

March 30, 2006



Export Controls

Controls Over Exports to China
(D-2006-067)

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Acronyms

DTSA
USXPORTS

Defense Technology Security Administration
US Exports System



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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March 30, 2006

MEMORANDUM FOR DEPUTY UNDER SECRETARY OF DEFENSE
FOR TECHNOLOGY SECURITY POLICY AND
NATIONAL DISCLOSURE POLICY
DIRECTOR, DEFENSE TECHNOLOGY SECURITY
ADMINISTRATION

SUBJECT: Report on Controls Over Exports to China
(Report No. D-2006-067)

We are providing this report for review and comment. We conducted the audit to comply with Public Law 106-65, "National Defense Authorization Act of Fiscal Year 2000," Section 1402, "Annual Report on Transfers of Militarily Sensitive Technology to Countries and Entities of Concern."

We requested and received comments from the Acting Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy, who is also the Director of the Defense Technology Security Administration.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Deputy Under Secretary's comments were responsive; however, we request additional comments on Recommendation 2.a. by May 2, 2006. We revised, redirected, and renumbered Recommendation 1.a. to the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy, based on the Deputy Under Secretary's comments.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to AudRLS@dodig.osd.mil. Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the /Signed/ symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Questions should be directed to Mr. Dennis L. Conway (703) 604-9172 (DSN 664-9172) or Mr. Jerry H. Adams at (703) 604-8775 (DSN 664-8775). The team members are listed inside the back cover. See Appendix D for the report distribution.

By direction of the Deputy Inspector General for Auditing:

A handwritten signature in black ink, appearing to read "Wanda A. Scott", is positioned above the printed name.

Wanda A. Scott
Assistant Inspector General
Readiness and Operations Support

Department of Defense Office of Inspector General

Report No. D-2006-067

March 30, 2006

(Project No. D2005-D000LG-0220.000)

Controls Over Exports to China

Executive Summary

Who Should Read This Report and Why? Personnel who are responsible for advising DoD management on releasing exports to China should read this report because it discusses the effectiveness of the DoD process for reviewing applications to export technology to China.

Background. Public Law 106-65, “National Defense Authorization Act for FY 2000,” requires the Inspectors General of the Departments of Commerce, Defense, Energy, and State to conduct annual reviews on the transfer of militarily sensitive technology to countries of concern. For 2006, the Inspectors General decided to review controls over exports to China.

According to the Export Administration Regulation, the Department of Commerce can consult with other Federal departments, including DoD, on reviews of export license applications. Within DoD, the Director of the Defense Technology Security Administration is responsible for reviewing license applications and making decisions on export license applications, to include documenting the analytical basis of the decisions. If the other departments disagree with DoD decisions, DoD can appeal.

Results. The Defense Technology Security Administration (the Administration) had controls in place and operating for its application review process. The Administration was reviewing and processing 97 percent of its export applications related to China exports within the 30-day regulatory time limit. However, improved controls were needed in:

- documenting its analyses on export applications. Of the 90 applications¹ reviewed, 69, or 76.6 percent, did not have sufficient analyses documented to support Administration decisions,
- inserting documents into its automated system to support its analyses. Of the 90 applications reviewed, 62, or 68.8 percent, did not contain documents supporting the analysis on applications, and
- elevating disagreements with its decisions. Of 21 denial decisions, 13, or 61.9 percent, of the export denial decisions were overturned and approved by the Department of Commerce; those decisions were not elevated in the appeal process.

¹ Judgment sample percentages do not generalize to the universe export applications processed by the Administration in FY2004.

As a result, the Administration made some unsupported decisions and other decisions were not elevated to the full extent. The Administration decisions could allow the export of technology that could threaten U.S. efforts to maintain regional stability; hinder nonproliferation of nuclear, chemical, and biological weapons; and adversely effect national security. The Director, Defense Technology Security Administration needs to record analyses and documentation supporting reviews in the export automated system. (See the Finding section of the report for the detailed recommendations.)

Management Comments and Audit Response. The Acting Deputy Under Secretary for Technology Security Policy and National Disclosure Policy concurred or partially concurred with five of the seven recommendations and nonconcurred with the other two recommendations. The Acting Deputy Under Secretary concurred with updating export review process guidance; informing users to maintain access with the automated export application processing system; and providing written responsibilities, as well as recording training, for the management control program.

The Acting Deputy Under Secretary partially concurred with adjusting her program for assessing the effectiveness of management controls, but during the audit, she revised the management control plan and issued it in March 2006. We consider this action as meeting the intent of this recommendation. The Acting Deputy Under Secretary also agreed to elevate decisions as much as the appeal process will allow, which meets the intent of the recommendation.

The Deputy Under Secretary stated that she nonconcurred with recording additional analyses and documents to support decisions on some export applications. However, the Export Administration Regulation requires any analyses to be recorded that includes the factual and analytical basis supporting the advice, recommendations, or decisions made on an export application. Therefore, we request the Acting Deputy Under Secretary reconsider her position and provide additional comments by May 2, 2006.

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Background

Annual Review of Technology Transfers. In FY 2000, Congress passed Public Law 106-65,¹ requiring that transfers of sensitive technology to countries of concern be reviewed starting in 2000 and ending in 2007. For 2006, six Inspectors General decided to review controls over exports to China. The six Inspectors General represented the Departments of Commerce, Defense, Energy, Homeland Security, State, and the Central Intelligence Agency. This audit report addresses the DoD portion of the 2006 interdepartmental review.

Legislative Controls Over Exports. The primary legislative authority for controlling the export of goods and technologies with both civilian and military uses (dual-use) is the Export Administration Act of 1979, as amended (section 2401, title 50, United States Code.)² The Export Administration Regulation states that the Export Administration Act authorizes the Secretary of Commerce to issue procedures for exporting dual-use items.

Department of Commerce. The Export Administration Act authorizes the Bureau of Industry and Security, Department of Commerce to oversee the export of dual-use items. The Export Administration Regulation implements the requirements of the Export Administration Act and includes the Commerce Control List of dual-use items—goods and technologies—that are subject to the export review process.

U.S. Export Process. All items on the Commerce Control List must have an approved license, or an exception granted by the Department of Commerce, to be exported from the United States. The type of item being exported, the country of final destination, and the end-use of the item determines whether an export license is needed or an exception can be granted.

DoD Role in the Export Process. Within DoD, the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy is responsible for developing and issuing policies controlling exports. The Deputy Under Secretary also serves as the Director of the Defense Technology Security Administration (DTSA), who is responsible for coordinating reviews of license applications and reporting decisions on those reviews to the Department of Commerce. DTSA processed 1,719 applications amounting to more than \$811 million in FY 2004 for exports to China.

¹ We performed this audit to comply with Public Law 106-65, “National Defense Authorization Act for FY 2000,” section 1402, “Annual Report on Transfers of Militarily Sensitive Technology to Countries and Entities of Concern,” October 5, 1999.

² The Export Administration Act expired in August 1994. However, the President, under the authority of the International Emergency Economic Powers Act (50 U.S.C. 1702), continued the provision of the Export Administration Act through Executive Orders 12924 and 13222, “Continuation of Export Control Regulations,” August 19, 1994, and August 17, 2001, respectively. Each year thereafter, and most recently on August 2, 2005, the President issued a notice, “Continuation of Emergency Regarding Export Control Regulations,” continuing the emergency declared by Executive Order 13222.

Objectives

The overall audit objective was to determine whether controls over exports to China were in place and operating as intended. Specifically, we determined whether DoD assessed applications for exports to China in accordance with the requirements of the Export Administration Regulation. We also reviewed the management control program as it related to the overall objective. See Appendix A for a discussion of the scope and methodology and Appendix B for prior coverage related to the objectives.

Managers' Internal Control Program

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of the Review of the Management Control Program. We reviewed the management controls over the export application review process, and we also reviewed the adequacy of management's self-evaluation of those controls.

Adequacy of Management Controls. DTSA established a management control program that included:

- maintaining an inventory of assessable areas (or units) based on its organizational functions;
- evaluating the effectiveness of its controls in those assessable units; and
- publishing an annual statement of assurance on the adequacy of its controls.

DTSA had established 11 assessable units. Of the 11 units, 3 (policy development, export license application processing, and technology security assessments), were controls for processing export applications. However, we identified weaknesses in the DTSA self-assessment of its controls for processing export applications. The recommendations in this report, if implemented, should correct the identified weaknesses and could result in preventing exports of potentially militarily sensitive technology to China. A copy of this report will be provided to the senior official responsible for management controls in the Office of the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy.

Adequacy of Management's Self-Evaluation. DTSA did not always support its decisions on export applications because it did not fully achieve requirements in

the export administration regulation and the self-assessment of its internal controls did not detect weaknesses in:

- providing complete analyses on export applications, and
- inserting documents into its automated system to support its analyses.

In addition, we determined that the senior management control official was not held responsible in writing for administering the program. Further, DTSA did not have evidence to show that operating and assessable unit managers were trained to perform their management control duties.

Controls Over Exports to China

The DTSA controls were in place and operating for reviewing applications to export to China. Specifically, the DTSA reviewed and processed 97 percent of its export applications for China within the 30-day regulatory time limit. However, improved controls were needed in:

- documenting its analyses on export applications. Of the 90 judgmentally selected applications³ reviewed, 69, or 76.6 percent, did not have sufficient analyses documented to support DTSA decisions,
- inserting documents into its automated system to support its analyses. Of the 90 applications reviewed, 62, or 68.8 percent, did not contain documents supporting the analysis on applications,
- elevating disagreements with its decisions. Of 21 decisions, 13, or 61.9 percent, of export denial decisions, were overturned and approved by the Department of Commerce; those decisions were not always elevated in the appeal process, and
- assigning management control responsibilities in writing and recording management control training.

These conditions existed because the DTSA did not fully achieve requirements in the Export Administration Regulation and because management's assessment of its internal controls did not detect weaknesses in the application review process.

As a result, DTSA made some unsupported decisions that could allow the export of technology that could threaten U.S. efforts to maintain regional stability; hinder nonproliferation of nuclear, chemical, and biological weapons; and adversely effect national security.

Controls Over the Export Application Process

DTSA controls were in place for reviewing applications for exports to China. However, DTSA analyses were not always sufficient and its decisions on those applications were not always supported with documents. DTSA processed 1,719 applications for export licenses to China during FY 2004.

Processing Export Applications. DTSA generally processed applications for exports to China in a timely manner. The Export Administration Regulation states that an agency such as DoD that is reviewing export applications must provide the Department of Commerce with a recommendation either to approve

³ Judgment sample percentages do not generalize to the universe of export applications processed by DTSA in FY 2004.

(with or without conditions) or deny a license application within 30 days of receipt. In FY 2004, DTSA processed 1,719 applications for exports to China and 1,668 of the 1,719 applications, 97 percent, were processed in 30 days or less.

License Review and Analysis Process. DTSA pre-screens applications from the Department of Commerce and decides whether to refer them to other DoD organizations for review. DTSA did not refer the applications to other DoD organizations if the applications could be processed in a thorough, responsive, and consistent manner, and complied with guidance. If the pre-screen criteria were not met, DTSA referred applications to other DoD organizations for review. The export application review process is shown in the following figure.

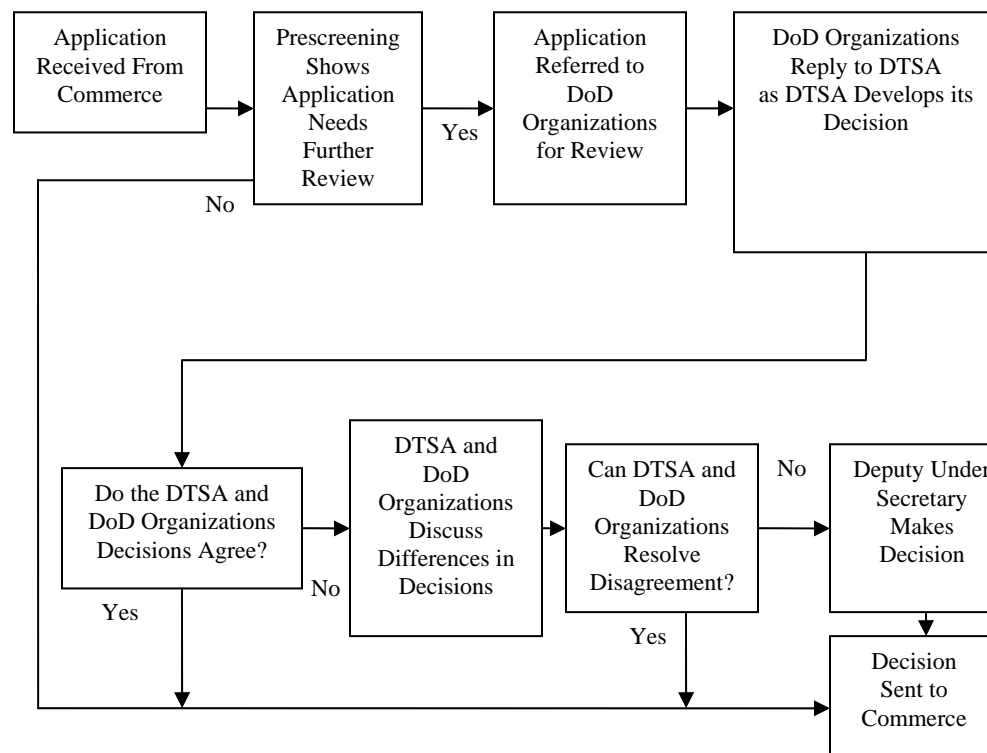


Figure 1. License Application Review and Analysis Process

Role of DoD Organizations in Review Process. The Deputy Secretary of Defense issued a memorandum on October 4, 1999, which directed DoD organizations to follow the review process for DoD export licenses. Subsequently, the Deputy Under Secretary of Defense for Technology and Security Policy (currently the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy) issued a memorandum on November 18, 1999, which provided detailed guidance to DoD organizations for reviewing export applications. In that guidance, the Deputy Under Secretary cited 18 DoD organizations that were responsible for reviewing export applications.

We compared the names of those 18 DoD organizations with a list that DTSA provided of 42 organizations with access to the U.S. Exports System (USXPORTS)—USXPORTS is the DTSA automated system for processing export applications. We determined that 4 of the 18 organizations in the Deputy Under Secretary’s guidance did not have access to the USXPORTS system; therefore, those organizations, such as the International Security Affairs’ office for Asia and the Pacific, were unable to electronically review export applications. Therefore, DTSA should provide the 4 DoD organizations with access to USXPORTS to facilitate reviews of export applications.

In addition, we noted that the Deputy Under Secretary for Technology and Security Policy memorandum was not updated to reflect current DoD responsibilities or organizations processing export applications. For example, the memorandum states that the Defense Threat Reduction Agency will develop the final DoD decision on export applications with input from DoD reviewing organizations even though DTSA currently has this responsibility.

In addition, the memorandum cites organizations, such as the Ballistic Missile Defense Organization, which is now the Missile Defense Agency. Therefore, the Deputy Under Secretary of Defense for Technology and Security Policy and National Disclosure Policy should update the guidance in the November 1999 memorandum to reflect the current organizations and responsibilities in the DoD application review process.

Developing Decisions on Export Applications. DTSA established a process for developing decisions on export applications, but the analyses and documentation supporting those decisions needed improvement. Table 1 shows DTSA decisions on applications requesting export licenses to China during FY 2004. Also, Table 1 shows that DTSA made decisions (with conditions) to approve 1,400 export applications and to deny 253 applications. Those 1,653 applications represented 96.1 percent of the 1,719 applications processed in FY 2004. We judgmentally selected 30 of the 1,400 applications that DTSA approved (with conditions) and 60 of the 253 applications that DTSA denied and reviewed them for sufficient documentation and analyses supporting the DTSA decisions.

Documentation and Analysis Supporting Decisions on Export Applications. Although export applications were generally processed timely, 69 of the 90 applications in our judgment sample, 76.6 percent, lacked either a sufficient written analysis or documentation supporting the DoD decision. According to the Principal Statutory Authority for the Export Administration Regulation:

Recordkeeping.--The Secretary [of the Department of Commerce], the Secretary of Defense, and any other department or agency consulted in connection with a license application under this Act or a revision of a list of goods or technology subject to export controls under this Act, shall make and keep records of their respective advice, recommendations, or decisions in connection with any such license application or revision, including the factual and analytical basis of the advice, recommendations, or decisions.

Table 1. Decisions Made on Applications for Export Licenses in FY 2004							
Type of Export	Approve	Approve with Conditions	Deny	Returned without Action	Split ⁴	No Decision	Total Types
Nuclear Materials	0	2	2	0	0	0	4
Chemicals and Toxins	0	128	14	8	4	0	154
Materials Processing	0	419	47	7	3	0	476
Electronics	0	356	84	18	8	1	467
Computers	0	80	4	2	0	0	86
Telecommunications	1	332	26	6	1	1	367
Sensors and Lasers	0	54	62	3	0	0	119
Navigation and Avionics	0	15	1	1	0	0	17
Marine	0	4	2	0	0	0	6
Propulsion Systems	0	4	2	0	1	0	7
Other Types of Exports	0	6	9	1	0	0	16
Total Applications	1	1,400	253	46	17	2	1,719

In addition, DoD Directive 5010.38 states that each DoD field activity—DTSA is a DoD field activity—must implement management controls that provide reasonable assurance that programs, as well as administrative and operating functions, are efficiently and effectively carried out in accordance with applicable laws and management policy. Further, the Government Accountability Office, “Standards for Internal Control in the Federal Government,” November 1999, state that:

Control activities occur at all levels and functions of the entity. They include a wide range of diverse activities such as approvals, authorizations, verifications, reconciliations, performance reviews, maintenance of security, and the creation and maintenance of related records which provide evidence of execution of these activities as well as appropriate documentation.

DTSA used the USXPORTS system to store documents that supported analyses of export applications; however, USXPORTS did not contain documents that supported the analysis of 62 of the 90 applications, 68.8 percent, in our review. For example, USXPORTS did not contain documents such as intelligence reports to support some analyses. For those 90 applications, DTSA approved 30 with conditions and denied the 60 other applications. For 69 of the 90 applications, 76.6 percent, in our review, the analysis recorded in USXPORTS was not sufficient to support the DTSA decision on the application. For example, DTSA

⁴ DTSA personnel informed us that split decisions involve approving and/or denying certain elements within the same license application. For example, DTSA might approve (with conditions) some end users on a license application but deny some of the other end users on that same application.

did not record any analyses for some items, but decided to approve the items (with conditions) for export.

During our review, we determined that DTSA returned some applications to the Department of Commerce that were not reviewed by other DoD organizations. In FY 2004, DTSA returned 276⁵ of the 1,719 applications, 16.1 percent, that it processed during pre-screening to the Department of Commerce without referring them to other DoD organizations. DTSA returned those applications to the Department of Commerce in an average of 5 days (25 days before the required time limit). We reviewed each of the 276⁶ applications and determined that DTSA did not record its analyses as well as documents did not exist that could support any of those applications in USXPORTS.

Although DTSA generally processed applications for exports to China timely, it should have recorded its analyses and documentation in USXPORTS to support the basis for its decisions. Previously documented analyses with supporting documentation from an identical application could be copied from prior application files and inserted into the current application file if no new information is received.

Also, in cases where an application is similar to a prior application, an analysis should be performed on the differences between the old and the new application and the results recorded in USXPORTS, along with the applicable analysis and documentation from the prior application. Those actions could help DTSA to comply with the Export Administration Regulation and DoD Directive 5010.38.

Elevating Decisions in the Export Application Review Process. The Export Administration Regulation requires the Departments of Commerce, Defense, Energy, and State to recommend decisions on reviewed applications to the Department of Commerce within 30 days. If all the decisions are the same, for example, if each Department recommends approval of an export application, the Department of Commerce generally makes a final decision that reflects the consensus of all the departments.

If the departments' decisions differ, the application is automatically elevated to the Department of Commerce Operating Committee⁷ for resolution. The Chairman of the Operating Committee considers the recommendations of each department and any information provided by the applicant before making a decision on the application.

Each department is informed of the chairman's decision and, if any department disagrees, that department may elevate the decision within 5 days by appealing to the Chairman of the Advisory Committee on Export Policy. This committee has assistant Secretariat-level membership.

⁵ Our sampling of 90 applications includes prescreened applications included in the 276 applications which were returned to the Department of Commerce without further review.

⁶ Sixteen of the 90 applications in our initial sample were also present in the sample of 276 applications.

⁷ The Operating Committee's membership includes representatives from the Departments of Commerce, State, Defense, Energy, the Arms Control and Disarmament Agency, the Joint Chiefs of Staff, and the Director of the Nonproliferation Center of the Central Intelligence Agency.

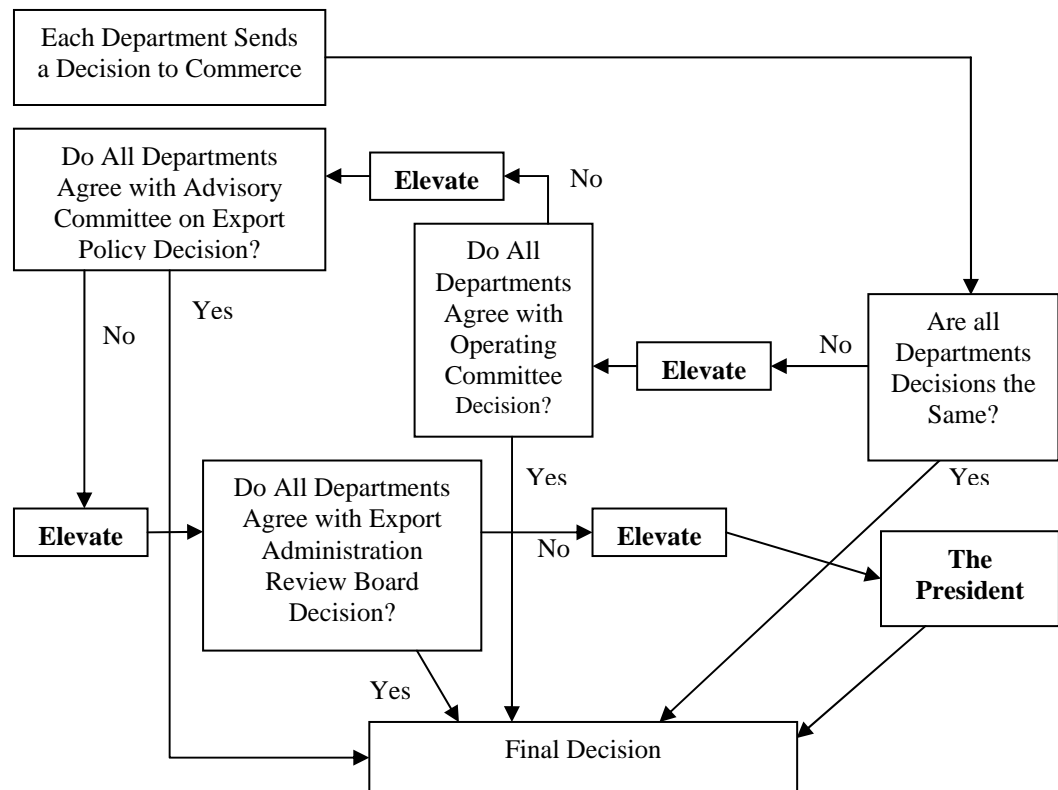


Figure 2. Export Application Appeal Process

DTSA did not always exercise its option to elevate decisions overturned by the Operating Committee. We determined that 13 of 21 DTSA denial decisions had sufficient analysis and documentation in USXPORTS, but that the Operating Committee overturned the decisions. DTSA decided not to appeal and elevate these decisions to the Advisory Committee; however, its records did not disclose why these decisions were not elevated in the appeal process.

If the Advisory Committee had not approved its decision, DTSA could have appealed to the Export Administration Review Board. This Board has Secretariat-level membership. If the Board disagreed with DTSA's decision, DTSA could elevate its decision to the President of the United States. See Appendix C for details on the membership and responsibilities of the committees and board in the application appeal process.

DTSA Actions to Gain Agreement with its Decisions to Deny Applications.

During the audit, DTSA took action to gain agreement on some of its denial decisions. For example, in September 2005, DTSA sent a memorandum to the Department of Commerce requesting a change in the Export Administration Regulation. DTSA requested the Department of Commerce to change the Export Administration Regulation to deny exports to China if an approval would have an effect on national security. To emphasize its concerns, DTSA provided the following examples:

. . . at the March 26, 2004 ACEP [Advisory Committee on Export Policy meeting], the agencies voted 3-1 to deny a gas analyzer to a Chinese end-user. . . . However, a denial could not be issued because the item was not controlled for NS [National Security] reasons.

A similar case, . . . for CB [Chemical and Biological] controlled hydrofluoric acid and nitric acid to a Chinese end-user was initially denied 4-0 at the December 19, 2003 meeting of the Advisory Committee on Export Policy. Commerce issued an approval, as the interagency could not legally sustain an NS [National Security]-based denial for CB [Chemical and Biological]-controlled items, despite serious concerns that this item was being used by the Chinese military.

Thus, DTSA took positive actions to appeal the final decision on these applications. However, for the 13 applications that DTSA denied and were subsequently approved, DTSA could have taken further actions toward appealing and elevating its decisions.

In FY 2004, DTSA made decisions to deny 253 of the 1,719, 14.7 percent, export applications it processed for China. We reviewed 60 of those 253 denial decisions, which represented all the DTSA denial decisions in our sample of 90 applications, to determine whether DTSA appealed and elevated its decisions. According to data recorded in USXPORTS, DTSA appealed and elevated one decision above the Operating Committee level.

Further review showed that 21 of the 60 decisions to deny applications had sufficient analysis and documentation in USXPORTS. The other 39 denial decisions may have been justifiable, but insufficient analysis or documentation in the USXPORTS system did not allow us to determine their validity. For 13 of the 21 decisions, 61.9 percent, DTSA decided not to elevate its denial decisions. Of the 13 decisions, 1 application was approved to export chemicals that may be used as precursors for toxic chemical agents. The other 12 applications were approved to export thermal imaging systems, which could potentially be used for military purposes by China.

In response to our findings, DTSA stated that the greatest obstacle to elevating decisions is a system bias that favors approving licenses. In addition, DTSA contended that DoD was burdened with the responsibility for elevating decisions because it was rendering a decision to deny a license. Further, DTSA responded to a draft of this report and stated that:

. . . DTSA has consistently made sound decisions about escalation based upon the relative importance of national security concerns, prior precedent, effectiveness of mitigation measures, and the likelihood of success, carefully weighting the collective judgment of licensing officers, technical experts, policy advisors, and threat assessment officers with years of experience in the export licensing business. . . .

While DTSA cited concerns that the Export Administration Regulation was written to promote the approval of export licenses, the regulation also establishes controls over exports to countries of concern to the United States. We coordinated with the Inspector General, Department of Commerce on potential

recommendations that could modify the current export policies, practices, and regulations related to China and focus on denying items that potentially contribute to China's military development. However, until the export rules for China change, DoD assumes part of the risk that exports may have an adverse effect on the United States when valid denial decisions are overturned and not elevated in the appeal process. The Department can mitigate this risk by elevating decisions to the fullest extent possible when the appeal process does not produce a decision that supports the national security posture.

Assessment of Controls for Export Applications

DTSA did not adequately document its decisions on applications for making exports to China because its program for assessing the adequacy of internal controls was not fully effective. DoD Instruction 5010.40 states that each DoD Component must establish and maintain a process that identifies, reports, and corrects management control weaknesses.

DTSA Management Control Program. The DTSA management control program included:

- maintaining an inventory of assessable areas or units based on its organizational functions;
- evaluating the effectiveness of its controls in those assessable units; and
- publishing an annual statement of assurance on the adequacy of its controls.

DTSA had established 11 assessable units. Three of the 11 units (policy development, export license application processing, and technology security assessments) were controls for processing export applications.

DTSA Assessment of Controls. The DTSA self-assessment of its internal controls for the three assessable units responsible for processing export applications, was not fully effective. An effective self-assessment program should have found the weaknesses in documenting analyses on export applications and inserting documents into USXPORTS to support analyses.

DTSA management did not provide written responsibilities to the senior management control official for administering the program. In addition, DTSA could not provide documentation showing that operating and assessable unit managers were trained to perform their duties. DTSA needs to adjust its self-assessment program to monitor more closely the analyses and documentation recorded in USXPORTS.

Impact of DoD Decisions on Exports

DTSA made some decisions that it did not support with sufficient documentation in USXPORTS. Also, DTSA accepted some risks to national security when it did not elevate valid denial decisions, which had been overturned and approved by the Department of Commerce. Those overturned decisions could allow exports of technology that may threaten U.S. efforts to maintain regional stability; hinder nonproliferation of nuclear, chemical, and biological weapons; or adversely affect national security. Table 2 shows the number of applications with insufficient analyses or documentation for the four types of exports in our review.

Table 2. Types of Items Approved for Export to China Without Sufficient Analysis or Documentation and their Potential Impact					
Type of Export	Regional Instability	Proliferation of Nuclear Weapons	National Security/ Regional Instability	Chemical and Biological Weapons	Total Applications Reviewed
Chemicals and Toxins	0	0	0	2	2
Materials Processing*	23	0	0	0	23
Electronics	0	7	0	0	7
Sensors and Lasers	0	0	37	0	37
Total	23	7	37	2	69

*Materials processing includes nuclear materials handling and processing.

The Acting Under Secretary for Industry and Security, Department of Commerce, testified on the potential effects of exports to China at the June 23, 2005, U.S.-China Economic and Security Review Commission hearing.

The Acting Under Secretary is responsible for overseeing the Bureau of Industry and Security's mission to advance U.S. national security, foreign policy, and economic interests by regulating the export of sensitive dual-use goods and technologies. The Bureau of Industry and Security works with other U.S. Government agencies, including the Departments of State, Defense, Energy, Homeland Security, and Justice to protect the national security of the United States.

The Acting Under Secretary testified to the following:

China poses particular challenges for U.S. dual-use export control policy, because there are immense potential benefits from expanding trade, but, there are also serious security concerns . . .

U.S. exports to China have continued to rise for the past 20 years, and in 2004, U.S. exports to China went up over 22 percent. The increase in U.S. exports, not surprisingly, has included some dual-use goods,

such as semiconductor manufacturing equipment, chemicals, chemical manufacturing equipment, and high performance computers.

From a security standpoint, the U.S. Government remains concerned about China's modernization of its conventional military forces and the risk of diversion of sensitive dual-use items and technology to Chinese military programs. . . . Advanced telecommunications equipment—if illegally diverted to military end-users—could provide the Chinese missile, nuclear weapons and other military programs with the means to enhance performance capabilities in military radar applications. . . .

In conclusion, it serves our common security, foreign policy, and economic interests for the United States and China to expand our economic relationship. At the same time, we continue to have significant differences with China on security and foreign policy issues that dictate a cautious way forward in our overall political, economic, and strategic relationship. While this may slow the entry of certain sensitive U.S. industry sectors into the Chinese marketplace, we must protect U.S. national security and foreign policy interests.

This testimony clearly depicts the potential adverse effects of exporting militarily sensitive items to China. Therefore, DTSA needs to record its analyses and insert documentation in USXPORTS to support its decisions. DTSA should also consider elevating decisions to the fullest extent possible when the appeal process does not produce a decision that supports the national security posture. These actions may help to reduce unjustified exports to China and strengthen U. S. efforts to maintain regional stability; hinder proliferation of nuclear, chemical, and biological weapons; and offset adverse effects on national security.

Recommendations, Management Comments, and Audit Response

Revised, Redirected, and Renumbered Recommendation. As a result of management comments from the Deputy Under Secretary of Defense for Technology and Security Policy and National Disclosure Policy, we revised, redirected, and renumbered Recommendation 1. in the draft report to the Director, Defense Technology Security Administration, shown as Recommendation 1.a. below. Draft Recommendations 2. and 3. have been renumbered as Recommendations 1.b. and 2., respectively.

1. We recommend that the Deputy Under Secretary of Defense for Technology and Security Policy and National Disclosure Policy:

- a. Grant access privileges to the four DoD organizations, currently without access to USXPORTS, to facilitate reviews of export applications.**
- b. Update the guidance for the export review process to reflect current organizations and responsibilities.**

Management Comments. The Deputy Under Secretary of Defense for Technology and Security Policy and National Disclosure Policy concurred and stated that they would inform users, within 60 days of becoming disconnected from USXPORTS, of the need to maintain access. In addition, the Deputy Under Secretary concurred with reflecting organizational changes accurately in the export review process guidance.

2. We recommend that the Director, Defense Technology Security Administration:

- a. Prepare written analyses to support decisions on export applications and maintain documents in USXPORTS to support those decisions.**
- b. Elevate decisions to the extent possible when the appeal process does not produce a decision that supports the national security posture.**

Management Comments. The Acting Deputy Under Secretary of Defense for Technology and Security Policy and National Disclosure Policy nonconcurred with Recommendations 2.a. and b., stating that the conclusions forming the basis of the recommendations were supported by incomplete and untimely data.

Although the Acting Deputy Under Secretary generally agreed that complete analysis was a necessary and proper part of the licensing process, she did not agree that inclusion of every facet of analysis was necessary in every application case file. Further, she stated that the need to augment application cases with additional documentation was unwarranted and demonstrated a lack of understanding of the review and decision process.

In addition, the Acting Deputy Under Secretary stated that USXPORTS was designed to avoid redundancy and to permit data retrievals via searches in USXPORTS. Further, the Acting Deputy Under Secretary stated she had a highly professional staff of engineers with advanced degrees and experience in DoD laboratories, as well as analysts with intelligence, policy, and licensing experience. This staff enabled DTSA to make most decisions without relying on outside experts or needing to extensively document analyses performed.

Audit Response. The comments were partially responsive. In regard to Recommendation 2.a., the Export Administration Regulation requires DoD to make and keep records of advice, recommendations, or decisions in connection with any license application or revision to include the factual and analytical basis of the advice, recommendations, or decisions.

Although DTSA recorded and documented thorough analyses for some decisions, other decisions either had no recorded analyses or needed additional analyses or documentation recorded to support the DoD recommended decisions. In addition, if supporting documentation exists in USXPORTS, DTSA should ensure that cross-references are placed within the case files to link the analyses to the stored or archived supporting documentation. Therefore, we request the Acting Deputy Under Secretary reconsider Recommendations 2.a. and provide additional comments by May 2, 2006, on this final report.

In regard to Recommendation 2.b., although the Acting Deputy Under Secretary non-concurred with our finding, she agreed to elevate decisions on applications to the extent possible; which meets the intent of the recommendation.

c. Provide written responsibilities to the senior management control official for administering the management control program.

d. Maintain documentation of training that managers of operating and assessable units receive.

Management Comments. The Acting Deputy Under Secretary concurred with Recommendations 2.c. and d. and stated that DTSA's management control plan, signed in March 2006, accomplished these recommendations.

e. Adjust the internal management control program to more effectively assess internal controls for recording analyses and documentation in USXPORTS.

Management Comments. The Acting Deputy Under Secretary partially concurred with Recommendation 2.e., stating that adjustments were made to the management control plan in March 2006 to accomplish the recommendations. Specifically, she stated that the plan was revised and updated to include standard operating procedures and position descriptions that assigned clear responsibilities, roles, and duties concerning the processing of licenses. This action met the intent of the recommendation.

Appendix A. Scope and Methodology

We reviewed the following documents to determine DoD responsibilities in the export license application review process. We reviewed Executive Orders and Federal laws and regulations, including the Export Administration Act and the associated Export Administration Regulation. In addition, we evaluated the adequacy of DoD directives, policies, and regulations related to the transfer of militarily sensitive technology to countries of concern.

We performed this audit from June 13, 2005, through March 15, 2006, in accordance with generally accepted government auditing standards.

We interviewed personnel in the following organizations:

- Department of Commerce;
- Immigrations and Customs Enforcement, Department of Homeland Security;
- Bureau of Economic and Business Affairs, Department of State;
- Department of the Army;
- Department of the Navy;
- Office of the Deputy Under Secretary of Defense for Technology Security Policy;
- Office of Export Controls and Conventional Arms Nonproliferation Policy;
- Washington Headquarters Services, Office of the Secretary of Defense;
- Defense Security Service;
- DTSA;
- Air Products and Chemicals, Incorporated;
- FLIR Systems, Incorporated; and
- Princeton Instruments, Incorporated.

Our contacts with personnel in these organizations included discussions on the export license application review process and their roles and responsibilities.

We assessed the effectiveness of the DoD export license application review process to determine that militarily sensitive goods and technology were not exported to countries of concern. To complete this assessment, we judgmentally selected a total of 350 items¹ from the 1,719 applications for China exports that the DTSA processed during FY 2004.

We reviewed the applications to determine whether the DTSA was properly analyzing, documenting, and opining on export license applications. Also, we compared the DTSA final decisions on the applications with the Department of Commerce final decisions on the applications to identify discrepancies.

For our sample, we obtained a database from the DTSA of all export license applications for exports to China. The database showed the Department of Commerce received 1,719 dual-use license applications requesting to make exports to China. We judgmentally designed a sample for reviewing 90 of the applications from the database. We judgmentally selected export applications which were approved with conditions or that DTSA denied. These two categories of applications represented 96.1 percent of the applications that DTSA processed in FY 2004. We reviewed these applications for the existence of documentation and the sufficiency of analyses supporting the DTSA decisions.

Use of Computer-Processed Data. We relied on computer-processed data from the USXPORTS system. We summarized detailed data contained within this automated export licensing system. We did not find any material errors that would preclude our use of the computer-processed data to meet the audit objectives or that would change the conclusions in this report. We concluded that the system controls were adequate for our purposes in conducting this audit.

Use of Technical Assistance. We received technical assistance from the DoD Office of Inspector General's Quantitative Methods Division, which advised us on the selection of the sample size. We also received technical assistance from the General Counsel and Assistant Inspector General for the Office of Legal Counsel on the Tiananmen Square sanctions.

¹ We initially selected 90 export applications to assess whether analyses were recorded and documents existed to support those analyses. We determined that DTSA was returning some applications to the Department of Commerce without review by other DoD organizations and that 276 of the total 1,719 applications were returned to the Department of Commerce without review by other DoD organizations. We reviewed each of the 276 applications to determine whether analyses were recorded and documents existed to support those applications. Of the 90 applications in our initial sample, 16 were also in the sample of 276 applications.

Appendix B. Prior Coverage

During the last 5 years, the Government Accountability Office (GAO) and the Department of Defense Inspector General (DoD IG) have conducted multiple reviews discussing the adequacy of export controls. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted DoD IG reports can be accessed at <http://www.dodig.mil/audit/reports>. The following previous reports are of particular relevance to the subject matter in this report.

GAO

GAO Report No. GAO-01-528, “Export Controls: State and Commerce Department License Review Times are Similar,” June 14, 2001

DoD IG

DoD IG Report No. D-2005-042, “Controls Over the Export Licensing Process for Chemical and Biological Items,” March 30, 2005

DoD IG Report No. D-2004-061, “Export Controls: Export-Controlled Technology at Contractor, University, and Federally Funded Research and Development Center Facilities,” March 25, 2004

DoD IG Report No. D2003-070, “Export Controls: DoD Involvement in Export Enforcement Activities,” March 28, 2003

DoD IG Report No. D-2003-021, “Security: Export Controls Over Biological Agents (U),” November 12, 2002

DoD IG Report No. D-2002-039, “Automation of the DoD Export License Application Review Process,” January 15, 2002

DoD IG Report No. D-2001-088, “DoD Involvement in the Review and Revision of the Commerce Control List and the U.S. Munitions List,” March 23, 2001

Interagency Reviews

Inspectors General of the Departments of Commerce, Defense, Energy, State, Homeland Security, Agriculture, and the Central Intelligence Agency Report No. D-2005-043, “Interagency Review of the Export Licensing Process for Chemical and Biological Commodities,” June 10, 2005

Inspectors General of the Departments of Commerce, Defense, Energy, Homeland Security, and State and the Central Intelligence Agency Report No. D-2004-062, “Interagency Review of Foreign National Access to Export-Controlled Technology in the United States,” April 16, 2004

Inspectors General of the Departments of Commerce, Defense, State, and the Treasury; the Central Intelligence Agency; and the United States Postal Service Report No. D-2003-069, “Interagency Review of Federal Export Enforcement Efforts,” April 18, 2003

Inspectors General of the Departments of Commerce, Defense, Energy, State, and the Treasury Report No. D-2002-074, “Interagency Review of Federal Automated Export Licensing Systems,” March 29, 2002

Inspectors General of the Departments of Commerce, Defense, Energy, and State Report No. D-2001-092, “Interagency Review of the Commerce Control List and the U.S. Munitions List,” March 23, 2001

Appendix C. Export Application Appeal Process

Operating Committee. The Operating Committee's voting members include representatives of appropriate agencies in the Departments of Commerce, State, Defense, Energy, and the Arms Control and Disarmament Agency. The appropriate representatives of the Joint Chiefs of Staff and the Director of the Nonproliferation Center of the Central Intelligence Agency are non-voting members. The Department of Commerce representative, appointed by the Secretary, is the chairperson of the Operating Committee and serves as the Executive Secretary of the Advisory Committee on Export Policy.

The Operating Committee may invite representatives of other Government agencies or departments (other than those identified in this definition) to participate in the activities of the Operating Committee when matters of interest to such agencies or departments are under consideration.

Advisory Committee on Export Policy. Voting members of the Advisory Committee on Export Policy include the Assistant Secretary of Commerce for Export Administration, and Assistant Secretary-level representatives from the Departments of State, Defense, Energy, and the Arms Control and Disarmament Agency. The appropriate representatives of the Joint Chiefs of Staff and the Director of the Nonproliferation Center of the Central Intelligence Agency are non-voting members. The Assistant Secretary of Commerce for Export Administration is the chairperson.

An acting Assistant Secretary, Deputy Assistant Secretary, or equivalent of any agency or department may serve instead of the Assistant Secretary. Such representatives, regardless of rank, will speak and vote on behalf of their agencies or departments. The Advisory Committee on Export Policy may invite Assistant Secretary-level representatives of other Government agencies or departments, other than those identified above, to participate in the activities of the Advisory Committee on Export Policy when matters of interest to such agencies or departments are under consideration. Decisions are made by majority vote.

Export Administration Review Board. The Export Administration Review Board's voting members are the Secretary of Commerce, the Secretary of State, the Secretary of Defense, the Secretary of Energy, and the Director of the Arms Control and Disarmament Agency. The Chairman of the Joint Chiefs of Staff and the Director of Central Intelligence are non-voting members. The Secretary of Commerce is the chairperson of the Board.

No alternate Export Administration Review Board members may be designated, but, the acting head or deputy head of any agency or department may serve instead of the head of the agency or department. The Export Administration Review Board may invite the heads of other Government agencies or departments, other than those identified in this definition, to participate in the activities of the Export Administration Review Board when matters of interest to such agencies or departments are under consideration.

Appendix D. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Deputy Under Secretary of Defense (Science and Technology)
Under Secretary of Defense (Comptroller)/Chief Financial Officer
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)
Under Secretary of Defense for Intelligence
Under Secretary of Defense for Policy
Deputy Under Secretary of Defense (Technology Security Policy and National Disclosure Policy)
Assistant to the Secretary of Defense (Nuclear and Chemical and Biological Defense Programs)
Director, Program Analysis and Evaluation

Joint Staff

Director, Joint Staff
Director, Plans and Policy Directorate (J-5), Joint Staff
Director, Force Structure, Resources, and Assessment Directorate (J-8), Joint Staff

Department of the Army

Inspector General, Department of the Army
Director, Joint Program Executive Office (Chemical and Biological Defense)

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Combatant Command

Inspector General, U.S. Joint Forces Command

Other Defense Organizations

Director, Defense Intelligence Agency
Director, Defense Logistics Agency
Director, Defense Security Service
Director, Defense Technology Security Administration
Director, National Security Agency

Non-Defense Federal Organizations

Office of Management and Budget
Inspector General, Department of Agriculture
Inspector General, Department of Commerce
Inspector General, Department of Energy
Inspector General, Department of Health and Human Services
Inspector General, Department of Homeland Security
Inspector General, Department of State
Inspector General, Central Intelligence Agency

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
Senate Select Committee on Intelligence
Senate Committee on Foreign Relations
Senate Committee on Banking, Housing, and Urban Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform
House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform
House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform
House Committee on International Relations
House Permanent Select Committee on Intelligence

Deputy Under Secretary of Defense (Technology Security Policy and National Disclosure Policy) Comments

CORRECTED COPY



POLICY

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

MAR 29 2006

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR READINESS AND LOGISTICS SUPPORT

FROM: Beth M. McCormick, Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy (Acting) *Beth M. McCormick*

SUBJECT: Response to Draft DoD/IG Report on "Controls Over Exports to China,"
Project No. D2005-D000LG-0220.000

In response to the draft Office of Inspector General (OIG) report dated March 15, 2006, as Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy (Acting) and Director (Acting), Defense Technology Security Administration (DTSA), the following comments are submitted. While we recognize this draft represents an improvement over earlier versions, we still have significant concerns with certain findings, nonconcurring with two recommendations. Of the remaining recommendations, we partially concur with one and concur with four. Our detailed comments follow.

The OIG report cites DTSA for not adequately documenting license determinations and analyses. However, we were able to show that documentation for our analyses does exist in USXPORTS, the automated export licensing system. The discrepancy in interpretations appears to revolve around a primary factor, i.e., that the information in USXPORTS is not consolidated in an "audit-friendly" way. To outsiders, without export control expertise or USXPORTS experience, it does not provide an easy audit trail. However, to persons experienced in export licensing within DTSA and other DoD offices, USXPORTS serves its intended purpose. These persons are expert in their fields, be they engineers, licensing officers or policy experts. They are experienced in the relevant laws and regulations related to export licensing, as well as national security concerns. While USXPORTS may not be "audit friendly," it does meet the needs of those technical, licensing and policy experts reviewing license applications. Nonetheless, we continue to make improvements and are working towards additions which will make USXPORTS even more user friendly and transparent. USXPORTS is aimed at making the license determination process even more efficient through automation, in keeping with the President's "e-government" initiative.

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DTSA COMMENTS ON REPORT RECOMMENDATIONS

DTSA concurs with the following recommendations:

1. *We recommend that the Under Secretary of Defense for Policy direct the organizations responsible for reviewing export applications to maintain access to USXPORTS.*

This action will serve as a timely reminder that USXPORTS is the automated system from which licensing information is readily available and that its use will both increase efficiency, as well as ensure all relevant licensing information is considered. However, it is more appropriate for the Deputy Under Secretary, Technology Security Policy and National Disclosure Policy, with responsibility for export license review, to ensure that the most efficient means of analysis are available to all users. The OIG staff informally advises that responsibility will be transferred. Based upon their assurance, ***we will concur with the recommendation.***

However, we would like to point out that the report could leave the impression that the only method for review of export applications is electronic. Organizations may receive hard copy, e-mails or be otherwise informed of the contents of the license application and the requirement for comment. Nonetheless, the recommendation for USXPORTS use embraces DTSA's goal and we will inform users within 60 days.

2. *We recommend that the Deputy Under Secretary of Defense for Technology and Security Policy update the guidance for the export review process to reflect current organizations.*

This action is required to ensure that the recent organizational changes to the Defense Technology Security Administration are accurately reflected in current guidance. **We concur with this recommendation** and the Deputy Under Secretary for Technology Security Policy and National Disclosure Policy, serving also as the Director, Defense Technology Security Administration, will ensure this action is completed within sixty days.

3. *We recommend that the Director, Defense Technology Security Administration:*
 - c. *Provide written responsibilities to the senior management control official for administering the management control program.*
 - d. *Maintain documentation of training that managers of operating and assessable units receive.*

Our Management Control Plan, which was signed by the Director (Acting), Defense Technology Security Administration, in March 2006, accomplishes these recommendations. **We concur with this recommendation** and note that the recommended action has already been completed.

Redirected,
renumbered,
and revised
to
Recommendation 1.a.

Renumbered
to
Recommendation 1.b.

Renumbered
to
Recommendation 2.c.
and 2.d.,
respectively

DTSA respectfully nonconcurs with the following recommendations:

3. *We recommend that the Director, Defense Technology Security Administration:*
 - a. *Prepare written analyses to support decisions on export applications and maintain documents in USXPORTS to support those decisions.*
 - b. *Elevate decisions to the extent possible when the appeal process does not produce a decision that supports the national security posture.*

DTSA comments on recommendation 3.a., prepare written analyses and maintain documents in USXPORTS:

Providing complete analyses on export applications: From our perspective, the OIG viewed a very narrow sample (e.g., limited to four ECCNs); did not look at all materials related to a case or all case files; looked only at licenses adjudicated in FY2004 – the “sample”—which were done prior to the current, robust, automated data system, USXPORTS; failed to acknowledge that a main purpose of USXPORTS is to serve as a repository of data relevant to the case and to eliminate the need for repetitive data entry; and did not recognize that the Tiger Team Standard Operating Procedures (SOP) address analysis requirements. Consequently, conclusions—which formed the basis of the recommendations—are unfounded because they are based on incomplete and untimely data.

- The report places great emphasis on the importance of providing, in each individual case file, complete analyses addressing recommendations as part of the export licensing process. Although we are in general agreement with the proposition that complete analysis is a necessary and proper part of the licensing process, we do not agree that inclusion of every facet of analysis considered in making a licensing determination is necessary to be included in every individual case file. We have an automated licensing system, USXPORTS, specifically designed to make such redundancy unnecessary as data can readily be identified through such features as the search process.
- USXPORTS, itself, is an automated licensing system that makes it unnecessary to repeat all information considered in each single case. For example, information regarding precedent cases and end users is easily searched in USXPORTS by those reviewing licenses. This information in turn is used to inform licensing determinations. To copy that information into the license application under consideration would be redundant and wasteful of US government resources.
- Further, there are certain fundamental assumptions that are expressly or implicitly provided by the Export Administration Regulations (EAR) or other regulatory guidance such as Executive Order 12981. For example, we believe it would be redundant to repeat the EAR-listed reasons for control, (i.e., Regional Stability (RS), Missile Technology (MT), Nuclear Nonproliferation (NP), etc.) for each item requested for export in each case file. That criterion is already included in the license file, which identifies the Export Commodity Classification Number (ECCN) for each item. Since the reason for control is the basis for requiring a license, it must be --and always is--considered during the license application review.

Renumbered
to
Recommendation 2.a.
and 2.b.,
respectively

Additionally, the report does not take into account the inclusion in the license record of minutes from the interagency Operating Committee (OC) and Advisory Committee on Export Policy (ACEP). This information clearly outlines agency positions, statements and recommendations, as well as the final US Government decision for the license. This information is already included in each relevant case file. Repeating this information in another section of a case's file would be wasteful and inefficient. It should be noted that part of the design and implementation of USXPORTS is to ensure that OC and ACEP minutes and findings can be electronically entered into the license record.

- The report's finding that electronic documentation supporting analysis in USXPORTS was insufficient fails to take into consideration the incremental progress made in bringing a new automated system on-line. This report examines only FY 2004 cases. It was not until December 04 (FY05) that DTSA had the capability to incorporate electronically all supporting documents and information into the license file. DTSA continues to maintain that all license -related documents required to properly evaluate the license application are documented within the USXPORTS database.
- The report asserts that of "90 judgmentally selected applications reviewed, 69, or 76.6 percent, did not have sufficient analyses documented to support DTSA decisions." Of the 69 cases, 46 were staffed for review sometime during the age of the case. 27 of these cases actually went to the OC for adjudication. All involved the same issue, a problematic intermediate consignee that was eventually removed from these license applications and replaced by another. Of the remaining 19 licenses in this group, 16 of them were actually returned without action at the request of the applicant or by the Department of Commerce due to a lack of information. (The DoD position on these cases was a denial recommendation.) However, because there was no license decision made on these cases, no harm to national security or regional stability was incurred since no export was made.
- The act of staffing the cases internally within DoD (in this example, 46 of the 90 cases judged to have insufficient analysis documentation) indicates that insufficient information was available to the Tiger Team to warrant a decision. This staffing action itself is evidence of consideration of possible diversion risks and policy concerns.
- Of the remaining 23 cases, the Tiger Team process, as outlined in the DTSA Tiger Team Standard Operating Procedures (SOP), found insufficient grounds for denial or returning the license without action. Consequently, the license met the approval criteria outlined within the SOP. This SOP criteria requires an evaluation of the bona fides of the license, e.g., the technology, relevant policies, end user and end use concerns, risk of diversion, the basis for control, and other relevant EAR considerations. In this way, adjudication at the Tiger Team is in accordance with the EAR and relevant Executive Order (EO), as well as internal DTSA SOP.

- It is important to note that the Tiger Team evaluation and approval position submitted by DoD on four of the 23 licenses was validated at a later date by the OC. All 23 of these licenses involved the same type of controlled equipment (ECCN 2A983) going to the same related end use. Therefore, the database already provided the support precedent case documentation to authorize approval of the licenses and adequately and appropriately documented the required analyses.
- A subject matter expert demonstration was provided to show how DTSA analysts and DoD license reviewers are able to point to data in the case file and/or USXPORTS that provided evidence of the documentation the OIG audit team was seeking. While the licensing system may not be transparent to a person unfamiliar with the intricacies of the system, it does provide a robust capability to confirm and document the bona fides of the license applications to the actual users of the database.
- It appears that the OIG requirement for additional documentation and analysis was based on the flawed conclusion that the analysis provided by the staffing points, both internal and external to DTSA, was insufficient. DTSA consists of a highly professional staff of engineers with advanced degrees who are selected for their vast experience in DOD laboratories and program management specifically to provide thorough evaluations and recommendations. Likewise analysts assigned to DTSA have been selected based on their expertise and experience with all facets of intelligence, policy and licensing issues. A suggestion that the input contained in the USXPORTS data would need to be augmented, in all cases, by “additional documentation” is unwarranted and demonstrates a lack of understanding of the review and decision process involved in over 30,000 cases a year.
- Further, accepting the OIG finding that additional, sufficient analysis and documentation is needed requires the acceptance of a potentially flawed assumption of the applicability of DoC controls to DoD recommendations. The OIG standard cited in the report refers to the 15 CFR 742, Control Policy – CCL Based Controls. These controls provide the DoC justifications for assignment of technologies to an entry on the Commodity Control List. Likewise, it provides that a review will “generally include” various factors. To suggest that analysis and documentation mirror DoC’s licensing policy is antithetical to DTSA mission as contained in DoDD 5130.72 and not required by the CCL itself.
- The report asserts that lack of license documentation could potentially harm US national security or contribute to proliferation or regional destabilization. As defined in the SOP that covers the review and evaluation of license applications, the reasons for control of the commodities such as national security, regional stability, or nuclear proliferation, are addressed during the licensing determination process that takes place at the Tiger Team or after the license is staffed for review. Since the report failed to review the results of license decisions, any perceived harm to national security cited by the report due to lack of documentation is not supported by any evidence of diversion or proliferation. Even if we were to agree –and we do not–that there is a lack of documentation, it would be the export license decision itself – not the lack of documentation—that could be faulted. For all these reasons, there is no basis for alleging potential harm.

Maintaining Documents: The USXPORTS database maintains a summary of the license applications, the DoD final position, and in all applicable cases, a record of the recommendations by other DoD agencies and departments. It is DTSA's opinion that the USXPORTS database fully complies with the requirements to retain "appropriate documentation." Likewise, repetition of applicable analysis and documentation from prior applications is not only unnecessary, but would be wasteful of US government resources. USXPORTS was designed to improve efficiency and to preclude the need to repeat database information that is readily available. USXPORTS provides DTSA the capability to incorporate all supporting documents and information into the license database.

- The Departments of State (DoS) and Commerce (DoC), not DTSA, have the ultimate responsibility for maintaining permanent records of US Munitions List (USML) and Commerce Control List (CCL) license applications. DTSA has coordinated with the US National Archives and Records Administration (NARA) and DoD's Directives and Records Branch and developed a record retention plan. The DoD Directive and Records Branch has DTSA's record retention plan and will forward it to NARA with other DoD retention plans. In the meantime, DTSA has complied with NARA's previous guidance with regard to record retention.
- Regarding concerns that DTSA does not retain needed licensing documentation, during the period of the OIG review, hardcopies of license information were retained as input documents for reference on both munitions and dual-use license applications. With USXPORTS, DTSA is able to scan hard copies of license related documents into the system. All record keeping is done in accordance with the General Records Schedule (Section 20). Note that both DoS and DoC are planning to implement requirements for applicants to provide all documentation electronically rather than via hardcopy. Once this data is in electronic form, it will be maintained in accordance with DTSA's records retention schedule.
- Improvements continue to be made to USXPORTS. As one example, prior approvals of similar exports are identified by using a search function. While this identifies the necessary information, it is more cumbersome than we would like. Consequently, a field of "precedent cases" is being developed in USXPORTS that is intended to identify similar cases, end users and end uses by use of a single search function. We expect this to be operational in the next several months.

DTSA comments on 3.b., elevate disagreements.

Elevating Disagreements: While not every license that DTSA had concerns with was elevated to the OC by the Commerce Department, at least 50% of cases in 2005 and 45% in 2004 were at the OC due to DoD denials. Similarly, 76% of licenses in 2005 that went to the ACEP were escalated by the Department of Defense. Historically, the Defense Department escalates over 75% of the licenses to the ACEP, a far greater percentage than any other agency.

Renumbered
to
Recommendation 2.b.

- This report does not adequately evaluate factors that influence the dispute resolution process. The dispute resolution process, like the overall license review process, places the burden of proof on those advocating denial of licenses rather than those advocating approval.
- We disagree with the tenor of the report, which questions DTSA's decisions about when it is productive to escalate cases in the interagency, without any analysis of relevant factors. In reaching these decisions, the relative importance of national security concerns, prior precedent, effectiveness of mitigation measures, and the likelihood of success are carefully weighed using the collective judgment of licensing officers and technical experts with years of experience in the export licensing business.
- Moreover, it appears that modifications to a license developed during the escalation process may mitigate DoD concerns, and result in DoD acceding to approval of the license were not considered. DoD frequently develops these conditions. They will not be reflected in the original DTSA license recommendation, but in the follow-on versions and will be incorporated into the final position of the license formally approved by DoC. One of the 21 licenses which the IG report recommended further escalation was actually approved by DoD after extensive discussion at the OC. The interagency crafted license conditions allowed the export to move forward, but with conditions and provisos that mitigated DoD diversion concerns. The minutes of the Operating Committee, which contain agency comments and positions, and the resultant licensing decisions are documented in USXPORTS, but the OIG viewed this as inadequate because certain OC information was not repeated in another part of the case file.
- In determining the likelihood of escalation success, DTSA also considers whether the ACEP has decided a precedent case in opposition to the DoD position. If this is the case, it may well be prudent for DTSA to maintain its denial at the OC to indicate its position, but to choose not to escalate the case in recognition that other agencies will not support the denial. One of the cases cited in the OIG report as requiring additional escalation was just such a case. In fact, this license file actually documented the prior ACEP case where DoD concerns were overruled on regulatory grounds. Consequently, although concerns remained, there was no legal basis, at that time, for a denial.
- The report considered none of these factors, nor that the elevation determination is made at the Assistant Secretary level. Instead, the report noted a difference between the ingoing DoD position and the final USG position and cited this as the basis for the recommendation to escalate more cases.
- Of the 21 licenses cited by the OIG that should have been elevated further, 13 of the licenses were actually returned without action at the request of the applicant or by the Department of Commerce due to a lack of information. Since there was no license decision made on these cases, escalation was unnecessary. In addition, no harm to national security or regional stability could have, by definition, occurred since no export was possible.

- Of the remaining 8 cases cited by the OIG as requiring escalation, as noted above, DoD actually approved one license after the OC crafted conditions that mitigated our original concerns and maintained a denial recommendation on another in light of the prior precedent ACEP cases, which indicated that the regulatory process trumped national security concerns.
- The remaining 6 licenses all involved the same issue, a problematic intermediate consignee that was eventually removed from these license applications and replaced by another. Although DoD maintained a denial recommendation on these cases, this action at the OC level, documented in all the licenses, was done at the OC at the behest of the ACEP. In these instances, the system worked at the lower levels to adjudicate the licenses in a way that alleviated diversion risks.
- In all cases where DTSA has concerns, we will escalate the case as far as the process will reasonably allow, considering the likelihood of success, which is dependent upon carrying the votes of at least two other departments. In our opinion, national security would be better served by requiring unanimous decisions on these cases (e.g., a consensus approach). Given the small percentage of such cases that this represents in relation to the overall number of licenses reviewed, this would be a limited burden to applicants and the USG.

DTSA partially concurs with the following recommendation:

3. *We recommend that the Director, Defense Technology Security Administration:*
 - e. *Adjust the internal management control program to more effectively assess internal controls for recording analyses and documentation.*

Adjust management control program: The report states that our self-assessment program did not detect “weaknesses” with:

- providing complete analyses on export applications,
- inserting documents into its automated system to support its analyses; and
- elevating disputed decisions to achieve agreement.

Per our presented critique, we cannot agree with the findings, which form the basis for the report’s contention that this reflects an inadequacy of our self-assessment program. However, **we partially concur with this recommendation.** We do acknowledge that there were revisions and updating required in the Management Control Plan which we had been working on at the time of the OIG review and which was issued in March 2006.

- We do agree there was no letter appointing the Director of the Management Directorate with responsibilities for the program, and our revised Management Control Plan rectifies this. However, as specifically concerns licensing, the Chiefs of both the Dual-Use Licensing Division and the Munitions Licensing Division were “held accountable in writing” for duties specifically related to the management control plan in their employee performance plans and results report (DD Form 2799), and Management Controls are an evaluated element in the performance appraisals of DTSA’s senior managers.

Renumbered
to
Recommendation 2.e.

-
- DTSA provided Standard Operating Procedures and position descriptions that assigned clear responsibilities, roles, and duties concerning the processing of licenses in accordance with the Management Control Program. Additionally, the directors of the Licensing Directorate and Technology Directorate have signed AU 9, which implements management controls on licensing and Management Controls and are an evaluated element in the performance appraisals of DTSA's senior managers.)

In summary, our Management Control Plan, which was signed by the Director (Acting), Defense Technology Security Administration, in March 2006, ensures that every management official is responsible for the relevant areas of responsibility, which include analysis and documentation of licenses. Consequently, the revisions we have made meet the recommendations of the report. Additionally, we are in the process of upgrading our internal licensing Standard Operating Procedures, which will further clarify responsibilities. This will be completed within sixty days.

We appreciate your consideration of our comments and anticipate that you will find them useful as you revise this report. If we can be of further assistance or if you have questions regarding these comments, please call Dr. Cheryl Opacinch at 703-325-3455.

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