

# Inspector General

United States  
Department of Defense



Followup Audit on Recommendations for Controls Over  
Exporting Sensitive Technologies to  
Countries of Concern

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### **Acronyms**

DDR&E	Director of Defense Research and Engineering
DFARS	Defense Federal Acquisition Regulation Supplement
DTSA	Defense Technology Security Administration
DUSD(TSP&NDP)	Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy
EAR	Export Administration Regulations
USD(AT&L)	Under Secretary of Defense for Acquisition, Technology, and Logistics
USD(P)	Under Secretary of Defense for Policy
USXPORTS	U.S. Exports System



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
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September 28, 2007

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

SUBJECT: Report on Followup Audit on Recommendations for Controls Over Exporting Sensitive  
Technologies to Countries of Concern (Report No. D-2007-XXX)

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."

DoD Directive 7650.3 requires that all recommendations be resolved promptly. We considered comments from the Under Secretary of Defense for Acquisition, Technology, and Logistics and from the Defense Technology Security Administration when preparing the final report. Because those comments did not provide concurrence or nonconcurrence with the recommendation, we request that those organizations send comments by October 29, 2007. We did not receive comments on a draft of this report from the Under Secretary of Defense for Policy or the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy; we request that they provide comments by October 29, 2007. Although not requested, Defense Research and Engineering provided comments. We made minor changes to the report in response to comments, the complete text of which is in the Management Comments section.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to [AudROS@dodig.mil](mailto:AudROS@dodig.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. Lamar Anderson at (703) 604-9640 (DSN 664-9640). The team members are listed inside the back cover. See Appendix E for the report distribution.

By direction of the Deputy Inspector General for Auditing:

Wanda A. Scott  
Assistant Inspector General  
Readiness and Operations Support



# Department of Defense Office of Inspector General

Report No. D-2007-131

September 28, 2007

(Project No. D2006-D000LG-0199.000)

## Followup Audit on Recommendations for Controls Over Exporting Sensitive Technologies to Countries of Concern

### Executive Summary

**Who Should Read This Report and Why?** Personnel who are responsible for developing and implementing controls over exports of sensitive technology should read this report. It discusses audit recommendations to strengthen controls over exporting sensitive goods, services, and technologies to foreign countries and persons.

**Background.** Public Law 106-65, “National Defense Authorization Act for Fiscal Year 2000,” requires the Inspectors General of the Departments of Commerce, Defense, Energy, and State to conduct annual reviews of the transfer of militarily sensitive technology to countries of concern. For the annual review due to Congress by March 30, 2007, these Inspectors General were joined by those of the Departments of Homeland Security, Treasury, the U.S. Postal Service, and the Central Intelligence Agency. The Inspectors General decided to follow up on recommendations made from FY 2000 through FY 2006 to improve controls over exports. Each year, the results of the individual agencies’ reviews are combined in a report to Congress.

**Results.** The DoD Inspector General made 39 recommendations during FYs 2000 through 2006 to strengthen controls and reduce risks contributing to the inappropriate export of goods, services, and technologies such as chemicals, toxins, electronics, explosives, sensors, and lasers. As of June 28, 2006, DoD organizations had implemented 25 of the 39 recommendations. During this audit, we found four additional recommendations were implemented for a total of 29 recommendations. Therefore, as of December 21, 2006, DoD organizations still needed to implement 10 recommendations. The 10 remaining recommendations request DoD organizations to develop, implement, or revise guidance to determine whether an export license is required; to prevent unauthorized access to or disclosure of export-controlled technology; and to establish roles and responsibilities for persons involved with export-controlled technology. Also, the recommendations relate to analyzing and documenting analysis of export applications; updating export guidance to reflect current organizational titles, responsibilities, and structure; giving users access to the DoD export application system; and developing effective management controls. Until our recommended actions are implemented, DoD continues to accept avoidable risks of inappropriately exporting sensitive goods, services, and technology that could threaten our national security. (See the Finding section of the report for the detailed recommendations.)

**Management Comments and Audit Response.** We issued a draft of this report on March 12, 2007. The Director of Defense Procurement and Acquisition Policy responded for the Under Secretary of Defense for Acquisition, Technology, and Logistics and neither concurred nor nonconcurred with our finding and recommendation. We considered the Director’s response related to explaining the process for revising the Defense Federal Acquisition Regulation Supplement; however, we did not see that an explanation of the process was needed to explain the status of our recommendation. We agreed with the Director’s comments and revised our report to state that the proposed changes in the Defense Federal Acquisition Regulation Supplement did not meet the intent of our prior recommendation. Also, we considered the Director’s comments and deleted our references to the Defense Federal Acquisition Regulation Supplement related to issuing guidance and training DoD personnel. We revised our finding to show that the draft policy issued by the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy

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should address our recommendation for issuing guidance and training DoD personnel on procedures for handling exports, if approved and implemented. In addition, we considered and revised our report to reflect the Director's comments concerning the responsibility of the Under Secretary of Defense for Policy for revising and issuing draft DoD Instruction 2040.2. We made no change in response to the Director's comment that no DoD Instruction is numbered 2040.2. A draft of the new DoD Instruction 2040.2 is being coordinated within the Department; this Instruction will replace DoD Directive 2040.2. Finally, we considered the Director's comments that his office's procedures for following up on our recommendation was timely and adequate. However, more timely action by the Director's office is needed to implement our recommendation. We issued our audit report on March 25, 2004, and one recommendation remained outstanding on March 29, 2007. Until changes are made, DoD will be at increased risk of other nations' countering or reproducing our technology. We request that management provide comments on this final report by October 29, 2007.

The Director (Acting) of the Defense Technology Security Administration nonconcurred with our findings related to her office. Specifically, the Director disagreed with our use of the policies in the Export Administration Regulations for evaluating her office's review of applications to export dual-use items. However, we used those export policies and procedures for evaluating the review of license applications after reviewing and considering DoD's directive on management controls. That directive requires organizations to perform functions to comply with applicable laws and management policy. The Export Administration Act is the law that establishes the requirements for processing export license applications and the Export Administration Regulations implement the management policies for processing those applications. DoD should consider those policies in making recommendations to the Department of Commerce on export license applications. Also, the Director disagreed with our finding that her office was required to document reasons for all recommendations made on export applications. We addressed the need to document reasons for all recommendations in our prior report, "Controls Over Exports to China," March 30, 2006. That report cited the Principal Statutory Authority for the Export Administration Regulations, which stated that DoD will make and keep records of its advice, recommendations, or decisions, including the factual and analytical basis, connected with export licenses. We agree with the Director's comment that her office had no statutory or regulatory authority to approve or deny export applications, merely to recommend a course of action to the licensing department. We modified our report to show that her office was only responsible for making recommendations to the Department of Commerce. Further, we considered and agreed with the Director's comment that DoD Instruction 2040.2 cannot be finalized until it has been coordinated with DoD activities and completed by the Under Secretary of Defense for Policy. We request that management provide comments on this final report by October 29, 2007.

We did not receive any written management comments on this report from the Under Secretary of Defense for Policy or from the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy. Therefore, we request that both provide management comments on this final report by October 29, 2007. Although no comments were required, we received and agreed with comments provided by the Director of Defense Laboratory Programs, who responded for the Director, Defense Research and Engineering. The Director commented that our recommendation to complete DoD Instruction 2040.2 should be redirected to the Under Secretary of Defense for Policy; we did so in the draft. Also, the Director asked us to consider revising the report to state that DoD Instruction 2040.2 will provide export procedures, the Defense Federal Acquisition Regulation Supplement will provide specific clauses concerning export procedures, and training on export compliance requirements depend on the content of the yet-to-be-published Defense Federal Acquisition Regulation Supplement and DoD Instruction 2040.2. See the Findings section for a discussion of management comments, and see the Management Comments section for the complete text of the comments.

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## Background

**Annual Review on Transfers of Technology.** In FY 2000, Congress passed Public Law 106-65,<sup>1</sup> which requires an annual review of transfers of sensitive technology to countries of concern. The law required annual reviews to begin in FY 2000 and end in FY 2007. To comply with the law, Inspectors General of affected departments and agencies formed an interagency team to conduct the reviews and produce the annual reports.

**Annual Report to Congress.** For the annual report due to Congress by March 30, 2007, the Inspectors General decided to review whether recommendations made in previous reports had been implemented. The Inspectors General participating in this year's review include those from the Departments of Commerce, Defense, Energy, Homeland Security, State, and Treasury; the U.S. Postal Service; and the Central Intelligence Agency. This audit report provides the legislatively required 2007 review of DoD controls over exports.

**Legislative Controls Over Exports.** Several laws give the U.S. Government authority to control the export of commodities and technologies. The primary legislative authority for controlling the export of goods and technologies that have both civilian and military use (dual use) is the Export Administration Act of 1979, as amended (title 50, United States Code, section 2401).<sup>2</sup> The Arms Export Control Act (title 22, United States Code, section 2778) authorizes the President to issue regulations for export of selected:

- defense-related articles (which are models, mockups, or technical data shown on the U.S. Munitions List);
- services, such as assistance provided to foreign persons in the design, development, and production of defense articles; and
- technical data including either classified or unclassified information, other than software, required for the design, development, or production of defense articles.

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<sup>1</sup> We performed this audit to comply with Public Law 106-65, "National Defense Authorization Act for Fiscal Year 2000," section 1402, "Annual Report on Transfers of Militarily Sensitive Technology to Countries and Entities of Concern," October 5, 1999.

<sup>2</sup> 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 3, 2006, the President issued a notice, "Continuation of Emergency Regarding Export Control Regulations," extending Executive Order 13222.

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**DoD Export Control Responsibilities.** DoD designated the following offices to develop and implement export control policy and to control exports to foreign countries and persons:

- **Under Secretary of Defense for Acquisition, Technology, and Logistics (USD[AT&L]).** The USD(AT&L), in coordination with the Under Secretary of Defense for Policy, is responsible for providing technology assessments that help DoD determine the national security implications of the transfer of technology, goods, services, and munitions.<sup>3</sup> Also, the USD(AT&L) advises the Under Secretary of Defense for Policy on the technological aspects of export control policies and procedures necessary to protect the national security interests of the United States.
- **Under Secretary of Defense for Policy (USD[P]).** The USD(P) is responsible for the formulation of defense policy and for the integration and oversight of DoD policies and plans to achieve national security objectives. Specifically, the USD(P) oversees all aspects of DoD transfers of international technology, including export controls, licensing of dual-use commodities<sup>4</sup> and munitions, and arms cooperation programs. As part of its oversight responsibilities, the USD(P) supervises the Office of the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy.
- **Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy (DUSD[TSP&NDP]).** The DUSD (TSP&NDP) is responsible for developing and implementing DoD technology security policies to control defense-related goods, services, and technology exports. The DUSD(TSP&NDP) also serves as the Director of the Defense Technology Security Administration (DTSA), responsible for coordinating reviews of license applications and reporting decisions made on the basis of those reviews to the Department of Commerce.

## Objectives

The overall objective of this audit was to determine whether DoD effectively implemented recommendations made by the DoD Office of Inspector General in our seven previous reports (FY 2000 to FY 2006) on controls over militarily sensitive exports. Management had implemented recommendations from four of the seven reports; therefore, we reviewed the three remaining reports to determine management action. Specifically, we evaluated management actions taken on:

- all recommendations contained in DoD IG Report No. D-2006-067, “Controls Over Exports to China,” March 30, 2006;

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<sup>3</sup> Munitions include arms and ammunition as well as any material, equipment, or goods used to make military items.

<sup>4</sup> Dual-use commodities can be used for commercial or military purposes.

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- Recommendations 1. and 2. in DoD IG Report No. D-2004-061, “Export-Controlled Technology at Contractor, University, and Federally Funded Research and Development Center Facilities,” March 25, 2004; and
  - Recommendations A.1. and A.2. in DoD IG Report No. D-2000-110, “Export Licensing at DoD Research Facilities,” March 24, 2000, which related to controls over exporting sensitive technologies to countries of concern.

See Appendix A for a discussion of the scope and methodology, and Appendix B for prior coverage related to the audit objective.

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## Extent of Implementation of Recommendations To Improve Export Controls

DoD organizations implemented 29 of 39 (74 percent) of the recommendations made in the 7 reports that we issued from FY 2000 through FY 2006. We made the 39 recommendations to strengthen controls and reduce risks of inappropriate exports of goods, services, and technologies such as chemicals, toxins, electronics, explosives, sensors, and lasers. However, DoD organizations need to take further actions to fully implement the 10 remaining recommendations in 3 of the 7 reports.

DoD organizations did not establish a fully effective process for following up and aggressively implementing the 10 outstanding recommendations as demonstrated by one recommendation that was not implemented for almost 7 years. Until recommended controls are implemented, DoD continues to accept avoidable risks of inappropriately exporting sensitive goods, services, and technology that could threaten our national security.

### DoD Guidance on Implementing Audit Recommendations

**Guidance on Implementing Recommendations.** DoD Directive 7650.3, “Follow-up on General Accounting Office (GAO),<sup>5</sup> DoD Inspector General (DoD IG), and Internal Audit Reports,” provides guidance to DoD managers on implementing audit recommendations. The Directive states:

- “The DoD Component managers recognize, support, and use auditors as important elements of DoD management systems.
- Timely decisions and responsive actions shall be taken and documented on audit findings and recommendations to reduce costs, manage risks, and improve management processes.
- Follow-up is an integral part of good management and is a responsibility shared by DoD managers and auditors.
- An effective, credible decision process shall be maintained to resolve disputes on audit findings and recommendations; prevent preemptive actions, such as proceeding with activities questioned in undecided audit reports; and provide prompt and well-documented decisions consistent with statutes and regulations.
- Follow-up systems shall provide for a complete record of action taken on findings and recommendations.”

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<sup>5</sup> The General Accounting Office was renamed the Government Accountability Office.

**Status of Recommendations.** We announced the audit on June 28, 2006, to determine whether DoD officials had implemented the recommendations we made from FY 2000 through FY 2006. The results of this audit will be combined with the results of reviews by seven other Inspectors General in a report to Congress. The report will provide an assessment of the extent to which export controls were implemented within the Federal Government from FYs 2000 through 2006.

As of June 28, 2006, DoD organizations had implemented 25 of 39 (64 percent) of the recommendations made in our reports from FYs 2000 through 2006. Those DoD organizations had agreed to implement all 39 recommendations.

During this audit, we found that DoD organizations had implemented four additional recommendations. Therefore, as of December 21, 2006, 29 of 39 (74 percent) of the recommendations were implemented. The table shows the number of recommendations we made and those implemented by DoD organizations.

#### **Status of Recommendations**

<u>Report Number</u>	<u>Number of Recommendations</u>	<u>Implemented</u>			
		<u>As of June 28, 2006</u>		<u>As of Dec. 12, 2006</u>	
		<u>Yes</u>	<u>No</u>	<u>Yes</u>	<u>No</u>
D-2006-067	7	0	7	1	6
D-2005-042	1	1	0	1	0
D-2004-061	4	1	3	1	3
D-2003-070	3	3	0	3	0
D-2002-039	4	4	0	4	0
D-2001-088	8	8	0	8	0
D-2000-110	12	8	4	11	1
<b>Total</b>	<b>39</b>	<b>25</b>	<b>14</b>	<b>29</b>	<b>10</b>

(See Appendix C for a complete list of the recommendations we reviewed.)

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## Work Needed To Implement Recommendations

As of June 28, 2006, DoD organizations still needed to implement 14 of the recommendations made during FYs 2000 to 2006.<sup>6</sup> One outstanding recommendation was almost 7 years old. Also, as of December 12, 2006, we found that 4 additional recommendations were implemented, which resulted in 10 remaining outstanding.

Five DoD organizations were responsible for implementing the 14 recommendations. We indicate responsibility for and discuss the status (outstanding or closed) of recommendations below, by organization:

- **Under Secretary of Defense for Acquisition, Technology, and Logistics (USD[AT&L]) was responsible for implementing 1 of the 14 recommendations, this recommendation remains outstanding;**
- **Under Secretary of Defense for Policy (USD[P]) was responsible for implementing 2 of the 14 recommendations, 1 of the 2 recommendations remains outstanding;**
- **Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy (DUSD[TSP&NDP]) was responsible for implementing 4 of the 14 recommendations, each of the 4 recommendations remain outstanding;**
- **Director, Defense Research and Engineering (DDR&E) was both responsible for implementing 2 of the 14 recommendations, recommendations were closed and a new recommendation was made in this report to USD(P); and**
- **Director, Defense Technology Security Administration (DTSA) was responsible for implementing 5 of the 14 recommendations, 4 of the 5 recommendations remain outstanding.**

**Under Secretary of Defense for Acquisition, Technology, and Logistics (USD[AT&L]).** The USD(AT&L) did not implement one of the recommendations in Report No. D-2004-061, “Export Controlled Technology at Contractor, University, and Federally Funded Research and Development Center Facilities.” We issued the report on March 25, 2004, and recommended that the USD(AT&L) develop and insert a clause in the Defense Federal Acquisition Regulation Supplement (DFARS) requiring contractors to:

Comply with Federal export regulations and DoD guidance for export-controlled technology and technical data by obtaining an export license, other authorized approval or exemption, and preventing unauthorized disclosure to foreign nationals.

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<sup>6</sup>As previously noted, we determined during this audit that 4 of the 14 recommendations were implemented, as of December 12, 2006.

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Incorporate the terms of the clause in all subcontracts that involve export-controlled technology.

Conduct initial and periodic training on export compliance controls for those employees who have access to export-controlled technology.

Perform periodic self-assessments to ensure compliance with Federal export laws and regulations.

Although the USD(AT&L) concurred with our recommendation in July 2004, the office had not implemented it as of December 21, 2006. However, USD(AT&L) did publish a draft of the proposed clause in the Federal Register dated August 14, 2006. USD(AT&L) officials stated that they received comments from the public in November 2006. However, as of February 5, 2007, USD(AT&L) had not completed the clause in the DFARS because those officials had not obtained the agreement from the Defense Acquisition Regulatory Council on the wording of the clause or the approval of the Office of Management and Budget's Office of Information and Regulatory Affairs.

We examined the proposed clause; it did not require contractors to conduct initial and periodic training or to perform periodic self-assessments on compliance with the Federal export laws and regulations. Therefore, we concluded that the clause did not meet the intent of the recommendation, which will remain outstanding (open) until the clause is revised to address the requirements of the recommendation and is published in the DFARS.

**Under Secretary of Defense for Policy (USD[P]).** The Office of the USD(P) implemented one of the two recommendations we made in Report No. D-2000-110, "Export Licensing at DoD Research Facilities," on March 24, 2000.

Specifically, we recommended that the USD(P):

Coordinate with Commerce and State to develop guidance regarding when a visit or assignment of a foreign national to a Defense facility requires a deemed export license.<sup>7</sup>

Revise DoD Directive 2040.2, "International Transfers of Technology, Goods, Services, and Munitions," to clearly state policies, procedures, and responsibilities of DoD and Military Department hosts for determining whether a deemed export license is required when a foreign national visits a Defense facility.

**Guidance on When To Obtain a Deemed Export License.** On March 24, 2000, the USD(P) agreed with the first recommendation to coordinate with the Departments of Commerce and State to develop guidance for when a visit or assignment of a foreign national to a DoD facility requires a deemed export

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<sup>7</sup> A deemed export is defined by Export Administration Regulations (EAR) as a release of technology to a foreign national in the United States through such means as visual inspection, oral exchanges, or application of personal knowledge or technical experience acquired in the United States.

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license. Also, on March 24, 2000, the USD(P) stated that DoD Directive 5230.20, “Visits, Assignments, and Exchanges of Foreign Nationals,” would be revised to include DoD policies for licenses of deemed exports. During this audit, we examined the revised directive and determined that it includes guidance that satisfies our recommendation; therefore, we consider the recommendation closed.

**Revision of DoD Directive.** For the second recommendation—to revise guidance by clearly stating how Departmental hosts<sup>8</sup> should determine whether a deemed export license is required when a foreign national visits a Defense facility—DoD took several actions. Specifically, DTSA, an office under the USD(P):

- issued guidance in November 2002 and June 2003 that restricted the access of foreign nationals to export-controlled technologies at DoD facilities, and
- continued to review DoD Directive 2040.2, “International Transfers of Technology, Goods, Services, and Munitions,”<sup>9</sup> as of February 2005.

During this audit, a DUSD(TSP&NDP) official assigned to the USD(P) provided a draft memorandum, “Interim Guidance on Export Controls for Biological Agents,” dated August 14, 2004. We determined that the proposed memorandum would fulfill our recommendation and clearly defines the policies, procedures, and responsibilities of DoD and Military Department hosts for determining whether a deemed export license is required when a foreign national visits a DoD facility. A USD(P) official stated that the guidance will be included in the revised DoD Instruction 2040.2; however, the Instruction remains in draft, and the USD(P) official could not provide an estimated completion date. Therefore, this recommendation remains open until the guidance is published in DoD Instruction 2040.2.

### **Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy (DUSD[TSP&NDP]).**

DUSD(TSP&NDP)<sup>10</sup> did not implement two recommendations from FY 2004 and the two from FY 2006. In FY 2004, we issued Report No. D-2004-061, “Export Controlled Technology at Contractor, University, and Federally Funded Research and Development Center Facilities.” We issued the report on March 25, 2004, and recommended that the DUSD(TSP&NDP):

Expand “Interim Guidance on Export Controls for Biological Agents,”  
November 7, 2002 to:

Encompass all export-controlled technology.

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<sup>8</sup> A host is a designated individual or organization that is responsible for coordinating foreign national visits to sensitive and nonsensitive U.S. Government facilities.

<sup>9</sup> DoD Directive 2040.2, “International Transfers of Technology, Goods, Services, and Munitions,” is now in draft as DoD Instruction 2040.2, “International Transfers of Technology, Goods, and Services.”

<sup>10</sup> DUSD(TSP&NDP) was formerly titled the Deputy Under Secretary of Defense for Technology Security Policy and Counter Proliferation.



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Require program managers, in coordination with counterintelligence, security, and foreign disclosure personnel to:

- identify export-controlled technology, foreign national restrictions, and licensing requirements.
- identify threats by foreign countries that are targeting the specific technologies.
- identify vulnerabilities and countermeasures to protect the export-controlled technology.

Require program managers and contracting officers to ensure that contracts identify the export-controlled technology and contain requirements to maintain an access control plan, including unique badging technology; perform export compliance training; conduct annual self-assessments; and comply with Federal export laws by obtaining an export license, other authorized approval or exemption, or by safeguarding the technology when contracts involve export-controlled technology or information.

**Expanding Interim Guidance.** The DUSD(TSP&NDP) generally concurred with this recommendation on February 17, 2004, and later stated that follow-on draft guidance was issued in August 2004. We examined the draft interim guidance and found the guidance did address a portion of the recommendation; however, the guidance did not include procedures that require program managers, in coordination with counterintelligence, security, and foreign disclosure personnel, to identify:

- export-controlled technology, foreign national restrictions, and licensing requirements;
- threats by foreign countries that are targeting the specific technologies; and
- vulnerabilities and countermeasures to protect the export-controlled technology.

In addition, the interim guidance was not expanded to require program managers and contracting officers to conduct annual self-assessments.

On January 17, 2007, a DUSD(TSP&NDP) official stated that his office was working to include these procedures in the draft interim guidance. On February 2, 2007, a DUSD(TSP&NDP) official told us that the draft interim guidance will not be issued as a separate memorandum because the guidance will be published in DoD Instruction 2040.2. However, our recommendation was not incorporated in either the interim guidance or the Instruction; therefore, we consider this recommendation open. Further, in this report, we issued a new recommendation that requests the USD(P) to complete and publish DoD Instruction 2040.2, because the USD(P) has the responsibility for updating and publishing this Instruction.

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**Incorporating Interim Guidance in a DoD Directive.** For the second recommendation, we requested the DUSD(TSP&NDP):

Incorporate the interim guidance into the revision of DoD Directive 2040.2, "International Transfers of Technology, Goods, Services, and Munitions," January 1984, to include the roles and responsibilities of the program managers, counterintelligence, security, and foreign disclosure personnel.

The DUSD(TSP&NDP) generally concurred with this recommendation on March 25, 2004, and planned to include the interim guidance in DoD Instruction 2040.2. In August 2004, the DUSD(TSP&NDP) issued interim guidance.

During this audit, we reviewed the interim guidance and the DoD Instruction; neither addressed the roles and responsibilities of counterintelligence and foreign disclosure personnel for controlling the release of technology and technical data. Also during the audit, a DUSD(TSP&NDP) official reiterated to us on February 2, 2007, that the interim guidance will not be re-issued as a separate memorandum because the guidance will be published in the revised DoD Instruction. Regardless, the DoD Instruction did not fully address our recommendation and remains in draft without a planned completion date. Therefore, this recommendation remains open.

**Gaining Access to USXPORTS.** In addition to the recommendations we made in FY 2004 to the USD(TSP&NDP), we examined the following two recommendations addressed to the USD(TSP&NDP) in Report No. D-2006-067, "Controls Over Exports to China." Specifically, we recommended on March 30, 2006, that the DUSD(TSP&NDP):

Grant access privileges to the four DoD organizations currently without access to USXPORTS to facilitate reviews of export applications.

Update the guidance for the export review process to reflect current organizations and responsibilities.

Audit Report No. D-2006-067 identified that 4 of the 18 DoD organizations responsible for reviewing export applications were disconnected from USXPORTS (USXPORTS is an automated system used by DoD to process electronic export license data). The audit report recommended that the four organizations' access to this system be restored. The DUSD(TSP&NDP) agreed with our recommendation on March 29, 2006, and stated she would inform users of USXPORTS, within 60 days of becoming disconnected from the system, of the need to maintain access.

As of December 21, 2006, we found that DUSD(TSP&NDP) did not inform the four organizations' users of the need to maintain access to USXPORTS. A DTSA official, who reports to the Office of the DUSD(TSP&NDP), suggested we coordinate with the USD(P) regarding users' access to USXPORTS. (The USD[P] is responsible for developing, maintaining, and operating USXPORTS.)

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We asked a USD(P) official why users at the four organizations were not informed of the need to maintain access to USXPORTS. The USD(P) official was unable to provide a reason. He told us that his office did not coordinate with DTSA when users were dropped from USXPORTS. Therefore, DTSA would not have known when users of USXPORTS were dropped from the system.

As a result of our discussions with the USD(P) official, we again asked the DTSA official why users of USXPORTS were not notified of the need to maintain access to USXPORTS. The DTSA official told us that the organizations were notified, but he could not provide documentation to show that they were notified. Also, the DTSA official told us that DTSA could not require organizations to use USXPORTS. In addition, the DTSA official stated that there were plans to transfer responsibility for USXPORTS from USD(P) to DTSA; however, he could not provide the date of transfer. Although the DTSA official could not provide a date when DTSA would assume the responsibilities for USXPORTS, he told us that when the transfer occurs his office will modify DoD Instruction 2040.2 to require users of USXPORTS to maintain access to USXPORTS. As a result, the recommendation remains open.

**Updating Guidance on the Export Review Process.** Our second recommendation asked DUSD(TSP&NDP) to update guidance on the export review process to reflect current organizations and responsibilities. DUSD(TSP&NDP) agreed with this recommendation on March 29, 2006, and stated that organizational changes would be accurately reflected in the guidance on the export review process.

We determined that DUSD(TSP&NDP) established draft guidance, but the guidance was not updated to reflect current DoD organizations and responsibilities. On November 14, 2006, a DUSD(TSP&NDP) official stated that the guidance is a draft and the current organizations and responsibilities cannot be completely determined until the Office of the Secretary of Defense completes its reorganization. As a result, the recommendation remains open.

**Director, Defense Research and Engineering (DDR&E).** The following two recommendations to DDR&E are in Report No. D-2000-110, "Export Licensing at DoD Research Facilities," March 24, 2000.

Develop an export control program document containing procedures for determining if technology or commodities at Defense research facilities can be exported, with or without a license, including circumstances that may constitute exemptions from requirements of the Export Administration Regulations or International Traffic in Arms Regulations.

Mandate training requirements for personnel at Defense research facilities on the deemed export licensing requirements of the Export Administration Regulations and International Traffic in Arms Regulations.

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**Guidance on Restricted Technology.** DDR&E officials stated that the DUSD(TSP&NDP) issued a memorandum on August 14, 2004, that included a revised draft policy memorandum and a guide, “Managing Foreign Access: Implementing DoD Guidance on Restricted Technology.” During this audit, we found the guide contained procedures for determining whether goods, services, and technology at DoD research facilities were exportable with or without a license. In addition, we determined that this guidance is in draft and will be included in DoD Instruction 2040.2, which will be completed by USD(P) because the USD(P) has the responsibility for updating and publishing this Instruction. Therefore, we decided to close our recommendation to the DDR&E and issue a new recommendation requesting that USD(P) complete and publish DoD Instruction 2040.2. The new recommendation requests that USD(P) merge procedures for determining whether goods, services, and technology at DoD research facilities were exportable with or without a license—procedures already contained in the draft policy guide, “Managing Foreign Access: Implementing DoD Guidance on Restricted Technology”—into the DoD Instruction.

**Training Requirements for Defense Research Personnel.** For the second recommendation, a DDR&E official informed us that the training requirements for personnel at DoD research facilities depend on the content of yet-to-be-published revisions of the DFARS and DoD Instruction 2040.2. In addition, DDR&E officials told us that they trained program managers, laboratory personnel, and security managers on deemed export licensing requirements of the Export Administration Regulations and the International Traffic in Arms Regulations.

Our review of the proposed revisions to DFARS and DoD Instruction 2040.2 determined that neither document included a mandate for training personnel at DoD research facilities on deemed export licensing requirements. As previously stated, DDR&E officials stated that the DUSD(TSP&NDP) issued a memorandum on August 14, 2004, that included a revised draft policy memorandum and a guide, “Managing Foreign Access: Implementing DoD Guidance on Restricted Technology.”

We found the guide prescribed training for personnel at DoD research facilities on export licensing requirements. However, on February 2, 2007, a DUSD(TSP&NDP) official reiterated to us that the interim guidance will not be issued as a separate memorandum because the guidance will be published in DoD Instruction 2040.2. As such, our recommendation was not included in the pending revisions to the DFARS and the Instruction.

Further, we issued a new recommendation that requests the USD(P) to complete and publish DoD Instruction 2040.2 because, as previously stated, the USD(P) has the responsibility for updating and publishing this Instruction. Therefore, we decided to close our recommendation to DDR&E and issue a new recommendation that requests USD(P) to complete and publish the DoD Instruction. Completing the Instruction will involve the insertion of a mandate contained in the draft policy guide, “Managing Foreign Access: Implementing DoD Guidance on Restricted Technology” for training personnel at DoD research facilities on deemed export licensing requirements.

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**Director, Defense Technology Security Administration (DTSA).** The DTSA implemented one recommendation but not four others made in Report No. D-2006-067, “Controls Over Exports to China,” March 30, 2006. During this audit, we examined DTSA actions to implement the following five recommendations:

Prepare written analyses to support decisions on export applications and maintain documents in USXPORTS to support those decisions.

Elevate decisions to the extent possible when the appeal process does not produce a decision that supports the national security posture.

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

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

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

**Documentation for Decisions on Export Applications.** In response to the first recommendation, on May 19, 2006, the Acting DUSD(TSP&NDP) replied for DTSA:

We are in general agreement with the proposition that complete analysis is a necessary and vital part of the licensing process. However, we disagree that inclusion of *every* facet of analysis considered in making a licensing determination is required-or even necessary-in *every* individual case. This is particularly true since implementation of a newer, automated license system, USXPORTS.

All cases that were reviewed for this Report occurred prior to USXPORTS deployment. Significant changes have been made to the automated license database including:

- USXPORTS maintains thorough data for each case, e.g., support documents, technical specification, end-user information, etc;
- USXPORTS provides an easy way for licensing experts to search for precedent decisions, e.g., cases that involve the same item to the same destination, or the same end user or an item of similar capability to the same country; and
- USXPORTS now contains complete analytic information for all cases escalated to the Operating Committee, the interagency committee that is the first line of escalation for disputed cases and where most are resolved.

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To determine whether the recommendation was implemented, we requested and received the files supporting 1,609 and 1,880 applications to export to China for calendar years 2005 and 2006, respectively. We found that DTSA made recommendations (with conditions) to approve 2,953 export applications and to disapprove 385 applications. Those 3,338 applications represented 96 percent of the 3,489 applications processed for exports to China in calendar years 2005 and 2006.<sup>11</sup> According to DTSA officials, the 3,489 applications contained complete and timely data.

**Selection Process for Application Review.** We judgmentally selected and reviewed 40 of the 3,489 applications that contained requests to export sensitive goods, services, and technology such as chemicals and toxins, electronics, explosives, sensors, and lasers. The sample of 40 applications had closing dates<sup>12</sup> from January 7, 2005, to December 29, 2006. We selected these applications because of the potential adverse impact the prospective exports would have on regional stability, proliferation of nuclear weapons, use of chemical and biological weapons, and national security, if sent to China.

**Results of Application Review.** The review of the application files showed that 29 of the 40 files did not contain adequate analysis. In addition, 39 of the 40 did not have adequate supporting documentation.

For example, one file contained an application that recommended approval with conditions to export a pulse neutron generator to China. For this item, the Export Administration Regulations state that eight factors should be considered when determining whether to recommend approval of an application. Those factors were:

- whether the items to be transferred are appropriate for the stated end use and whether that stated end use is appropriate for the end user,
- the significance for nuclear purposes of the particular item,
- whether the item can be used in a nuclear reprocessing or enrichment facility,
- the types of assurances given that the item will not be used for nuclear explosive purposes or proliferation,
- whether any party to the transaction has been engaged in clandestine or illegal procurement activities,
- whether an application has previously been denied, or whether the end user has previously diverted items,

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<sup>11</sup> The remaining applications were either approved, returned to the applicant without action, or partially approved.

<sup>12</sup> DTSA defined “closing date” as the date when it completed work on an application, developed its final recommendation for the application, and returned the application to the Department of Commerce.

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- whether the export or re-export would present an unacceptable risk of diversion to a nuclear explosive activity or a nuclear fuel-cycle activity, and
  - the nonproliferation credential of the importing country.

A review of this application file determined that the analysis and documentation were inadequate to justify the decision made by DTSA to recommend approval of this application. Specifically, the file did not include adequate analysis or documentation for any of the eight factors. Therefore, the file did not support the recommendation to approve the application. Because 29 of 40 files did not contain adequate analysis and 39 of 40 lacked documentation, our recommendation remains open. See Appendix D for the results of our analysis of the 40 application files we selected for review.

**Decisions To Elevate Recommendations.** For our second recommendation, we suggested that DTSA elevate its recommendations to the extent possible in the export application appeal process, if the majority of the representatives from the Departments of Commerce, Energy, and State did not agree with a DTSA recommendation (DTSA is responsible for recommending whether to approve export applications for DoD). We selected 11 applications that DTSA disapproved. One of the 11 was approved (with conditions) by all the other Departmental representatives. Thus, the majority of the Departments opposed the DTSA recommendation. Therefore, DTSA had the opportunity to appeal, but instead changed its recommendation and decided to approve the application with conditions.

Export Administration Regulations do not require a Department to appeal if the majority of the other Departments disagree with its recommendation. Also, Export Administration Regulations allow a Department to add conditions that it considers appropriate to offset the risk associated with approval of an application. As a result, our sample did not detect any instances in which DTSA did not use the appeal process to the extent it considered possible. Therefore, we consider this recommendation closed.

**Management Control Plan.** For the remaining three recommendations, which pertain to management controls, DTSA agreed with the recommendations on March 29, 2006, and stated it had adjusted its management control plan to:

- provide written responsibilities to the senior management control official,
- maintain training documentation for managers of operating and assessable units, and
- more effectively assess internal controls for recording analyses and maintaining documentation in USXPORTS.

DTSA provided a draft management control plan that did not meet the intent of the recommendations. On November 16, 2006, a DTSA official stated that

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controls were in place but not written into the draft management control plan because of significant personnel turnover. Although he stated that the plan would be updated by December 31, 2006, we were unable to obtain this plan before we completed the audit. The three recommendations cited above will remain open until DTSA updates and approves the management control plan, including the requirements of our recommendations.

## **Effective Process for Following Up on Prior Recommendations**

While the five DoD organizations responsible for managing export activities implemented most of the recommendations, they did not establish a fully effective process for following up on and implementing all of our recommendations. Those organizations had agreed to implement each of our 39 recommendations; however, 1 recommendation remained open for almost 7 years.

DoD Instruction 5010.40, "Managers' Internal Control (MIC) Program Procedures," January 4, 2006, states that the Managers' Internal Control Program should identify and promptly correct ineffective internal controls. Also, the Instruction requires DoD managers to track corrective actions taken to expedite prompt resolution of control deficiencies. In addition, the Instruction states that the deficiencies identified, whether through internal review or by an external audit, should be evaluated and corrected.

Office of Management and Budget Circular No. A-123, "Management's Responsibility for Internal Control," December 21, 2004, requires DoD Component managers to take prompt and effective actions to correct weaknesses in their internal control processes. The Circular states that management must make a decision regarding Inspector General audit recommendations within a 6-month period and complete implementation of management's decision within 1 year, to the extent practicable.

The audit showed that four DoD organizations were not prompt in implementing 10 of the recommendations. While DoD organizations made improvements in export controls and implemented 74 percent of the recommendations, they told us that implementation of the remaining recommendations was restricted, in part, by the ongoing DoD reorganization, personnel turnover, insufficient numbers of personnel, and the formal process for updating the DFARS. However, we contend that DoD managers are constantly confronted with constraints on resources and with organizational changes and must take action to implement audit recommendations to manage risks and improve management processes.

## **Risks of Not Implementing Export Controls**

Until the recommended controls are implemented, DoD continues to accept avoidable risks of exporting sensitive goods, services, and technology that could threaten our national security. During this audit, we found that 10 recommendations remain open. We made 1 of the 10 recommendations in FY 2000, 3 in FY 2004, and 6 in FY 2006.



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**Controls Recommended in FY 2000.** Our review in FY 2000 recommended that the USD(P) revise DoD Directive 2040.2 to clearly state policies, procedures, and responsibilities of DoD and Military Department hosts for determining whether a deemed export license was required when a foreign national visits a Defense facility. Such a revision is important because, during the review in FY 2000, we found that more than 11,000 foreign nationals visited 6 research facilities within only 2 fiscal years.

**Controls Recommended in FY 2004.** Our review in FY 2004 recommended that DUSD(TSP&NDP) expand interim guidance on export controls for biological agents and include the interim guidance in the DoD Directive. The guidance should include the roles and responsibilities of program managers and of counterintelligence, security, and foreign disclosure personnel.

Also, we recommended the USD(AT&L):

- develop and include in the DFARS an export clause that requires a contractor to comply with Federal export regulations and DoD guidance,
- include an export-controlled technology clause in all subcontracts, and
- conduct training and self-assessments.

However, until DoD program managers are held accountable for identifying export-controlled technology and have controls in place to protect the export-controlled technology, DoD will be at increased risk of other nations' countering or reproducing our technology.

**Controls Recommended in FY 2006.** Most recently, in FY 2006, we recommended that DTSA:

- record its analyses and insert documentation in the USXPORTS database to support recommendations made on export applications;
- update export guidance to reflect current organizational titles, responsibilities, and structure;
- grant DoD organizations without access to USXPORTS the access needed to facilitate reviews of export applications; and
- develop effective management controls.

Our recommendations were intended to help reduce the risk of allowing unjustified exports to China and to strengthen U.S. actions to maintain regional stability; hinder proliferation of nuclear, chemical, and biological weapons; and offset adverse effects on our national security. Until management fully implements the 10 recommendations, DoD will continue to accept avoidable risks in exporting sensitive goods, services, and technology that could threaten our national security.

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## Conclusion

DoD organizations did implement 74 percent of the recommendations in seven reports issued from FY 2000 through FY 2006. However, these organizations need to continue taking actions to fully implement the 10 remaining recommendations.

Normally, we request DoD organizations to comment on each recommendation, but we received those comments during the audit. Therefore, additional comments are not necessary on the prior recommendations. As a result of this audit, we are making new recommendations and asking management to comment on them.

We will ask our Report Followup Division to continue to track the status of actions taken on the unimplemented recommendations during its periodic reviews. The division will monitor the status of the 10 unimplemented recommendations shown in Appendix C of this report.

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## Management Comments on the Finding and Audit Response

**USD(AT&L) Comments on the Finding.** We issued a draft of this report on March 12, 2007. The Director of Defense Procurement and Acquisition Policy responded for the Under Secretary of Defense for Acquisition, Technology, and Logistics and neither concurred nor nonconcurred with our finding and recommendations, but provided comments. For the full text of the comments, see the Management Comments section of the report.

The Director suggested that we edit and augment the finding to reflect the procedures involved with updating the Defense Federal Acquisition Regulation Supplement (DFARS). In addition, the Director requested clarification on the issuance of export guidance, training requirements for DoD research personnel, and responsibility for DoD Instruction 2040.2. For full text of the comments, see the Management Comments section of the report.

**Audit Response.** We considered the Director's comments related to the process for updating the DFARS. In consideration of the Director's comments, we did not see that the addition of an explanation of the process for coordinating changes to the Supplement was needed to explain the current status of our recommendations. However, we revised the report to clarify our position that the proposed clause in the DFARS did not meet the intent of our prior recommendation, which requires contractors to conduct initial and periodic training and to perform periodic self-assessments on their compliance with Federal export laws and regulations. Therefore, the recommendation remains open until the clause is revised and published in the DFARS to address our recommendation.

Also, we considered the Director's comments on the proposed revision to the DFARS, related to issuing export guidance to and training of DoD personnel. As a result of reviewing those comments, we revised our finding to show that the draft policy guide issued by the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy, "Managing Foreign Access: Implementing DoD Guidance on Restricted Technology," should address our recommendations on issuing export guidance and training DoD personnel. However, the guide is a draft and the policies listed in the guide must be included in the revised DoD Instruction 2040.2 and published by USD(P). The recommendation remains open until the requirements are addressed in formal policy documents.

In addition, we considered the Director's comments concerning the responsibility for revising DoD Instruction 2040.2. We revised our report and requested that the Under Secretary of Defense for Policy complete the revisions and issue the Instruction (the Under Secretary of Defense for Policy is responsible for issuing DoD Instructions related to international transfers of technology, goods, services, and munitions). We acknowledge, but made no change in response to, the Director's comments that no DoD Instruction is numbered 2040.2. The draft DoD Instruction 2040.2, "International Transfers of Technology, Goods, and Services,"

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is replacing DoD Directive 2040.2, “International Transfers of Technology, Goods, Services, and Munitions.”

Finally, we considered the Director’s comments related to responsiveness in implementing recommendations. The Director stated that he believed his office’s procedures for following up on our recommendations were adequate to ensure timely and responsive actions. However, management actions are still needed to implement our recommendations in a timely manner since we issued our audit report on March 25, 2004, and the recommendations remained outstanding as of March 29, 2007. Until the recommendations are implemented, some DoD program managers will not be held accountable for identifying and protecting export-controlled technology, and we will be at increased risk of other nations’ countering or reproducing our technology.

**DTSA Comments on the Finding.** The Director (Acting) of the Defense Technology Security Administration nonconcurred with our findings related to her office. Specifically, the Director disagreed with our use of the policies in the Export Administration Regulations (EAR) for evaluating her office’s review of applications to export dual-use (military or civilian use) goods, services, and technologies. The Director stated that it is the responsibility of the Department of Commerce, not DoD, to use the EAR as a basis for evaluating export license applications. Also, the Director disagreed with our finding that her office was required to document reasons for all recommendations made on export applications. She commented that a statement of reasons was required only for recommendations to deny export licenses. In addition, the Director commented that her office had no statutory or regulatory authority to approve or deny export applications, merely to recommend a course of action to the licensing department.

Further, she commented that DoD Instruction 2040.2 could not be finalized until the process for coordinating it within the Department was complete. Also, she stated that our audit did not consider the steps taken by her office to incorporate prior audit recommendations, many of which are included in the upcoming revision of DoD Instruction 2040.2, which has been in process for many months. For the full text, see DTSA Management Comments on page 37 of this report.

**Audit Response.** The Director disagreed with our use of the policies identified in the EAR. However, DoD Directive 5010.38, “Management Control (MC) Program,” August 26, 1996, states that each DoD field activity (the Defense Technology Security Administration is a 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, such as the Export Administration Act (EAA) and the EAR.

The EAA authorizes the Secretary of Commerce to issue policies and procedures for exporting dual-use items. The Secretary issued those policies and procedures in EAR for use in controlling and overseeing the export of dual-use items. Those export policies and procedures are applicable to agencies involved in overseeing, evaluating, recommending, and approving the requests for exports of sensitive technologies to countries of concern. Although the EAR does not require the

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federal agencies involved in the export license process to review all export license applications submitted for consideration, those agencies responsible for making recommendations on exports of dual-use items, including DoD, are subject to addressing the requirements of the EAA and applicable regulations for those applications reviewed. Accordingly, it would be prudent for DTSA to follow those requirements when assessing export license applications because DTSA is the DoD activity responsible for reviewing, evaluating, and making recommendations to the Department of Commerce on such requests for dual-use items. The requirements of the EAR may help reduce the risk of allowing unjustified exports to China and to strengthen U.S. actions to maintain regional stability; hinder proliferation of nuclear, chemical, and biological weapons; and offset adverse effects on our national security. Although, our review was limited to evaluating export license applications to China, it would be prudent for DTSA to consider those factors in the EAR for all export license applications.

Also, the Director disagreed with our finding that her office was required to document reasons for all recommendations made on export applications. She commented that a statement of reasons was required only for recommendations to deny export licenses. We addressed the need to document reasons for all recommendations in our report, "Controls Over Exports to China," March 30, 2006. That report cited the Principal Statutory Authority (Export Administration Act) for the EAR, which states that DoD will make and keep records of its advice, recommendations, or decisions, including the factual and analytical basis, connected with export licenses.

In addition, that report cited the Government Accountability Office's "Standards for Internal Control in the Federal Government," November 1999, which stated, "Control activities occur at all levels and functions of the entity." Those control activities include "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." Furthermore, as demonstrated by our audit, DTSA did not maintain appropriate documentation to show the factual and analytical basis for recommending to the Department of Commerce their position on export license applications.

We agree with the Director's comment that her office had no statutory or regulatory authority to approve or deny export applications. We modified our report to show that her office was responsible only for recommending approval or denial of export applications to the Department of Commerce. Further, we agreed with the Director's comment that DoD Instruction 2040.2 cannot be finalized until the coordination process is completed. We acknowledged this fact in our draft report; therefore, no change was made in this final report.

**DDR&E Comments on the Finding.** Although not required to comment, the Director of Defense Laboratory Programs, responding for the Director, Defense Research and Engineering, pointed out that our recommendation to complete DoD Instruction 2040.2 should be redirected to the Under Secretary of Defense for Policy. For the full text of the comments, see the Management Comments section of the report.

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**Audit Response.** We agree with the comment by the Director of Defense Laboratory Programs about redirecting the responsibility for completing the draft DoD Instruction 2040.2 to the Under Secretary of Defense for Policy and adjusted the draft of this report accordingly. Also, we made the other changes that the Director requested to clarify statements he made during the audit. For instance, we adjusted this final report to show that training requirements for personnel at Defense research facilities depend on the content of yet-to-be-published revisions of the DFARS and DoD Instruction 2040.2. We also adjusted this final report to reflect the comments made regarding procedures included in the DFARS and DoD Instruction 2040.2.

## **Recommendations, Management Comments, and Audit Response**

For clarity of presentation, we split a single recommendation (Recommendation 1. in our draft report) addressed to four organizations with open recommendations into four distinct recommendations below (Recommendations 1. through 4.). This format highlights each organization's management comments. Also, we renumbered draft Recommendation 2. as Recommendation 2.b.

**1. We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics establish followup procedures to ensure that timely and responsive actions are taken to implement all audit recommendations.**

**Management Comments.** The Director of Defense Procurement and Acquisition responded for the Under Secretary of Defense for Acquisition, Technology, and Logistics and neither concurred nor nonconcurred with our finding and recommendation, but provided comments. Specifically, the Director commented that his office's followup procedures are adequate to ensure timely and responsive actions to implement our recommendations. The Director also stated implementation will be complete upon publication of the final DFARS rule.

**Audit Response.** The Director's comments were not fully responsive. Timely implementation of this recommendation is still needed. We issued our audit report on March 25, 2004, and the recommendation remained outstanding on March 29, 2007. Therefore, the potential risks we mentioned in our report on March 25, 2004, remain. That is, until DoD program managers are held accountable for identifying export-controlled technology and have controls in place to protect the export-controlled technology, DoD will be at increased risk of other nations' countering or reproducing our technology. In accordance with DoD Directive 7650.3, we request that USD(AT&L) reconsider his response and send comments by October 29, 2007.

**2. We recommend that the Under Secretary of Defense for Policy:**

**a. Establish followup procedures to ensure that timely and responsive actions are taken to implement all audit recommendations.**

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**b. Complete and publish DoD Instruction 2040.2, “International Transfers of Technology, Goods, and Services.”**

**Management Comments Required.** The Under Secretary of Defense for Policy did not comment on a draft of this report. We request that the Under Secretary of Defense for Policy provide comments on the final report.

**3. We recommend that the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy establish followup procedures to ensure that timely and responsive actions are taken to implement all audit recommendations.**

**Management Comments Required.** The Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy did not comment on a draft of this report. We request that the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy provide comments on the final report by October 29, 2007.

**4. We recommend that the Director, Defense Technology Security Administration establish followup procedures to ensure that timely and responsive actions are taken to implement all audit recommendations.**

**Management Comments Required.** The Director, Defense Technology Security Administration did not comment on the recommendation. We request that the Director, Defense Technology Security Administration provide comments on the recommendation for the final report by October 29, 2007.

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## Appendix A. Scope and Methodology

We conducted this performance audit from June 28, 2006, through March 12, 2007, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We reviewed documents such as Executive Orders, Federal laws, and regulations, including the Export Administration Act and the associated Export Administration Regulations. 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 interviewed personnel in the following organizations:

- Department of Commerce;
- Under Secretary of Defense for Acquisition, Technology, and Logistics;
- Office of the Deputy Under Secretary of Defense for Technology Security Policy and National Disclosure Policy;
- Director, Defense Research and Engineering; and
- Defense Technology Security Administration.

Our contacts with personnel in these organizations included discussions on the implementation of recommendations in the previously issued audit reports.

We limited our review to open recommendations in audit reports we issued to comply with Public Law 106-65. Only DoD IG Reports No. D-2006-067, D-2004-061, and D-2000-0110 contained open recommendations.

To complete this review, we judgmentally selected a sample of 40 export license applications from 3,489 export license applications processed in calendar years 2005 and 2006. We obtained the complete USXPORTS file on each of the 40 selected applications to determine whether DTSA analysis, documentation, and elevation procedures achieved the recommended actions made in DoD IG Report No. D-2006-067.

**Use of Computer-Processed Data.** USXPORTS is the automated system that DTSA uses for processing export applications. We used computer-processed data from USXPORTS to identify export license applications for China. Testing the reliability of the computer-processed data was not the purpose of this audit; the data were used strictly as source documentation. We thoroughly compared the contents of each selected export license application with supporting



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documentation. Nothing came to our attention as a result of the testing that caused us to doubt the reliability of the computer-processed data.

**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.

**Government Accountability Office High-Risk Area.** The Government Accountability Office has identified several high-risk areas in the Department of Defense. This report does not cover any DoD high-risk areas, but this report does address the Government Accountability Office's newly designated Federal Government-wide high-risk area of "Ensuring the Effective Protection of Technologies Critical to U.S. National Security Interests."<sup>13</sup>

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<sup>13</sup> The Government Accountability Office designated this area as being high-risk in January 2007.

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## 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 regarding 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 1, 2001

### DoD IG

DoD IG Report No. D-2006-067, "Controls Over Exports to China," March 30, 2006

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. D-2003-070, "Export Controls: DoD Involvement in Export Enforcement Activities," March 28, 2003

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

DoD IG Report No. D-2000-0110, "Export Licensing at DoD Research Facilities," March 24, 2000

### 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

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Inspectors General of the Department of Commerce, Defense, Energy, Homeland Security, and State and the Central Intelligence Agency Report No. D-2004-061, "Interagency Review of Foreign National Access to Export Controlled Technology in the United States," April 16, 2004

Offices of Inspector General Department of Commerce, Defense, State, and the Treasury; the Central Intelligence Agency; and the U.S. Postal Service Report No. D-2003-060, "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

Office of the Inspector General Department of Defense, Office of Intelligence Review, Report No. 00-OIR-05, "Measures to Protect Against the Illicit Transfer of Sensitive Technology," March 27, 2000

Offices of the Inspectors General Departments of Commerce, Defense, Energy, and State Report No. D-2000-109, "Interagency Review of the Export Licensing Process for Foreign National Visitors," March 24, 2000

## Appendix C. Status of Prior Recommendations

Implementation of Recommendations					
Report	Recommendation Number	Status of Recommendations			
		As of June 28, 2006		As of December 21, 2006	
		Implemented	Not Implemented	Implemented	Not Implemented
D-2006-0067-D000LS-0001	1.a	0	1	0	1
D-2006-0067-D000LS-0001	1.b	0	1	0	1
D-2006-0067-D000LS-0001	2.a	0	1	0	1
D-2006-0067-D000LS-0001	2.b	0	1	1	0
D-2006-0067-D000LS-0001	2.c	0	1	0	1
D-2006-0067-D000LS-0001	2.d	0	1	0	1
D-2006-0067-D000LS-0001	2.e	0	1	0	1
D-2005-0042-D000LG-0002	1	1	0	1	0
D-2004-0061-D000LG-0001	1.a	0	1	0	1
D-2004-0061-D000LG-0001	1.b	0	1	0	1
D-2004-0061-D000LG-0001	2.a	0	1	0	1
D-2004-0061-D000LG-0001	2.b	1	0	1	0
D-2003-0070-D000LG-0001	A.1	1	0	1	0
D-2003-0070-D000LG-0001	A.2	1	0	1	0
D-2003-0070-D000LG-0001	A.3	1	0	1	0
D-2002-0039-D000LG-0001	1	1	0	1	0
D-2002-0039-D000LG-0001	2	1	0	1	0
D-2002-0039-D000LG-0001	3	1	0	1	0
D-2002-0039-D000LG-0001	4	1	0	1	0
D-2001-0088-D000LG-0001	A.1	1	0	1	0
D-2001-0088-D000LG-0001	A.2	1	0	1	0
D-2001-0088-D000LG-0001	A.3	1	0	1	0
D-2001-0088-D000LG-0002	B.2.a	1	0	1	0
D-2001-0088-D000LG-0002	B.2.b	1	0	1	0
D-2001-0088-D000LG-0002	C.2	1	0	1	0
D-2001-0088-D000LG-0003	B.1	1	0	1	0
D-2001-0088-D000LG-0003	C.1	1	0	1	0
D-2000-0110-D000LA-0001	A.1.a	0	1	1	0
D-2000-0110-D000LA-0001	A.1.b	0	1	0	1
D-2000-0110-D000LA-0001	A.1.c	1	0	1	0
D-2000-0110-D000LA-0001	A.2.a	1	0	1	0
D-2000-0110-D000LA-0001	A.2.b	1	0	1	0
D-2000-0110-D000LA-0001	A.2.c	0	1	1	0
D-2000-0110-D000LA-0001	A.2.d	0	1	1	0
D-2000-0110-D000LA-0002	B.1.a	1	0	1	0
D-2000-0110-D000LA-0002	B.1.b	1	0	1	0
D-2000-0110-D000LA-0002	B.2	1	0	1	0
D-2000-0110-D000LA-0002	B.3	1	0	1	0
D-2000-0110-D000LA-0002	B.4	1	0	1	0
<b>Total</b>		<b>25</b>	<b>14</b>	<b>29</b>	<b>10</b>

## Appendix D. Assessment of Export Applications

<b>CY 2005 and CY 2006 Assessment of DTSA Applications for Making Exports to China</b>					
<u>Sample Number</u>	<u>USXPORTS File Number</u>	<u>Export Control Classification Number</u>	<u>Adequate Analysis</u>	<u>Adequate Documentation</u>	<u>DTSA Recommendation</u>
1	D347546	2A983	No	No	AWC
2	D337344	1C350	No	No	AWC
3	D344327	3A231	No	No	AWC
4	D340340	6A003	No	No	AWC
5	D333544	1C350	No	No	AWC
6	D333545	1C350	No	No	AWC
7	D329056	6A003	No	No	AWC
8	D337063	1C350	No	No	AWC
9	D342226	6A003	No	No	AWC
10	D331360	6A003	No	No	AWC
11	D322475	6A003	No	No	AWC
12	D340947	1C350	No	No	AWC
13	D348973	2A983	No	No	AWC
14	D332675	6A003	Yes	No	AWC
15	D344183	6A003	No	No	AWC
16	D343704	1C350	No	No	AWC
17	D347548	2A983	No	No	AWC
18	D336673	1C350	No	No	AWC
19	D336321	1C350	No	No	AWC
20	D332824	2A983	No	No	AWC
21	D326299	1C350	No	No	Disapproved
22	D332399	6A003	No	No	Disapproved
23	D332835	6A003	No	No	Disapproved
24	D335081	6A003	Yes	No	Disapproved
25	D335082	6A003	Yes	No	Disapproved
26	D340344	6A003	Yes	No	Disapproved
27	D342044	6A003	Yes	No	Disapproved
28	D345271	6A003	Yes	No	Disapproved
29	D349729	6A003	Yes	No	Disapproved
30	D346795	6A003	Yes	No	Disapproved
31	D363862	1C350	No	No	AWC
32	D359155	1C350	No	No	AWC
33	D357867	1C350	No	No	AWC
34	D367495	2A983	No	No	AWC
35	D361730	2A983	No	No	AWC
36	D368316	2A983	No	No	AWC
37	D364144	3A231	No	No	AWC
38	D360724	3A231	Yes	No	AWC
39	D355231	6A003	N/A	N/A	RWA
40	D364201	6A003	Yes	No	Disapproved

(The first 30 applications represent Calendar Year (CY) 2005 and the remaining 10 represent CY 2006 applications.) 6A003–Sensors and Lasers; 1C350–Chemicals and Toxins; 2A983–Explosives; 3A231–Electronics; AWC–Approved With Conditions; RWA–Returned Without Action; and N/A–Not Applicable.

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## **Appendix E. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense for Acquisition, Technology, and Logistics  
Director, Defense Research and Engineering  
Deputy Under Secretary of Defense (Science and Technology)  
Under Secretary of Defense for Policy  
Deputy Under Secretary of Defense (Technology Security Policy and National Disclosure Policy)  
Under Secretary of Defense (Comptroller)/Chief Financial Officer  
Deputy Chief Financial Officer  
Deputy Comptroller (Program/Budget)  
Under Secretary of Defense for Intelligence  
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

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## **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, Department of Treasury  
Inspector General, Central Intelligence Agency  
Inspector General, U.S. Postal Service  
U.S.-China Economic and Security Review Commission

## **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 Homeland Security and Governmental Affairs  
Senate Select Committee on Intelligence  
Senate Committee on Foreign Relations  
House Committee on Appropriations  
House Subcommittee on Defense, Committee on Appropriations  
House Committee on Armed Services  
House Committee on Oversight and Government Reform  
House Subcommittee on Government Management, Organization, and Procurement,  
Committee on Oversight and Government Reform  
House Subcommittee on National Security, and Foreign Affairs, Committee on Oversight  
and Government Reform  
House Subcommittee on Information Policy, Intergovernmental Relations, and the  
Census, Committee on Government Reform  
House Subcommittee on Terrorism, Nonproliferation, and Trade, Committee on Foreign  
Affairs  
House Permanent Select Committee on Intelligence  
House Subcommittee on Oversight and Investigations  
House Committee on Homeland Security





# Under Secretary of Defense for Acquisition, Technology, and Logistics Comments

Final Report  
Reference



ACQUISITION,  
TECHNOLOGY  
AND LOGISTICS

## OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON  
WASHINGTON, DC 20301-3000

MAR 26 2007

MEMORANDUM FOR PROGRAM DIRECTOR, READINESS AND OPERATIONS  
SUPPORT, OFFICE OF THE INSPECTOR GENERAL

THROUGH: DIRECTOR, ACQUISITION RESOURCES AND ANALYSIS

*ED/AMB  
2/27/07*

SUBJECT: Followup Audit on Recommendations for Controls Over Exporting Sensitive Technologies to Countries of Concern (Project No. D2006-D000LG-0199.000) (Your Memo dated March 12, 2007)

As requested, we have reviewed the draft report and offer the following comments.

1. The Office of Defense Procurement and Acquisition Policy (DPAP) has responsibility for Recommendations 2.a. and 2.b. in Report D-2006-061 dated 25 March 2004.
  - a. The finding (on page 6 of the draft report) regarding the status of OUSD(AT&L) DPAP action on these recommendations should be edited and augmented to reflect that (1) completing the action to implement Recommendations 2.a. and 2.b. requires compliance with the formal rulemaking process that applies to the DoD Federal Acquisition Regulation Supplement (DFARS), (2) the implementing action is not limited to publication of a single clause but involves publication of a DFARS rule that includes contract clauses for use in particular circumstances, (3) DoD published a proposed rule on 12 July 2005, and based on public comments received by the October 2005 deadline, made substantial revisions to it; (4) DoD published the *second* proposed rule on 14 August 2006, and received public comments from 167 persons or organizations by the deadline of 2 November 2006; (5) the DAR Council has agreed upon a draft final rule based on consideration of public comments received on the second proposed rule, and the draft final rule is now in the last stages of the formal rulemaking process. Publication of the final rule is expected within about 90 days.
  - b. A clarification is needed on page 11 under "Issuance of Guidance". The DFARS rule does not contain procedures for determining whether goods, services, and technology at Defense research facilities are exportable with or without a license. What the DFARS rule does is to assign responsibility to requiring activities for determining if, during performance of a contemplated contract, the contractor will generate or require access to export-controlled information or technology.
  - c. A correction is needed on pages 11-12 under "Training Requirements for Defense Research Personnel". There are no training requirements in the DFARS rule. Although the DFARS rule does not mandate training, the

Revised

Revised



DFARS R&D Committee, the DAR Council, DPAP, DDRE, and DTSA recognize the importance of training for contracting officers and requiring activity officials who will implement the new DFARS rule. DDRE will lead the effort to ensure appropriate training is available to requiring activities and DPAP will lead the effort to ensure appropriate training is available for contracting officers. The two training efforts will be coordinated since the requiring activities and the contracting officers work interactively. The content of contracting officer training is dependent upon the specifics of the DFARS rule. The content of the requiring activity training is dependent upon the specifics of both the DFARS rule and the revised DoDD 2040.2. Therefore a comprehensive training syllabus cannot be designed until the rule and directive are complete.

Revised

2. DPAP does not have responsibility for DoD Directive 2040.2. There is a suggestion in the draft report that there is a linkage between publication of the DFARS rule, for which DPAP has responsibility, and publication of a new 2040.2. There is no such linkage. (Incidentally, references in the report to DoDI 2040.2 should be changed to DoDD 2040.2. There is not DoD Instruction numbered 2040.2.)

Page 22

Deleted

3. The draft report's references to USD(AT&L) being responsible for DoDD 2040.2 are confusing, especially since the summary regarding previous recommendations directed to USD(P) (at the top of page 7) and Recommendation 2 (on page 18) of this draft report recognize that responsibility for publishing 2040.2 rests with the USD(P). For example, the statements on pages 11 and 12 of the draft report that a USD(AT&L) official "could not provide a planned completion date for DoDI 2040.2, which remains in draft" are irrelevant since USD(AT&L) is responsible for neither the draft nor the final document. We suggest that the report be clarified in this regard.

Page 22

4. DPAP defers to OUSD(AT&L) ARA with regard to Recommendation 1 on page 18 of the draft report. From DPAP's perspective, OUSD(AT&L) follow-up procedures are adequate to ensure timely and responsive actions are taken to implement the IG recommendation assigned to DPAP. DPAP has provided periodic follow-up status reports on actions taken to implement Recommendations 2.a. and 2.b. of OIG Report D-2004-061. Implementation will be complete upon publication of the final DFARS rule.

If you require further information, please contact Barbara Glotfelty at 703-697-9351 or [barbara.glotfelty@osd.mil](mailto:barbara.glotfelty@osd.mil).

*for Richard Gorman*  
Shay D. Assad  
Director, Defense Procurement  
and Acquisition Policy

# Defense Research and Engineering Comments

Final Report  
Reference



OFFICE OF THE DIRECTOR OF  
DEFENSE RESEARCH AND ENGINEERING  
3040 DEFENSE PENTAGON  
WASHINGTON, DC 20301-3040

MAR 26 2007

MEMORANDUM FOR PROGRAM DIRECTOR, READINESS AND  
OPERATIONS SUPPORT, OFFICE OF THE  
INSPECTOR GENERAL

SUBJECT: Follow-up Audit on Recommendations for Controls Over Exporting  
Sensitive Technologies to Countries of Concern, Project No. D2006-  
D000LG-0199.000 (Draft of a Proposed Report dated March 12,  
2007)

As requested, I have reviewed the draft report. The draft report is generally well written. The findings germane to DDR&E are commendable. A few statements within the report contain errors, and while the errors do not lead to incorrect findings, the errors should be corrected to increase the overall accuracy and credibility of the report, its findings, and recommendations.

1. The Director, Defense Research and Engineering (DDR&E) has responsibility for two recommendations in Report D-2000-110 dated March 24, 2000. I do not repeat those recommendation. They appear on page 11 of the draft report.
  - a. The statement in the Issuance of Guidance section (page 11) "...the Defense Federal Acquisition Regulation Supplement (DFARS), together with DoDI 2040.2 will include these procedures." is not precisely correct. The DDR&E official should have said "...the pending DoDI 2040.2 will provide procedures and the pending Defense Federal Acquisition Regulation Supplement (DFARS) rule will provide specific contract clauses to use in particular circumstances."
  - b. The first sentence in the next paragraph should be changed. It says USD(AT&L) is responsible for finalizing DoDI 2040.2. That is incorrect. The last sentence in the same paragraph is correct. USD(P) is responsible for DoDI 2040.2. Change the first sentence to read "a DDR&E official told us that the USD(AT&L) is responsible for finalizing the DFARS rule and the USD(P) is responsible for finalizing DoDI 2040.2."
  - c. The statement in the Training Requirements for Defense Research Personnel section (pages 11 & 12) "...a DDR&E official informed

Revised

Revised

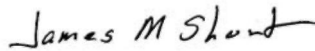
Revised



us that the training requirements for personnel at Defense research facilities are in a proposed revision of the DFARS and a draft revision of DoDI 2040.2” is not precisely correct. The DDR&E official should have enabled you to write “...a DDR&E official informed us that the training requirements for personnel at Defense research facilities are dependent upon the content yet to be published in a revision of the DFARS rule and a revision of DoDI 2040.2.”

- d. The last sentence in the next paragraph (page 12) should say “Further, DDR&E officials told us that the USD(AT&L) is responsible for finalizing the DFARS and USD(P) is responsible for finalizing DoDI 2040.2.”

If you require further information, please contact Jon Porter at 703-588-1415 or [jonathan.porter@osd.mil](mailto:jonathan.porter@osd.mil).



James M. Short  
Director, Defense Laboratory Programs

# Defense Technology Security Administration Comments

Final Report  
Reference



DEFENSE TECHNOLOGY SECURITY ADMINISTRATION  
2900 DEFENSE PENTAGON  
WASHINGTON, DC 20304-2900

APR 27 2007

Mr. Dennis L. Conway  
Program Director  
Readiness and Operations Support  
Office of the Inspector General  
Department of Defense  
400 Army Navy Drive  
Arlington, Virginia 22202

Dear Mr. Conway:

My staff has reviewed your draft report entitled: "Followup Audit on Recommendations for Controls Over Exporting Sensitive Technologies to Countries of Concern" (Project No. D2006-D000LG-0199.000). While I appreciate the effort your staff expended on this project, I am concerned that it does not accurately portray the actions DTSA has undertaken based upon your earlier findings. In fact, I am compelled to non-concur in several areas that we feel are inaccurate or misleading. The two recommendations I am referring to follow:

1. IG Recommendation: Documentation of Decisions on Export Applications

DTSA does not concur with the IG finding and recommendation. This non-concurrence is based upon the fact that the IG audit was based upon several erroneous assumptions:

First, the IG selected the Export Administration Regulation (EAR) as the standard for analysis. Though DTSA does not disagree that these are important policies to be confirmed prior to approval of a license, they are the responsibility of the Department of Commerce (DoC), not the DoD. EO 12981 grants DoD the authority to review any license received by the DoC and permits DoD to notify DoC of any application it does not wish to review. However, the EO prescribes no standard to be used by DoD to either request or defer review. It should therefore be assumed that the standard for analysis likewise rests with DoD, not DoC and its policies in the EAR. DTSA has provided copies of numerous standard operating procedures and identified policies which form the basis of DoD analysis. These, not the EAR standards, should be considered controlling in this case. For DoD to concentrate its review solely on the DoC policies would be both redundant and could indeed jeopardize review of DoD equities.

Second, when using the EAR as a standard for review, the auditors' findings state that the analysis and documentation were inadequate to justify the decision by DTSA to "approve" license applications. We believe this is incorrect on several levels. DTSA

Revised

**DTSA**   
Department of Defense

has no statutory or regulatory authority to approve or deny license applications, merely to recommend a course of action to the licensing department. More importantly, the EO requires that only recommendations to deny a license "include a statement of the reasons for such recommendation that are consistent with" the EAR. No such requirement exists for other recommendations. Finally, the EO further states that if no recommendation is received within 30 days of referral, the referral department will "be deemed to have no objection to the decision" by the Secretary of Commerce. Devoting resources to document analysis and recommendations that DoD has determined to have no national security implications would not be a prudent use DoD assets and could potentially jeopardize DoD's ability to provide the documentation and analysis required to stop exports of national security concern.

Third, despite many discussions, reviews, and instruction by the DTSA staff, we believe that the auditors did not fully take into account the extensive information that was available in the USXports database, the relationship between the requirements of the procedures in place and the entries made therein, nor the significance of the decision to the overall process. The procedures in place require that the analyst review the end user, the end use and the technology to determine if there are concerns raised by the application in these areas. At each level of review, whether by the "tiger team" on receipt or after staffing, the analyst is required to analyze these areas and determine if there is a national security concern generated by any of these elements of the prospective export using these guidelines. The releasing official is certifying, in the case of a recommendation of approval, that no national security concern exists or, in the case of an approval with conditions, that these concerns have been adequately addressed in the conditions. Ergo, the entire case, the procedural requirements and final determination constitute the documentation that these issues have been addressed. The auditors seem to require that a "checklist" or other summary, redundantly documenting these requirements were met, be appended to each case record. The IG comments included a recommendation that reference to a precedent case in the USXports database, by case number, was insufficient documentation to support its use as a precedent, but rather the entire case would have to be copied into the case at the tool bar. The cost in analysis' time and resources would be extraordinary and would probably not be considered a wise use of resources, unsupported by risk involved.

Given the facts above, DTSA will take no further action on this recommendation.

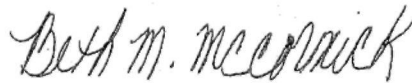
2. Recommendation: Implementation of prior recommendations in 2040.2

DTSA does not concur with the IG finding and recommendation. This non-concurrence is based upon the fact that the IG audit did not take into account the steps taken by DTSA in incorporating their prior suggestions.

Revised

DTSA personnel have on many occasions explained and demonstrated to the Audit team that their recommendations are incorporated into the revised version of 2040.2 that has been in the staffing process for many months and is now approaching approval. Unfortunately, as my staff explained to the IG team, 2040.2 cannot be finalized until the coordination process is complete.

My point of contact for IG matters is Dr. Peter Leitner, [peter.leitner@osd.mil](mailto:peter.leitner@osd.mil), or 703-325-4080.



Beth M. McCormick  
Director (Acting),  
Defense Technology  
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## **Team Members**

The Department of Defense Office of the Deputy Inspector General for Auditing, Readiness and Operations Support prepared this report. Personnel of the Department of Defense Office of Inspector General who contributed to the report are listed below.

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# Inspector General Department of Defense

