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**United States Department of State
and the Broadcasting Board of Governors**

Office of Inspector General

Office of Audits

**Compliance Follow-Up Review
on Export Controls**

Report Number AUD/IP-07-44, August 2007

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Summary

The Department of State Office of Inspector General (OIG) found, based on its review, that the Bureau of Political-Military Affairs, Directorate of Defense Trade Controls (PM/DDTC), had implemented 28 of the 29 recommendations contained in OIG reports on export controls issued from 2000 to 2006. OIG's recommendation from its 2006 report that PM/DDTC should establish performance measures that detail benchmarks and timeframes for reducing and eliminating the number of unfavorable post-license end-use checks remains unresolved. Nevertheless, PM/DDTC stated that over the next year it would consider whether such measures, along with time-lines and benchmarks, would be of value in its compliance and licensing functions. As a result, this recommendation will remain unresolved until PM/DDTC makes its final determination.

Background

In response to requirements of Section 1402 of the National Defense Authorization Act (NDAA) for FY 2000,¹ the Inspectors General of the Departments of Commerce, Defense, Energy, Homeland Security, and State, in consultation with the Director of Central Intelligence and the Director of the Federal Bureau of Investigation, are required to conduct an annual review through 2007 to assess the adequacy of current export controls and counterintelligence measures to prevent the acquisition of sensitive U.S. technology and technical information by countries and entities of concern. The Offices of Inspector General of these agencies conduct both agency-specific and interagency reviews.

Sound export controls and licensing operations are essential to preventing the spread of weapons of mass destruction technologies and to provide conventional technologies only to those entities that will use them responsibly. The Department registers U.S. companies and universities and issues licenses for the export of defense articles and defense services, including sensitive technical information, on the U.S. Munitions List (USML). PM/DDTC is responsible for controlling the export and temporary import of defense articles and defense services covered by the USML. A primary responsibility is to take final action on license applications for defense trade exports and for addressing matters related to defense trade compliance, enforcement, and reporting.

The Arms Export Control Act (AECA), as amended in 1996,² requires the President to establish a program for end-use monitoring of defense articles and services sold or exported under the provisions of the AECA and the Foreign Assistance Act.³ The requirement states that, to the extent practicable, end-use monitoring programs should provide reasonable assurance that recipients comply with the requirements imposed by the U.S. government on the use, transfer, and security of defense articles and services. In

¹ Public Law 106-65.

² 22 U.S.C. 2785.

³ 22 U.S.C. 2151.

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addition, monitoring programs, to the extent practicable, are to provide assurances that defense articles and services are used for the purposes for which they are provided.

To comply with the AECA, PM/DDTC conducts end-use monitoring of the commercial export of defense articles, services, and related technical data. End-use monitoring refers to the procedures used to verify that foreign recipients of controlled U.S. exports use such items according to U.S. terms and conditions of transfer. PM/DDTC's end-use monitoring is conducted through the "Blue Lantern" Program and entails an in-depth review either before (prelicense) or after (postlicense) the license is issued. U.S. embassy or, in some cases, PM/DDTC personnel conduct end-use checks abroad to verify the specific use and recipient of commercial defense exports and transfers controlled under the AECA.

Objective, Scope, and Methodology

To comply with the requirements of the NDAA for FY 2007, the overall objective of the Inspectors General, as defined in the Interagency Implementation Agreement, was to determine whether management had effectively addressed recommendations contained in export control reports required by the NDAA and that were issued between 1999 and 2007. The 2007 report will contain the results of reviews performed by the Inspectors General of the Departments of Commerce, Defense, Energy, Homeland Security, State, Treasury, United States Postal Service, and the Central Intelligence Agency. The Department of State's objective was to follow up on prior recommendations that remained open and determine the actions needed to implement the recommendations.

To achieve its objective, OIG reviewed the status of each recommendation contained in its export control reports issued from 2000 to 2006. (The reports and the status of each recommendation are detailed in the Results of Audit section of this report.) Additionally, OIG obtained and reviewed current PM/DDTC licensing policies and procedures, conducted interviews with appropriate staff, and reviewed applicable documentation and system checks. OIG also evaluated the Bureau Performance Plans for FYs 2006 and 2008. Finally, OIG discussed the status of each report recommendation with PM/DDTC officials.

To guide OIG's determination for the resolution of audit findings and recommendations, OIG examined guidance from the Government Accountability Office (GAO) concerning the definition of "Open Recommendation" and the standard in regard to the length of time that a recommendation should remain open. Additionally, OIG's Office of Audits (AUD) Manual, July 2006, Chapter 19, "Audit Resolution," defines AUD's policies and procedures for the resolution of audit findings and recommendations.

OIG's Office of Audits, International Programs Division, conducted this review from November 2006 through July 2007 in the Washington, DC, area. OIG performed this work in accordance with government auditing standards and included such tests and auditing procedures that were considered necessary under the circumstances.

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Results of Audit

Based on its review of the audit reports it had issued from 2000 to 2006 on export controls, OIG determined that 28 of the 29 recommendations contained in six reports (one report did not have any recommendations)⁴ had been implemented. The one remaining recommendation is unresolved because PM/DDTC officials stated that they would consider, over the next year, whether to implement the recommendation.

Reports With All Recommendations Closed

All of the recommendations contained in the following reports are considered closed as follows:

- “Department of State Controls Over the Transfer of Military Sensitive Technologies to Foreign Nationals From Countries and Entities of Concern” (00-CI-008), issued in March 2000, contained three recommendations relating to the transfer of military sensitive technologies to foreign nationals. OIG found that all of the recommendations had been implemented.
- “U.S. Munitions List and the Commodity Jurisdiction Process” (01-FP-M-027), issued in March 2001, contained seven recommendations relating to the USML and the commodity jurisdiction process. OIG found that all of the recommendations had been implemented.
- “Streamlined Processes and Better Automation Can Improve Munitions License Reviews” (IT-A-02-02), issued in March 2002, contained four recommendations relating to improving the munitions license reviews. OIG found that all of the recommendations had been implemented.
- “Review of End-Use Monitoring of Munitions Exports” (AUD/PR-03-31), issued in March 2003, contained nine recommendations relating to end-use monitoring of munitions exports. OIG found that all of the recommendations had been implemented.
- “Review of Export Controls for Foreign Persons Employed at Companies and Universities” (AUD/PR-04-24), issued in April 2004, contained four recommendations relating to export controls for foreigners employed at companies and universities. OIG found that all of the recommendations had been implemented.

Report With Unresolved Recommendation

OIG’s report “Review of Export Controls” (AUD/IP-07-01), issued in October 2006, found that although PM/DDTC had followed its policies and procedures before

⁴ “Export Licensing of Chemical and Biological Commodities” (AUD/PR-05-29), issued in April 2005.

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issuing a license, there were instances in which its end-use check, conducted either before or after a license was issued, resulted in “unfavorable determinations.” Unfavorable means that PM/DDTC had found derogatory, incomplete, or inaccurate information in the license application or there was a violation of export control policies and procedures. OIG discussed its report findings and proposed recommendations with PM/DDTC officials before it issued its draft report. OIG then provided a copy of the draft report to PM/DDTC officials, who reviewed the draft but did not provide comments on it. Subsequently, in an October 6, 2006, memorandum to OIG, PM/DDTC officials stated that they were “fully consider[ing]” the report’s two recommendations. As a result, both recommendations were considered unresolved, which required OIG to follow up on the recommendations to determine their statuses.

Recommendation Closed

OIG recommended (Recommendation 1) that PM/DDTC reassess its licensing policies and procedures and report to OIG within 60 days of report issuance the changes it will make to reduce and eliminate unfavorable post-license end-use checks.

PM/DDTC, in a May 14, 2007, e-mail to OIG, said that it was “always willing to consider any recommendation that would improve [its] licensing and compliance functions.” Its response provided a summary of “new and continuing” initiatives “to improve upon [its] work product” as follows:

- Education and Training

- PM/DDTC said that management from all of its divisions provide periodic training to incoming and current licensing staff “to help understand end-use monitoring and identify potential cases” and that in 2006 it had issued an updated Blue Lantern Guidebook.

- PM/DDTC also said that U.S. government staff and management participated in educational outreach efforts with federal law enforcement and intelligence communities that had “led to the establishment of better working relationships among staff and organizations.”

- PM/DDTC said that staff from the Research and Analysis Division (RAD), the division that implements the Blue Lantern end-use program, had visited over 20 countries in Europe, Asia, Latin America, and the Middle East to educate these governments on U.S. end-use monitoring and to improve their support to U.S. embassy officials. Also, PM/DTCC staff and management participate in forums on public training and education, including the Blue Lantern Program.

- Personnel

- PM/DTCC said that each licensing division has a compliance specialist from RAD who performs compliance duties and that RAD has added another contractor to its staff.

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- Coordination and Staff Visits

- PM/DTCC said that there would be better coordination among its three divisions and that it had made 23 compliance staff visits to U.S. defense companies in FY 2006.

OIG Analysis

OIG recognizes the significant enhancements PM/DDTC has both made and formulated to its licensing and compliance program and therefore to implement Recommendation 1. As a result, OIG considers Recommendation 1 closed.

Recommendation Unresolved

In its October 2006 report, OIG recommended (Recommendation 2) that PM/DDTC establish performance measures that detail benchmarks and timeframes for reducing and eliminating the number of unfavorable post-license end-use checks.

In its October 6, 2006, response, PM/DDTC said that it would “examine whether to incorporate the measures already used by DDTC in managing the Blue Lantern Program into the Bureau’s performance metrics.” It also said, in its May 14, 2007, e-mail to OIG, that it would “over the next year . . . agree to consider whether such measures, along with time-lines and benchmarks, would be of value in . . . overall compliance and licensing functions.”

OIG Analysis

OIG believes that the recommendation should be implemented. Performance measures for end-use checks could demonstrate progress in reducing and eliminating unfavorable determinations. Additionally, PM/DDTC could use the measures to track performance, identify areas for improvements, and make decisions about resource

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allocations. Therefore, the recommendation remains unresolved until PM/DDTC makes a final determination.