



Testimony



STATEMENT OF
DONALD MANCUSO
ACTING INSPECTOR GENERAL,
DEPARTMENT OF DEFENSE
BEFORE THE
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
ON
EXPORT LICENSING PROCESSES FOR
DUAL-USE COMMODITIES AND MUNITIONS

Report Number 99-212

DELIVERED: June 23, 1999

Office of the Inspector General
Department of Defense

Hold for Release
Until Delivery
Expected 10:00 a.m.
June 23, 1999

Statement by
Donald Mancuso
Acting Inspector General
Department of Defense
Before the
Senate Committee on Governmental Affairs
on
Export Licensing Processes for
Dual-Use Commodities and Munitions

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to be here today to discuss the Federal Government's export licensing process for dual-use commodities and munitions. In response to Chairman Thompson's letter of August 26, 1998, an extensive review has been conducted by Inspector General (IG) teams from the Departments of Commerce, Defense, Energy, State, Treasury and the Central Intelligence Agency. The efforts of the review teams were coordinated by a working group, which avoided duplication and enabled us to track individual export license application cases across agency lines and to address interagency issues. The results of our review are contained in the interagency report signed by the participating IGs on June 18, and six individual agency reports, signed by the respective IGs between May 28 and June 18.

Because my office assembled and published the interagency report, I will begin my testimony by summarizing its main points. I again emphasize, however, that the report represents a joint effort.

Background

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

The dual-use export licensing process is managed and enforced by the Department of Commerce while the munitions export licensing process is managed by the Department of State. The advisory roles of other agencies are similar in both of these license application processes. The Departments of Defense and Energy review the applications and make recommendations to Commerce and State. The Central Intelligence Agency and the U.S. Customs Service (Department of Treasury) provide relevant information to Commerce and State to assist them in the license review. Customs also enforces licensing requirements for all U.S. export shipments except outbound mail, which is handled by the U.S. Postal Service.

In FY 1998, the Department of Commerce received 10,696 dual-use export license applications and the Department of State received 44,212 munitions export license applications.

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

Interagency Review Results

To a considerable extent, our June 18, 1999, interagency report is an update of a similar report that was issued jointly by the IGs of Commerce, Defense, Energy and State in 1993. The previous report, titled, "The Federal Government's Export Licensing Processes for Munitions and Dual-Use Commodities," covered the pertinent issues under seven headings. The current report is structured along similar lines.

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

The second area pertains to procedures used in the export license review processes. The Commerce, Defense, Energy and State IG teams concluded that processes for the referral of dual-use license applications and interagency dispute resolution

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

The third area pertains to the cumulative effect of multiple exports to individual foreign countries. The U.S. Government lacked an overall mechanism for conducting cumulative effect analysis. However, some of the agencies involved in the export licensing process performed limited cumulative effect analyses, with the degree of analyses performed varying across the agencies. The Commerce, Defense, Energy and State IG teams

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

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

The fifth set of issues concerns guidance, training and undue pressure on case analysts. The review indicated that Defense, Energy and State licensing officials had adequate guidance to perform their mission; however, Department of Commerce licensing officers and Central Intelligence Agency licensing analysts could benefit from additional guidance. On-the-job training was the primary training available at the Departments of Commerce, Defense, Energy, and State for licensing officers. The Commerce, Defense and State IG teams identified a need for a

standardized training program in their agencies. With very few exceptions, Commerce and Defense licensing officials reported they were not pressured to change recommendations on license applications. No Energy or State export licensing officials indicated they were pressured regarding their recommendations.

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

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

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

Recommendations and Other Reports

The IG teams made specific recommendations relevant to their own agencies. Those recommendations and management comments are included in the separate reports issued by each office, which are in Appendix C (Commerce), Appendix D (Defense), Appendix E (Energy), Appendix F (State), Appendix G (Treasury), and Appendix H (Central Intelligence Agency) of the interagency report. Appendixes D, E, and F are in Volume II. Appendixes G and H, which are classified, are in Volume III. Because of time constraints and the fact that there are no additional recommendations in the interagency report, management was not asked to respond separately to it.

Department of Defense Export Licensing Issues

Now I would like to change focus from the interagency report to the report issued by my office on Defense participation in the export control processes. Again, I would like to emphasize that our objective was to review the export licensing process and not to assess the appropriateness of individual license

applications. To summarize the results of the Defense IG team's review, I will address each of the 14 issues that Chairman Thompson posed in his August 1998 letter.

Issue 1. Examine whether the current, relevant legislative authority contains inconsistencies or ambiguities regarding the licensing of dual-use and munitions commodities, and the effect of any such inconsistencies and ambiguities.

Conclusion: The general nature of the Export Administration Act and the Arms Export Control Act creates a broad framework, but we found no inconsistencies or ambiguities in either law. The Acts give Federal departments and agencies flexibility to change details regarding the components of the dual-use commodities and munitions export licensing processes, without requiring frequent changes to legislation. We also concluded that the dual-use licensing process would be best served through reenactment of the Export Administration Act.

Issue 2: Examine whether Executive Order 12981 (1995) as implemented is consistent with the objectives of the Export Administration Act and other relevant legislative authority.

Conclusion: Executive Order 12981, as implemented, is generally consistent with the relevant objectives of the Export Administration Act, the principal legislative authority that we considered under this question. However, Executive Order 12981 decreased from 40 to 30 days the time that the Department has to review dual-use license applications. As a result of the shortened review period, the ability to locate the information necessary to inject into the license review process may have been diminished. However, it is difficult to measure the effect the decreased review time has had on the Department's review of dual-use license applications.

Issue 3: Determine whether there is a continued lack of interagency accord, as stated in the 1993 interagency report, regarding whether the Department of Commerce is properly referring export license applications (including supporting documentation) out for review by the other agencies.

Conclusion: Defense officials expressed general satisfaction with the dual-use export license applications that Commerce referred for review, although Defense officials disagreed with Commerce's decision not to refer 5 of 60 sampled dual-use license applications. They also expressed concern that Commerce referred too few commodity classification requests to

Defense for review. As a result, in some cases, Commerce made decisions on license applications with national security implications without the benefit of Defense input.

Issue 4: Determine whether the interagency dispute resolution (or "escalation") process for appealing disputed license applications allows officials from dissenting agencies a meaningful opportunity to seek review of such applications, and assess why this process is so seldom used.

Conclusion: With one possible exception, the interagency escalation process provided Defense a meaningful opportunity to appeal disputed dual-use license applications, although the outcome of the process often favored the Commerce position. The number of applications appealed to the Advisory Committee on Export Policy decreased as a result of Executive Order 12981, and Defense elected not to escalate disputed dual-use applications for a variety of reasons. Defense officials stated the, in general, decisions about escalating cases were made on the basis of the substance of the case, the viewpoints expressed by Department principals and the likelihood of prevailing at the Advisory Committee on Export Policy. Disputes over munitions applications were resolved between office chiefs at Defense and State.

Issue 5: Review whether the current dual-use licensing process adequately takes into account the cumulative effect of technology transfers resulting from the export of dual-use items, and the decontrol of munitions commodities.

Conclusion: The licensing process at the Technology Security Directorate, Defense Threat Reduction Agency, occasionally takes into account the cumulative effect of technology transfers, but participants in the licensing process did not routinely analyze the cumulative effect of proposed exports or receive assessments to use during license reviews. In addition, Defense organizations did not conduct required annual assessments of the impact of technology transfers that could provide information on the cumulative effect of proposed exports. As a result, the Department cannot ensure that the licensing process takes into account the cumulative effect of technology transfers. As of March 1999, the Technology Security Directorate, Defense Threat Reduction Agency, had initiated actions designed to increase the degree to which cumulative effect analysis was incorporated into the licensing process, but the matter is still under review. We recognize that organizing and resourcing a meaningful cumulative effect analysis process

pose a significant challenge, but this is clearly an area that needs more emphasis.

Issue 6: Review whether the current munitions licensing process adequately takes into account the cumulative effect of technology transfers resulting from the export of dual-use items, and the decontrol of munitions commodities.

Conclusion: The observations made on Issue 5 also apply to the munitions licensing process.

Issue 7: Determine whether license applications are being properly referred for comment (with sufficient time for responsible review) to the military services, the intelligence community, and other relevant groups (the "recipient groups") by Defense and other agencies. Consider in particular numerical trends in the frequency of such referrals, trends in the type of applications referred, trends in the nature of the taskings made in connection with the referrals, and the perceptions of officials at the recipient groups.

Conclusion: The Defense Components, except the Defense Intelligence Agency, have received about the same number of case referrals annually over the past 8 years. However, the

Technology Security Directorate, Defense Threat Reduction Agency, did not always appropriately refer license applications to other Components for review. Of the applications we reviewed, various Components considered that 12 percent of the dual-use and 24 percent of the munitions license applications were not properly referred. If the Technology Security Directorate, Defense Threat Reduction Agency, does not properly refer a case to other knowledgeable Component for review, the Department's position may be developed with incomplete information.

Issue 8: Determine whether license review officials at each of the agencies are provided sufficient training and guidance relevant for reviewing license applications, and whether more formal training and guidance is warranted.

Conclusion: The Technology Security Directorate, Defense Threat Reduction Agency, and other Defense organizations involved in the review processes received appropriate guidance from a range of sources, and nearly all licensing officers stated the guidance was adequate for performing their duties. Licensing officers also stated that they generally had sufficient training; however, some licensing officials believed that a classroom training program and training plan for

personnel reviewing export license applications should be established. We were unable to determine if the lack of a classroom training program or a training plan has materially affected licensing duties, but we concluded that putting more emphasis on training would be prudent.

Issue 9: Review the adequacy of the databases used in the licensing process, such as the Defense Foreign Disclosure and Technical Information System [FORDTIS] paying particular attention to whether such databases contain complete, accurate, consistent, and secure information about dual-use and munitions export applications.

Conclusion: FORDTIS provides a useful communication and coordination mechanism for the Department on export control matters, although limitations existed in the system that reduced the support provided to decisionmakers. In addition, as will be discussed in our response to Issue 13, inadequacies existed in the use of FORDTIS to provide an audit trail for export licensing decisions.

Issue 10: In congressional testimony, a Defense licensing officer described instances where licensing recommendations he entered on FORDTIS were later changed without his consent or

knowledge. Examine those charges, and assess whether such problems exist at your agencies.

Conclusion: Instances occurred in which recommended positions entered in FORDTIS by a licensing officer were changed without the consent or knowledge of that officer, although the number of such occurrences could not be determined. These changes appear to have been based on supervisors' disagreements with the licensing officers conclusions. Such changes are permissible under Department policy. In addition, documentation related to the changes was not always complete.

Issue 11: Determine whether license review officials are being pressured improperly by their superiors to issue or change specific recommendations on license applications.

Conclusion: We interviewed all Defense Threat Reduction Agency licensing officers and, with one exception, they indicated to us that they had not been subjected to any improper pressure to change specific recommendations on license applications. Other staff at the Technology Security Directorate, Defense Threat Reduction Agency, who did not formulate proposed recommendations on license applications, but who were at times involved with reviewing or processing license

applications, also did not report any improper pressure directed at them to change positions on specific license applications. However, several of the Technology Security Directorate staff members stated that management applied indirect pressure to encourage certain viewpoints. We are aware that at least one licensing officer has alleged retaliation by management for disclosing problems in the licensing review process.

Issue 12: Determine whether our Government still uses foreign nationals to conduct pre-license or post-shipment licensing activities and whether such a practice is advisable.

Conclusion: In general, Commerce and State conduct pre-license and post-shipment licensing activities. Defense provides limited support to Commerce and State pre-license and post-shipment licensing activities through Defense Attaché' Offices. Defense also supports State by monitoring certain foreign space launch activities under the provisions of munitions licenses. Defense has not used and does not plan to use foreign nationals to support Commerce or State pre-license and post-shipment licensing checks or to monitor space launches.

Issue 13: Determine whether the agency licensing process leaves a reliable audit trail for assessing licensing performance.

Conclusion: FORDTIS provided a long-term audit trail for positions on license reviews, but it did not always contain complete and accurate records of Defense and U.S. Government positions. The audit trail provided by FORDTIS for the sample reviewed generally agreed with the Commerce electronic records. However, in one instance the Commerce records showed a change to the conditional license approval from Defense that was not shown in FORDTIS. In another instance, a conditional approval recommended by Defense for a license application was not included in the Commerce record. In addition, the audit trail provided by FORDTIS did not include new information presented at interagency decision meetings, detailed results of those meetings, records of all applications referred to the National Security Agency, as well as key correspondence or technical data. As a result, the audit trail provided by FORDTIS cannot be used as a reliable means of assessing the degree to which overall Defense positions were in agreement with positions taken by the U.S. Government.

Issue 14: Describe the procedures used by agencies to ensure compliance with conditions placed on export licenses (for example, no retransfers without U.S. consent, no replications,

and peaceful use assurances) and assess the adequacy and effectiveness of such procedures.

Conclusion: The Department has a limited formal role in ensuring compliance with conditions placed on export licenses. In its support to State, the Technology Security Directorate, Defense Threat Reduction Agency, had adequate procedures for monitoring foreign space launch activities. Its informal process for reporting potential violations of license conditions and technology assessment control plans was also adequate. However, expected increases in the number of launch monitoring missions coupled with a programmed increase in staff to support these missions dictates the Department move to a more formal approach to reporting violations. If not, the informality of the current reporting process could fail to ensure that State receives the highest quality of reporting from Defense.

Recommendations

We made a number of recommendations to the Department to improve the effectiveness and efficiency of export licensing review efforts, as follows:

- The Under Secretary of Defense for Policy should revise Defense Directive 2040.2 to clearly state responsibilities and procedures regarding the performance of assessments designed to analyze the cumulative effect of technology transfers and the monitoring of compliance with any requirements established and to obtain FORDTIS access for country desk officers reviewing export license applications.
- The Director, Defense Threat Reduction Agency, should develop an agency-wide training policy, training plan, and a classroom training program for Defense Threat Reduction Agency licensing officers; provide other Defense Components the classroom training program for licensing officers; and, in coordination with the Department of State, develop and implement a memorandum of understanding on reporting requirements for the Space Launch Safeguards and Monitoring Program.
- The Director, Technology Security Directorate, Defense Threat Reduction Agency, should work with the Assistant Secretary of Commerce for Export Administration to develop additional guidance and procedures on how to implement 1996 National Security Council guidance on commodity

jurisdiction and commodity classification; develop an action plan with milestones for the integrated process team on the Militarily Critical Technologies Program that includes defining a process for identifying, prioritizing, and obtaining decisions on assessments related to the cumulative effect of technology transfers; reiterate his request that the Defense Components identify the types of licenses they would like to review; notify the Assistant Secretary of Defense (Strategy and Threat Reduction) of any Defense Component that does not identify the cases it wants to review; maintain a list of the types of export license applications that Defense Components have requested to review; establish procedures to ensure adequate documentation of changes to the position of a licensing officer; and establish procedures to ensure that FORDTIS records include the correct Defense position, additional information presented at the Operating Committee, an explanation of why Defense did not escalate disputed cases, the results of encryption cases referred to the National Security Agency, and key correspondence and technical data.

- The Deputy Under Secretary of Defense (Policy Support) should provide guidance to Defense Components on how to query FORDTIS in order to generate dual-use and munitions

reports; monitor modernization efforts of Commerce's export control information systems; and ensure that initiatives on electronic imaging in support of the export review process are successfully implemented within Defense.

Management Response

The Principal Deputy Under Secretary of Defense for Policy provided comments on our draft report that were generally responsive to the findings and recommendations. We made relatively minor adjustments in the final report, based on those comments, and have requested the Department to provide additional comments to clarify what corrective actions are going to be taken on a few specific items. We will track the progress of all agreed-upon actions through our audit followup procedures.

Conclusion

In conclusion, Mr. Chairman, we hope that this extensive multi-agency review will be useful to both the involved agencies and the Congress as efforts to update and improve U.S. export licensing practices continue. I would be remiss if I did not make a point of noting, in closing, that we received excellent

cooperation from agency personnel at all levels during this review.

This concludes my statement.