDTC's end-use monitoring program. The number of authorized compliance officers remained fairly consistent over the 6-year period, with the number of positions filled increasing through fiscal year 2004 and then decreasing at the start of fiscal year 2005.

Over the six fiscal years, DDTC has shifted some authorized FTEs to policy and management. For example, between fiscal years 2003 and 2005, the number of licensing officers authorized decreased by five positions, while the number of authorized FTEs for DDTC management and policy functions increased by five.

DDTC personnel are supplemented by detailees from other agencies, most notably Defense. To assist in expediting license reviews, the Foreign Relations Authorization Act for Fiscal Year 2003 called for Defense to ensure that 10 military officers are continuously detailed to DDTC. However, DDTC officials informed us that only four military officers are currently detailed to DDTC. Additionally, contractor personnel provide support to all of DDTC's functions. For fiscal year 2003, DDTC officials informed us that they spent $4.3 million on contractor support.

[9] FTE is a measure of federal civilian employment. One FTE is equal to 1 work-year of 2,080 hours.

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Table 3: Number of Cases Reviewed by DDTC and Median Processing Times

		Fiscal year					
		1999	2000	2001	2002	2003	2004 (through 4/30)
All	**Cases**	43,926	45,994	50,078	50,403	54,736	33,211
	Median	26 days	25 days	15 days	13 days	14 days	17 days
Nonstaffed	**Cases**	29,054	30,470	34,525	33,948	36,128	22,288
	Median	14 days	15 days	10 days	8 days	8 days	11 days
Staffed	**Cases**	14,872	15,524	15,553	16,455	18,608	10,923
	Median	77 days	69 days	58 days	52 days	49 days	51 days
Defense	***Cases***	*13,240*	*14,475*	*14,543*	*15,336*	*17,122*	*9,900*
	Median	*39 days*	*29 days*	*28 days*	*29 days*	*29 days*	*27 days*

Source: GAO analysis of State data.

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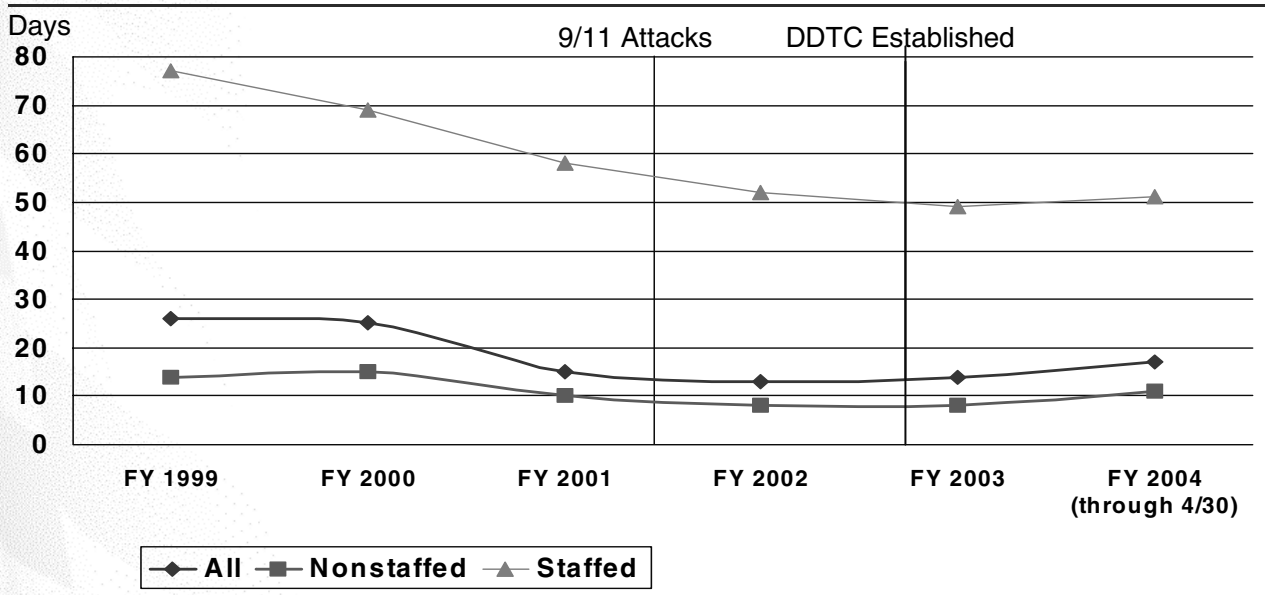
Figure 1: Median Processing Times for Cases



Source: GAO analysis of State data.

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Number of Cases Reviewed by DDTC and Median Processing Times

The number of arms export cases reviewed by DDTC increased steadily from 43,926 cases in fiscal year 1999 to 54,736 cases in fiscal year 2003, which is almost a 25 percent increase. For most of that time period, the median processing times[10] declined—from 26 days in fiscal year 1999 to 13 days in fiscal year 2002. However, in fiscal year 2003, the median processing time increased to 14 days and this upward trend continued through the first 7 months of fiscal year 2004.

DDTC processed the majority of cases without referring—or staffing—them to other State offices or DTSA for additional review. DDTC has staffed about one-third of its cases for additional review. Defense conducts technical reviews and identifies national security concerns associated with cases, while other State offices review cases for foreign policy, human rights, and non-proliferation concerns.

For staffed cases, the majority were referred to Defense's DTSA for review, some of which were referred to DTSA more than once for additional consideration. The cases referred to Defense represent a subset of staffed cases. Thus, of the 18,608 cases that were staffed in fiscal year 2003, 17,122 were referred to Defense. The number of cases staffed to DTSA increased 29 percent from fiscal year 1999 to fiscal year 2003. DTSA officials informed us that despite the increase in workload, their resources for reviewing cases have remained constant. The Defense median processing time reflects the number of days between the date State referred the case to DTSA and the date DTSA provided DDTC with its input, which for fiscal year 2003 was 29 days. DTSA officials, however, noted that there can be a delay between the time State decides to refer a case and the time DTSA physically receives the case and supporting documentation for review.

[10] The median processing time is the point at which 50 percent of the cases took more time and 50 percent less time. We are reporting the median processing time because the average or mean processing time can be significantly affected by a small number of cases that had much longer review times than the majority of cases.

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State's Explanation for Increased Processing Times

- According to the Deputy Assistant Secretary of State for Defense Trade, median processing times have increased primarily because licensing officers resumed screening all parties listed on applications against State's export licensing watchlist.
  - DDTC officials explained that between June 2002 and December 2003, not all parties listed on applications were entered into the licensing database so they could be automatically screened against the watchlist.
  - When they became aware of the situation in December 2003, DDTC officials directed licensing officers to ensure that all parties were entered in the database, which meant manually entering multiple parties for some applications. According to the officials, the manual entry of the parties resulted in increased processing times.
- DDTC officials also said that cases have become more complex and involve more sensitive technologies that take longer to review, but acknowledged the difficulty in substantiating this view.

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State's Explanation for Increased Processing Times

State's watchlist identifies entities whose appearance on an application should prompt closer scrutiny and, in some cases, denial of the application. Under the AECA,[11] State is required to identify and deny licenses to persons convicted of violating various laws, including certain laws related to export controls, foreign corrupt practices, espionage, and improper communication of classified information, as well as persons who are ineligible to receive import or export licenses from any U.S. agencies. State may also deny licenses to persons who have been indicted for violating these same laws or are ineligible to contract with any U.S. agencies. In addition to identifying individuals who meet those criteria, State's watchlist includes individuals and companies under U.S. economic sanctions, identified by intelligence sources as suspected or known diverters or proliferators, or identified from negative pre-licensing or post-shipment checks.

DDTC officials informed us that while they instituted measures to ensure that all parties on applications are screened against the watchlist, they have not retroactively reviewed all applications submitted between June 2002 and December 2003, to determine if any of the parties to those applications appear on the watchlist. As a result, they do not know whether any applications involving parties on the watchlist were approved. Further, DDTC officials do not know how many applications were not screened against the watchlist.

The manual entry of parties into the licensing database does not fully account for the increased processing times. The median processing time for all cases began increasing in fiscal year 2003, which predates when DDTC took action to ensure that all parties are screened against the watchlist.

[11] 22 U.S.C. 2778.

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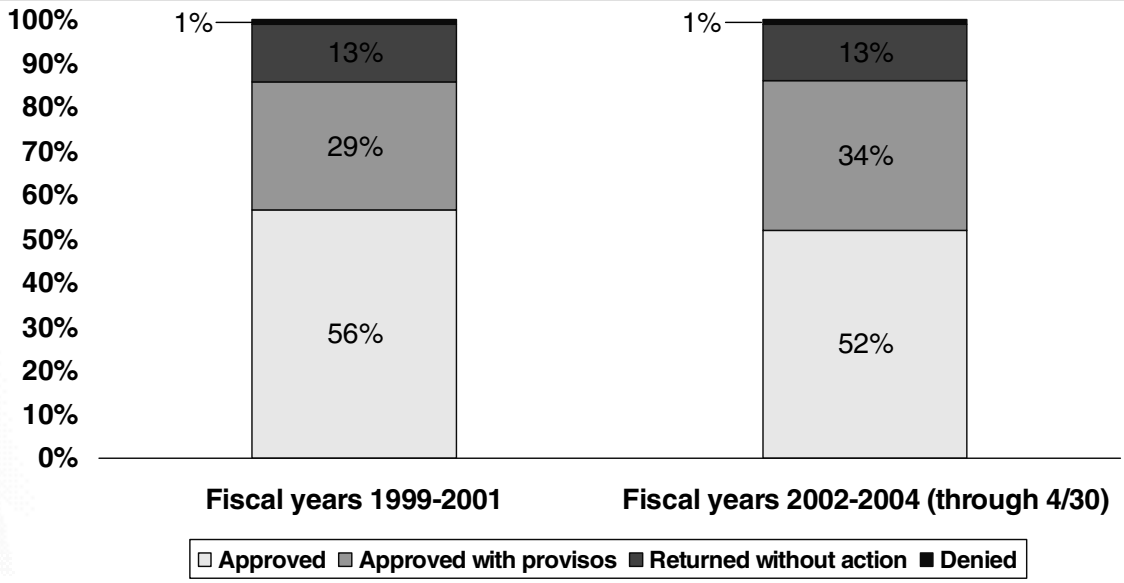
Figure 2: Final Actions for License Applications



Source: GAO analysis of State data.

Note: Totals do not add to 100 percent due to rounding.

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Final Actions for License Applications

In its final disposition of an export license application,[12] DDTC essentially has four options. It can approve the application, approve the application with provisos—conditions that limit the use of the exported items and technologies, deny the application, or return it without action. DDTC returns applications without action when it determines that the applications either do not meet regulatory requirements or do not provide adequate documentation and details.

Both prior to and after the events of September 2001, DDTC approved more than half of the license applications without placing conditions on the use of the items and technologies. However, the percentage of applications approved with provisos increased after September 2001, which coincided with an increase in the number of nonstaffed applications approved with provisos by DDTC.

The percentage of applications returned without action has remained constant since September 2001. Likewise, the percentage of applications denied remained at 1 percent. Other final actions, such as an application being lost or withdrawn by the exporter, represented less than 1 percent.

[12] License applications include applications for the permanent export of arms, the temporary export and import of arms, agreements between U.S. industry and foreign entities to provide technical assistance or manufacturing capability, and amendments to existing licenses.

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Special License Application Processes: Operation Enduring Freedom and Operation Iraqi Freedom

- State and Defense established an "expedited" process for reviewing license applications in support of Operation Enduring Freedom (OEF) and Operation Iraqi Freedom (OIF). DDTC officials informed us that the goals are to process applications
  - within 2 days if not staffed outside of DDTC for review and
  - within 4 days if staffed outside DDTC for review.
- Processing time goals for OEF and OIF applications have generally not been met.

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State's Explanation for Operation Enduring Freedom and Operation Iraqi Freedom Processing Times

- According to DDTC officials, applications for Operations Enduring Freedom and Iraqi Freedom are their highest priority.
- Officials explained that processing times exceeded the goals, in part, because
  - the applications were frequently incomplete and
  - licensing officers kept the cases open so that applicants could submit required information, instead of returning incomplete applications without action.

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Table 4: Operation Enduring Freedom - Number of Applications and Median Processing Times

		Fiscal year		
		2002	2003	2004 (through 4/30)
Nonstaffed	**Applications**	94	182	64
2-day goal	**Median**	2 days	***6 days***	***8 days***
Staffed	**Applications**	70	116	30
4-day goal	**Median**	***12 days***	***14 days***	***11 days***
Defense	***Applications***	*76*	*116*	*20*
	Median	*5 days*	*7 days*	*6 days*

Source: GAO analysis of State data.

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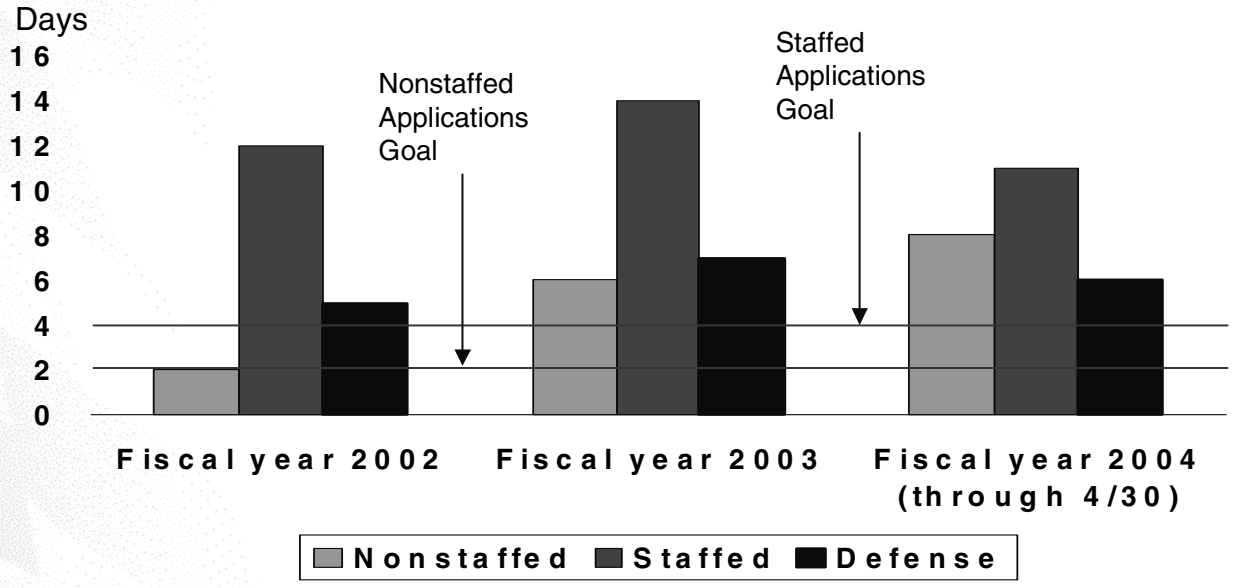
Figure 3: Operation Enduring Freedom - Median Processing Times for License Applications



Source: GAO analysis of State data.

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Table 5: Operation Iraqi Freedom - Number of Applications and Median Processing Times

		Fiscal year	
		2003	2004 (through 4/30)
Nonstaffed	**Applications**	14	66
2-day goal	**Median**	***6 days***	***7 days***
Staffed	**Applications**	13	25
4-day goal	**Median**	***7 days***	***22 days***
Defense	***Applications***	*8*	*18*
	Median	*1.5 days*	*6 days*

Source: GAO analysis of State data.

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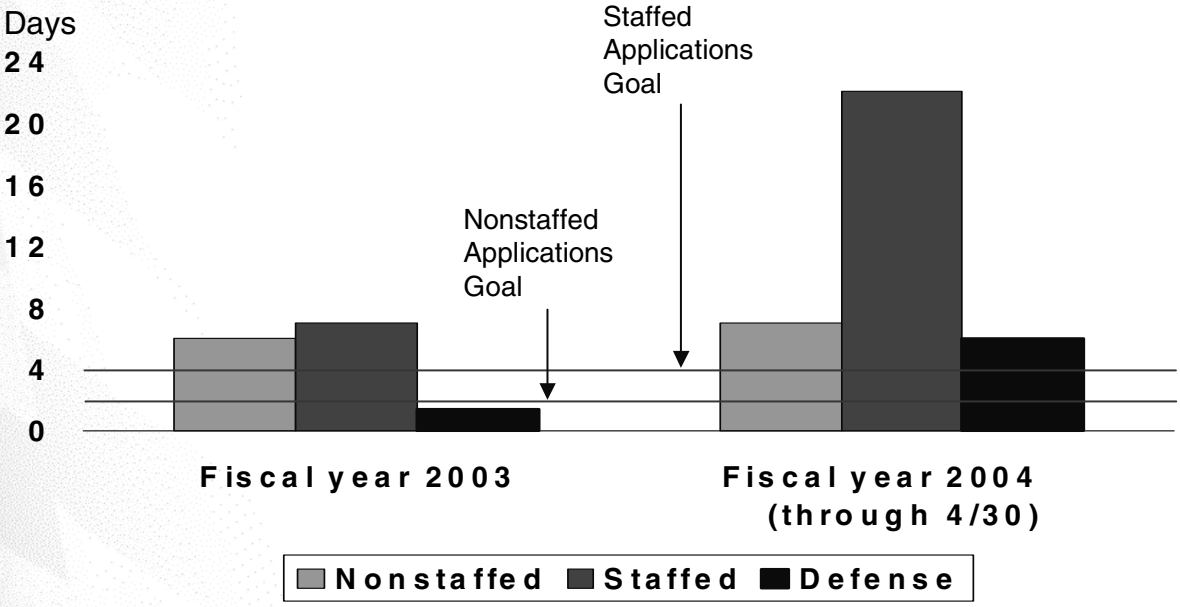
Figure 4: Operation Iraqi Freedom - Median Processing Times for License Applications



Source: GAO analysis of State data.

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Special License Application Processes: Defense Capabilities Initiative and Embassy Applications

- DTSI called for the expedited review of license applications
  - determined to be in support of the North Atlantic Treaty Organization's (NATO) Defense Capabilities Initiative (DCI) to assist allies in increasing their military capabilities or
  - submitted by the embassies of NATO countries, Australia, or Japan for key supplies.
- DDTC established special processes for these applications—
  - applications must be submitted electronically and
  - applicant must indicate that it is seeking special processing.
- Goal is to review
  - DCI-related applications within 10 days (nonstaffed) or 20 days (staffed).
  - embassy applications within 10 days (nonstaffed) or 23 days (staffed).
- Median processing times for these initiatives have met the established goals for nonstaffed applications, but have generally not met the established goals for staffed applications.

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Table 6: DCI - Number of Applications and Median Processing Times

		Fiscal year			
		2001	2002	2003	2004 (through 4/30)
Nonstaffed	Applications	6	26	47	8
10-day goal	Median	6.5 days	5 days	7 days	7 days
Staffed	Applications	6	18	24	14
20-day goal	Median	*27.5 days*	*27 days*	*30.5 days*	*48 days*
Defense	*Applications*	*6*	*19*	*23*	*14*
	Median	*22 days*	*17 days*	*17 days*	*9.5 days*

Source: GAO analysis of State data.

Note: NATO's DCI was launched in April 1999 as an effort to improve the alliance's military capabilities in terms of force mobility; logistical support; ability to effectively engage adversaries and protect against threats; and interoperable communications to enable forces from different countries to work together.

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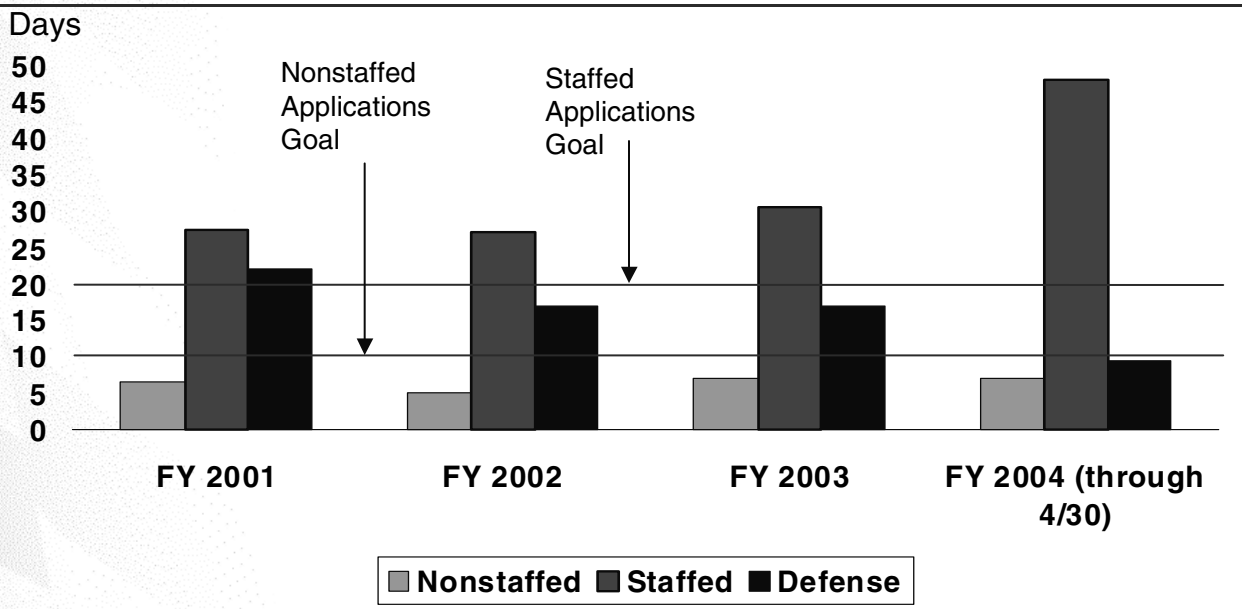
Figure 5: DCI - Median Processing Times for License Applications



Source: GAO analysis of State data.

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Table 7: Embassy - Number of Applications and Median Processing Times

		Fiscal year			
		2001	2002	2003	2004 (through 4/30)
Nonstaffed	**Applications**	5	151	135	88
10-day goal	**Median**	6 days	4 days	6 days	7 days
Staffed	**Applications**	0	22	11	13
23-day goal	**Median**	N/A	16.5 days	22 days	***37 days***
Defense	***Applications***	*0*	*24*	*10*	*13*
	Median	*N/A*	*8 days*	*10.5 days*	*16 days*

Source: GAO analysis of State data.

Note: Of the 425 applications processed under this initiative through April 2004, 307 were submitted by the United Kingdom, 113 by Australia, 3 by Canada, and 1 each by the Netherlands and Romania.

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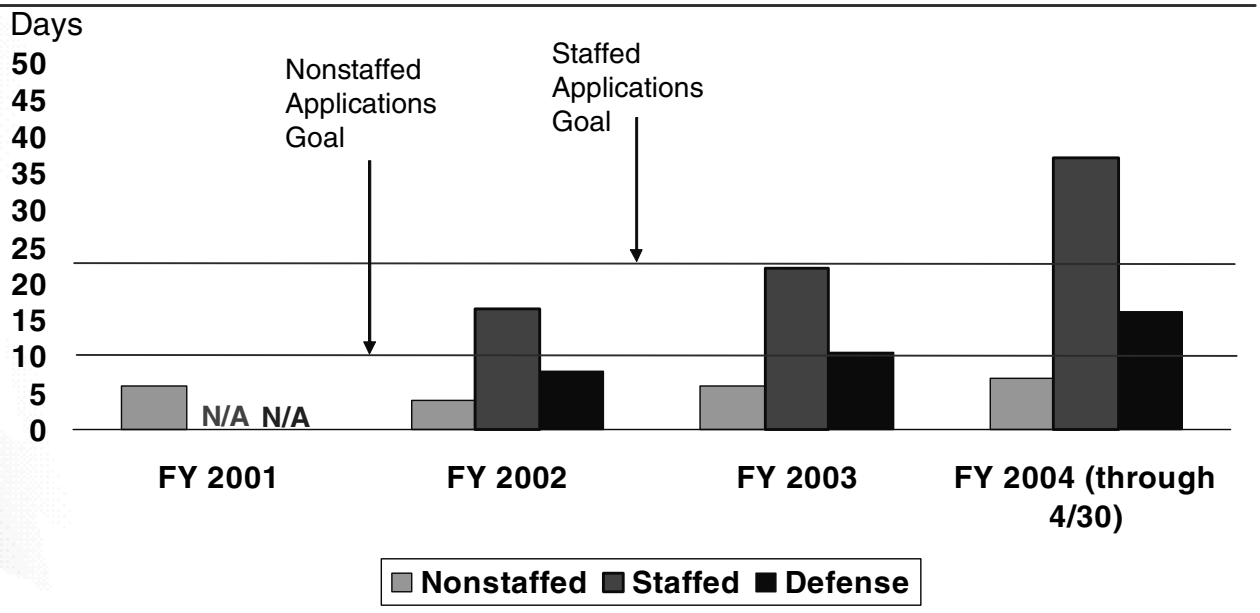
Figure 6: Embassy - Median Processing Times for License Applications



Source: GAO analysis of State data.

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Table 8: Electronic Licensing D-Trade - Number of Applications and Median Processing Times

	January 2004	February 2004	March 2004	April 2004	January – April 2004
Number of applications	24	18	46	47	135
As percent of total applications	*0.55%*	*0.39%*	*0.81%*	*0.95%*	*0.69%*
Median processing time	40 days	76 days	15 days	16 days	24 days

Source: GAO analysis of State data.

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Electronic Licensing: D-Trade

DDTC's D-Trade is a Web-based license application submission and review system, which allows companies to electronically submit export authorization requests and supporting documentation for review. The system officially went on-line in January 2004. DDTC officials expected that D-Trade would be more efficient than the existing system that permitted electronic submissions of requests but required hardcopy submissions of supporting documentation, which could be voluminous. However, from January through April 2004, few applications were submitted via D-Trade. Based on an analysis of State's data, none of the applications processed via D-Trade during this time frame was staffed outside of DDTC for review.

DDTC is now reporting increased use of the D-Trade system as well as reduced median processing times. According to the DDTC website, D-Trade processed 154 nonstaffed applications and 146 staffed applications in November 2004. Median processing times for applications submitted via D-Trade in November 2004 were 9 days for nonstaffed applications and 18 days for staffed applications. DDTC officials said that processing times should improve as licensing officers and exporters become more familiar with the D-Trade system and enhancements make the system more user-friendly.

When D-Trade came on-line in January 2004, it accepted applications for both permanent exports—the most common type of application DDTC receives—and technical assistance agreements, which allow for the export of controlled technical data. However, citing industry complaints regarding the electronic format for submitting information, DDTC suspended the acceptance of technical assistance agreements via D-Trade in mid-August 2004. DDTC officials told us that the acceptance of technical assistance agreements via D-Trade would be reinstated once the electronic form for submitting agreements has been redesigned, which is expected to occur by April 2005.

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Electronic Licensing: Capabilities

- P.L. 107-228 section 1403 directed State to establish an electronic system for filing and reviewing export license applications and to ensure the system is capable of exchanging data with export control-related information systems maintained by Commerce, Defense, Energy, and the Central Intelligence Agency (CIA).
  - According to State information technology officials, D-Trade is technically capable of exchanging data with other systems as required by P.L. 107-228.
    - D-Trade is currently exchanging data on a daily basis with Defense's system.
    - State is waiting for final administrative approval to begin exchanging data with Commerce's system.
    - No discussions have occurred with Energy or CIA officials regarding data exchanges with their systems.

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Comprehensive Export Authorizations

- As part of DTSI, three export authorizations were created to promote transnational defense cooperation with NATO countries, Australia, Japan, and Sweden—
  - Major Program Authorization—designed to provide a single U.S. exporter with a comprehensive authorization for a range of export activities, including hardware, technical data, and defense services, at the beginning of a project.
  - Major Project Authorization—designed to provide a comprehensive authorization for a range of export activities associated with a foreign government's commercial acquisition of defense technologies.
  - Global Project Authorization (GPA)—designed to provide a comprehensive authorization to cover all exports planned to occur under a government-to-government international agreement for a cooperative project.

- To date, DDTC has received three applications for comprehensive authorizations. Two of these applications have been approved—
  - one major program authorization for the Eurofighter program and
  - one GPA for the Joint Strike Fighter (JSF) program.
- There have been no applications for a major project authorization.

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Comprehensive Export Authorizations (cont.)

- According to DDTC officials, companies have disclosed 23 potential violations of export control law/regulations related to the JSF program, one of which involved a potential violation of the GPA. DDTC officials explained that of the remaining 22 potential violations, 8 pre-date the October 2002 GPA and 14 were not related to the GPA, but that
    - two involved the disclosure of low-observable/counter low observable technology,
    - one involved the disclosure of controlled technology over a computer network, and
    - one involved a foreign company releasing U.S. controlled technology to a national of another country
- DDTC officials stated that to their knowledge, there have not been any violations associated with the major program authorization for the Eurofighter program.

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Additional Initiatives Introduced by DDTC and DTSA

- Internal Realignment of DDTC and DTSA
  - DDTC officials have described their realignment efforts as a means to focus staff work to more effectively achieve foreign policy and national security goals and to raise the profile of DDTC within the department.
  - DTSA officials have described their reorganization efforts as a means to better meet Defense and industry needs, provide a more technological basis for DTSA's review of arms and dual-use exports, and ensure more consistent treatment of similar technologies.
- Night Vision and Thermal Imaging
  - Due to a Combatant Commander's concerns about night vision-related exports, DTSA began requiring a higher level of review within DTSA and additional end-user checks for defense and dual-use night vision-related applications.
    - For fiscal year 2003, night vision equipment accounted for 1.9 percent of the 54,736 cases processed by State's DDTC. By comparison, thermal imaging and light intensifying cameras accounted for 23 percent of the 12,443 cases reviewed by Commerce's BIS.
- Industry Response Team
  - DDTC effort to respond to general questions from industry regarding basic processes and provide information on the status of applications.

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Additional Initiatives Introduced by DDTC and DTSA (cont.)

- Proviso Reform
  - Described by a senior DTSA official as an effort to ensure that provisos recommended by DTSA license reviewers are applicable to the proposed export and more appropriately applied to licenses, as well as improve the quality and clarity of license applications.
  - DDTC officials have raised concerns that the implementation of this initiative may adversely affect compliance and enforcement efforts. DDTC officials explained that in response to this initiative, exporters have started including self-imposed conditions in their applications to obtain DTSA approval. However, there could be differing interpretations as to what these conditions mean and, therefore, what is allowable under the license.
- Top 10 Technologies
  - DTSA effort to identify emerging technologies before they become widely available. According to a senior DTSA official, the results of this effort have provided a basis for Defense proposals on how exports of these emerging technologies should be controlled.

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Coordination on Initiatives

- According to Homeland Security and Justice officials, State has sought only limited coordination regarding the implementation of DTSI and other initiatives. The only exceptions have been regarding
  - the proposed extension of the country exemption and
  - the proposed aircraft and aircraft spare parts exemption.

- The Deputy Assistant Secretary of State for Defense Trade explained that coordination was limited to the two proposed exemption initiatives because they would fundamentally change how some arms and related technologies are exported and would, therefore, affect enforcement efforts.

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Coordination on Initiatives (cont.)

- Homeland Security and Justice officials informed us that they generally do not favor export licensing exemptions because exemptions increase the risk of diversion and complicate enforcement efforts. They noted, for example,
  - individuals seeking to obtain U.S. arms illicitly can establish "front companies" overseas that obtain arms under an exemption and then divert those items to other countries. Further, the investigation of such diversions frequently requires lengthy undercover operations and the assistance of officials in the country where the front company is located.
  - export violations under an exemption are difficult to prosecute because it is hard to obtain evidence of a "willful" violation, the legal standard in the AECA for a criminal conviction, particularly since there is a limited "paper trail" of documents to prove a violation.

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Coordination on Initiatives (cont.)

- As part of DTSI, there was a proposal to extend licensing exemptions for exports to qualified countries. Under current arms export regulations, many defense items can be exported to Canada without a license.[a] State has negotiated agreements with the governments of Australia and the United Kingdom to provide a basis for allowing the license-free export of certain defense items to these countries, but the exemptions have not been put into effect.

- While Homeland Security and Justice have officially indicated that they do not have objections to the agreements reached with the governments of Australia and the United Kingdom to allow for license-free exports, the departments have cautioned that there are risks associated with the implementation of these agreements.

[a] For additional information regarding the exemption for arms exports to Canada, see GAO, *Defense Trade: Lessons to Be Learned from the Country Export Exemption*, GAO-02-63 (Washington, D.C.: Mar. 29, 2002).

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Coordination on Initiatives (cont.)

- In addition to the country exemptions, State has proposed
  - creating a new regulatory exemption to allow the license-free export of standard configurations of specific aircraft models, such as the C-130 Hercules airlift airplane and the UH-1 Huey helicopter, to NATO and other allies, such as Australia and Japan and
  - raising the regulatory threshold from $500 to $5,000 on military aircraft spare parts that can be exported without a license provided that certain prerequisites are met.
- In 2004, CBP's Assistant Commissioner for Field Operations wrote a letter to State that indicated CBP would have difficulty enforcing the proper use of the aircraft-related exemptions. Specifically, CBP warned its officers
  - would not be able to distinguish configurations eligible for the exemption from upgraded configurations requiring licenses, which would make targeting potential violations difficult, if not impossible and
  - lack access to the information needed to ensure that an exporter meets the prerequisites for using the spare parts exemption.

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Coordination on Initiatives (cont.)

- Aircraft spare parts, even with the current export licensing requirements, are at risk of diversion to countries that seek to circumvent U.S. embargoes and increase the operational readiness of their military aircraft.
- Since 9/11, Homeland Security has conducted multiple criminal investigations involving illegal exports of aircraft components. Examples include alleged exports of
  - F-4 jet components to Israel with an unknown final destination and
  - components for F-4 jets, F-5 jets, F-14 jets, and C-130 aircraft to a British company procuring the equipment for the Iranian military.
- U.S. Attorneys have secured convictions involving illegal exports of aircraft components. Examples include guilty pleas for
  - exports of helicopter components to Iran and
  - exports of F-4 and F-5 jet components to China.

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Information Resources and Sharing

- CBP officers and ICE agents have access to
  - Automated Export System (AES), which is a joint venture among multiple federal agencies—including Commerce, Homeland Security, and State—used by exporters to electronically provide CBP with documentation required prior to export. By comparing the items being shipped to shipping information provided by the exporters via AES and State-issued export licenses, enforcement officials can identify potential export control violations.
    - While some information from a State-issued license is available through AES, specific descriptions of the items approved for export and other information useful for enforcement purposes are generally not available due to AES data storage limitations.
  - Automated Targeting System, which targets questionable shipments for inspection at ports and border crossings.
- Officers and agents can also obtain information, such as whether an item requires a State-issued license or is eligible for export without a license under an exemption, from State through the ICE-operated Exodus Command Center.

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AES: State's Access to the System

- DDTC recently gained access to AES when a memorandum of understanding outlining an information sharing arrangement between State, CBP, and Commerce's Census Bureau was signed.
  - Census provides DDTC with weekly electronic updates of AECA-related shipments.
- Access to AES allows DDTC to know what defense items have actually been exported, so it can reconcile shipments with authorized exports and help ensure exporter compliance with laws and regulations.

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AES: Notification of Shipments and Transfers

- As of October 2003, all shipments of hardware controlled under the AECA must be reported through AES.
- Transfers of technical data and defense services are not reported through AES.
  - DDTC was to have a system in place by January 2004 for exporters to electronically notify DDTC of initial exports of technical data and services pursuant to a license or agreement, but the implementation of that system has been delayed. Until the electronic system is in place, exporters are to submit letters to DDTC notifying it of initial exports.
  - DDTC does not require exporters to notify it of technical data and defense service transfers when an exemption is claimed.

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AES: State Funding

- Under P.L. 107-228 section 1404(a), $250,000 was "authorized to be available" for
  - providing State with full access to AES,
  - ensuring that the AES is modified to meet the needs of State, and
  - providing operational support to AES.
- Per DDTC officials, DDTC did not spend funds on AES improvements in fiscal year 2003. The Census official who oversees AES confirmed that State did not spend funds for AES operations and improvements.

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Challenges Identified by Enforcement Officials in Enforcing Arms Export Controls Since 9/11

- Challenges identified by enforcement officials
  - Budgetary constraints
  - Limited personnel resources for CBP's outbound enforcement
  - Ability to acquire and maintain trained and experienced personnel
  - Licensing exemptions[a]
    - Place burden on CBP officers to determine if shipment is eligible to be exported without a license
    - Require investigations of "front companies" in other countries
    - Limited documentation to ensure proper use of exemption and investigate suspected violations
  - Legal standard of needing to prove a "willful" violation of the AECA to secure a criminal conviction

[a] For additional information regarding licensing exemptions, see GAO-02-63.

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Customs and Border Protection: Initiatives and Resources

- No new arms export enforcement initiatives introduced by CBP in response to the events of 9/11.
- CBP has limited resources and funding for enforcement activities. According to Homeland Security officials, relatively more resources have been devoted to ensure that dangerous goods and individuals do not enter the country through the 317 official ports and border crossings.
  - Prior to 9/11, 400 officers were dedicated to outbound enforcement.
  - Currently, 256 officers are dedicated to outbound enforcement, but can be pulled to fulfill inbound inspection requirements as needed.
  - Cancellation of courses on outbound inspections in fiscal year 2004
- Improvements in officers' ability in recent years to conduct outbound inspections at ports and borders due to
  - AES automation enhancements and
  - regulatory requirement for information on a State-controlled shipment to be submitted via AES prior to arriving at the port or border, which improves targeting.

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Immigration and Customs Enforcement: Initiatives and Resources

- ICE initiatives introduced in response to the events of 9/11:
  - Identification of arms export control investigations as a top priority.
  - Project Shield America to improve outreach with industry and develop new sources of information.
  - Efforts to improve cooperation with intelligence community and participation in interagency taskforces.
- Overall increase in number of agents since 9/11 with efforts underway to expand the number with export control expertise:
  - Creation of dedicated export control investigative teams in major field offices.
  - Expansion of training on conducting export control investigations in fiscal year 2004, but courses for fiscal year 2005 cancelled for budgetary reasons.

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Table 9: Arms Seizures

	Fiscal year			
	2001	2002	2003	2004
Number of seizures	661	663	665	923
Total value of seizures	$83.72 million	$65.85 million	$105.79 million	$136.00 million

Source: CBP officials and GAO analysis of CBP data.

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Table 10: Arms Export Investigations, Arrests, Indictments, and Convictions

	Fiscal year				
	2000	2001	2002	2003	2004
Investigations opened[a]	570	395	1,145	824	633
Arrests[b]	48	62	40	98	92
Indictments[c]	47	53	29	65	61
Convictions[d]	56	39	38	46	45

Source: ICE officials.

[a] Investigations opened refer to the number of cases opened during a particular fiscal year. A single case may involve multiple individuals or entities, such as a corporation.
[b] Arrests refer to the number of individuals arrested during a particular fiscal year.
[c] Indictments refer to the number of individuals and/or entities indicted during a particular fiscal year.
[d] Convictions refer to the number of individuals and/or entities convicted during a particular fiscal year and include guilty pleas and pleas of *nolo contendere*.

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Arms Export Investigations, Arrests, Indictments, and Convictions

The number of investigations opened and individuals arrested by ICE agents for suspected arms export violations has widely fluctuated over the past 5 fiscal years. Similarly the number of individuals indicted and convicted for arms export violations has also fluctuated from year to year. When ICE opens an investigation in response to an alleged arms export control violation, it may take several years for agents to build a case and eventually make an arrest—if one is made at all. Once an arrest is made, several years may pass before Justice brings the case to trial and obtains a conviction. For example, an investigation opened in 1999 may not result in an arrest until 2002. Similarly, an arrest in 2000 may not result in a conviction until 2003.

According to ICE officials, the drop in arms export-related arrests and indictments in fiscal year 2002 may be the result of a more intensive focus on ensuring that dangerous goods and individuals did not enter this country in the immediate aftermath of the September 2001 attacks. However, with the passage of time, ICE became increasingly concerned with the defense-related items leaving this country and the threat they could pose. The officials explained that this prompted ICE to focus its attention on illegal arms exports and increase its agents' knowledge and skills as they relate to arms export investigations, which has resulted in increased arrests, indictments, and convictions. The officials also attributed the increases to leads obtained through its industry outreach program—Project Shield America—and the intelligence community.

In addition to investigations by ICE, the Attorney General clarified the Federal Bureau of Investigation's (FBI) jurisdiction in November 2004 to specify that it has the lead in investigating potential AECA violations relating to foreign counterintelligence matters.[13] While the table does not include FBI investigations, Justice officials informed us that the FBI has initiated a number of AECA-related investigations. ICE officials informed us that there has been some initial uncertainty regarding which agency will have the lead in investigating potential AECA violations, but Homeland Security and Justice officials have been working together to resolve jurisdictional issues.

[13] See 69 FR 65542 (Nov. 15, 2004).

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Table 11: State's Administrative Enforcement - Blue Lantern Program

	Fiscal year					
	1999	2000	2001	2002	2003	2004
Blue Lantern checks	360+	218	410	428	413	530
Unfavorable determinations	34	35	71	50	76	93

Source: State annual reports.

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State's Administrative Enforcement: Blue Lantern

State's end-use monitoring program, known as Blue Lantern, consists of pre-license and post-shipment verification checks of the parties to and the end-use of defense exports. From fiscal year 1999 through 2004, the number of end-use monitoring checks performed under the Blue Lantern program remained relatively constant, averaging about 400 checks per year. One exception to this average occurred in fiscal year 2000 when State targeted higher value exports in its Blue Lantern checks, which resulted in only 218 checks for the year.

Blue Lantern checks may result in unfavorable determinations by State based on evidence uncovered during the checks, such as illegitimate end-users or the possible diversion of defense exports. Unfavorable determinations result in the denial of a license or are turned over for investigation by law enforcement and compliance entities. According to State's fiscal year 2003 end-use monitoring report, 49 percent of the 76 unfavorable determinations involved firearms and ammunition. Also, unfavorable determinations involving aircraft spare parts increased from 18 percent in fiscal year 2002 to 24 percent in fiscal year 2003.

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Table 12: State's Administrative Enforcement - Voluntary Disclosures

	Fiscal year					
	1999	2000	2001	2002	2003	2004
Voluntary disclosures	216	255	316	256	339	394

Source: State compliance officials.

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State's Administrative Enforcement: Voluntary Disclosures

Voluntary disclosures are disclosures to DDTC by companies or individuals that believe they may have violated the AECA, arms export control regulations, or terms of a license. Upon reviewing the circumstances of the disclosure, DDTC may take administrative action against the responsible party or refer the matter to Justice for appropriate action.

According to DDTC officials, the increase in disclosures from fiscal year 1999 through 2004 was due to increased industry education and outreach efforts on the part of DDTC to encourage companies to self-report export control violations. These officials explained that the submission of voluntary disclosures is an indication of a robust compliance effort on the part of industry. Further, voluntary disclosures may be considered a mitigating factor in determining what administrative penalties, if any, should be imposed upon a company.

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Table 13: State's Administrative Enforcement - Penalties Imposed in Administrative Cases

	Calendar year				
	2000	2001	2002	2003	2004
Number of settlements	2	2	2	5[a]	2
Number of satellite-related settlements	*1*	*1*	*2*	*1*	*0*
Total penalty amount (in millions)	$13.10	$4.95	$26.10	$43.48	$28.00
Total penalty amount for satellite-related violations (in millions)	*$13.00*	*$0.75*	*$26.10*	*$32.00*	0
Amount suspended (in millions)	$5.00	$0.55	$6.05	$16.50	$15.00
Amount suspended for satellite-related violations (in millions)	*$5.00*	*$0.15*	*$6.05*	*$12.00*	0

Source: GAO analysis of State's administrative settlement agreements.

[a] One settlement was a joint criminal and administrative settlement with a total penalty amount of $25 million. Of the $25 million, $5 million was a civil administrative penalty paid to State and is included in the table. Two million of the civil administrative penalty was suspended, provided that the company applied the funds toward compliance efforts. In addition to the $5 million civil administrative penalty, there was a $20 million penalty paid to the U.S. Customs Service (now part of Homeland Security) and that amount is not reflected in the table.

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State's Administrative Enforcement: Penalties Imposed in Administrative Cases

State can pursue administrative penalties against companies for violations of the AECA. These administrative penalties can consist of debarment from participation in defense exports and/or civil penalties in the form of monetary damages. In some cases, State has suspended a portion of the civil penalty, provided the funds are invested in a company's export compliance program. For example, in calendar year 2003, there were five settlements for AECA violations resulting in $43.48 million in administrative penalties. However, $16.5 million of that amount was suspended on the condition that companies invest the money in their compliance efforts.

According to DDTC compliance officials, when a portion of an administrative penalty is suspended, the company is required to provide DDTC with an accounting of how those funds were spent. DDTC officials then review the information provided to ensure that funds were spent in accordance with the settlement agreement. However, DDTC does not conduct a formal financial audit to verify the information provided. These officials also informed us that Defense auditors previously found that some companies have attempted to bill Defense for the required improvements to their compliance programs. After learning of this, DDTC compliance officials met with company officials to address the issue. According to DDTC compliance officials, all but one of the companies have agreed that the U.S. government should not pay for the compliance penalties imposed as part of the settlement agreements and to change their billing practices. Additionally, DDTC compliance officials have included standard language in settlement documents to explicitly preclude such charges in the future.

Five of the 13 settlements imposed in 2000 through 2004 involved satellite-related exports. However, the majority of administrative penalties imposed in those years were associated with the satellite-related settlements. For example, all $26.1 million of the administrative penalties in 2002 was for satellite-related settlements.

Appendix II: Scope and Methodology

To identify changes to the arms export system since September 11, 2001, we interviewed officials at the State Department's Directorate of Defense Trade Controls (DDTC) and the Defense Department's Defense Technology Security Administration (DTSA). We also reviewed the Arms Export Control Act;[14] the International Traffic in Arms Regulations;[15] the Foreign Relations Authorization Act, Fiscal Year 2003;[16] and other relevant agency guidance, policies, and documents including those related to each agency's budget and staffing levels. To assess overall trends in arms export licensing, we analyzed DDTC's export license application data covering October 1, 1998 through April 30, 2004. The data were extracted by DDTC officials based on the final action date for each case. We analyzed the data to determine trends in processing times and license application final actions. The processing time represents the number of calendar days between the receipt of a case and the final action date entered into State's database. Defense's processing time represents the number of calendar days between the date State decided to refer the case to DTSA and the date DTSA provided its recommendation for final action. Median processing times rather than average (mean) processing times are reported because average values can be significantly affected by a small number of cases that had much longer review times than the majority of cases. Our analysis did not include licenses that were approved and then subsequently suspended or revoked during this period.

To evaluate the implementation of initiatives designed to streamline and expedite the arms export licensing process, we reviewed State and Defense-issued guidance and consulted with State and Defense officials to identify the initiatives and their goals. We then analyzed State export license application data for October 1, 1998 through April 30, 2004 to determine the number of license applications received for each initiative and associated processing times, which we then compared to the processing time goals established by State and Defense. State assigned unique identifiers to each initiative, which we used to identify applications processed under each initiative.

State has not assessed the reliability of its license application database nor does it have a data dictionary explaining its data, which prompted us to

[14] 22 U.S.C. 2751 *et. seq.*

[15] 22 CFR pts. 120-130.

[16] P.L. 107-228.

assess the reliability of the database for the purposes of this report. We randomly selected 98 license applications from our data set that were stored on-site at State and then compared the original hardcopy application files to the corresponding information in the database. The data in the application database matched the information in the original hardcopy files for 89 percent of the fields we checked. Therefore, we are 95 percent certain that the accuracy rate of the fields we checked is between 87 percent and 90 percent, which we have determined to be sufficiently reliable for the purposes of this report. Our reliability assessment was designed to measure whether data used in our analyses matched information in State's files and did not include every field in the database. Our results may not be generalizable to the entire database or to all uses of the data within the database. Additionally, we discussed key elements of the database with State officials to ensure that we accurately interpreted the data. Because we had partial data for fiscal year 2004, we cannot provide median processing times for the entire fiscal year. However, based on our review of monthly median processing times posted on DDTC's website for the last 5 months of fiscal year 2004, the upward trend in median processing times continued through the remainder of the fiscal year. While the data presented on DDTC's website for the last 5 months of fiscal year 2004 were not included in our data reliability assessment, the monthly median processing times on DDTC's website for the first 7 months of fiscal year 2004 correspond with our analyses of that time period.

To determine the extent of coordination between State and enforcement agencies regarding the implementation of initiatives, we interviewed officials and obtained supporting documents from the Justice Department and the Homeland Security Department's U.S. Customs and Border Protection (CBP) and U.S. Immigration and Customs Enforcement (ICE). We also discussed coordination efforts with Defense and State officials. To identify enforcement challenges, we interviewed CBP, ICE, and Justice officials. We also met with CBP officials responsible for export enforcement at two ports in Maryland and Virginia to obtain their perspectives. Additionally, we obtained and analyzed data from Homeland Security and State regarding enforcement actions such as the number of arms export control investigations opened and administrative penalties.

Appendix III: Comments from the Department of State

Note: GAO's comments supplementing those in the report's text appear at the end of this appendix.

United States Department of State

Assistant Secretary and Chief Financial Officer

Washington, D.C. 20520

Ms. Jacquelyn Williams-Bridgers
Managing Director
International Affairs and Trade
Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548-0001

JAN 31 2005

Dear Ms. Williams-Bridgers:

We appreciate the opportunity to review your draft report, "DEFENSE TRADE: Arms Export Control System in the Post-9/11 Environment," GAO Job Code 120333.

The enclosed Department of State comments are provided for incorporation with this letter as an appendix to the final report.

If you have any questions concerning this response, please contact Michael Dixon, Director, Bureau of Political and Military Affairs, Office of the Defense Trade Controls, at (202) 663-2798.

Sincerely,

Christopher B. Burnham

cc: GAO – Johanna Ayers
PM – Lincoln Bloomfield
State/OIG – Mark Duda

Department of State Comments on Draft GAO Report
DEFENSE TRADE: Arms Export Control System in the Post-9/11 Environment (GAO 05-234, GAO Code 120333)

The Department of State (DOS) thanks the Government Accountability Office (GAO) for the opportunity to respond to their draft report, Defense Trade: Arms Export Control System in the Post-9/11 Environment. In general, the draft report fails to reflect the strong initiatives, ranging from organizational realignment to electronic processing to strengthened enforcement efforts, that the Department has successfully undertaken in reshaping the defense export controls function.

See comment 1.

While we agree there have been some increase in export license processing timelines, we firmly believe the background activity behind them (e.g., renewed emphasis on training of all officers, assurance that licensing review is thorough, review of business process rules, increased referral to outside offices and agencies to address increasingly complex cases) has reinforced the ability of the Directorate of Defense Trade Controls (DDTC) to carry out its multi-faceted mission and to ensure that defense export transactions are, in fact and in accordance with U.S. law, carried out in furtherance of foreign policy and national security objectives.

See comment 2.

Moreover, many of the statements in the draft report are inaccurate or misleading. We address them as follows:

- "State has not made significant changes to its arms export control regulations or proposed statutory changes in response to the terrorist attacks" (cover page and subsequently in the report, e.g., on p. 2).

See comment 3.

This statement would seem to indicate that some "significant changes" to the arms export control regulations should have occurred and does not make clear that "significant changes" were not needed to respond to or to address terrorist attacks. We believe that the GAO might well have reported that, "The arms export control system operated by State has adequate means in terms of statutory and regulatory authority to address terrorist attacks in a post-9/11 environment." Instead, as drafted, the statement implies that the State Department has been indifferent to the terrorist attacks of 9/11/01. In fact, the defense trade control system was, prior to 9/11/01, and remains an

effective instrument in keeping U.S. defense technology out of the hands of our enemies while ensuring that our allies and coalition partners have access to the U.S. defense technology they need to fight alongside our forces. As stated in the State Department report to the United Nations made in accordance with relevant sanctions (UNSC Resolutions 1390 and 1455), "the U.S. munitions export control regime is designed to deny adversaries and parties whose interests are inimical to those of the U.S. access to U.S.-origin defense equipment and technology...As a matter of long-standing policy, rooted in law, the U.S. strictly regulates exports and re-exports of defense items and technologies to protect its national interests and those interests in peace and security of the broader international community. In addition to seeking technical support and national security assessments from DOD, the State Department relies on extensive interagency cooperation and coordination to perform the arms export control function..."

There is no reason to believe that any U.S. defense items have been used in terrorist attacks, or that our enemies have used them against U.S. military forces or those of our coalition partners. That is because the existing U.S. defense trade control system has been remarkably successful in depriving our enemies of access to U.S. defense technology.

- "... (T)hey have not evaluated the effects of these initiatives (to streamline export licensing) on the export control system or revised these initiatives" (cover page and subsequently in the report, e.g., on p. 3).

See comment 4.

As was noted during the GAO audit, a review of the DTSI initiatives was part of the tasking of NSPD-19. That review was brief, to be sure, because it was recognized by all concerned these initiatives were very modest in scope (e.g., to allow build-to-print technical specifications for DOD contracts to be shared without an export authorization) and that they were generally applicable only to NATO countries, Japan and Australia (although Sweden was added to some DTSI initiatives in 2001), which are among our coalition partners and not our enemies. The DTSI initiatives have themselves not been revised, as there has been no need to do so. However, the Administration has sought to build upon and expand the DTSI initiatives pursuant to the President's tasking in NSPD-19. These additional measures have not been implemented, for reasons known to the Congress and the GAO.

- "State has sought limited coordination with the agencies responsible for enforcing U.S. arms export laws – the Departments of Homeland Security and Justice – regarding initiatives designed to streamline arms export licensing. The only exceptions have been regarding proposed export licensing exemptions. Enforcement officials have raised concerns regarding licensing exemptions…" (cover page).

See comment 5.

These statements are very misleading. While whether coordination with law enforcement agencies has been "limited" on issues other than exemptions is a matter of judgment, it is certainly true that only exemptions depart from the case-by-case licensing approval and documentation that are routinely relied upon for prosecution of violators. One wonders, for example, what interest law enforcement agencies would have in expedited licensing for high-priority NATO programs or coalition partners, which are subjected to normal licensing procedures, only with target deadlines for decisions.

See comment 6.

Moreover, Customs and Justice were both involved in the DTSI initiatives in the previous Administration, and the only measure on which they took any position was the proposal to negotiate ITAR waiver agreements with the UK and Australia. When those agreements were finally negotiated, however, the official positions of DHS and Justice (submitted in writing to the Chairman of the HIRC) were that there was no objection to these agreements. Copies of this correspondence were provided to the GAO audit team. While it may be that individual representatives of DHS and DOJ have reservations about these exemption agreements, it is highly misleading not to reference in this context the official positions of the Departments of Homeland Security and Justice.

See comment 7.
Now on pp. 46-47.

In the matter of the proposed $5,000 license exemption for aircraft spare parts (mentioned explicitly in the slides on pp. 41-42 of the draft report), John C. Varonne, Assistant Commissioner of the Office of Investigations of what was then still the U.S. Customs Service, wrote the Director of what was still the Office of Defense Trade Controls on May 10, 2002, that while "an exemption at the $10,000 level raises serious concerns for Customs… we could possibly work with an increase in the exemption to $5,000." Moreover, the acceptability of the $5,000 threshold was explicitly reaffirmed by DHS/ICE Assistant Secretary Michael Garcia. While DHS/CBP has since taken a position that the proposed $5,000 threshold should be lowered to $2,500 (in a letter from Assistant Commissioner Jayson P. Ahern on July

15, 2004), this does not reflect the seemingly categorical concerns regarding licensing exemptions suggested on the cover page and in the slides.

Finally, regarding more recent (and as yet unimplemented) initiatives in the context of NSPD-19, these were personally briefed to DHS and DOJ representatives who are responsible for export control enforcement, and they found no basis for objection to the proposed measures.

- "...(A)pplications for Operation Iraqi Freedom are to be processed in 4 days if they require interagency review, but the median processing time for these applications in the first 7 months of fiscal year 2004 was 22 days" (cover page and subsequently in the report).

Now on p. 26.

See comment 8.

As referenced briefly in the report (slide 15, p. 24 of the report), these delays in Iraq licenses were caused by frequently incomplete applications, and "licensing officers kept the cases open so that applicants could submit required information, instead of returning incomplete applications without action." To present the data on delays in Iraq licensing on the cover page without explaining the excellent reason why such delays occurred gives a very misleading impression of the responsiveness of the defense trade control system to the highest-priority licenses we are handling. After all, our objective was to make the U.S. defense articles available to our allies and coalition partners as quickly as possible, not just to meet deadlines we had set for ourselves, and this more important purpose was served by keeping the case open while trying to correct its deficiencies.

See comment 9.

- The report statement that, "...(T)he Department has transferred some of its licensing resources to other functions. For example, between fiscal years 2003 and 2005, five licensing officer positions were transferred to policy and management functions" (p.3) is incorrect. Authorized FTE for Licensing Officer positions have consistently increased since a $2 million budgetary baseline plus-up in FY-1999 when export jurisdiction over comsats reverted to the Department of State. Some confusion that is reflected here might be traced to the 2003 realignment of the defense export controls function. Some senior positions (GS-14 and GS-15) that had been created in accordance with CJS Authorization provisions once appeared on staffing patterns as licensing personnel, but the relevant Position Descriptions and assigned duties for these personnel were of a special advisory nature and focused on specific tasks and initiatives (e.g., CWC- and DTSI-related activities) that are outside the immediate realm

of normal arms export licensing responsibilities. As a result of the realignment, some of these personnel moved to the newly formed Office of Defense Trade Controls Policy. In addition, administration of the Commodity Jurisdiction process moved from the Licensing Office to Policy. Notably, one of positions created as a result of the FY-1999 personnel plus-up has been converted to an additional deputy director position in the Licensing Office.

- "...(T)he officials stated they regard the 40 cases per week average as a target" (Slide 8, p. 13).

Now on p. 15.

See comment 10.

In fact, as explained to the GAO auditors, 40 cases per week workload is more than a target but a current reality. Even at a level of 60,000 cases per year, with 30 licensing officers with signature authority and 2,000 person-hours per year (40 hours, 50 workweeks), the average workload is 40 cases per officer per week. Of course, some officers are responsible for many more than 40 cases a week, and some many less, as the complexity of cases differs significantly. But the average holds true.

Now on p. 22.

See comment 11.

"Plus-Names" (p. 20) The paragraph beginning "DDTC officials informed us..." would much more accurately reflect the watchlist review process if modified as follows:

"DDTC officials note that omission of names from watchlist review occurred only when there were lists of parties to the transaction in hardcopy attachments to license application submissions. While DDTC officials do not know how many applications had names that were not fully screened against the watchlist, they are certain that the majority of cases received by DDTC do not have lists of persons attached and that even when this occurs the vast majority of the names are those of U.S. freight forwarders regularly subject to watchlist review by other means. DDTC officials informed us that while they instituted measures to ensure that all parties on applications are screened against the watchlist, they have not completed a retroactive review of the applications submitted between June 2002 and December 2003, to determine if parties to those applications appear on the watchlist. Based on the retroactive review that has been conducted, no party has been identified that would have resulted in removal of that party from a license approval or the denial of that particular license. DDTC officials also informed us that as part of a projected spending plan for funds to be received through the

increase in defense industry registration fees, DDTC identified the requirement for additional contractor support for watchlist screening, to include retroactive checks on prior submission in the period that all names were not made subject to watchlist review. This is a priority endorsed by relevant Department offices, but initiation of the project will depend upon how much additional revenue will be received in the near future."

Now on p. 27.

- The chart regarding Operation Enduring Freedom cases (p. 25) indicates that median processing times are significantly off target.

See comment 12.

In reviewing cases and statistics with the Department of Defense, we have come to the conclusion that the list of cases reviewed by the GAO included cases that were not identified by State as OEF cases (e.g., no record of notification or, in a number of cases, no direct connection to OEF) even though Coalition partners were involved. Therefore, several of the cases that were sampled did not receive expedited processing required of the OEF export licensing processing regime. Again, in a number of cases, the documentation that was submitted was incomplete (e.g., no signed contract) or important information for consideration was not spelled out (e.g., the end-user was not clearly identified). These cases were usually held by Licensing Officers pending receipt or clarification of information rather than returned without action (RWA'd) precisely because they were OEF cases. We do not have a full analysis regarding these matters, but there is every reason to believe that a review of truly OEF cases would result in significantly different statistics (i.e., lower median processing times).

GAO Comments

1. Our report identifies various arms export control initiatives implemented by State, as well as discusses State's compliance efforts. Initiatives identified include DTSI, expedited processing for Operations Enduring Freedom and Iraqi Freedom applications, electronic licensing, and organizational realignment. We evaluated those initiatives for which data were available. As we reported, license applications processed under various initiatives have generally not been processed within the time frames established by State and several initiatives have not been widely used by exporters. Senior State officials also informed us that they have not evaluated the initiatives' effects on the arms export control system. We are, therefore, uncertain what the basis is for State's conclusion that it has successfully undertaken these initiatives, particularly since State did not provide any additional data to support its contention.

2. It is not clear from existing data why carrying out activities integral to the arms export license process would contribute to increased processing times, particularly since State has received increased resources over the years to carry out these activities. State suggested that ensuring a thorough license review has contributed to increased processing times. However, as noted in the report, processing times began increasing during the period State was not screening all parties against the watchlist as required by law. State also suggested that more referrals of increasingly complex cases have contributed to increased processing times. Yet our analyses of State's data clearly show that the relative number of cases referred, or staffed, remained fairly constant from fiscal year 1999 through the first 7 months of fiscal year 2004. Further, this would not explain why processing times have increased for nonstaffed cases. Also during the course of our audit, State officials only provided anecdotal support for their assertion that cases have become more complex.

3. Our report does not imply whether changes to the arms export control system were needed following the September 2001 terror attacks. Rather, it clearly states what has or has not occurred in terms of changes to the system after the attacks. During the audit, senior State officials acknowledged that State has not proposed statutory or regulatory changes in response to the September 2001 attacks. Our report already includes a senior State official's explanation of why such changes were not needed. We also note that beyond describing what the arms export control system is intended to do, State does not provide support for its comments regarding the effectiveness of its arms export controls in the post-9/11 environment.

4. Our report already notes that while State reviewed the status of implementation, it did not evaluate the effects of various initiatives on the arms export control system. Further, GAO has previously reported[17] that DTSI was launched in 2000 without a demonstration of how the measures would achieve identified goals or an analysis of existing problems. At that time, there was little assurance that any underlying problems with the U.S. export control system had been sufficiently analyzed to determine what the causes of the problems were and whether the DTSI measures would remedy any existing problems. Given this continued lack of evaluation, we are uncertain as to the basis for State's conclusion that the initiatives do not need to be changed in the aftermath of the September 2001 terror attacks.

   Our report refers to the White House-directed comprehensive assessment of the effectiveness of U.S. defense trade policies, which is commonly known as NSPD-19. However, because the NSPD-19 assessment was ongoing during the time of our audit and its results have not been released, we were unable to evaluate it. Further, State did not brief us on the NSPD-19 assessment or any resulting proposals.

5. During the course of our audit, State, Homeland Security, and Justice officials characterized coordination with law enforcement regarding the implementation of initiatives as limited. The only exceptions identified were the proposed licensing exemptions. Our report already cites State's explanation, which is consistent with that offered in State's comments, as to why coordination was limited to the proposed exceptions. Therefore, our report does not need to be revised.

6. As explained in our report, Homeland Security and Justice officials generally oppose licensing exemptions because exemptions increase the risk of diversion and complicate enforcement efforts. Our report also acknowledges that the two departments have officially stated that they do not object to the agreements reached with the governments of Australia and the United Kingdom to allow for license-free exports to those countries. However, in the letters cited in State's comments, both departments noted that there are risks associated with the proposed exemptions.

[17] See GAO, *Defense Trade: Analysis of Support for Recent Initiatives*, GAO/NSAID-00-191. (Washington, D.C.: Aug. 31, 2000).

7. State's comments do not address the strong concerns raised in CBP's letter regarding the proposed aircraft-related exemptions. As we noted in our report, CBP warned it would not be able to enforce the proper use of the exemptions. State's comments also do not address Homeland Security and Justice officials' general comments regarding the risks and enforcement difficulties associated with licensing exemptions.

8. During the course of our audit, State export licensing officials informed us that the quality of applications submitted under this initiative remained constant. Thus, the quality of applications does not explain the increased processing times from fiscal year 2003 through the first part of fiscal year 2004 for Operation Iraqi Freedom applications.

9. State's comment that the number of authorized licensing officers has consistently increased contradicts information State provided during the course of our audit. According to the information provided by State, the number of authorized licensing officer positions decreased from 37 in fiscal year 2003 to 32 in fiscal year 2005. Because State did not provide revised figures in its comments, we have no basis to change the information contained in the report. Further, in analyzing the information provided by State, authorized positions clearly shifted from licensing officers to other positions within DDTC's management and policy functions. While this may have been part of DDTC's realignment efforts, it nevertheless has resulted in fewer authorized licensing officer positions and coincides with a decrease in the number of licensing officer positions filled.

10. State officials repeatedly informed us that they do not track average weekly caseloads and did not know whether they were meeting the required weekly average of 40 cases for each licensing officer. Further, State's comments provide a theoretical average that appears based on the number of cases closed by licensing officers during a given year. This is not an accurate reflection of licensing officer caseloads because it does not include open cases being processed. For example, State officials informed us that on June 21, 2004, there were 5,343 open cases. Given that State had 31 licensing officers in fiscal year 2004, that averages to 172 cases per licensing officer on that date.

11. Our report does not need to be revised because it accurately conveys information provided to us during the course of our audit. We are uncertain as to the basis for State's comment that the majority of cases were screened against the watchlist given that State acknowledged it

does not know how many applications had parties that were not fully screened against the watchlist as required by law. Also, given that State has not completed its retroactive review of applications submitted between June 2002 and December 2003, it is not clear how State concluded that the vast majority of the parties to those applications were screened by other means. Finally, in light of the risks posed by not screening all parties against the watchlist, it is not clear why available resources have not been dedicated to completing the retroactive review.

12. State's comment that our analyses of Operation Enduring Freedom applications included cases not identified by State is inaccurate. As explained in our scope and methodology, we used the unique identifiers entered into State's licensing database to identify applications processed under various initiatives, including the Operation Enduring Freedom initiative. Thus, the information in the report regarding the number of Operation Enduring Freedom applications and their associated processing times is based on our analyses of applications coded by State. As part of our data reliability analysis, we assessed whether information contained in State's database matched State's hardcopy files and found it to be reliable for the purposes of our report. It is not clear from State's comments how or why it has since determined only certain cases coded in its database are "truly" related to Operation Enduring Freedom. We cannot verify State's assertion about possibly lower Operation Enduring Freedom processing times because State did not provide us with information regarding which cases it now considers "truly" related to Operation Enduring Freedom. We also note that State did not conduct its own analysis despite having all available data. Further, State's comments, along with those provided by Defense, indicate inconsistencies in the identification of cases for special processing. It appears that State coded cases in the database as related to Operation Enduring Freedom, but, for reasons that are not clear in State's comments, did not expedite the processing of those cases.

Appendix IV: Comments from the Department of Defense

Note: GAO's comments supplementing those in the report's text appear at the end of this appendix.

OFFICE OF THE UNDER SECRETARY OF DEFENSE
2000 DEFENSE PENTAGON
WASHINGTON, DC 20301-2000

JAN 2 4 2005

POLICY

Ms. Katherine V. Schinasi
Managing Director
Acquisition and Sourcing Management
U.S. Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Ms. Schinasi:

This is the Department of Defense (DoD) response to the draft GAO report, "Defense Trade: Arms Export Control System in the Post-9/11 Environment" (Code 120333, Report #GAO 05-234). We have reviewed the draft and submit the attached comments.

If you have any questions regarding our inputs, please contact my point of contact, Mr. Charles Shotwell, (703) 325-3784.

Lisa Bronson
Deputy Under Secretary of Defense,
Technology Security Policy and
Counterproliferation

Attachments
As stated

Now on p. 13.

See comment 1.

See comment 2.

Department of Defense (DoD) Comments on Draft GAO Report "Defense Trade: Arms Export Control System in the Post-9/11 Environment" (Proj. # 120333, Report #GAO 05-234)

We note that though we are in general agreement with the report, our detailed review of the report indicates that in certain cases the data requires further explanation. Details are provided below.

Page 11, Table 1, Workload: Figures provided for DTSA somewhat overstate the organizational assets available for licensing. These figures include 31 personnel assigned to the Space Directorate. This directorate was established in 1999 solely for the purpose implementing the space launch and space systems monitoring requirements of PL 105-261 on a reimbursable basis. As Space Directorate's role is not appropriated, they are prohibited from actions involving the review of licenses (a governmental function). Thus, including them in the total overstates the assets DTSA has available for license review. Figures for DTSA should be adjusted as follows:

Number of Personnel	132
Expenditures (in millions)	$20.492

Pg 18, Processing Times: The chart on page 16 refers to a constant median processing time of cases referred to DoD by the Directorate of Defense Trade Controls (DDTC) between FY 00 and FY 03, despite the increased workload. The chart also indicates an improvement for FY 04. Though DoD agrees with the trend, we cannot validate the numbers. The figures used to generate the data were based on the date DDTC "staffed" the case to DoD. This is the date a licensing officer at DDTC makes the decision to staff the case and does not represent the date the case is actually transferred to DoD nor the date of receipt by DoD. Since the processing times are based on calendar days, this "transit time" added between one and four days to any given license; time not available for review, but counted against, DoD.

Review of the DoD database for the same time frames revealed the following:

FY	1999	2000	2001	2002	2003	2004 (to 30 Apr)
Cases	13488	14395	13698	14844	16720	9478
Median*	32 days	19 days	20 days	22 days	21 days	18 days
Difference from DDTC data	-7 days	-10 days	- 9 days	-7 days	-8 days	-9 days

* date of creation to date released to DDTC

1

The caveat on the table above is important. Up until January 2004, all cases received by DoD were received in hardcopy. From the date of receipt to creation date, the cases were at DoD but were not available for review pending input to DoD's database. This "creation time" does account for some of the difference in the reported median age, but spot checks of the data available to DoD do not support a median creation time sufficient to make up the difference between the chart above and the State reported figures. More importantly, with the fielding of the USXports database, creation times can now be accurately tracked. In November, 2004, the average time a case was reviewed by DoD, from receipt from DDTC to position release back to DDTC, averaged just 18 days.

Now on p. 24.

See comment 3.

Pg 22, Final Actions: As written, the report gives the impression that there is a direct correlation between the increase in the number of cases not staffed and the increase in the number of cases approved without provisos. Rather, this may have been coincidental impact of a concerted effort, begun by DTSA in 2003, at Proviso Reform. This initiative constituted analysis of provisos previously imposed, training of reviewers and a careful screening of provisos recommended for final positions. The goal of the initiative was to eliminate provisos which were either duplicative of the ITAR, unenforceable by the applicant, or redundant or not applicable to the license application. As a consequence of this effort, DTSA has recommended provisos on a third fewer cases and this may have contributed to the overall drop in cases approved without provisos. Likewise, it must be noted that provisos are correctly applied in only two circumstances: when the application does not sufficiently describe the export or when the export exceeds what would be in the national security interest to approve but can be limited through the use of provisos. Likewise, since part of proviso reform included outreach to applicants, a decline in the application of provisos may also indicate that the quality of the applications received from exporters is improving and there is anecdotal evidence to support this conclusion.

Now on p. 25.

See comment 4.

Pg 23, Operation Enduring Freedom (OEF)/Operation Iraqi Freedom (OIF): Procedures established between DDTC and DoD for special handling required that the case be staffed to DoD by facsimile and the facsimile cover sheet identifies the case as OEF or OIF. This eliminated the "transit" time referred to above on routine cases and these cases were created (inputted into the database at DoD) on a priority basis. Discussions with the GAO indicate that the identification of the cases used to develop the tables was based upon the "coding" of cases as OEF or OIF by DDTC in their database. In-depth review of the cases on file at DTSA that were handled as OEF or OIF based on facsimile requests indicates that the cases coded as OEF or OIF in State's database understates the number of cases actually treated as such by DoD by over 50% and includes cases that, while perhaps related to OEF or OIF based on the end user, *were not handled as such by either DDTC or DoD* at the time of processing. DoD does not have the information available on final case disposition to do a complete review, but an update of the tables based on the information available does alter the basic data and suggests that the conclusions of the GAO may be overstated.

2

Likewise, consideration should be given to the possibility that the logical goal of OEF and OIF expedite, to get material to US forces and coalition partners engaged in operations, may have been more broadly interpreted to the detriment of processing time. While the majority of cases reviewed by DoD were for items required by forces in country or about to deploy, a large number appear to be for exports that did not go to that limited end use. Indications of this can by seen in the high number of technical assistance agreements (TAAs) processed under OEF and OIF (26 for OEF in FY 03 alone), licenses to non coalition partners (an export of a baggage screening system to proscribed country for example), or export licenses for "marketing." Most TAAs were for the long term in home country support of weapons programs (these licenses require more staffing and analysis than hardware licenses due to the long term impact of the technology transfer); licenses to non-coalition partners required extensive review and licenses for marketing of first time exports, however laudable, seem to support the applicant more than the deployed forces. Current instructions contain no limitation on use of the expedited process; DDTC's instructions on their database merely provide the procedures for identifying a case as OEF or OIF and leave it to the applicant, presumably, to determine the applicability. Review of the cases suggests that specific instructions regarding qualification of a license for the expedited process and a more rigorous screening of the cases was warranted before the cases were selected for expedited handling. Such qualification and screening would have reserved this channel to those licenses genuinely required for support of the operations and would be in the best interests of the USG.

Now on p. 27.

Page 25, Table 4, Operation Enduring Freedom:

	Cases Staffed		Median Processing (Days)	
	GAO Spreadsheet	DoD Matrix	GAO Spreadsheet	DoD Matrix
FY 02	70	207	5	4
FY 03	116	187	7	7
FY 04	20	29	6	4

OEF Discrepancies by FY other than case totals:

FY 02:

Two cases listed as staffed to DoD were staffed, but not identified as OEF Expedite.

FY 03:

DoD has no record of staffing four cases. Eleven cases on the spreadsheet were staffed to DoD for review but were not identified as OEF Expedite. All were for OEF involved

3

countries. One case counted was for OIF not OEF and was counted against that program.

FY 04:

Two cases were OIF cases and handled under that program. DoD has no record of one case listed being staffed by DDTC. Another case appears to be on OEF spread sheet erroneously. It is an advisory opinion for the sale of an air defense/air traffic control radar to Iraq. One case is for a baggage screening system to a proscribed country that was not a coalition partner. It did come over as "anti-terrorism, expedite" but without affirmative identification with OEF. It was treated as an OEF case at DoD.

Now on p. 29.

Page 27, Table 5:

Operation Iraqi Freedom:

	Cases Staffed		Median Processing (Days)	
	GAO Spreadsheet	DoD Matrix	GAO Spreadsheet	DoD Matrix
FY 03	8	26	1.5	1
FY 04	18	36	6	2.5

OIF Discrepancies other than case totals by FY:

FY03:

Two cases on the GAO list were not treated by DoD as OIF. Since both cases were electronically transmitted, it is presumed that they were not identified as requiring special handling as no fax had been received. Cases were clearly OIF related. Note: Including these two cases as OIF would make the total cases reviewed by DoD total 28 but would not effect DoD median processing days (still 1).

FY 04:

One case was received in hardcopy in normal distribution. Export was for Gen III image intensification tubes for tank night sights for Italy, no record of Iraq connection with end use. Note: if this case were included, it would raise the number of staffed cases to DoD to 37 and change the median processing days to 3 vice 2.5.

In one case, DoD has no record of staffing from DDTC. In another case, DoD has no record of staffing from DDTC as an OEF case but was clearly for Iraq. DoD treated this case as OIF and it is counted under that program.

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Now on p. 37.

See comment 5.

Pg 35, D-Trade and Electronic Licensing: Paragraph 1 contains a factual inaccuracy. Electronic cases were staffed to DoD during the period covered by this report, but the number was insignificant (52 of 2950 DSP-5s). DoD agrees that there is a "transition cost" in converting to electronic licensing as analysts adjust to new case presentations. However, the transition can be mitigated by standardizing the format of documents submitted electronically to PDF text searchable. Also, it must be noted that for staffed cases, any increased reviewer time would be more than offset, as indicated by the timeliness of staffed D-Trade cases in November 2004, by the capability of an electronic system to eliminate the time wasted in the transit and database input of hardcopy cases.

Now on p. 42.

See comment 6.

Page 40, Proviso Reform: The term "self-imposed provisos" inaccurately depicts one facet of the proviso reform effort. As discussed above, proviso reform was initiated to insure that provisos recommended for imposition on licenses be applicable to the export, enforceable by the applicant and not redundant to either the ITAR or the application. The ITAR, in 22 CFR 127.2(a) defines using any export control document "containing a false statement, misrepresentation or material omission" as unlawful. 22 CFR 127.2(b) defines an export control document to include "an application for permanent export or a temporary import license *and supporting documentation*." (Emphasis added) Some applicants, rather than reviewing and modifying supporting documentation provided in a license application, have instead chosen to include previously imposed provisos in an attachment to the license application or transmittal letter. DoD's reviewers evaluate the restrictions included in this manner as part of the review process. If it is felt that the export application adequately describes and limits the requested export (including any the applicant explains in attachments), provisos are not recommended. However, if the application, including these applicant attachments, does not clearly limit the export to the satisfaction of DoD, provisos are recommended to ensure clarity. It is unclear to DoD, given 22 CFR 127.2, how reliance on the applicants' own statements would adversely effect enforcement. Likewise, it is difficult to understand why reliance on applicant limitations presents greater compliance concerns than a system that imposed redundant or unnecessary provisos.

Now on p. 43.

See comment 7.

Page 41, Coordination on Initiatives: The opening statement that DoD has "sought only limited coordination" with the Department of Homeland Security and the Department of Justice on the Defense Trade Security Initiative and other initiatives leaves the false impression that DoD has a role in the enforcement process. DoD's role as expressed on Page 8 is far more limited and contains no statutory requirement for enforcement. DoD stands ready to support the Department of State in any coordination required to support enforcement of these necessary measures.

Now on p. 61.

Page 59, Voluntary Disclosures: As with licenses, DTSA reviews only a portion of the total number of voluntary disclosures received by DDTC. As such, it is difficult to dispute DDTC's claim that the increase in voluntary disclosures was a result of "a robust compliance effort on the part of industry." It should be noted that, of the 137 cases

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See comment 8.

reviewed by DTSA in FY 03, only 11 were determined to have been detrimental to or possibly detrimental to US national security. Further, a significant number of the voluntary disclosures reviewed by DoD were initiated following mergers (24) or by the direction of DDTC (8) or after a USG office "recommended" that a "voluntary" disclosure be submitted (2). The former suggest that the merging company submitted the voluntary disclosure to address liability issues, the latter can hardly be considered voluntary in the classic sense.

6

GAO Comments

1. We have revised our report to reflect that a portion of DTSA's resources were not involved in the review of license applications.

2. As explained in our scope and methodology, and as acknowledged by Defense, median processing times in our report are based on our analyses of State's licensing data. Because we did not analyze Defense's data or assess its reliability, we cannot verify the accuracy of the data provided in Defense's comments. However, our report acknowledges Defense's observation regarding the lag between when State decides to refer cases and when Defense begins its review. Regardless of the reasons for delays, transit time contributes to the overall time it takes the government to process a case and provide its final determination to the exporter.

3. We have clarified the report language regarding the overall increase in the number of cases approved with provisos following the events of September 2001.

4. As discussed in our scope and methodology and Defense's comments, the information provided in our report regarding the number of Operation Enduring Freedom and Operation Iraqi Freedom cases and their associated processing times is based on our analyses of applications identified in State's database as related to the two operations. As part of our data reliability analysis, we assessed whether information contained in State's database matched State's hardcopy files and found it to be reliable for the purposes of our report. While Defense identified discrepancies between its files and the corresponding records in State's database, we cannot validate these discrepancies or their frequency as we did not review or assess the accuracy or completeness of Defense's files. Nevertheless, Defense's comments, along with those provided by State, suggest a lack of agreement and inconsistencies in the process for identifying cases for expedited review.

5. Our report reflects information provided by State during the course of our audit and our analysis of State's licensing database. We have revised the report to indicate the basis for our statement that applications processed via D-Trade during the 4-month period were not staffed outside DDTC for review.

6. The use of the term "self-imposed conditions" is a reflection of State's characterization of the proviso reform initiative and State's concerns with that initiative's possible effects on enforcement efforts. Defense's comments, along with information provided to us by State, indicate

that there is a fundamental disagreement between the two departments regarding the appropriate use of provisos and the ability to enforce limitations contained in license applications.

7. We have revised our report based on Defense's comment.

8. We did not evaluate the factors that prompted companies to submit specific disclosures. Therefore, we cannot comment on the validity of Defense's comment and whether it is applicable to the majority of disclosures, which were not reviewed by Defense. However, according to a State compliance official, the number of disclosures presented in our report only includes disclosures of potential violations voluntarily submitted by companies and not disclosures submitted at the direction of the U.S. government.

Appendix V: Comments from the Department of Homeland Security

U.S. Department of Homeland Security
Washington, DC 20528

Homeland Security

February 1, 2005

Ms. Katherine Schinasi
Managing Director, Acquisition and Sourcing Management
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Ms. Schinasi:

RE: GAO-05-234, Arms Export Control System in the Post-9/11 Environment
(GAO Job Code 120333)

Thank you for the opportunity to comment on the subject draft report. The Department of Homeland Security (DHS) appreciates the work done related to enforcement challenges. Although the report contains no recommendations, we are providing the following comments that may enhance the report.

Now on p. 14.

After the first paragraph on page 12, we suggest including the following statements: "CBP is a regulatory and enforcement arm of the export process. CBP supports the system by reviewing licenses, permits and other requirements before items are exported, and also conducts on-site inspections. During this process, CBP officers compare export documentation with on-site commodities for compliance purposes. Discrepancies are aggressively pursued. Commodities are identified, tallied, referred for license verification, detained, seized, as appropriate and exporters referred for investigation and prosecution, as warranted."

Now on p. 57.

Please substitute the following sentence for the one on page 55. U.S. Immigration and Customs Enforcement officials present during the GAO interview believe it more accurately reflects what was said.

"According to ICE officials, the drop in arms export-related arrests and indictments in fiscal year 2002 may be the result of a more intensive focus on ensuring that dangerous goods and individuals did not enter the country in the immediate aftermath of the September 2001 attacks."

Now on p. 59.

Please consider inserting the following statement after the first paragraph on page 57: "CBP participated in the Blue Lantern Program from fiscal year 1999 through April 2004 by conducting export compliance inspections, identifying, and reporting potential violations to State and Defense."

www.dhs.gov

Now on p. 61.

Insert the following statement after the first paragraph on page 59:
"CBP participated in the Voluntary Disclosures program throughout the monitoring period (FY 1999 through April 2004) by conducting export compliance outreach programs and training endeavors with the Department of Commerce."

Now on p. 63.

Insert the following statement after the first paragraph on page 61:
"CBP actively participated in this program throughout the monitoring period by conducting export compliance inspections, identifying, and reporting potential violations to the responsible agencies."

Technical comments will be provided separately.

Sincerely,

Michael McPoland
for Steven Pecinovsky
Acting Director
Departmental GAO/OIG Liaison Office

MMcP

Appendix VI: GAO Contacts and Staff Acknowledgments

GAO Contacts

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Acknowledgments

In addition to those named above, Johana R. Ayers; E. Brandon Booth; Richard K. Geiger; Arthur James, Jr.; Masha Pastuhov-Pastein; and Lisa Simon made key contributions to this report.

Related GAO Products

Nonproliferation: Further Improvements Needed in U.S. Efforts to Counter Threats from Man-Portable Air Defense Systems. GAO-04-519. Washington, D.C.: May 13, 2004.

Defense Acquisitions: DOD Needs to Better Support Program Managers' Implementation of Anti-Tamper Protection. GAO-04-302. Washington, D.C.: March 31, 2004.

Joint Strike Fighter Acquisition: Cooperative Program Needs Greater Oversight to Ensure Goals Are Met. GAO-03-775. Washington, D.C.: July 21, 2003.

Defense Trade: Better Information Needed to Support Decisions Affecting Proposed Weapons Transfers. GAO-03-694. Washington, D.C.: July 11, 2003

Export Controls: Processes for Determining Proper Control of Defense-Related Items Need Improvement. GAO-02-996. Washington, D.C.: September 20, 2002.

Defense Trade: Lessons to Be Learned from the Country Export Exemption. GAO-02-63. Washington, D.C.: March 29, 2002.

Export Controls: Reengineering Business Processes Can Improve Efficiency of State Department License Reviews. GAO-02-203. Washington, D.C.: December 31, 2001.

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Defense Trade: Analysis of Support for Recent Initiatives. GAO/NSIAD-00-191. Washington, D.C.: August 31, 2000.

Defense Trade: Status of the Department of Defense's Initiatives on Defense Cooperation. GAO/NSIAD-00-190R. Washington, D.C.: July 19, 2000.

Export Controls: License Screening and Compliance Procedures Need Strengthening. GAO/NSIAD-94-178. Washington, D.C.: June 14, 1994.

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