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Description of document: Thirteen (13) Department of Commerce (DOC) Inspector General (OIG) Reports, 1997-2007 Requested date: 25-May-2016 Released date: 18-July-2016 Posted date: 07-November-2016 Source of document: FOIA Officer Office of Inspector General U.S. Department of Commerce 1401 Constitution Avenue, N.W. Room 7898C Washington, DC 20230 202.501.7335 Fax: Email: FOIA@oig.doc.gov FOIAonline (account required).

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UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Washington, D.C. 20230

July 18, 2016

# RE: FOIA Request No. DOC-OIG-2016-001211

This letter is to regarding your Freedom of Information Act (FOIA) request, tracking number DOC-OIG-2016-001211, dated May 25, 2016 and received by the Department of Commerce, Office of Inspector General (OIG) on May 26, 2016, in which you seek, as modified June 2, 2016 and June 23, 2016, copies of nine (9) named OIG reports. On June 7, 2016, you indicated that the OIG should initially proceed with processing only those documents that could be searched for and retrieved after two (2) hours of search time.

A search of records maintained by the OIG has located, within the two hours of search time, six (6) reports consisting of 125 pages that are responsive to your request. In this interim response, we are providing copies of the following four (4) reports consisting of fifty-five (55) pages:

- The Census Bureau Should Redefine Its National-Critical Systems (OSE-16519-2)
- Federal Audit Clearinghouse Reimbursable Agreements (ATL-18113-7-0001)
- Audits Divisions of Business and Trade, Science and Technology, and Economics and Statistics, Internal Quality Control Review (DEN-15928-3-0001)
- Seattle Regional Office of Audits, Internal Quality Review (DEN-15928-3-0004)

We did not locate copies of the following three (3) reports within the two hours of search time:

- Financial Statements Audit Division, Internal Quality Review (DEN-15928-3-0002)
- Denver Regional Office of Audits, Internal Quality Review (HQA-15928-3-0005)
- Atlanta Regional Office of Audits, Internal Quality Review (DEN-15928-3-0003)

We will not continue searching for these documents absent an agreement to pay estimated fees.

As for this interim response, we have reviewed 55 pages under the terms of FOIA and, after consulting with the U.S. Census Bureau over the release of certain of them, have determined that they may be released as follows:

- 49 pages may be released to you in full;
- Two (2) pages have been partially withheld under FOIA exemption (b)(5), 5 U.S.C. § 552(b)(5), which protects inter-agency and intra-agency records that would not be

available by law to a party other than an agency in litigation with the agency, including documents that are predecisional and deliberative in nature; and

• Four (4) pages must be partially withheld under FOIA exemption (b)(6), 5 U.S.C. § 552(b)(6), which protects information in personnel, medical or similar files, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Copies of the 55 pages are enclosed with the relevant withholdings noted. Responses on the release of the remaining documents are forthcoming.

For your information, Congress excluded three discrete categories of law enforcement and national security records from the requirements of FOIA. See 5 U.S.C. § 552(c) (2012 & Supp. III 2015). This response is limited to those records that are subject to the requirements of FOIA. This is a standard notification to all OIG requesters and should not be taken as an indication that excluded records do, or do not, exist.

You have the right to appeal this partial denial of your request. An appeal must be received within thirty (30) calendar days of the date of this response letter by the Counsel to the Inspector General, U.S. Department of Commerce, Office of Inspector General, Office of Counsel, Room 7898C, 14th and Constitution Avenue, N.W., Washington, D.C. 20230. Your appeal may also be sent by e-mail to FOIA@oig.doc.gov, by facsimile (fax) to 202-501-7335, or by FOIAonline, if you have an account in FOIAonline, at

https://foiaonline.regulations.gov/foia/action/public/home#.

The appeal should include a copy of the original request and this initial denial letter. In addition, the appeal should include a statement of the reasons why the records requested should be made available and why the adverse determination was in error. The appeal letter, the envelope, the email subject line, and the fax cover sheet should be clearly marked "Freedom of Information Act Appeal." The e-mail, fax machine, FOIAonline, and Office of Counsel mailbox are monitored only on working days during normal business hours (8:30 a.m. to 5:00 p.m., Eastern Time, Monday through Friday). FOIA appeals posted to the e-mail box, fax machine, FOIA online, or the Office of Counsel mailbox after normal business hours will be deemed received on the next normal business day. If the 30<sup>th</sup> calendar day falls on a Saturday, Sunday, or legal public holiday, an appeal received by 5:00 p.m., Eastern Time, the next business day will be deemed timely. An appeal received after the 30-day limit will not be considered.

If you have any questions, please contact me via email at FOIA@oig.doc.gov, or by phone at (202) 482-5992.

Sincerely,

Raman Santra FOIA Officer

Enclosures



UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Washington, D.C. 20230

OCT 6 2004

Ms. Kristy LaLonde Executive Office of the President Office Of Management And Budget Washington, D.C. 20503

Dear Ms. LaLonde:

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This letter transmits our final inspection report, *The Census Bureau Should Redefine Its National Critical Systems*, OSE-16519-2, July 2004. Please be advised that the report is not a public document and is being provided to OMB as a routine, intra-governmental transfer of information outside of the provisions of the Freedom of Information Act. This report is for official use only. It discusses security vulnerabilities and should be protected from unauthorized release. It also may contain information, which must be withheld under exemption (b)(2) of the Freedom of Information Act in order to prevent circumvention of a statute or agency regulation. Its release should not therefore be construed as a public release. Accordingly, we request that none of the information contained in the report be released beyond OMB.

If you have any questions regarding the limitations placed on the use of this report, please call me at (202) 482-5643.

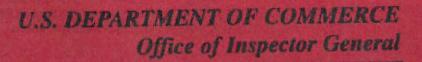
Sincerely,

Judith & Gordon

Judith J. Gordon Assistant Inspector General for Systems Evaluation

cc: Daniel Costello, OMB

Enclosure





# BUREAU OF THE CENSUS

The Census Bureau Should Redefine Its National-Critical Systems

Final Inspection Report No. OSE-16519-2

This report is for official use only 1t discusses security vulnerabilities and should be protected from unauthorized release. It also may contain information, which must be withheld under exemption (b)(2) of the Freedom of Information Act in order to prevent circumvention of a statute or agency regulation. Therefore, any requests for this report must be directed to the Office of Inspector General

Office of Systems Evaluation

Copy\_12



UNITED STATES DEPARTMENT OF COMMERCE The Inspector General Washington, D.C. 20230

# JUL 30 2004

MEMORANDUM FOR:

Charles Louis Kincannon Director U.S. Census Bureau

FROM:

Johnnie E. H

SUBJECT:

The Census Bureau Should Redefine Its National-Critical Systems Final Inspection Report No. OSE-16519-2

The Federal Information Security Management Act (FISMA)<sup>1</sup> requires agencies to review their information security program annually and Offices of Inspector General (OIGs) to perform independent evaluations of those programs annually as well. Pursuant to FISMA, we evaluated the Census Bureau's information technology (IT) security program and detailed our results in a draft inspection report entitled *Weaknesses in Census Bureau's Certification and Accreditation Process Leave Security of Critical Information Systems in Question.*<sup>2</sup> We are presenting our findings for one of our evaluation objectives separately, in this limited distribution report, because they address the bureau's two highly sensitive national-critical systems—Economic National Critical Processes and Demographic National Critical Systems. That objective was to assess the bureau's consolidation of IT systems to determine whether these systems (and the data they produce) are secure and appropriately certified and accredited.

The bureau's national-critical systems are part of the federal government's critical infrastructure and must therefore be protected from terrorist attacks. The goal is to ensure that any physical or virtual disruption is rare, brief, geographically limited in effect, manageable, and minimally detrimental to the economy, human and government services, and national security of the United States.<sup>3</sup> Under Executive Order 12656, "Assignment of Emergency Preparedness Responsibilities," the Secretary of Commerce is responsible for providing for the collection and reporting of census information on human and economic resources as required for national security emergencies.

FOR OFFICIAL USE ONLY

<sup>&</sup>lt;sup>3</sup> Critical Infrastructure Act of 2001, 42 U.S.C. 5195c, which is part of the USA Patriot Act of 2001 (P.L. 107-56).



<sup>&</sup>lt;sup>1</sup> Title III, E-Government Act of 2002 (P.L. 107-347).

<sup>&</sup>lt;sup>2</sup> Weaknesses in Census Bureau's Certification and Accreditation Process Leave Security of Critical Information Systems in Question, Draft Inspection Report No. OSE-16519, July 2004.

As this report details, we found the following:

- 1. In the event of a terrorist attack or other national security emergency, the Census Bureau's national-critical systems—as currently defined—may not have the capability to perform required processing. Furthermore, national-critical systems maintained by Commerce's Bureau of Economic Analysis (BEA) and the Department of Labor's Bureau of Labor Statistics (BLS) rely on Census Bureau systems that have not been deemed national critical. Not designating as national critical systems needed in an emergency and on which other agencies' national-critical systems depend reduces management's ability to ensure that these systems have adequate security controls. It also disregards the intent of Homeland Security Presidential Directive 7 (HSPD-7), which requires federal agencies to, among other things, coordinate the protection of critical infrastructure and key resources in order to "prevent, deter, and mitigate the effects of deliberate efforts to destroy, incapacitate, or exploit them."
- 2. The bureau has not designated its national-critical systems as having the highest sensitivity for purposes of certification and accreditation<sup>4</sup> and thus does not test their security controls as rigorously as the Department's IT security policy requires for its most sensitive but unclassified systems.

# Discussion of Census Bureau's Response to the Draft Report

In the written response to our draft report, you state that you generally agree with the results of our review and discuss our two recommendations. Our first recommendation is that the bureau review the functions required of its national-critical systems, identify all interrelationships with national-critical resources in other agencies, and redefine these systems to encompass all needed processing resources. You indicate that you will establish a formal working group to review the bureau's critical infrastructure plan and those of the other agencies the bureau supports. The review is to include a reassessment of the internal processes needed to support national-critical systems and the criticality of the programs supported by these systems. Recommendations will be made to the Census Bureau's Operating Committee by the end of the fiscal year. We agree that such a reassessment is appropriate.

Noting that the Department's IT security policy sets certification and accreditation levels from 1 to 4, with more rigorous testing required at each successive level, our second recommendation is to certify and accredit all national-critical systems at level 4. You state that you agree that all national-critical systems need to be certified and accredited against rigorous criteria and that you will certify and accredit any new system or process identified as national critical by your reassessment at the appropriate level. However, it is unclear from your response what you consider the appropriate level to be and whether all systems identified as national critical by the reassessment will be certified and accredited at level 4. Given the importance of national-critical systems and the mandate that any physical or virtual disruption must be rare, brief, and

<sup>&</sup>lt;sup>4</sup> Certification is the formal testing of the security safeguards implemented in a computer system to determine whether they meet applicable requirements and specifications. Accreditation is the formal authorization by management for system operation, including an explicit acceptance of risk.

manageable, we continue to believe that all national-critical systems should be certified and accredited at level 4, and therefore reaffirm our recommendation.

Your complete response is included as an attachment to this report. Please provide your action plan addressing the recommendations in our report within 60 calendar days. In addition to actions to reassess the bureau's national-critical systems, the plan should address the timeframes for choosing and implementing appropriate actions resulting from the reassessment, including actions pertaining to certifying and accrediting Census's national-critical systems. Your action plan should be in the form of a plan of action and milestones (POA&M) to facilitate tracking of corrective actions in accordance with the Office of Management and Budget's FISMA guidance. If you have any questions regarding the report or the requested action plan, please contact me on (202) 482-4661 or Judith Gordon, Assistant Inspector General for Systems Evaluation on (202) 482-5643.

# INTRODUCTION

Several mandates require the Census Bureau to ensure its critical infrastructure assets, including systems that provide specific data collection and reporting capabilities, are available in the event of a national security emergency. HSPD-7, "Critical Infrastructure Identification, Prioritization, and Protection," dated December 17, 2003, states that all federal department heads are responsible for identifying, prioritizing, assessing, remediating, and protecting their respective internal critical infrastructure and key resources. It further requires agencies to provide information security protections for their critical infrastructures that are consistent with FISMA and commensurate with the risk and magnitude of harm that would result from the unauthorized access, use, disclosure, disruption, modification, or destruction of information. HSPD-7 defines critical infrastructure as "systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems and assets would have a debilitating impact on security, national

economic security, national public health or safety, or any combination of those matters."<sup>5</sup> Executive Order 12656, "Assignment of Emergency Preparedness Responsibilities," dated November 18, 1988, charges the Secretary of Commerce with providing for the collection and reporting of census information on human and economic resources and maintaining a capability to conduct emergency surveys to report on the status of these resources as required for national security emergencies.

According to the bureau, at the end of calendar year 2002, it reexamined its IT inventory and determined that—based on the overall mission, organizational structure, and responsibilities of individual directorates—this inventory was not reflective of operations. Census's IT Security Office therefore worked with contractors, system owners, and administrators to reorganize and consolidate the bureau's 87 systems. Grouping systems according to shared missions, ownership, and management yielded 11 program area systems, each having an associated set of component

<sup>&</sup>lt;sup>5</sup> HSPD-7 states that the term "critical infrastructure" has the meaning given to that term in section 1016(e) of the USA Patriot Act of 2001.

systems. Of those 11 systems, the bureau designated 2 as national critical, 7 as mission critical, and 2 as business essential.<sup>6</sup>

The bureau developed security plans for each of the 11 program area systems, as well as the component systems. The program area security plans are intended to document the management, operational, and technical controls that apply to *all* component systems, whereas the security plans for the individual component systems are to describe controls specific to each component.

# **OBJECTIVES, SCOPE, AND METHODOLOGY**

We conducted a review to evaluate (1) the Census Bureau's information technology (IT) security program policy, (2) the impact of its IT systems consolidation on the integrity of those systems and the certification and accreditation process, (3) its plan to provide specialized IT security training to IT security officers and IT staff, (4) management and implementation of the plan of action and milestones (POA&M) process for program and system level weaknesses,<sup>7</sup> (5) the patch management process for correcting system security vulnerabilities, and (6) the bureau's incorporation of IT security into its capital planning and investment control process. This report presents the findings regarding our second objective, IT systems consolidation. We used HSPD-7, USA Patriot Act of 2001, Executive Order 12656, and FISMA as our criteria for addressing this objective.

We conducted our evaluation in accordance with the Quality Standards for Inspections issued by the President's Council on Integrity and Efficiency and under the authority of the Inspector General Act of 1978, as amended. We performed our fieldwork between November 2003 and April 2004.

### THE BUREAU'S NATIONAL-CRITICAL SYSTEMS COULD LACK CAPABILITIES NEEDED FOR PROCESSING IN AN EMERGENCY AND FOR FULLY SUPPORTING OTHER AGENCIES' NATIONAL-CRITICAL SYSTEMS

As part of their responsibilities for conducting the economic and demographic statistical programs of the bureau, the Office of the Associate Director for Economic Programs and the Office of the Associate Director for Demographic Programs have management, operational, and budgetary authority over the IT systems used to support these programs. Thus, in accordance with FISMA and Department policy, senior officials in these offices are responsible for ensuring the security of these systems. The Office of the Associate Director for Information Technology is to assist them in carrying out their IT security responsibilities. In consolidating its systems, the bureau designated two economic and demographic systems as national critical—Economic National

<sup>&</sup>lt;sup>6</sup> According to OMB, an infrastructure or resource is considered mission critical if its damage or destruction would have a debilitating impact on the organization's ability to perform essential functions and activities. All systems that are not mission critical or national critical are considered business essential.

<sup>&</sup>lt;sup>7</sup> According to OMB, POA&Ms must reflect all known security weaknesses within an agency including its components or bureaus and shall be used by the agency, major components and program officials, and the IG as the authoritative agency management mechanism to prioritize, track, and manage all agency efforts to close security performance gaps.

Critical Processes (CEN09) and Demographic National Critical Systems (CEN10). (See table 1 for a listing of the systems discussed in this report, along with their identifiers and criticality.)

| System<br>Identifier* | System Name   | Criticality          |
|-----------------------|---|----------------------|
|                       | Census Bureau   |                      |
| CEN01                 | IT Infrastructure   | Mission Critical     |
| CEN03                 | Economic Census and Surveys and<br>Special Processing                                 | Mission Critical     |
| CEN06                 | National Processing Center  | Mission Critical     |
| CEN09                 | Economic National Critical Processes  | National Critical    |
| CEN10                 | Demographic National Critical<br>Systems  | National Critical    |
| CEN11                 | Demographic Census, Surveys and<br>Special Processing                                 | Mission Critical     |
|                       | Bureau of Economic Analysis   |                      |
| BEA016                | National Economic Accounts  | National Critical    |
|                       | dentifier is a unique number assigned by the oper agement and capital asset planning. | ating unit's CIO for |

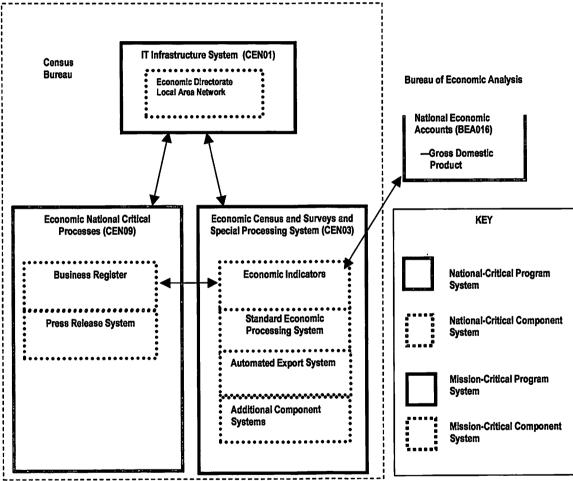
Table 1. Systems Discussed in This Report

However, the bureau defined the two national-critical systems very narrowly—as a set of computing resources incapable of performing all of the processing required in an emergency without relying on other bureau systems that are not deemed national critical. Additionally, CEN09 provides the primary data used by BEA to produce the gross domestic product (GDP), a principal economic indicator. Although the GDP and the system BEA uses to produce it, National Economic Accounts, are national critical. CEN10 provides essential data used by BLS to produce principal economic indicators on the labor force, employment, and unemployment, classified by a variety of demographic, social, and economic characteristics. Derived from the Current Population Survey (CPS), a monthly survey conducted by the bureau for BLS, these indicators and the system BLS uses for developing them are considered national critical. Like BEA, BLS must heavily rely on bureau systems not deemed national critical.

The relationship among the systems needed to conduct economic surveys is illustrated in figure 1. CEN09 includes a component system, the Business Register, that contains information about domestic companies and the goods and services they provide. The Economic Indicators component system of the Economic Census and Surveys and Special Processing System, CEN03, both provides input to the Business Register and uses Register information to generate data that

BEA's National Economic Accounts system uses in developing the GDP. As noted previously and shown in figure 1, CEN09 and BEA's system are both national critical. However, CEN03 has been designated only mission critical, even though this system processes data from the Business Register to produce economic survey results for Census and information for BEA's national-critical system. Furthermore, the Economic Directorate Local Area Network, which supports CEN09 and CEN03, is a component of CEN01, the IT Infrastructure system, which has not been designated as national critical either.

Figure 1. National Critical and Related Systems for Producing Principal Economic Indicators



In addition to what is shown in figure 1, component systems of the National Processing Center (CEN06) also support CEN09 and are needed to perform economic surveys and processing. Like CEN03 and CEN01, CEN06 is designated as mission critical, not national critical. Similarly, Demographic National Critical Systems, CEN10, as well as BLS, depend on processing resources in CEN11, CEN01, and CEN06—all mission-critical systems.

The rationale provided by bureau officials for the definition of national-critical systems was that the scheduled economic indicators and demographic surveys could be discontinued for a short period of time if an event occurred, but the event's economic or demographic impacts may have to be assessed. They maintained that the needed data for such assessments reside in the components designated as national critical, and any additional processing resources required for analyzing and transmitting the data could be recreated if they were not available. However, given the executive order's requirement to maintain the capability to collect as well as analyze data in an emergency and the dependence of other agencies' national-critical systems on bureau systems, a more comprehensive definition of the bureau's economic and demographic computing resources is needed. Not designating as national critical computing resources needed in an emergency and on which other agencies' national-critical systems depend reduces management's ability to ensure that these resources have adequate security controls and disregards the intent of HSPD-7, which states, "Federal departments and agencies will identify, prioritize, and coordinate the protection of critical infrastructure and key resources in order to prevent, deter, and mitigate the effects of deliberate efforts to destroy, incapacitate, or exploit them."

HSPD-7 requires the Department to develop and submit for OMB approval, plans for protecting its physical and cyber-critical infrastructure by July 31, 2004. The Department CIO will prepare this plan using input from the operating units. To ensure that the bureau's national-critical resources are appropriately identified in the plan and adequately protected, the functions the bureau's national-critical systems may have to perform in an emergency should be reviewed, all interrelationships with national-critical resources in other agencies identified, and these systems redefined to encompass all needed processing resources.

### **Recommendation**

The director of the Census Bureau should ensure that the associate director for economic programs and the associate director for demographic programs, with support from the bureau's CIO, review the functions required of the bureau's national-critical systems, identify all interrelationships with national-critical resources in other agencies, and redefine these systems to encompass all needed processing resources.

### CERTIFICATION AND ACCREDITATION LEVELS FOR NATIONAL-CRITICAL SYSTEMS ARE NOT COMMENSURATE WITH THEIR SENSITIVITY

FISMA sets three security objectives for information and information systems: *confidentiality*, *integrity*, and *availability*. System owners must assign a sensitivity level of high, medium, or low to each objective to reflect the impact on the agency's mission that would result if the information or system were compromised. The sensitivity assignments are used to establish the system's security controls and provide the basis for determining its certification and accreditation level; this level, in turn, dictates the rigor of certification testing. The Department's IT security policy sets certification and accreditation levels from 1 to 4, with more rigorous testing required at each successive level.

Although all of the bureau systems discussed in this report—CEN01, CEN03, CEN06, CEN09, CEN10, and CEN11—were designated "high" for confidentiality, integrity, and availability, CEN01 was certified and accredited at level 3 and the remaining systems, including those that are national critical, were certified and accredited at level 2. Given the importance of the bureau's national-critical systems and the mandate that any physical or virtual disruption must be rare, brief, and manageable, these systems should be designated as level 4 for certification and accreditation purposes to ensure their security controls receive the most rigorous testing. Census Bureau systems used to produce principal economic indicators have significant commercial value, may affect the movement of commodity and financial markets, may be taken as a measure of the impact of government policies, and many indicators are based on confidential data voluntarily provided by businesses, which also must be protected. Thus, even if the systems used to produce the indicators were not national critical, they would still need to be subjected to thorough testing.

### **Recommendation**

The director of the Census Bureau should ensure that the associate director for economic programs and the associate director for demographic programs, with support from the bureau's CIO, certify and accredit all national-critical systems at level 4.

### Attachment

cc: Kathleen B. Cooper, Under Secretary for Economic Affairs Hermann Habermann, Deputy Director and Chief Operating Officer, U.S. Census Bureau Nancy M. Gordon, Associate Director for Demographic Programs, U.S. Census Bureau Frederick T. Knickerbocker, Associate Director for Economic Programs, U.S. Census Bureau Richard W. Swartz, Associate Director for Information Technology and Chief Information Officer, U.S. Census Bureau Timothy P. Ruland, Information Technology Security Officer, U.S. Census Bureau Thomas N. Pyke, Jr., Chief Information Officer, U.S. Department of Commerce Otto J. Wolff, Chief Financial Officer and Assistant Secretary for Administration, U.S. Department of Commerce



ATTACHMENT

UNITED STATES DEPARTMENT OF COMMERCE Economics and Statistics Administration U.S. Census Bureau Washington, DC 20233-0001 OFFICE OF THE DIRECTOR

# JUL 28 2004

#### MEMORANDUM FOR:

Judith J. Gordon Assistant Inspector General for Systems Evaluation

Through:

afflee & loge iic Affairs Muncaun Kathleen B. Cooper Under Secretary for Economi

Charles Louis Kincannon Director

Subject:

From:

The Census Bureau Should Redefine Its National-Critical Systems, Draft Inspection Report No. OSE-16519-2

This is in response to your memorandum of July 12, 2004, transmitting the above-referenced audit report. We appreciate the efforts of the Department of Commerce's Office of Inspector General staff in conducting this review and generally agree with their results. We address the recommendations in the report as follows:

**Recommendation 1:** The Director of the Census Bureau should ensure that the Associate Director for Economic Programs and the Associate Director for Demographic Programs. with support from the Bureau's CIO, review the functions required of the Bureau's national-critical systems, identify all interrelationships with national-critical resources in other agencies, and redefine these systems to encompass all needed processing resources.

Census Bureau Response: The U.S. Census Bureau will establish a formal working group, chaired by the Chief, Information Technology (IT) Security Office, and consisting of members from the economic, demographic, IT, and field directorates. The working group will identify internal processes needed to support our national-critical systems, establish a central repository of all support provided to other agencies in the IT Security Office and identify the criticality of these programs as reported in the Census Bureau Critical Infrastructure Plan (CIP), as well as those of the supported agencies to ensure consistency. The working group will present their recommendations to the Census Bureau's Operating Committee for consideration.

The Census Bureau has already begun work on the first phase of this effort. A memorandum from the Chief, IT Security Office, to the CIO, dated July 6, 2004, identified the requirements of HSPD-7 and recommended that based on the information gained during your inspection, the Census Bureau must re-evaluate our CIP to address the recommendation. This correspondence was shared with the associate directors for the economic and demographic areas, as well as key management officials within the IT directorate.

www.census.gov

The Census Bureau takes the security of the data collected very seriously. Internal processes and procedures are continually reviewed to ensure that the appropriate levels of control needed to meet the growing security challenges are in place. Due to the complexity of our network infrastructure and the number of other agencies supported by the Census Bureau data collection efforts, it will take until the end of the fiscal year before the working group can present their recommendations to the Census Bureau Operating Committee. The Census Bureau Operating Committee will then begin to determine the impact of implementing the results of the findings as phase two of this process.

**Recommendation 2:** The Director of the Census Bureau should ensure that the Associate Director for Economic Programs and the Associate Director for Demographic Programs, with support from the Bureau's CIO, certify and accredit all national-critical systems at level 4.

**Census Bureau Response:** The Census Bureau agrees that all national-critical systems need to be certified and accredited against rigorous criteria. Any new system or process identified as national-critical, following the review cited in the first recommendation, will be certified and accredited at the appropriate level.

cc: US/EA



U.S. DEPARTMENT OF COMMERCE Office of Inspector General



# U.S. CENSUS BUREAU

# Federal Audit Clearinghouse Reimbursable Agreements

Final Audit Report No. ATL-18113-7-0001/September 2007

Office of Audits, Atlanta Regional Office





SEP 1 3 2007

MEMORANDUM FOR:

Stephanie H. Brown, Chief, Governments Division U. S. Census Bureau

John M Leelen

FROM:

John M. Seeba Assistant Inspector General for Auditing

SUBJECT:

Federal Audit Clearinghouse Reimbursable Agreements Final Audit Report No. ATL-18113-7-0001

This report informs Census officials of the results of our audit of the reimbursable agreements that provided the funding for the Federal Audit Clearinghouse for the period October 1, 2002, through September 30, 2006. Our audit disclosed that the project managers generally did a good job matching the Clearinghouse spending authorities to expenditures; however, improvements are needed to the way that the project is funded, as funding uncertainties are jeopardizing the Clearinghouse's ability to fulfill its mission. We recommend that Census ensure that only charges allocable to the Clearinghouse are charged to that project and that personnel who work on the Clearinghouse project do not inappropriately charge their time to other Census projects. We also recommend that Census officials along with OMB, the President's Council on Integrity and Efficiency, the Chief Financial Officers Council, and the federal funding agencies that rely upon the Clearinghouse database should continue their efforts to develop a budget that fully funds the work the Clearinghouse is required to do and eliminates the current backlog as soon as possible. Additionally, we recommend that Census work with OMB to improve or replace the current reimbursable funding mechanism. A much more efficient and timely process is needed to ensure that the Clearinghouse knows in advance of the start of the fiscal year its approved funding level. Further, a new process is needed to facilitate the transfer of approved funds to the Clearinghouse at the beginning of the fiscal year.

We are providing Census officials with a copy of the final report which incorporates its requested changes to the draft and includes the complete version of the Bureau's response to the draft report as an attachment. We are also providing a copy of the final report to OMB, the PCIE, the CFO Council and the single audit coordinators of each federal agency that participates in and funds the Clearinghouse.

If you would like to discuss this report or its contents, please do not hesitate to contact Kathleen McKevitt, Regional Inspector General for Audits, at (404) 730-2063 or Belinda Riley, Assistant Regional Inspector General for Audits, at (404) 730-2067. We appreciate the cooperation and courtesies extended to us by Census officials during our audit.

# INTRODUCTION

The Single Audit Act of 1984<sup>1</sup> established uniform entity-wide audit requirements for state and local governments and non-profit organizations receiving federal financial assistance. In 1996, Congress amended the act<sup>2</sup> to streamline and improve its effectiveness. Reports required under the act provide valuable information on how federal dollars are spent and whether the funds are spent in accordance with applicable laws, and regulations. In FY 2006, approximately \$1 trillion in federal expenditures were included in single audit reports sent to the Clearinghouse.<sup>3</sup> All entities expending \$500,000 or more in federal funds are required to have an annual single audit.

The Federal Audit Clearinghouse is the repository for all single audit reports. Staff at the Clearinghouse is responsible for incorporating information about each auditee, its federal awards, and audit results into a government-wide database available to the public. Clearinghouse management and programming staff are part of the Census Bureau's Governments Division located in Suitland, Maryland. Reports are processed at a Census Bureau facility in Jeffersonville, Indiana, and are made available to users through the Clearinghouse's website, <u>http://harvester.census.gov/sac/</u>.

The Clearinghouse receives between 30,000 and 40,000 reports annually for processing. Some reports are submitted in both paper and electronic formats, while others are submitted only in paper form. The Clearinghouse's database goes back to 1997 and is accessible at its website. This web-based system allows the public access to audit findings in most federal grant programs operating in the U.S. and also provides government managers with information that can be used to identify major flaws in a program's administration.

"The Single Audit Act was designed to ensure the integrity of the manner in which we choose to distribute hundreds of billions of Federal program dollars annually. It has as its basic requirement that if you receive Federal dollars, you should be audited on a regular basis. Today, there are thousands of audits conducted in every corner of this country that give us assurance that almost all Federal grant dollars receive some level of scrutiny. In fact, current data indicate that over 95 percent of Federal grant dollars are audited under the Single Audit Act. The American people deserve to know that their investment in the Federal government is not being squandered and that it is achieving its intended purpose."

Source: Statement of the Honorable Mark W. Everson, Controller, Office of Federal Financial Management, Office of Management and Budget, before the House Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations, June 26, 2002

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We performed this audit of the Clearinghouse's reimbursable agreements from June 2006 through March 2007. Onsite fieldwork took place at the bureau's offices in Maryland. The objectives of this review were to:

• Match the revenue received by the Clearinghouse with the costs of operations,

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• Determine whether the costs charged to the reimbursable agreement are reasonable, allowable, and allocable.

OIG has done previous audits of the Federal Audit Clearinghouse. At the request of OMB, our office previously performed two Agreed Upon Procedure reviews of the Clearinghouse's processing of single audit reports. For both fiscal years 1998 and 2002, our office found that the Clearinghouse processed single audit reports accurately and ensured that the data provided over the public website was reliable. In March 2005, the OIG Office of Audits' Financial Statements and Accountability Division issued Management Controls Over Reimbursable Agreements at the U.S. Census Bureau Need Improvement. Originally, the audit scope was to cover the period from October 1, 2003, through March 31, 2006. Once we began our work, we noticed the funding problems experienced by the Clearinghouse in recent years. Census officials requested we expand the audit to include fiscal year 2003 so we would be reviewing a year not plagued with funding issues. Additionally, we expanded the period to cover the review of Reimbursable Agreement authorities and signatures for the second half of 2006. We did not review expenditures for the second half of 2006.

We examined pertinent Census records, and

interviewed agency officials. We relied on computer-processed data and a computer download of project transactions supplied by the bureau as the basis for our audit findings and recommendations. We tested the accuracy of the data by tracing and comparing it to original source and other supporting documents. Based on our tests, we concluded that the computerized data was sufficiently reliable for use in meeting our objectives.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain significant appropriate evidence that provides 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.

# Management Oversight of the Clearinghouse Project is Generally Good, but Funding Problems Jeopardize the Clearinghouse's Ability to Achieve Its Mission

Our audit of the funding provided by the reimbursable agreements required us to match the revenue received by Census with the costs of operating the Clearinghouse. By matching the revenue with expenditures, we gained an understanding of the process for allocating costs to the reimbursable agreements, so we could determine whether the costs charged to each agreement were reasonable, allowable, and allocable.

Our review of the process for allocating expenditures to the reimbursable agreements disclosed that while Census officials generally did a good job of matching the Clearinghouse expenditures to the appropriate reimbursable agreements, there were a few instances where expenditures were not allocable to the project charged. It is possible that the funding problems which have plagued the Clearinghouse in recent years contributed to the examples of mischarging we found. Those funding uncertainties have created a backlog of approximately 36,000 unprocessed reports as of February 2007. Such a significant backlog diminishes grant-making agencies' ability to utilize the critical data required by the Single Audit Act for program management.

# Management Oversight on Allocating Project Costs Is Generally Good

The Census bureau is required by federal law<sup>4</sup>, regulation<sup>5</sup>, and Departmental policy<sup>6</sup> to achieve full cost recovery for work performed under certain agreements. Specifically, the Economy Act requires federal agencies to recover actual costs for work performed for other federal agencies. The Clearinghouse is expected to recover the costs of its operations from the federal agencies it services. To do this, it has entered into reimbursable agreements with those agencies. Over the four years our audit covers, the reimbursable agreements totaled: \$2.6 million in FY 2003, \$2.5 million in FY 2004, \$2.8 million in FY 2005, and \$3.6 million in FY 2006.

We reviewed the Reimbursable Project Management (RPM) report, which compares the agreement authority<sup>7</sup> with obligations, actual expenditures and any adjustments to a prior year obligation. This report tracks all expenditures to specific reimbursable projects.

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In addition, in fiscal year 2005, the Clearinghouse project manager and an analyst, who had both previously charged 100 percent of their time to the Clearinghouse, did not charge any time to that project for the months of July, August or September. Two other Clearinghouse analysts who had been 100 percent charged to the Clearinghouse project did not charge any of their time to the project for the month of September 2005. These employees would have had responsibilities requiring their attention on the Clearinghouse project during this time.

Census management told us that during the last three months of fiscal year 2005, these employees charged their time to an annual special project the Clearinghouse performs for the Department of Education. The funds for this project become available later in the fiscal year, at a time when funding for the Clearinghouse was running low.

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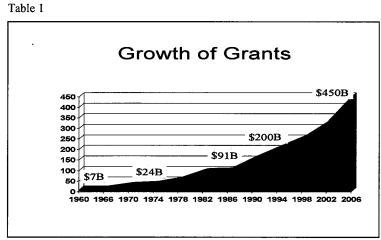
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### Inadequate Funding Jeopardizes the Clearinghouse's Ability to Provide Critical Data

The Clearinghouse provides essential information used by grant making agencies to manage more than \$450 billion in grants to states, local governments, universities and other non-profits as shown in Table 1.<sup>8</sup>



Beginning in FY 2004 through the end of our audit period, funds provided the Clearinghouse for processing single audit reports have not been sufficient to enable Clearinghouse staff to provide the services required by the statement of work (see Table 2) for all submitted reports. The funding shortages have resulted in a backlog of approximately 36,000 unprocessed single audit reports as of February 2007. A backlog of this size not only hinders federal managers from using the financial reports as a monitoring tool, as intended by the Single Audit Act, but could ultimately have an impact on the financial statements of the large grantor agencies.<sup>9</sup> We have been informed that the inspector general of one large grantor agency considered including a reportable condition in the agency's financial statements because, given the backlog at the Clearinghouse for its financial assistance awards. Another federal agency was told by their financial statement auditors that the backlog of unprocessed reports might result in a finding related to the agency's grants management system. While no agency has yet failed to receive a clean opinion on its financial statements as a result of this backlog, the longer it exists and the

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larger it gets, the more likely it is that one of the large grantor agencies' financial statements will be negatively affected.

#### Table 2

#### Services Provided by the Federal Audit Clearinghouse from FY 2003 through 2005

#### **Base Services**

- Processed, distributed, and archived single audit reports.
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- Maintained electronic database of Internet-accessible data collection forms.
- Handled inquires from auditees, auditors, federal agencies and general public concerning audit reporting requirements and use of database.

#### Additional Services Beginning in FY 2003

- The number of reports received by the Clearinghouse is not a constant. Reports received increased each year except 2005 when the threshold to perform a single audit was raised from \$300,000 to \$500,000.
- In 2003 and 2004, expanded standard reports available to web site users.
- OMB made changes to the data collection form to be used for FY 2004. This required new programming and testing. In addition, program maintenance is required for current and prior forms.
- In 2004, the Image Management System was launched. This is a web-based query system for federal agency authorized users to download full copies of single audit reports
- In 2005, Image Management System was expanded.

A further problem we noted was the way in which Census must obtain its reimbursable funding. In order to cover the costs of running the Clearinghouse, Census officials must execute reimbursable agreements with 16 different federal agencies. Obtaining and tracking multiple agencies' reimbursable agreements and budgets takes time that could better be spent on overall project management. Some of the problems noted by Census with managing multiple reimbursable agreements were:

- Reconciling contract language requirements between the legal counsels of Census and the 16 funding agencies.
- Identifying the correct agency contact persons.
- Negotiating 15 separate agreements for one federal agency instead of a single, MOU.
- Preparing 31 reimbursable agreements along with the supporting budgets.
- Tracking project costs to the 31 agreement authorizations. FY 2006 costs could not be allocated to the agencies until after March 2006 when the agreements were signed.
- Obtaining timely signed agreements. One agency did not sign the FY 2006 contract until year end so the money was not available until FY 2007.

We were informed by Census officials that prior to 2004, Census and OMB officials held regularly scheduled meetings to discuss workload requirements, programming enhancements, unexpected problems and priorities along with the funding requirements of the Clearinghouse. These meetings contributed to a cohesive operation with OMB's leadership, funding and regulatory commitment to single audit user needs and Census implementing the processes to accurately and efficiently process the single audit reports in a timely manner. Census officials would like to reinstate regular meetings with OMB to work jointly on meeting single audit user needs and ensure that both agree on project direction for available funding.

### Recommendations

We recommend that the Bureau's Government Division officials:

- Ensure that only charges allocable to the Clearinghouse project are charged to the project and that personnel who work on the Clearinghouse project are not inappropriately charged to other Census projects.
- Continue to work with OMB, the PCIE, the CFO Council, and the Single Audit Community to develop a budget that fully funds the work the Clearinghouse is required to do and eliminates the current backlog as soon as possible.
- Work with OMB to improve or replace the current reimbursable funding mechanism. A much more efficient and timely process is needed to ensure that the Clearinghouse knows in advance of the start of the fiscal year its approved funding level. Further, a new process is needed to facilitate the transfer of approved funds to the Clearinghouse at the beginning of the fiscal year.

## Bureau Response

In its August 16, 2007, response to the draft report, the Director of the U.S. Census Bureau and the Under Secretary for Economic Affairs stated that they were in agreement with the recommendations contained in the report. They noted that Clearinghouse staff is carefully examining monthly spending reports, increasing vigilance over this fiscal year's project charging, and instituting additional internal controls over project spending. Also, the report states that the Bureau will make every effort to work with OMB and other stakeholders to develop a budget that fully funds the Clearinghouse and eliminates the current backlog as quickly as possible and suggested that we add a recommendation focused on that issue. Finally they made editorial comments to the draft report.

# **OIG Comments**

We appreciate the Bureau's concurrence with the audit recommendations. We agreed with the Bureau's requested clarifications and its request for an additional recommendation and have modified the final report in the appropriate places to reflect those changes.

Attachment

Jay Waite - Deputy Director and Chief Operation Officer cc: Ted Johnson, Associate Direct for Administration and CFO Thomas Mesenbourg, Associate Director for Economic Programs Harvey Monk, Jr., Assistant Director for Economic Programs Andrew Moxam, Comptroller, Census Wesley Dias, Audit Liaison, Census Jill O'Brien, Project Manager, FAC, Federal Programs Branch, Census Clay Johnson III, Deputy Director for Management, Office of Management and Budget Linda Combs, Controller, Office of Federal Financial Management, Office of Management and Budget Carrie Hug, Chief Financial Standards & Grants, Office of Federal Financial Management, Office of Management and Budget Gil Tran, Technical Manager, Financial Standards & Grants, Office of Federal Financial Management, Office of Management and Budget Honorable John P. Higgins, Jr., Audit Committee Chair, President's Council on Integrity and Efficiency Danny Werfel, Chair, Chief Financial Officers Council John Fisher, Single Audit Coordinator, Department of Health and Human Services Hugh Monaghan, Single Audit Coordinator, Department of Education Marbie L. Baugh, Single Audit Coordinator, Department of Agriculture George Datto, Single Audit Coordinator, Department of Housing and Urban Development Robert Kaufman, Single Audit Coordinator, Department of Justice John Sysak, Single Audit Coordinator, Department of Transportation Zaunder Saucer, Single Audit Coordinator, Department of Labor Iris Hudson, Single Audit Coordinator, Department of Homeland Security Leah Nikaidoh, Single Audit Coordinator, Environmental Protection Agency Morgan Aronson, Single Audit Coordinator, Department of the Interior Janet Stem, Single Audit Coordinator, Department of Defense Deborah Cureton, Single Audit Coordinator, National Science Foundation Doug Gerry, Single Audit Coordinator, Corporation for National and **Community Service** John Lucas, Single Audit Coordinator, Department of Energy

Thelma Amos, Single Audit Coordinator, Department of Commerce John Pacious, Single Audit Coordinator, National Aeronautics and

Space Administration



UNITED STATES DEPARTMENT OF COMMERCE Economics and Statistics Administration U.S. Census Bureau Washington, DC 20233-0001

OFFICE OF THE DIRECTOR

ATTACHMENT 1 Page 1 of 10

# AUG 1 6 2007

#### MEMORANDUM FOR

John M. Seeba Assistant Inspector General for Auditing Office of the Inspector General

Through:

Cynthia A. Glassman CKU Under Secretary for Economic Affairs

From:

Charles Louis Kincannon Director

lil

Subject:

Federal Audit Clearinghouse Reimbursable Agreements Draft Report No. ATL-18113-7-0001

This is in response to the memorandum of July 9, 2007, to Ms. Stephanie H. Brown, Chief, Governments Division, requesting U.S. Census Bureau comments on the subject draft audit report for the Federal Audit Clearinghouse Reimbursable Agreements.

In response to the problems identified in the audit report associated with the Federal Audit Clearinghouse reimbursable project, we are in agreement with your recommendations. Our Clearinghouse staff is carefully examining monthly spending reports and increasing vigilance over this fiscal year's project charging, and we are instituting additional internal controls over project spending. We will make every effort to work with the Office of Management and Budget and other stakeholders to develop a budget that fully funds the Clearinghouse and eliminates the current backlog as quickly as possible.

Editorial comments are annotated in red within the attached draft audit report document. Please contact Adrienne Oneto at 301-763-1538 or Jill O'Brien at 301-763-1557 if you have further concerns.

Attachment

# BUREAU OF CENSUS

USE Either (U.S.) Bureau Of The Census or (U.S.) Census Bureau

# Federal Audit Clearinghouse Reimbursable Agreements

# Draft Audit Report No. ATL-18113-7-0001/July 2007

This is a draft report prepared by the Office of Audits, Office of Inspector General. It is made available for review and comment to the organizations responsible for the matter addressed. It contains preliminary conclusions, tentative recommendations and includes material subject to revision. This draft should be safeguarded against unauthorized use or premature release of what may be incomplete information. Questions should be referred to the appropriate OIG office.

Office of Audits, Atlanta Regional Office

#### **INTRODUCTION**

The Single Audit Act of 1984<sup>1</sup> established uniform entity-wide audit requirements for state and local governments receiving federal financial assistance. In 1996, Congress amended the act<sup>2</sup> to streamline and improve its effectiveness. Reports required under the act provide valuable information on how federal dollars are spent and whether the funds are spent in accordance with applicable laws, and regulations. In FY 2006, approximately \$1 trillion in federal expenditures were included in single audit reports sent to the Clearinghouse.<sup>3</sup> All entities expending \$500,000 or more in federal funds are required to have an annual single audit. <u>This paragraph should include a reference to "nonprofits" (state-locals already cited).</u>

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#### **Purpose and Scope of Audit**

We performed this audit of the Clearinghouse's reimbursable agreements from June 2006 through March 2007. Onsite fieldwork took place at the bureau's offices in Maryland. The objectives of this review were to:

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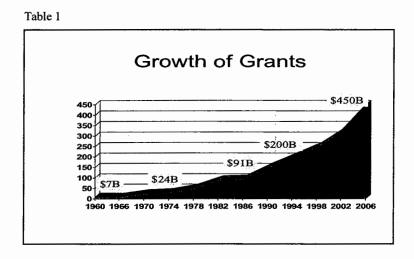
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#### Recommendations

We recommend that the Bureau's Government Division officials:

- Ensure that only charges allocable to the Clearinghouse project are charged to the project and that personnel who work on the Clearinghouse project are not inappropriately charged to other Census projects.
- Continue to work with OMB, the PCIE, the CFO Council, and the Single Audit Community to develop a budget that fully funds the work the Clearinghouse is required to do and eliminates the current backlog as soon as possible.
- ADD \*Work with OMB to improve or replace the current reimbursable funding mechanism. A much more efficient and timely process is needed to ensure that the Clearinghouse knows in advance of the start of the fiscal year its approved funding level. Further, a new process is needed to facilitate the transfer or approved funds to the Clearinghouse at the beginning of the fiscal year.





# U.S. DEPARTMENT OF COMMERCE Office of Inspector General

Room 7099C, HCHB 1401 Constitution Avenue, N.W. Washington, D.C. 20230

> Internet Web Site: www.oig.doc.gov



UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Office of Audits ATLANTA REGIONAL OFFICE 401 W. Peachtree St., N.W. - Suite 2742 Atlanta, Georgia 30308 (404) 730-2780 FAX: (404) 730-2788

August 11, 2003

MEMORANDUM FOR:

Michael Sears Assistant Inspector General for Auditing

2. MNON

THROUGH:

Larry B. Gross Deputy Assistant Inspector General for Auditing

Deputy Assistant Inspector General for Regional Audits

SUBJECT:

FROM:

Business and Trade Audits Division Economics and Statistics Audits Division Science and Technology Audits Division Internal Quality Control Review Final Audit Report No. DEN-15928-3-0001

I am pleased to transmit the final report for the Internal Quality Review (IQR) of the Business and Trade Audits Division (BTD), the Economics and Statistics Audits Division (ESD), and the Science and Technology Audits Division (STD). The IQR scope was to review each division's compliance with the Government Audit Standards and Office of Inspector General Directives Manual. We found no material non-compliance with the Government Audit Standards or OIG Directives; however, there were three issues requiring additional attention in order to fully comply with OIG Directives.

We noted that one final report issued by ESD did not contain independence declarations for all staff that assisted on the audit, as required by the OIG Directives. In addition, we noted two final reports did not fully comply with OIG Directives regarding referencing substantive changes to audit reports. The agency responses and OIG comments were not referenced for seven others. We also noted that two non-audit report work products were incorrectly classified as audit reports in the Semiannual Report to Congress. We recommended that BTD, ESD, and STD adhere to OIG policies regarding documenting staff independence, and referencing of substantive changes to audit reports. We further recommended that the Office of Audits either exclude non-audit report products from the Semiannual Report or include them in a separate table.

In response to the draft report, the Deputy Assistant Inspector General for Auditing concurred with the recommendations, and provided a responsive action plan.

The draft audit report also contained a finding related to a report issued by BTD for which summaries and schedules were not cross-indexed to the supporting working papers. BTD staff provided documentation indicating that the required cross-indexing had, in fact, been performed. We, therefore, withdrew that draft audit report finding and recommendation.

Attachment

cc (w/att): Johnnie E. Frazier, Inspector General Edward Blansitt, Deputy Inspector General Chuck Tegeler, Director, Economics and Statistics Audits Division Ron Lieberman, Director, Science and Technology Audits Division

# BUSINESS AND TRADE AUDITS DIVISION ECONOMICS AND STATISTICS AUDITS DIVISION SCIENCE AND TECHNOLOGY AUDITS DIVISION INTERNAL QUALITY REVIEW DRAFT REPORT NO. DEN-15928-3-0001

# INTRODUCTION

We have reviewed the system of quality control for the audit function of the Business and Trade Audits Division (BTD), the Economics and Statistics Audits Division (ESD), and the Science and Technology Audits Division (STD) in effect for the three years ended March 31, 2003. We conducted our review in conformity with standards and guidelines established by the President's Council on Integrity and Efficiency (PCIE). We tested compliance with each of the three divisions' system of quality control to the extent we considered appropriate. These tests included a review of audits identified in attachment 1.

In performing our review, we have given consideration to the policy statement on quality control and external reviews dated February 2002 issued by the PCIE. That statement indicates that an OIG's quality control policies and procedures should be appropriately comprehensive and suitably designed to provide reasonable assurance that the objectives of quality control will be met. It also recognizes that the nature, extent and formality of an OIG's system of quality control depends on various factors such as the size of the OIG, the location of its offices, the nature of the work and its organizational structure.

In our opinion, the system of quality control for the audit function of the BTD, ESD and STD in effect for the three years ended March 31, 2003, has been designed in accordance with the quality standards established by the PCIE and was being complied with for the year then ended to provide the OIG with reasonable assurance of material compliance with professional auditing standards in the conduct of its audits. Therefore, we are issuing an unqualified opinion on the BTD, ESD and STD systems' of audit quality control.

# PURPOSE, SCOPE AND METHODOLOGY

We tested compliance with the BTD, ESD and STD systems' of quality control to the extent we considered appropriate. These tests included a review of a sample of audits conducted by the three divisions during the period April 1, 2000 through March 31, 2003. We used the Semiannual Reports to Congress as the basis for determining the audits to review. We selected 12 audit reports listed in the semiannual reports for our review sample, however, one turned out to be an audit termination memorandum and another a non-audit report or product. Therefore, we reviewed 11 audits that produced 10 audit reports and a review memorandum, which we are reporting in the Findings and Recommendations section of this report. We are also reporting on the non-audit product in the Other Matters section of this report.

By division, BTD conducted seven audits during the period and we reviewed four. STD conducted four audits and we reviewed all four. ESD conducted three audits, which produced two audit reports and the audit termination memorandum, and the division produced the non-audit report product. We reviewed all three audits and the non-audit report. A list of the reviewed audits and products is attached.

We also conducted followup reviews of the internal quality control reviews of BTD, ESD and STD, performed by the Bradson Corporation, dated February 18, 2000; March 24, 2000; and January 21, 2000, respectively, and of the external quality control review performed by the U.S. Department of State dated December 22, 2000.

# FINDINGS AND RECOMMENDATIONS

We found that BTD, ESD and STD have generally complied with the Government Auditing Standards (GAS) and OIG Directives during our period of review. However, our review identified two non-material findings for which we have recommendations for corrective actions. The findings relate to documenting auditor independence and referencing of audit reports.

# INDEPENDENCE DECLARATIONS NOT DOCUMENTED IN ONE INSTANCE

Our review found no evidence of personal or external impairments. However, for one audit (ESD-12593), independence declarations were not included in the working papers for the Atlanta, Denver and Seattle regional office staff that assisted on the audit. OIG Directives Manual, Section 5340 describes policies and procedures for maintaining independence. The manual states that for all audits, each auditor and supervisor is required to complete and sign an Independence Declaration at the beginning of the audit assignment.

### Recommendation

We recommend that the Audit Division Directors require all personnel working on audits to sign independence declarations for each of their assignments.

### **Response to Finding Regarding Independence Declarations**

The Deputy Assistant Inspector General for Auditing concurs with the draft report finding and recommendation regarding Independence Declarations and has agreed to fully implement the report recommendation. To ensure implementation of the recommendation, he will instruct the division directors to, within the next two weeks:

- Meet with the staffs of the three divisions to discuss the Internal Quality Review and the report recommendation.
- Ensure that all managers and auditors review working papers for assignments currently in process for signed independence declarations for each staff member that worked on the assignment.
- Provide each auditor with a copy of the memorandum containing the DAIGA's response to the draft IQR report.

### **Reviewer's Comments**

We consider the actions planned adequate to address this recommendation.

# **REFERENCING PROBLEMS NOTED**

We found that nine of the audit reports reviewed had been issued without having the agency responses or OIG comments referenced, which we consider to be substantive changes from the draft to the final report. The tenth audit report was issued in final without draft; therefore, it did not include an agency response. OIG Directives Manual, Section 5651, states that the referencer is responsible for determining whether opinions, conclusions, and recommendations are reasonable and consistent with, or supported by, the factual material examined. Therefore, we believe that the addition of the agency's response and OIG comments into the final audit report should be referenced. However, because a copy of the agency responses were attached to the final reports, we do not consider this a material weakness. Nor do we consider not having the OIG comments referenced a material weakness due to the number of reviewers in the report processing procedures.

Two of the 10 reports had some other referencing weaknesses. According to the OIG Directives Manual, Section 5651, all draft reports, including any substantive changes made during the clearance process or for the final report, should be referenced. The directives make an exception to the referencing requirement only if relatively few changes are made after referencing that *do not* (sic) affect the factual basis for the report's message, such as changes to improve clarity, tone, and format, in which case the division director can take full responsibility for these changes and note such approval on the referencer's point sheet.

One report (BTD-12650), had substantive changes to questioned costs and refund amounts from the draft to the final report that were not referenced. Our basis for determining that the changes were substantive is that the dollar amount of the costs questioned in the draft report was revised in the final report from (b) (5) and the refund due the government was changed from (b) (5) the changes were not referenced, we noted a weakness in internal controls over verifying report accuracy.

In another report (ESD-15499), a paragraph was added to the report after it was referenced but the change was not referenced. The lack of referencing was significant because the paragraph contained (b) (5)

### (b) (5)

OIG Directives Manual, Section 5651, requires that the OIG/OA Referencing Checklist be completed for each audit. A checklist step requires the division director to attest to whether all substantive changes after original referencing have been re-referenced. The director attested that subsequent revisions were indexed and referenced; however, the unreferenced paragraph was added 11 days later. Nonetheless, the paragraph was supported by the working papers indexed, therefore we do not consider this to be a material weakness.

# Recommendation

We recommend that the Audit Division Directors ensure adherence to the OIG's policy regarding independent report referencing of substantive changes made from the draft to the final reports and substantive changes made after original referencing.

# **Response to Finding Regarding Referencing Final Reports**

The DAIGA concurs with the draft report finding and recommendation regarding referencing final reports. However, he requested that the final IQR report be revised to reflect that at least one of the nine audit reports cited in the draft IQR fully complied with the referencing requirement and that documentation to this effect was provided to the IQR review team.

The DAIGA further states that OIG Directive Manual, Section 5651 was unclear regarding the referencing of agency responses and the OIG comments into the final report. As a result, the established practice for headquarters divisions did not call for the re-referencing of final reports unless the facts or findings changed since the issuance of the draft report.

The revised OIG Audit Directives, effective July 1, 2003, clarifies the language regarding the referencing of final reports by stating in Directive Manual, Number 5610, that the independent referencing of final reports should be limited to narrative text and numerical data that has either been changed from the draft report or added to the final report, including the Agency Response and OIG Comments report sections.

To ensure implementation of the recommendation, the DAIGA will instruct the division directors to, within the next two weeks:

- Meet with their respective staffs to discuss the IQR recommendation.
- Ensure that all managers and auditors review final reports in process for adherence to the OIG's policy regarding independent report referencing of substantive changes made from the draft to the final reports and substantive changes made after original referencing.
- Provide all auditors with a copy of the memorandum containing the DAIGA's response to the draft IQR report.

# **Reviewer's Comments**

We consider the actions planned adequate to address this recommendation. However, we did not find sufficient documentation in the response to revise the number of final reports cited in the IQR as not fully complying with the referencing requirement.

# **OTHER MATTERS**

# Non-Audit Report Products Misclassified in Semiannual Reports to Congress

ESD issued two non-audit report products that were incorrectly classified as audit reports in the Semiannual Reports to Congress. The first product (ESD-12593) was an audit termination memorandum and the other (ESD/OIG-14431) was a report summarizing 2000 Census work conducted by various OIG units including audits, inspections, system evaluations, and investigations.

### Recommendation

We recommend that the Office of Audits either exclude non-audit products in the Semiannual Report or include them in a separate table for non-audit products.

### Response to Finding Regarding Non-Audit Report Products Misclassified

The DAIGA states that all products related to the 2000 Decennial Census were of special interest to the OIG, and the OIG needed a way to publicize that they had been issued. The semiannual was viewed as the best means of doing this. However, in the future, separate tables will be requested for the different OA work products.

### **Reviewer's Comments**

We consider the actions planned adequate to address this recommendation.

Attachment 1

# AUDIT ASSIGNMENTS SELECTED FOR INTERNAL QUALITY REVIEW

#### **BUSINESS AND TRADE AUDITS DIVISION:**

# Improved Internal Controls Needed for USPTO's Office of Human Resources

BTD-12830-0-0001, Final report issued September 2000

#### Software and Information Industry Association

BTD-12650-1-0001, Final report issued March 2001

# Internal Controls for Travel Cards at OAR's Environmental Technology Laboratory Can Be Strengthened

BTD-14908-2-0001, Final report issued September 2002

Travel Card Program at National Weather Service Headquarters Needs Additional Management Controls

BTD-14972-3-0001, Final report issued March 2003

# ECONOMICS AND STATISTICS AUDITS DIVISION:

#### **Re-enumeration at Three Local Census Offices in Florida**

ESD-13215-0-0001, Final report issued September 2000

### International Trade Administration's Market Access and Compliance Unit Successfully Recruited for Trade Compliance Positions,

ESD-15499-3-0001, Final report issued (without draft) March 2003

#### **Review of Special Population Enumerations and Questionnaire Assistance Centers**

ESD-12593, Termination memorandum issued September 2000

Improving Our Measure of America: What Census 2000 Can Teach Us in Planning for 2010

ESD/OIG-14431, Special report issued (non-audit report) Spring 2002

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# SCIENCE AND TECHNOLOGY AUDITS DIVISION:

### Work on Electronic Charting Database Should Be Re-competed

STD-13440-1-0001, Final report issued March 2001

#### Program for Acquiring Fisheries Research Vessels Needs Stronger Management Controls

STD-14428-2-0001, Final report issued June 2002

# Northwest Fisheries Science Center Needs Improved Research Management Processes to Better Implement Its Salmon Research Plan

STD-14440-2-0001, Final report issued September 2002

### NOAA's Corporate Costs Process Needs Improvement

STD-14427-3-0001, Final report issued March 2003



UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Washington, D.C. 20230

August 7, 2003

MEMORANDUM FOR:

John S. Bunting Regional Inspector General for Audits Denver Regional Office

illiam F. Bedwell, Jr.

THROUGH:

Deputy Assistant Inspector General for Regional Audits

Larry B. Gross Deputy Assistant Inspector General for Auditing

SUBJECT:

FROM:

Economics and Statistics Audits Division Business and Trade Audits Division Science and Technology Audits Division Internal Quality Control Review Draft Audit Report No. DEN-15928-3-0001

I have reviewed the subject report and, except as discussed below, concur with the recommendations. To ensure implementation of the recommendations, I will instruct the division directors to, within the next two weeks, (1) meet with the staffs of the three divisions to discuss the Internal Quality Review and the report recommendations, (2) instruct all managers and auditors to review reports currently in process and related working papers for compliance with independence declarations, referencing, and cross-indexing requirements, and (3) provide all auditors with a copy of this memorandum.

My specific comments on the findings are as follows:

<u>Recommendation No. 1</u>: Audit Division Directors require all personnel working on audits to sign independence declarations for each of their assignments.

This condition was found on one audit, ESD-12593. Headquarters auditors assigned to the job had signed independence declarations. However, the three regional assistant inspector generals for audits did not obtain declarations from the staff they later assigned to assist in data collection. Neither the headquarters division director nor the audit manager responsible for the assignment detected this oversight.

To ensure implementation of this recommendation, I will instruct the division directors to:

- Meet with their respective staffs to discuss the IQR report recommendation.
- Ensure that all managers and auditors review working papers for assignments currently in process for signed independence declarations for each staff that worked on the assignment.
- Provide all auditors with a copy of this memorandum.

**<u>Recommendation No. 2</u>**: Audit Division Directors ensure adherence to the OIG's policy regarding independent report referencing of substantive changes made from the draft to the final reports and substantive changes made after original referencing.

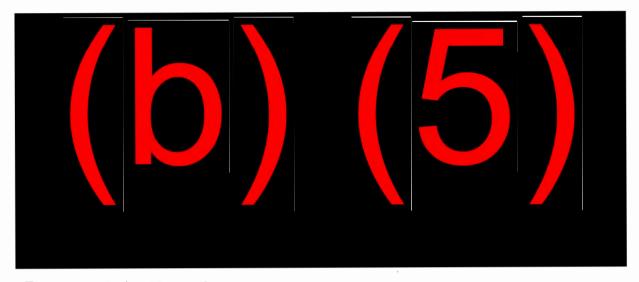
The audit report states that nine of the audit reports reviewed had been issued without having the agency responses or OIG comments referenced. The tenth audit report was issued in final without a draft report; therefore it did not include an agency response. However, at least one of the nine audit reports (BTD-14972-3-0001, *Travel Card Program at National Weather Service Headquarters Needs Additional Management Controls*) reviewed did have both the agency response and the OIG comments indexed and referenced. Documentation has been provided to the auditors demonstrating this. We request that the final report be revised to recognize that.

OIG Directive Manual, Section 5651, was unclear regarding the referencing of agency responses and the OIG comments into the final report. As a result, the established practice for headquarters divisions did not call for the re-referencing of final reports unless the facts or findings had changed since the issuance of the draft report.

The revised OIG Audit Directives, effective July 1, 2003, clarifies the language regarding referencing final reports by stating in Directive Manual, Number 5610, that the independent referencing of final reports should be limited to narrative text and numerical data that has either been changed from the draft report or added to the final report, including the Agency Response and OIG Comments report sections.

To ensure implementation of this recommendation, I will instruct the division directors to:

- Meet with their respective staffs to discuss the IQR report recommendation.
- Ensure that all managers and auditors review final reports currently in process for adherence to the OIG's policy regarding independent report referencing of substantive changes made from the draft to the final reports and substantive changes made after original referencing.
- Provide all auditors with a copy of this memorandum.



**<u>Recommendation No. 4</u>**: The Office of Audits should either exclude non-audit products in the Semiannual Report or include them in a separate table for non-audit products.

All work products related to the 2000 Decennial Census were of special interest to the OIG, and the OIG needed a way to publicize that they had been issued. The semiannual was viewed as the best means of doing this. However, in the future, separate tables will be requested for the different OA work products.

As described above, I believe these actions fully address the implementation of the Internal Quality Control Review recommendations. I appreciate the thorough and constructive efforts of Randal Skalski, Karen Blechschmidt, Crystal Miller, and Karen Barron on this review.

cc: Chuck Tegeler, Director, Economics and Statistics Audits Division Ron Lieberman, Director, Science and Technology Audits Division



August 11, 2003

MEMORANDUM FOR: Michael Sears

Assistant Inspector General for Auditing

William F. Bedwel

THROUGH:

Departy Assistant Inspector General for Regional Audits

FROM:

Larry B/Gross Deputy Assistant Inspector General for Auditing

SUBJECT:

Seattle Regional Office Internal Quality Review Final Report No. DEN-15928-3-0004

I am pleased to transmit the final report for the June 2003 Internal Quality Review (IQR) of the Seattle Regional Office (SRO). The IQR scope was to review SRO's compliance with the Government Auditing Standards and the Office of Inspector General Directives Manual. We found no material non-compliance with the Government Audit Standards or OIG Directives; however, there were three issues requiring additional attention in order to fully comply with GAS and OIG directives.

We noted that the SRO audits often lacked evidence of supervisory review of working papers as required by the GAS and OIG policies and procedures. We also noted that final reports issued by SRO were not referenced as required by the OIG Directives. In addition we noted one audit report, which was indexed to a summary that was not cross-indexed to supporting working papers as required by the OIG Directives. We recommended that SRO adhere to GAS and OIG policies regarding supervisory review of working papers, referencing final reports, and cross-indexing summaries.

In response to the draft report, the Deputy Assistant Inspector General for Regional Audits concurred with the recommendations, and provided a responsive action plan.

Attachment

cc (w/att): Johnnie E. Frazier, Inspector General Edward Blansitt, Deputy Inspector General David Sheppard, Regional Inspector General for Audit, SRO

# SEATTLE REGIONAL OFFICE INTERNAL QUALITY REVIEW AUDIT REPORT NO. DEN-15928-3-0004

#### INTRODUCTION

We have reviewed the system of quality control for the audit function of the Seattle Regional Office (SRO), in effect for the three years ended March 31, 2003. We conducted our review in conformity with standards and guidelines established by the President's Council on Integrity and Efficiency (PCIE). We tested compliance with SRO's system of quality control to the extent we considered appropriate. These tests included a review of audits identified in attachment 1.

In performing our review, we have given consideration to the policy statement on quality control and external reviews dated February 2002 issued by the PCIE. That statement indicates that an OIG's quality control policies and procedures should be appropriately comprehensive and suitably designed to provide reasonable assurance that the objectives of quality control will be met. It also recognizes that the nature, extent and formality of an OIG's system of quality control depends on various factors such as the size of the OIG, the location of its offices, the nature of the work and its organizational structure.

In our opinion, the system of quality control for the audit function of the SRO in effect for the three years ended March 31, 2003, has been designed in accordance with the quality standards established by the PCIE and was being complied with for the period then ended to provide the OIG with reasonable assurance of material compliance with professional auditing standards in the conduct of its audits. Therefore, we are issuing an unqualified opinion on the SRO systems' of audit quality control.

#### PURPOSE, SCOPE AND METHODOLOGY

We tested compliance with the SRO systems' of quality control to the extent we considered appropriate. These tests included a review of a sample of audits with final reports issued by the SRO during the period April 1, 2000 through March 31, 2003. We used the Semiannual Reports to Congress as the basis for determining the reports issued. SRO issued 22 audit reports during the period and we reviewed a sample of four audits. A list of the reviewed audits and products is attached.

We reviewed and conducted followup of the internal quality control reviews of SRO, performed by the Bradson Corporation, dated March 30, 2000. We also reviewed and conducted followup of the external quality control review performed by the U.S. Department of State, dated December 22, 2000.

#### FINDINGS AND RECOMMENDATIONS

We found that SRO has generally complied with the GAS and OIG Directives during our period of review. Our review identified three findings with recommendations for corrective actions. We noted findings related to working paper reviews, referencing of audit reports, and cross-indexing working papers.

# **EVIDENCE OF SUPERVISORY REVIEW OFTEN LACKING**

The four SRO audits reviewed often lacked evidence of supervisory review of working papers as required by GAS and OIG policies and procedures. GAS, Section 4.37, states, "Working papers should contain evidence of supervisory reviews of the work performed." Furthermore, OIG Manual 5651, Section 4, states, "Audit managers should review all working papers and document their review." Each of the four audits that we reviewed involved only one auditor who reports directly to the Regional Inspector General for Audits (RIGA). The RIGA reviews the audit reports but usually does not review summary or detailed working papers and often does not signoff on quality control checklists and forms such as the OIG Form GA-1, GAGAS Determinations and Related Standards Certifications and the OIG/OA Referencing Checklist. Since the SRO does not delegate an audit manager to oversee audits, the responsibility for reviewing working papers rests solely with the RIGA. The problem may be corrected by the RIGA spending more time reviewing working papers or by delegating the responsibility to an audit manager. Furthermore, OIG Directives Manual, Section 5651, describes responsibilities in the quality control process of the audit manager, RIGA and report referencer. As a result of SRO not employing an audit manager to review audits, one of the three levels of review intended by OIG policies and procedures, has been omitted.

#### Recommendation

We recommend that the Regional Inspector General for Audits ensure that supervisory review of working papers is documented for all audits.

#### **Response to Finding Regarding Supervisory Review**

The Deputy Assistant Inspector General for Regional Audits concurs with the draft report finding and recommendation regarding supervisory review of working papers. He states that the lack of supervisory review was caused by SRO's management turnover and staff decreases. Nonetheless, the DAIGRA has agreed to fully implement the report recommendation regarding supervisory review of working papers. To ensure implementation by all auditors and supervisors in the region, he will instruct the Seattle Regional Inspector General for Audits to within two weeks:

• Conduct a staff meeting for all auditors to discuss the SRO Internal Quality Review, and the report recommendations to adhere to the policy regarding supervisory review of working papers.

-2-

- Instruct all auditors to review all final reports in process for compliance with the supervisory review requirements.
- Provide each auditor with a copy of the memorandum containing the recommendations of the IQR.

In addition, the DAIGRA will on his next visit to SRO review a test sample of working papers to ensure that working papers have sufficient evidence of supervisory review.

### **Reviewer's Comments**

We consider the actions planned adequate to address this recommendation.

### FINAL REPORTS NOT REFERENCED

The referencing process was not followed for the changes from the draft to the final reports. The unreferenced changes included additions that are made to the draft report in preparation of final audit report issuance, such as agency responses and OIG comments. Although the findings in each audit remained essentially the same, additions to the final reports included the auditor's summary of the agency's response and a detailed analysis and rebuttal of the response. According to OIG Directives Manual, Section 5651, the referencer is responsible for determining whether opinions, conclusions, and recommendations are reasonable and consistent with, or supported by, the factual material examined. Incorporation of the agency response and the OIG comments into the final report should be properly referenced. However, we do not consider the lack of referencing the final report a material finding because a copy of the response is normally attached to the final report and the report contains the material facts that form the basis for the recommendation.

#### Recommendation

We recommend that the Regional Inspector General for Audits ensure adherence to the OIG's policy regarding independent report referencing so that all changes made from draft to final reports are referenced.

### **Response to Finding Regarding Referencing Final Reports**

The DAIGRA concurs with the draft report finding and recommendation regarding referencing final reports. He states that although OIG Directive Manual, Section 5651 was unclear regarding the referencing of agency responses and the OIG comments into the final report, it is normally SRO's practice to reference changes to draft reports in preparing final reports, including grant recipients' response and OIG comments. However, in the cited cases, the referencing of the responses was not done.

The revised OIG Audit Directives, effective July 1, 2003, clarifies the language regarding the referencing of final reports by stating in Directive Manual, Number 5610, that the independent referencing of final reports should be limited to narrative text and numerical data that has either been changed from the draft report or added to the final report, including the Agency Response and OIG Comments report sections.

The DAIGRA has agreed to fully implement the report recommendation regarding final report referencing. To ensure implementation by all auditors in the region, he will instruct the Seattle Regional Inspector General for Audits to within two weeks:

- Conduct a staff meeting for all auditors to discuss the Seattle Regional Office, Internal Quality Review, and the report recommendations to adhere to the policy of referencing final reports.
- Instruct all auditors to review all final reports in process for compliance with the referencing requirements.
- Provide each auditor with a copy of the memorandum containing the recommendations of the IQR.

### **Reviewer's Comments**

We consider the actions planned adequate to address this recommendation.

# SUMMARY NOT CROSS-INDEXED IN ONE INSTANCE

For one audit (STL-14322), the report was indexed to a working paper summary that was not cross-indexed to supporting working papers as required by OIG Directives Manual, Section 5315. Not cross indexing the summary was significant because it was the primary working paper used to support the overall finding of the audit report. Furthermore, the independent referencer did not detect the problem. According to the OIG Directives Manual, Section 5651, the referencer should test check that the summaries and lead schedules used to support the audit report are properly cross-indexed to detailed working papers. We do not consider this instance to be a material weakness; however, because we were able to verify the information contained in the report with other working papers.

### Recommendation

We recommend that the Regional Inspector General for Audits ensure adherence to the OIG's policies regarding cross-indexing working paper summaries, and having the referencer test check the cross indexing system.

# **Response to Finding Regarding Summary Not Cross-Indexed**

The DAIGRA concurs with the draft report finding and recommendation regarding referencing the summary not cross-indexed to supporting working papers. He states that it is normally SRO's practice to cross-index working paper summaries to supporting working papers, in accordance with Audit Directive Number 5610 (formerly contained in section 5651). In the cited case the cross-indexing was not done, nor did the referencer detect the oversight.

The DAIGRA has agreed to fully implement the report recommendation regarding crossindexing summaries to supporting working papers. To ensure implementation by all auditors in the region, he will instruct the Seattle Regional Inspector General for Audits to within two weeks:

- Conduct a staff meeting for all auditors to discuss the Seattle Regional Office, Internal Quality Review, and the report recommendations to adhere to the policy of cross-indexing summaries to supporting working papers.
- Instruct all auditors to review all final reports in process for compliance with the cross-indexing requirement.
- Provide each auditor with a copy of the memorandum containing the recommendations of the IQR.

# **Reviewer's Comments**

We consider the actions planned adequate to address this recommendation.

Attachment 1

# SEATTLE REGIONAL OFFICE AUDITS SELECTED FOR INTERNAL QUALITY REVIEW

# Town of Quartzsite, Arizona Audit of EDA Public Works Financial Assistance Award

STL-14253-2-0001, Final report issued October 2001

# Beaumont Redevelopment Agency, California Audit of EDA Public Works Financial Assistance Award

STL-14258-1-0001, Final report issued September 2001

Internal Controls Over Consultant Services Provided to Clients by Trade Adjustment Assistance Centers

STL-14322-1-0001, Final report issued September 2001

Pacific States Marine Fisheries Commission, Gladstone, Oregon Audit of NOAA Financial Assistance Award

STL-14956-2-0001, Final report issued September 2002

Bunting Klein Buchtel Skalski Blechschmidt Chron

bc:



UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Washington, D.C. 20230

August 6, 2003

MEMORANDUM FOR:

John S. Bunting Regional Inspector General for Audits Derver Regional Office

THROUGH:

Deputy Assistant Inspector General for Auditing

vell. Jr.

Gross

Deputy Assistant Inspector General for Regional Audits

SUBJECT:

FROM:

Seattle Regional Office Internal Quality Control Review Draft Audit Report No. DEN-15928-3-0004

I have reviewed the subject report and concur with the recommendations regarding evidence of supervisory review of working papers, referencing final audit reports, and ensuring adequate cross-indexing of working paper summaries.

### **Evidence of Supervisory Review Often Lacking**

We recognize that there was often a lack of evidence of supervisory review of working papers. There were a number of reasons for this, the most prominent being that the audits reviewed were conducted during a transition period for the Seattle Regional Office. The office had several managers in an acting capacity during this period. The current Regional Inspector General for Audits was officially appointed in February 2002 after being in an acting capacity for approximately seven months. Prior to that, another OIG employee served in an acting capacity for approximately three months. In addition, during this period the staffing for the office was significantly reduced from prior years, resulting in fewer audit managers.

Nonetheless, corrective action will be taken to ensure that audit working papers have sufficient evidence of supervisory review. The revised OIG Audit Directives, effective July 1, 2003, provides clear instructions on this. The new directives specifically state in section 5610 "Audit supervisors must carefully review all audit workpapers in a timely manner and document their review by signing or initialing each individual workpaper."

#### Final Report Needs Referencing

Although OIG Directive Manual, Section 5651, was unclear regarding the referencing of agency responses and the OIG comments into the final report, it is normally SRO's practice to reference grant recipient's responses and OIG comments in the final report. However, in the cited case the referencing of the response and comments was not done.

The revised OIG Audit Directives, effective July 1, 2003, clarifies the language regarding referencing final reports by stating in Directive Manual, Number 5610, that the independent referencing of final reports should be limited to narrative text and numerical data that has either been changed from the draft report or added to the final report, including the Agency Response and OIG Comments report sections.

#### Summary Not Cross-Indexed in One Instance

It is normally Seattle's practice to cross-index working paper summaries to supporting working papers, in accordance with Audit Directive Number 5610 (formerly contained in section 5651). In the cited case the cross-indexing was not done, nor did the referencer detect the oversight.

#### **Implementing Recommendations**

The Seattle Regional Office of Audits will fully implement the report recommendations. To ensure implementation by all auditors and supervisors, I will instruct the Regional Inspector General for Auditing to within two weeks:

- Conduct a staff meeting for all auditors to discuss the SRO Internal Quality Review and the report recommendations to adhere to the policy regarding evidence of supervisory review of workpapers, referencing final reports, and cross-referencing summaries to supporting workpapers.
- Instruct all auditors to review final reports currently in process for compliance with the supervisory review, referencing, and cross-referencing requirements.
- Provide each auditor with a copy of this memorandum.

In addition, I will on my next site visit to SRO review a test sample of working papers to ensure that working papers have sufficient evidence of supervisory review.

I believe these actions will fully address the implementation of the Internal Quality Control Review recommendations.

I appreciate the thorough and constructive Internal Quality Control Review conducted by your staff.

cc: David Sheppard, Regional Inspector General for Audits, SRO David Charbonneau, Assistant RIGA, SRO



UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Washington, D.C. 20230

August 2, 2016

# RE: FOIA Request No. DOC-OIG-2016-001211

This letter is to regarding your Freedom of Information Act (FOIA) request, tracking number DOC-OIG-2016-001211, dated May 25, 2016 and received by the Department of Commerce, Office of Inspector General (OIG) on May 26, 2016, in which you seek, as modified June 2, 2016 and June 23, 2016, copies of nine (9) named OIG reports. As you directed on June 7, 2016 and July 18, 2016, the OIG processed only those documents that could be searched for and retrieved after two (2) hours of search time.

A search of records maintained by the OIG has located, within the two hours of search time, six (6) reports consisting of 125 pages that are responsive to your request. This letter is a final response to your request; we previously processed four (4) reports consisting of fifty-five (55) pages on July 18, 2016. As we noted previously, we did not locate copies of three (3) reports within the two hours of search time. As for this final response, we have reviewed (2) reports consisting of seventy (70) pages under the terms of FOIA and, after consulting with the National Institutes of Science and Technology (NIST), the Bureau of Industry and Security (BIS), and the National Oceanic and Atmospheric Administration (NOAA) over the release of certain of the pages, have determined that they may be released as follows:

- Sixty-six (66) pages may be released to you in full; and
- Four (4) pages have been partially withheld under FOIA exemption (b)(7)(E), 5 U.S.C. § 552(b)(7)(E), which protects law enforcement information the disclosure of which would disclose techniques and procedures for law enforcement investigations or prosecutions, or would disclose guidelines for law enforcement investigations or prosecutions if such disclosure could reasonably be expected to risk circumvention of the law.

Copies of the seventy pages are enclosed with the relevant withholdings noted.

For your information, Congress excluded three discrete categories of law enforcement and national security records from the requirements of FOIA. See 5 U.S.C. § 552(c) (2012 & Supp. III 2015). This response is limited to those records that are subject to the requirements of FOIA. This is a standard notification to all OIG requesters and should not be taken as an indication that excluded records do, or do not, exist.

You have the right to appeal this partial denial of your request. An appeal must be received within thirty (30) calendar days of the date of this response letter by the Counsel to the Inspector General, U.S. Department of Commerce, Office of Inspector General, Office of Counsel, Room 7898C, 14th and Constitution Avenue, N.W., Washington, D.C. 20230. Your appeal may also be sent by e-mail to FOIA@oig.doc.gov, by facsimile (fax) to 202-501-7335, or by FOIAonline, if you have an account in FOIAonline, at

https://foiaonline.regulations.gov/foia/action/public/home#.

The appeal should include a copy of the original request and this initial denial letter. In addition, the appeal should include a statement of the reasons why the records requested should be made available and why the adverse determination was in error. The appeal letter, the envelope, the e-mail subject line, and the fax cover sheet should be clearly marked "Freedom of Information Act Appeal." The e-mail, fax machine, FOIAonline, and Office of Counsel mailbox are monitored only on working days during normal business hours (8:30 a.m. to 5:00 p.m., Eastern Time, Monday through Friday). FOIA appeals posted to the e-mail box, fax machine, FOIAonline, or the Office of Counsel mailbox after normal business hours will be deemed received on the next normal business day. If the 30<sup>th</sup> calendar day falls on a Saturday, Sunday, or legal public holiday, an appeal received by 5:00 p.m., Eastern Time, the next business day will be deemed timely. An appeal received after the 30-day limit will not be considered.

If you have any questions, please contact me via email at FOIA@oig.doc.gov, or by phone at (202) 482-5992.

Sincerely,

Raman Santra FOIA Officer

Enclosures



MAR 28 1997

MEMORANDUM FOR:

Diana Josephson Deputy Under Secretary for Oceans and Atmosphere National Oceanic and Atmospheric Administration

FROM:

Frank DeGeorge Inspector 8

SUBJECT:

Northwest Emergency Assistance Plan Needs Focus Final Audit Report No. STL-8518-7-0001 March 1997

Attached is our final report on the review of NOAA's Northwest Emergency Assistance Plan. Four copies of the audit report are attached for your convenience. An executive summary of the report is presented on page I and the recommendations are on pages 7 and 12.

We have reviewed NOAA's response to the draft report and appreciate the comments provided. NOAA agreed that the program was achieving its goals, that projects other than the permit buyback projects may provide more direct conservation benefits, and to a more careful monitoring of future NEAP funding to ensure projects comply with NEAP goals.

NOAA disagreed that overall program effectiveness would be increased by eliminating funding for the permit buyback program and would not make any commitments that preclude the use or design of future permit or vessel buyback programs.

NOAA's response to the draft audit report is summarized throughout the report with the comments in full included as Appendix I.

In accordance with DAO 213-5, you have a maximum of 60 days to submit, for our concurrence, an Audit Action Plan for implementation of each of the report's recommendations. Exhibit 7 of the DAO should be used to format the Audit Action Plan. The Audit Action Plan should include specific details and dates as to how and when each recommendation will be implemented, and must also include the rationale and/or legal basis for not implementing any of the report's recommendations. Should you have any questions regarding the preparation of the



Audit Action Plan, please contact Ray McIntosh, Regional Inspector General for Audits at (206) 220-7970. Please inform the Office of Inspector General of the names of the key officials responsible for resolution of this audit. We suggest a meeting within 30 days to discuss the resolution of the report's findings and recommendations. To arrange such a meeting, NOAA officials should also contact Ray McIntosh.

We appreciate the cooperation and courtesies extended to us by NOAA officials during the review.

### Attachments

cc: Barbara Martin, NOAA Audit Liaison
 William W. Stelle, Jr., Northwest Regional Director, NMFS
 John K. Bullard, Director, Office of Sustainable Development
 and Intergovernmental Affairs, NOAA

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# NATIONAL OCEANIC AND ATMOSPHERIC ADMINISTRATION NORTHWEST EMERGENCY ASSISTANCE PLAN NEEDS FOCUS

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#### **EXECUTIVE SUMMARY**

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To help alleviate the economic impacts of a west coast salmon fishery disaster, the National Oceanic and Atmospheric Administration, through its Office of Sustainable Development and Intergovernmental Affairs and the National Marine Fisheries Service, administers the Northwest Emergency Assistance Plan. The NEAP program is designed to provide economic assistance to eligible salmon fishers and fund projects that conserve or help restore the salmon fishery resource.

The NEAP program consists of three segments: (1) buybacks of commercial salmon permits issued by Washington State to provide economic assistance to salmon fishers and reduce commercial salmon harvest capacity, (2) funding of habitat restoration projects that employ fishers to restore salmon habitats, and (3) funding data collection projects that employ fishers to assist in studies desired by fishery resource scientists and managers.

We conducted a management review of the program to determine the effectiveness of the program in providing economic assistance to salmon fishers and conserving or restoring the salmon resource. We also reviewed the program's compliance with the enabling legislation and regulations, and whether improvements to the program could be identified. We found that while the program was achieving the goals of providing economic assistance to eligible salmon fishers, funds could be used more effectively to conserve or restore the salmon resource. Specifically,

- o The permit buyback program, implemented for only Washington State, was not an effective method for conserving or restoring the salmon resource. The \$9.25 million allocated for this program could have been used more effectively by being applied to habitat restoration and data collection projects. (See page 4.)
- o The habitat restoration and data collection programs were effective in achieving NEAP goals. However, benefit to the salmon resource was questionable for a few projects. (See page 10).

We recommend on pages 7 and 12 that the Deputy Under Secretary for Oceans and Atmosphere:

o Eliminate funding of future permit buyback programs and reallocate the funds to salmon habitat restoration or data collection programs. If the permit buyback program continues to be funded, revise the program selection criteria to ensure that fishers who sell permits agree to cease fishing in the regional salmon fishery.



Require NOAA to revise project funding criteria to ensure that habitat restoration and data collection projects comply with the requirements of the Interjurisdictional Fisheries Act and the Secretary's disaster declaration.

With implementation of the above recommendations, the Department would achieve \$10.5 million in funds to be put to better use by redirecting permit buyback program funds to the salmon habitat restoration and data collection programs which can be used to assist more needy salmon fishers and fund more projects that benefit the salmon resource.

NOAA agreed with our findings that the NEAP program was achieving its goals, but disagreed that the projects identified in the report did not meet the program's goals. However, NOAA agreed to more carefully monitor future NEAP funding to ensure that projects comply with program goals. NOAA disagreed that funds for the permit buyback program segment should be redirected to habitat restoration and data collection, and also disagreed with the funds to be put to better use. The agency's complete response is attached as Appendix I.

After careful consideration of NOAA's response, we found no basis to cause us to change our conclusions or recommendations. We still believe that a few projects are questionable because they did not improve salmon habitat or collect data needed by salmon resource managers. NOAA's assurance that future NEAP funding of projects will receive more careful monitoring to ensure compliance with program goals is reassuring. However, NOAA did not address the issue of revising project funding criteria to ensure compliance with authorizing legislation. We also continue to believe that program effectiveness could be increased by directing permit buyback funding to habitat restoration and data collection projects, which address all of the NEAP program goals. Our complete comments are provided throughout applicable sections of the report.

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### **INTRODUCTION**

In May 1994, the Secretary of Commerce declared a salmon fishery resource disaster along the West Coast because of depleted salmon stocks despite stringent fishery management measures. To offset the economic impacts of reduced salmon abundance, the Secretary established the Northwest Emergency Assistance Plan (NEAP I), a \$12 million economic emergency assistance program for affected commercial salmon fishers in the Pacific states of California, Oregon and Washington. In August 1995, the Secretary declared that the fishery resource disaster continued to exist for these Pacific States, and provided an additional \$13 million (NEAP II) that built upon the program started under NEAP I.

The NEAP program is authorized under the Interjurisdictional Fisheries Act, section 308(d) which allows grants to persons engaged in commercial fisheries for uninsured and uncompensated losses suffered as a direct result of a fishery resource disaster, or to be used to restore the affected fishery or prevent a similar future failure.

NOAA, through its Office of Sustainable Development and Intergovernmental Affairs and the National Marine Fisheries Service, designed a three-pronged approach to provide economic assistance to commercial salmon fishers and conserve or restore the salmon resources through a (1) salmon permit buyback program administered by the Washington Department of Fish and Wildlife, (2) habitat restoration jobs program administered by the USDA Natural Resource Conservation Service, and (3) data collection jobs program administered by the Pacific States Marine Fisheries Commission.

The salmon permit buyback program was to reduce the number of troll, gillnet and charter licenses and thereby improve the opportunity for fishers who remained in the industry; provide economic assistance to fishers who wanted to leave the industry; and reduce the number of boats and thereby lessen the salmon harvest pressure. Program funding totaled \$9.25 million, \$4 million from NEAP I funds and \$5.25 million from NEAP II funds. Washington State was the only state to participate in the salmon permit buyback program.

The habitat restoration program utilized the existing working arrangements maintained by the Department of Agriculture's Natural Resource Conservation Service. NEAP funds were transferred from NOAA to NRCS; NRCS then passed the funds on to state level agencies. For California, the state level organization was the Humboldt County Resource Conservation District; for Oregon, the agency was the Oregon Department of Agriculture; and for Washington, the coordinating agency was the Washington State Conservation Commission. NEAP funds to the habitat program totaled \$10.8 million, \$6 million from NEAP I and \$4.8 million from NEAP II.

The Pacific States Marine Fisheries Commission administered the data collection jobs program for the three-state area. As a federally established five-state commission (California, Oregon, Washington, Idaho, and Alaska), one of its organizational objectives is the facilitation of research



and management of projects relating to interstate fisheries. The list of NEAP funded projects was identified by a multi-agency committee and contracted to a mixture of state, private, and non-profit organizations for implementation. NEAP funding totaled \$4.65 million, \$2 million from NEAP I and \$2.65 million from NEAP II.

### Purpose and Scope of Audit

The purpose of our audit was to determine (1) how well the programs provided jobs to eligible commercial fishers, (2) how well the organizations designated to administer the program complied with legislation, regulations, and agreements, and (3) whether organizational and/or operational alternatives exist to improve the achievement of program goals and objectives. We reviewed program files and records at the NOAA Trade and Industries Office in Seattle, Washington. We also interviewed NOAA Office of Sustainable Development and Intergovernmental Affairs officials in Washington, D.C., the NMFS Regional Director, and a regional Trade and Industry Official in Seattle, Washington.

We also interviewed and discussed the separate program segments with officials responsible for administering and managing the programs. For the permit buyback program we interviewed and obtained information from the Licence Manager and Environmental Planner of the Washington Department of Fish and Wildlife in Olympia, Washington. For the habitat restoration program we interviewed and obtained information from the NRCS project coordinator in Washington, D.C.; the NRCS Salmon Recovery Coordinator in Davis, California; the NRCS Information Officer and Fisheries Biologist in Portland, Oregon; the Director and staff of the Washington Conservation Commission in Olympia, Washington; the Project Coordinator of the Oregon Department of Agriculture in Salem, Oregon; and the Project Coordinators of the Humboldt County Resource Conservation District in Fields Landing, California. For the data collection jobs program, we interviewed and obtained information from the Field Program Administrator, the Fiscal Manager and staff of the Pacific States Marine Fisheries Commission in Gladstone, Oregon. We conducted our review from April through August, 1996.

We reviewed the internal control procedures used by the various organizations to determine fishers eligible to participate and benefit from the program. We also reviewed the process used by organizations to evaluate projects for funding by the habitat restoration and data collection jobs programs. The projects were evaluated by a multi-agency group of representatives as recommended by NMFS. The criteria used by the groups in selecting projects to be funded are discussed in our report. No material internal control weaknesses were found.

The many organizations involved in the NEAP program utilize computer information systems to track the various projects and programs. We did not perform any reviews of controls over computer generated data validity or reliability because our audit objectives were to determine overall program compliance and effectiveness.



We reviewed compliance with the Interjurisdictional Fisheries Act, the Commerce Secretary's Declarations of Fishery Disasters, Federal Register Notices, the Interagency Agreement with the Natural Resource Conservation Service, and the agreements with the individual state level organizations. We concluded that seven projects not benefitting the salmon resource were inappropriately funded under NEAP.

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This review was conducted in accordance with generally accepted government auditing standards and was performed under the authority of the Inspector General Act of 1978, as amended, and Department Organization Order 10-13, dated May 23, 1980, as amended.

# FINDINGS AND RECOMMENDATIONS

# NEAP FUNDING CAN BE MORE EFFECTIVE BY FUNDING HABITAT AND DATA PROGRAMS

Funding for the Northwest Emergency Assistance Program can better achieve program goals by being applied to habitat restoration and data collection projects that address all program goals rather than buying back salmon permits which address only one program goal. NEAP program goals included providing financial assistance to eligible fishers and funding projects that conserve or restore the salmon resource. Buying back salmon permits provided financial assistance to fishers but had no direct relationship to conserving or restoring the salmon resource. In addition, the program was designed to retire only Washington salmon permits allowing some fishers with multiple state permits who sold their Washington permit to remain in the regional salmon fishery. We also found that important conclusions and suggestions against funding permit buyback programs published in past reviews were not addressed by NOAA when it cited these reviews as justification for funding permit buybacks.

Eliminating the permit buyback program would provide additional funding for habitat restoration and data collection projects. Overall program effectiveness would be increased by using funds to address all program goals and funding projects that result in direct long-term benefits to the salmon resource.

<u>The Permit Buyback Program</u> <u>Did Not Significantly Conserve or</u> <u>Restore the Salmon Resource</u>

The harvest of salmon off the coasts of Washington, Oregon, and California has decreased by 80 to 95 percent from about 1988 to 1993 despite management measures enacted by fishery agencies to ensure salmon survival. The depletion of salmon stocks was attributed to both over harvesting and unfavorable environmental conditions such as El Nino ocean warming and drought in the western states. In order to provide immediate economic assistance to commercial salmon fishers and conserve and/or restore the salmon resource by reducing the number of fishers, NMFS designed and provided \$9.25 million of the available \$25 million of NEAP funds to implement a permit buyback program.

NOAA based its support and design of the buyback program on two studies:

- o A May 1994 report of the Snake River Salmon Recovery Team which recommended actions for reducing long-term negative effects on the salmon resources; and
- o A buyout program conducted by the State of Oregon in 1983-1986 that reduced the Columbia River gill net salmon fleet.



The buyout program was available only to governments that administered limited entry commercial salmon troll and gillnet fisheries and that could ensure permits would not be replaced. Only Washington State volunteered to participate by adopting the federal program criteria and requirements into State regulation. Washington estimated that the \$4 million initially allocated to the program (NEAP I) would be sufficient to reduce both the troll and gillnet fleets by 50 percent. Washington implemented the buyback program efficiently and effectively, requiring only seven months from program start to funds disbursement. The State met all program requirements and only charged \$119,000 of the maximum allowed \$300,000 in administrative expenses.

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Although purchasing permits provided economic assistance to salmon fishers, it is not an effective method for conserving or restoring the salmon resource, a NEAP program goal. Purchasing permits is not an effective salmon conservation tool because harvest seasons and catch levels for the Pacific Northwest region are set by the Pacific Fishery Management Council and the individual states. Reducing the number of outstanding permits allows more salmon to be caught per existing permit; it does not reduce the total salmon that can be caught. In addition, over one-third of the permit buyback participants held additional salmon fishing permits in neighboring states. Purchasing only the Washington permits of multi-state permit holders was not an effective salmon resource conservation method because the fishers remain in the regional salmon fishery.

The \$4 million used to purchase permits also did not achieve the 50 percent reduction of outstanding permits as initially estimated. Of the 1,378 permits outstanding, the Washington State purchased 296, achieving only a 21 percent reduction.

|                 | <u># Outstanding</u> | # Purchased |
|-----------------|----------------------|-------------|
| Troll permits   | 666                  | 190         |
| Gillnet permits | 506                  | 83          |
| Charter permits | 206                  | 23          |
| Total           | 1,378                | 296         |

Even this apparent reduction in permit holders is misleading because a significant number of these fishers have not left the regional fishery. Of the 296 fishers who sold their Washington permits, 109 (36.8 percent) held permits in neighboring states.

- o 65 of 190 troll fishers (34.2 percent) who sold permits also held permits in Oregon or Alaska -- 35 had Oregon permits, 17 had Alaska permits, and 13 had permits from both states.
- o 43 of the 83 gillnet fishers (51.8 percent) who sold permits also held permits in Oregon or Alaska -- 4 had Oregon permits, 27 had Alaska permits, and 12 had permits from both states.



o 1 of the 23 charter fishers (4.3 percent) who sold permits also had a permit in Oregon.

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Washington State officials defended the effectiveness of the buyback program by stating that buying permits reduces the total number of outstanding permits for the state and the west coast fleet. By permanently reducing the number of outstanding permits, the number of potential fishers who may reenter the industry in the future is reduced and the maximum potential harvest capacity of the west coast fleet is reduced.

However, the Snake River Salmon Recovery Team report, referred to by NOAA as a basis for including a buyback program in NEAP, also stated that:

"A purely voluntary buy-back program <u>alone</u> will prove to be a costly way of accomplishing little or nothing. The licenses (and gear) tendered will always be the least productive; past experience indicates that at least 75% of the licenses must be retired before there is any significant reduction in effective fishing capacity. Once the buy-back reaches that level, the prices demanded for further tenders will increase rapidly, since the remaining units will become more and more profitable. This will force the licenses into the hands of more professional and efficient operations, further blunting the reduction in catching capacity."

The report stated "Buying back licenses alone will shift pressure to other fisheries, and/or leave an idle stock of boats and gear ready to jump back in as soon as the political climate is right (e.g., one or two good runs)."

The final report on the Oregon Columbia River Gillnet Salmon Fleet Reduction Program conducted between 1983-1986, states in part that the removal of some permits will reduce the maximum combined fleet size, but may not remove a vessel from the fleet because fishers hold multiple permits. The report also states that the two most influential factors in reducing fishing capacity is the condition of the resource and the restrictiveness of regulations. NOAA did not address these report issues before deciding on a buyback permit program.

An Oregon official stated that the reason Oregon did not participate in the NEAP funded buyback program was because the governor decided to apply the NEAP funds on habitat restoration and data collection efforts as a better way to assist more salmon fishers, restore the salmon resource, and aid the salmon dependent communities. The State of California also decided not to participate in a permit buyback program.

Permit buybacks do not reduce the number of commercial fishers because fishing is a preferred life style according to a Sea Grant College study conducted at Oregon State University. The study documented how salmon fishers were adapting to changes in the industry and reported in part that:



- o In response to the decrease in salmon, 68 percent of the gillnetters fished other areas or other fisheries, and only 8 percent sold boats, property, equipment or gear; and 10 percent left the industry.
- o Commercial trollers were less likely to rely on non-fishing jobs, less likely to have left the industry, relied on other fisheries and/or moved to other geographic areas.
- o Trollers spent disaster relief funds on living expenses, required Coast Guard safety equipment, and salmon fishing gear.

The troller survey concluded that "...the disaster relief programs served mainly to keep people in the fishery." "Few used the money to move into other occupations."

The use of NEAP funds to buyback commercial salmon permits has not been demonstrated to be an effective method to aid the recovery of the salmon resource. Redirecting funds and concentrating efforts into the salmon habitat restoration jobs program and the data collection jobs program will achieve the dual goals of the NEAP program -- provide economic assistance to commercial salmon fishers and restore and/or conserve the salmon resource.

# Recommendation

We recommend that the Deputy Under Secretary of Oceans and Atmosphere eliminate funding of future NEAP permit buyback programs and reallocate the funds to habitat restoration or data collection programs that benefit the commercial salmon fishery. If the permit buyback program continues to be funded, revise the program selection criteria to ensure that fishers who sell permits agree to cease fishing in the regional salmon fishery.

# Funds to Be Put to Better Use

Current funding for the NEAP program will expire in January 1998. NOAA has stated, however, its intent to consider utilizing a permit buyback program as a potentially appropriate response to certain resource conservation problems. Should NOAA seek additional funding for the NEAP Program under either the Interjurisdictional Fisheries Act, the Magnuson-Stevens Act, or other sources, we estimate that implementing the above recommendation to redirect the permit buyback program funding will provide \$10.5 million in funds to be put to better use. This amount represents the funding for two years of the permit buyback program for continued NEAP funding at \$5.25 million per year, the amount received in 1996.

# Agency Response

NOAA agreed that other projects may provide more direct conservation benefits but disagreed that overall program effectiveness would be increased by eliminating funding for the permit buyback program and reallocating the funding to habitat restoration and data collection projects. NOAA stated that the permit buyback program fulfills the Interjurisdictional Fisheries Act (IFA) mandate to provide disaster assistance to commercial fishermen, and supports NOAA's mission to protect and conserve the nation's marine resources. According to NOAA, two years of NEAP funds (\$9.25 million of the total \$25 million) will result in a reduction of approximately 32

percent of all Washington State salmon permits. NOAA considers 32 percent to be a significant reduction of licenses that will provide substantial conservation benefits to the Pacific Northwest salmon fishery. NOAA stated that the buyback program aids in the conservation and restoration of the salmon fishery resource by creating a smaller fishing fleet, which allows:

- o the Pacific Fishery Management Council, which sets harvest quotas, to more accurately set optimum yield levels that encourage stock conservation and rebuilding;
- o better management to avoid overfishing; and
- o harvests to occur over a longer time period.

NOAA states that it will not make any commitments that preclude the use or design of future permit or vessel buyback programs. In addition, NOAA will not revise buyback program selection criteria to permanently exclude fishers who have previously sold their permits. NOAA stated that such an action is impractical because the salmon fishery is managed by states and tribes, and imposing federal criteria would undercut cooperative relationships.

#### OIG Comments

We continue to believe that program effectiveness could be increased by redirecting permit buyback funding to habitat restoration and data collection projects, which address all of the NEAP program goals. Our report states that the program achieved its goals of providing economic assistance to eligible salmon fishers. However, we concluded that buying permits from only one state was not an effective use of limited funds to conserve or help restore the salmon fishery resource. We cited the Snake River Salmon Recovery Team report, which states that at least 75 percent of the licenses must be retired before there is any significant reduction in effective fishing capacity. In addition, NOAA conceded that other projects may provide more direct conservation benefits or greater disaster assistance than the permit buyback program.

NOAA provided no evidence that purchasing permits actually affected the Pacific Fishery Management Council's setting of the salmon harvest quota. In fact, according to a Council official, determining the optimum yield for salmon is based not on the number of salmon permits, but on the abundance of salmon and the agreed escapement level. Reducing the total number of outstanding salmon permits from Washington State by 32 percent falls short of the State's goal of a 50-percent reduction in permits. Therefore, the fishing capacity of the remaining fleet probably still exceeds the allowed harvest quota of salmon and ensures that all the salmon allowed to be caught will be caught. While claiming that reducing the size of the fishing fleet may make quota management easier, NOAA admits that the buyback program will not reduce the total number of salmon caught in the regional fishery under the Pacific coastwide quota. NOAA's declared position of not precluding NEAP funding for future buyback programs is unfortunate. The limited funding level for the NEAP program requires that efficient use and effective results be obtained for every dollar. Funding a permit buyback program is questionable, especially considering that the State of Oregon, which pilot-tested a permit buyback program, declined to participate and chose instead to fund habitat restoration and data collection projects.

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NOAA's reluctance to revise federal program rules based on a potential undermining of cooperative relationships with states and tribal entities appears to be an overreaction. Federal program rules are common in federally funded programs, and ensuring that the 296 fishers that have sold permits will not benefit from future license buyback programs seems to be a minor procedural requirement. Our conclusions and recommendations remain unchanged.

## NEAP FUNDING SHOULD BENEFIT COMMERCIAL SALMON SPECIES

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Projects funded under the NEAP I habitat restoration and data collection programs achieved the dual goals of the NEAP program by funding 106 total projects which hired about 400 fishers. NEAP funds allocated to habitat restoration were transferred to USDA's Natural Resource Conservation Service under an Interagency Agreement to hire eligible salmon fishers to improve salmon habitat on private lands. Appropriate projects included planting vegetation along stream banks to reduce soil erosion, constructing livestock fencing to protect stream bank vegetation, and installing logs and stumps for in-stream fish habitat and protection.

However in a small number of projects the benefit to the salmon resource is questionable. Seven projects did not improve salmon habitat or collect data needed by salmon resource managers. Specifically, four habitat restoration projects funded at \$300,600 (out of 92 projects funded at \$6 million) did not improve salmon habitat and three data collection projects funded at \$276,000 (out of 14 projects funded at \$2 million) did not benefit the salmon resource.

NMFS allowed the NRCS and state level organizations to fund non-salmon related projects because the projects employed fishers and were desired by local fishery managers. However, the Interjurisdictional Fisheries Act and the Secretary's disaster declaration clearly stipulated that NEAP funds be spent to provide economic aid to salmon fishers and conserve and/or restore the salmon fishery resource. Increased program emphasis and oversight by NMFS will ensure that NEAP funds are expended as intended by the Act.

#### Habitat Restoration Projects

The state agencies reported funding a total of 92 habitat restoration projects which hired a total of about 293 fishers. However, we identified four projects that did not meet the criteria for funding as authorized by the federal regulations, but were allowed by the NRCS interagency agreement. These four projects were as follows:

- o Construction of a day park in Polk County, Oregon on land owned by the Confederated Tribes of the Grand Ronde. The project totaled about \$224,000, of which NEAP provided \$176,000 and matching funds of \$48,000 provided the balance. The project was to improve the habitat of Agency Creek which included planting trees, constructing instream fish habitat structures, constructing a recreational and educational day park with a picnic area, restrooms, parking lot, a half mile of trail, educational signs, and a kiosk. Prior to the funding decision, NRCS was aware that Agency Creek was not a habitat for salmon, and the day park was included at the specific suggestion of NRCS staff.
- The funding of three public outreach and education projects located in Humboldt, Del
   Norte, and Mendocino Counties. The projects were funded at a total cost of \$75,600 \$26,300 for Humboldt, \$32,900 for Del Norte, and \$16,400 for Mendocino County. The



projects were similar in design in that each was to promote the NEAP program by conducting education talks at schools and organizations, issuing news and press releases, and documenting the habitat restoration projects with photographs. One eligible fisher was hired to conduct both of the projects in Humboldt and Del Norte Counties.

When questioned about the funding of these projects, officials stated that they were approved by the interagency review group and were in compliance with project review criteria. The NRCS biologist involved in evaluating the Oregon day park project stated that the Interagency Agreement allows funding for habitat projects for anadromous fish, not just salmon. The biologist added that steelhead is a game fish and anadromous. The county officials responsible for administering the three California public relations projects stated that the results of the projects are very useful in convincing private landowners to allow access and support the restoration projects.

The Federal Register guidelines also require that only projects that directly improve important salmon habitat be funded. Although steelhead is a species within the salmon family, it is a gamefish, not a commercial salmon species and therefore is not authorized to benefit from NEAP funds. The funding of three public relations projects (one in each California county) is excessive and duplicative. Each of the three projects has the same goals of documenting the projects, providing education, and promoting the program. One project may be justified and achieve the stated goals; however, most of the \$75,000 of NEAP funds can be better utilized on projects that directly improve the salmon habitat.

#### **Data Collection Projects**

NEAP funds for the data collection jobs program were administered by the Pacific States Marine Fisheries Commission which hired commercial salmon fishers to collect information on research projects. The employed fishers performed work such as operating fishing equipment and boats, recording data, and tagging fish.

Data collection projects were identified from a number of sources such as state fish and wildlife agencies, conservation groups and associations, and fishery management councils. The projects were then evaluated and selected by a multi-agency team that included members from federal and state agencies, Indian tribes, fisher associations, and conservation groups. The list of projects was then advertised and contractor proposals were evaluated by the PSMFC multi-agency team and contracts finalized.

As of September 30, 1995, PSMFC reported that NEAP I had funded 14 data collection projects that employed 107 fishers. However, two projects funded for \$276,000 did not benefit the salmon fishery resource. The two projects were:

- The Columbia River sturgeon tagging study was contracted to the Oregon Department of Fish and Wildlife, and funded at \$20,199 and employed six eligible fishers. The objective of the project was to tag 5,000 3-6 foot sturgeon in the lower Columbia River in order to estimate the population of white sturgeon needed to achieve and maintain sustainable commercial harvest management levels. The sturgeon tagging project will be continued under NEAP II in the Columbia River and also expanded to a portion of the Washington coast.
- The Nearshore Rockfish and Lingcod study was contracted to the Salmon Trollers Marketing Association, Inc. of Mendocino County, California at an estimated cost of \$256,000 over two years. The PSMFC reported that the project would employ 10 fishers and charter one boat to tag 6,000-16,000 rockfish in order to determine maturity and hooking mortality rates. The rockfish study is not scheduled to continue under NEAP II.

A NOAA official justified funding non-salmon studies because they provided economic assistance to salmon fishers and may help develop alternative fisheries for salmon fishers. However, the Interjurisdictional Fisheries Act authorizes grants to individual fishers when the fishery has been declared a disaster by the Secretary of Commerce. The Secretary's disaster declaration is specific for the west coast commercial salmon resource. NEAP program funds should be focused on providing economic assistance to eligible commercial salmon fishers and benefitting the salmon fishery. NOAA, in issuing its implementing instructions, has allowed the NRCS and PSMFC to dissipate funds away from projects that directly benefit salmon resource conservation and restoration efforts.

#### Recommendation

We recommend that the Deputy Under Secretary for Oceans and Atmosphere require NOAA to revise project funding criteria to ensure that habitat restoration and data collection projects comply with the requirements of the Interjurisdictional Fisheries Act and the Secretary's disaster declaration

#### Agency Response

NOAA agreed to carefully monitor future NEAP programs to ensure consistency with NEAP goals and compliance with appropriate statutory authority and the Secretary's disaster declaration. However, NOAA disagreed that the six projects identified in our report did not improve the salmon habitat or collect data needed by salmon managers. NOAA claimed that the specific projects are consistent with the goals of NEAP, the IFA, and the Secretary's disaster declaration.



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NOAA stated that the decision to employ fishers in habitat restoration jobs was made after extensive consultation with affected individuals, community leaders, and state and local elected officials. NOAA executed a Memorandum of Understanding with NRCS to administer the Habitat Restoration segment of the program.

For the Grand Ronde Educational Day Park project, NOAA stated that a clause in the MOU provides for critical or essential habitat needs and the enhancement of the biological sustainability of anadromous species. NOAA claimed that NRCS interpreted this clause to include habitat for salmon and other salmonid species, such as steelhead trout, which were present in the creek. NOAA also stated that the day-use park is to educate tribal members, the general public, and fishers about how the riparian zone, the stream channel and the associated watershed uplands, are related to and directly affect the health of salmon and steelhead in the creek. Further, NOAA stated that in the park, the fishers helped design and build the foot bridges and the picnic tables, skills that can be transferred to other construction jobs.

NOAA believes that all three Public Outreach and Education Projects were worthwhile and necessary to conduct the outreach activities vital to NEAP's conservation goals. NOAA stated that the \$75,600 spent for the three projects was not excessive; rather, it enabled NOAA to reach as many affected salmon fishers as possible, and facilitated efficient management and completion of the projects. NOAA stated that it relies on the expertise of local officials in selecting projects that meet program guidelines and that it is satisfied that the specified projects are consistent with NEAP guidelines.

NOAA stated that the two projects identified in the Data Collection Jobs Program segment also met NEAP criteria. Concerning the Columbia River Sturgeon Tagging Study, NOAA said the study was necessary because the sturgeon are caught during salmon gillnet fishing. According to NOAA, the two species are managed as a single unit. The mesh size of salmon nets is directly related to the allowable sturgeon harvest, as determined by population studies. Good population data is needed from both species for the fishery to be well managed and the stocks of both species protected. NOAA stated that the study provided additional sturgeon tagging information to support better management and stock rebuilding of salmon and protection for sturgeon for more viable future fisheries.

Concerning the Nearshore Rockfish and Lingcod Study, NOAA stated that the salmon charterboat industry can affect the health of rockfish stocks. When salmon seasons are closed, rockfish charterboat trips provide some income for salmon charterboats, but may also result in increased fishing of the rockfish stocks. NOAA stated that this study was designed to assist the state in gathering data on a planned five-year study that will be funded in the last three years by the state. Salmon fishers who have been trained in this work may have opportunities to continue with this work after the current NEAP program.

#### **OIG** Comments

NOAA's assurance that future NEAP funding of projects will receive more careful monitoring to ensure compliance with program goals is reassuring. However, NOAA did not address the issue of revising project funding criteria to ensure compliance with the requirements of the IFA and the Secretary's disaster declaration.

We found that the NEAP program achieved its goals except for seven projects that did not improve salmon habitat or collect data to improve the salmon resource. Determining whether a specific project should be funded is a process of comparing the project to the authorized and required criteria. Ensuring that federal funds are used as required by federal law and regulation is a basic governmental and program administration responsibility. Although cooperation with state and local government is highly desirable, it is not sufficient justification for NOAA to abdicate its administrative responsibility and allow local officials to direct funding uses.

The Grand Ronde Day Park project was highly questionable in several respects. The NOAA/NRCS memorandum of agreement allowed NEAP funding for anadromous fish, which is not authorized by the Secretary's disaster declaration. The creek in the Day Park is not a habitat for salmon, which is a requirement of the Secretary's declaration. NOAA's response cited education and job training purposes for the Day Park, but such goals are excluded from NEAP by federal regulation.

As to the three public education and outreach projects that share the goal of documenting, educating, and promoting the NEAP program, NOAA has not provided any support showing that any fundamental differences between the projects that would justify the duplication.

Finally, for the Sturgeon Tagging and the Rockfish and Lingcod studies, their results do not directly benefit the conservation and restoration of the salmon resource, as required by the Secretary's disaster declaration and federal regulations. NOAA's response did not provide support to cause us to change our conclusion.



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UNITED STATES DEPARTMENT OF COMMERCE National Oceanic and Atmospheric Administration CHIEF FINANCIAL OFFICER/CHIEF ADMINISTRATIVE OFFICER

MAR 7 1997

MEMORANDUM FOR:

Frank DeGeorge Inspector General

FROM:

Joseph T. Kammerer Unchen A

SUBJECT:

OIG Draft Audit Report on the Northwest Emergency Assistance Plan (NEAP) Needs Focus, Report No. STL-8518-7-XXXX

Thank you for the opportunity to respond to the draft report on the Northwest Emergency Assistance Plan (NEAP). We are pleased that the report reflects that the NEAP program was achieving the goals of providing economic assistance to eligible salmon fishers.

We do not agree with the findings and recommendations and do not agree with the funds to be put to better use. Our detailed response is attached.

Attachment





03/21/87 FRI 12:01 FAX 1 206 220 7967

Office of Inspector General (OIG) Report: Northwest Emergency Assistance Plan Needs Focus Draft Audit Report No. STL-8518-7-XXXX/December 1996

#### OIG Finding: NEAP FUNDING CAN BE MORE EFFECTIVE BY FUNDING HABITAT AND DATA PROGRAMS

NOAA Response: NOAA disagrees with the OIG finding that overall program effectiveness would be increased by eliminating funding for the permit buyback program and reallocating the funding to habitat restoration and data collection projects. The twin objectives of economic assistance and environmental stewardship are the guiding principles underlying the permit buyback program. The OIG concludes that while the program was achieving the goals of providing economic assistance to eligible fishermen, funds could be used more effectively to conserve or restore the salmon resource. However, the permit buyback program fulfills the Interjurisdictional Fisheries Act (IFA) mandate to provide disaster assistance to commercial fishermen, while supporting NOAA's mission to protect and conserve the nation's marine While other projects may provide more direct resources. conservation benefits, or greater disaster assistance, NOAA believes that the buyback achieves significant success in both areas.

## OIG Finding: The Permit Buyback Program Did Not Significantly Conserve or Restore the Salmon Resource

NOAA Response: NOAA disagrees with this OIG finding. The buyback program does aid in the conservation or restoration of the salmon fishery resource in several ways. The reduction in licenses (and fishermen) via the buyback conserves the salmon resource because in setting the optimum yield for a fishery, the Pacific Fishery Management Council must consider socio-economic factors. These factors include dependence of local communities on a fishery and way of life, satisfaction of consumer needs, and the [health of] economies of coastal areas. With fewer fishermen dependent upon the Washington salmon fishery, the Council is better able to set optimum yield at a level that encourages stock conservation and rebuilding.

Furthermore, a smaller fishing fleet is more amenable to precise management than a large fleet, and fishery managers are therefore better able to avoid overfishing. The quotas available to commercial fishermen in Washington are very small, and a large fleet has a greater risk of exceeding the quota through a pulse fishery, i.e., greatly exceeding and/or overwhelming the quota before the NMFS can assess the landings and close the fishery. A smaller fleet allows fishery managers to better predict the

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anticipated effort and allows for "smaller bites" of the quota to be taken. In addition, smaller fleets allow the harvest to occur over longer time periods, which provides more information to fishery managers on the abundance, timing, and presence of different stocks, as well as provides the stock with additional time to mate and spawn.

The OIG provided information that of the 296 fishermen who sold their Washington permits, 109 (36.8 percent) held permits in neighboring states of Oregon and Alaska indicating that a number of significant fishermen have not left the regional fishery. In designing the buyback program, both NOAA and Washington Department of Fish and Wildlife (WDFW) understood that many fishermen with Washington State salmon permits already were participating in salmon fisheries outside the State and in other non-salmon fisheries, and that the buyback program would not substantially influence their continued participation in fisheries outside Washington. However, 63.2 percent of fishermen participating in the buyback did not hold multiple state permits, and many fishermen with Washington State salmon permits targeted stocks either in the Exclusive Economic Zone (EEZ) outside of Washington state waters, or in Washington waters as the fish returned to the rivers to spawn. Without a Washington salmon permit, many fishermen will no longer target Washington salmon runs that school in the EEZ outside of Washington State waters. The fuel and time costs associated with skirting Washington waters in order to land a fresh catch in Oregon, assuming the fisherman has an Oregon salmon permit, make such trips costinefficient. Furthermore, without a Washington salmon permit, fishermen cannot fish for salmon inside Washington State waters, which is where many fishermen directed their efforts. Once Washington-run salmon reach Washington State waters, they stand a much better chance of surviving in order to return to their original spawning grounds and reproduce.

Therefore, although the buyback program does not reduce the total number of salmon caught in the regional fishery under the Pacific coastwide quota, the buyback program reduces the fishing pressure inside State waters, and in certain circumstances, in the EEZ outside of Washington State waters, allows the Council more flexibility in setting optimum yield, and enhances the Council's ability to manage the quota and prevent overfishing. The total number of permits purchased with two years of NEAP funds will result in a reduction of approximately 32 percent of all Washington State salmon permits. NOAA considers this to be a significant reduction of licenses that will provide substantial conservation benefits to the Pacific Northwest salmon fishery.

#### Other OIG Comments: Exit, Displacement of Effort into Other Fisheries, Return to the Fishery

The OIG cited the Snake River Salmon Recovery Team's statement that "Buying back licenses alone will shift pressure to other fisheries, and/or feave an idle stock of boats and gear ready to jump back in as soon as the political climate is right (e.g., one or two good runs)." NOAA approved a buyback program for Washington, because Washington, unlike Oregon and California, has the proper regulations for permanent reduction of licenses. Under the first round of the NEAP buyback program, those fishermen who sold their licenses cannot return to the Washington salmon fisheries to fish unless they purchase another fisherman's license. Under the second round of the buyback program, participants who sold their licenses cannot purchase another license for 10 years. Finally, because the Washington seasons are so short and almost all Pacific Coast fisheries are managed under limited entry regimes, the buyback program should not increase pressure on other fisheries because fishermen are either already participating in these fisheries or will have to buy another fisherman's license to fish.

The OIG also quotes from a Oregon State University Sea Grant College study whose purpose was to assess the adequacy of disaster relief programs and asserts that permit buybacks do not reduce the number of commercial fishermen because fishing is a preferred life style. NOAA notes that conclusions of this study were based on a survey of Oregon troll permit holders including those who already left the fishery and discusses all disaster programs including those of the Small Business Administration and the Federal Emergency Management Administration. Therefore, the conclusions of this study cannot be applied to buyback participants.

#### OIG Recommendations:

1. That the Deputy Under Secretary of Oceans and Atmosphere eliminate funding of future NEAP permit buyback programs and reallocate the funds to habitat restoration or data collection programs that benefit the commercial salmon fishery.

NOAA Action: NOAA disagrees with the OIG recommendations. At this time, NOAA will not make any commitments precluding the use or the design of future permit or vessel buyback programs. Future buyback proposals will be reviewed on their own merits and will be consistent with the statutory authority available to implement such programs and the relevant management regimes. NOAA will continue to consider utilizing a permit buyback program as a potentially appropriate response to certain resource

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conservation problems. We note that if a buyback program is instituted under either the Interjurisdictional Fisheries Act or the Magnuson-Stevens Act, the Secretary will be required to seek public comment and will continue to work closely with state officials and the public.

2. If the permit buyback program continues to be funded, revise the permit buyback program selection criteria to ensure that fishermen who sell permits agree to cease fishing in the regional salmon fishery.

NOAA Action: NOAA will not implement this recommendation because it is not practical and undercuts the cooperative relationships between NOAA, tribal entities, and the states. The OIG recommendation that any future buyback program should preclude fishermen from fishing throughout the region would necessitate a major restructuring of the current salmon fishery regime. Unlike the New England Groundfish fishery, there is no federal salmon permit that can serve as a unifying focal point for a buyback program and a practical means for enforcement. Each state issues salmon permits to residents and non-resident fishermen allowing them to fish for salmon in both their respective state waters and adjoining Federal waters. These licenses may also be tied to specific state waters such as the Columbia River or Puget Sound. Furthermore, because of the migratory nature of salmon, salmon are co-managed by different groups depending on the sub-region. For example, the Pacific Fishery Management Council and NOAA have the lead in managing ocean salmon fisheries, but the Columbia River salmon fisheries are managed under a compact between the states of Washington and Oregon. All state, subregion, and regional salmon processes involve consultation with tribal governments and compliance with the Pacific Salmon Treaty with Canada, which also involves coordination with Alaska Department of Fish and Game.

NOAA will continue to adapt and improve programs where possible. For example, in consultation with WDFW, NOAA revised the bidding procedure utilized in the second permit buyback program to provide more opportunity for a more professional fisherman to have his permit purchased but the fisherman must also agree to not re-enter Washington State fisheries for 10 years.

## FUNDS TO BE PUT TO BETTER USE

NOAA disagrees with the OIG contention that the funds utilized for buyback program could be put to better use. The goals of providing assistance to fishermen and seeking conservation

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benefits reflect a wise use of public funds, complies with the statutory authority and supports NOAA's mission to protect and conserve marine resources. NOAA believes that the buyback program was an appropriate response to the disaster situation.

#### OIG Finding: NEAP FUNDING SHOULD BENEFIT COMMERCIAL SALMON SPECIES

NOAA Response: NOAA disagrees with the OIG's finding that a small number of projects undertaken did not improve salmon habitat or collect needed data by salmon managers. The OIG defines the goals of the program narrowly. NOAA finds these projects to be consistent with the goals of NEAP, the IFA, and the Secretary's disaster declaration.

#### 1. HABITAT RESTORATION PROJECTS

Employing displaced fishermen in habitat restoration jobs was a decision reached after extensive consultation with affected individuals, community leaders, and State and local elected officials. To date, it is estimated that in the three affected states of Washington, Oregon, and California, 538 jobs have been created at living wages ranging from \$10-15 per hour. The program offers short-term economic assistance in exchange for employment that is intended to enhance the restoration of fish-friendly habitats. NOAA believes that this program, which enjoys widespread bipartisan support from the Northwest Congressional delegation and support among State and local officials, and representatives of the fishing industry, including affected fishermen and their families, is a model sustainable development initiative.

It should be noted that NOAA has entered into a Memorandum of Understanding (MOU) with the U.S. Department of Agriculture s Natural Resources Conservation Service (NRCS) to administer this program. The interagency cooperation between NOAA and NRCS represents the very best in seamless government. The fact that NRCS has a long tradition with private landowners, and already had in place the delivery mechanisms and administrative infrastructure to put into operation the habitat restoration jobs program, obviated the need for NOAA to establish such infrastructure. Working through local review panels in resource conservation districts, projects and personnel were selected by individuals with the most intimate knowledge and expertise of local problems and conditions. NOAA views this program as a highly successful model of not only intergovernmental/interagency coordination but also illustrative of the emphasis NEAP has placed on having decisions made at the most appropriate level of interaction, the local level.

\*\*\* CR055

Specifically, the OIG report questioned the use of NEAP habitat restoration funds on the following projects:

Grand Ronde Educational Day Park Project --

The NOAA/NRCS MOU provides for support for critical or essential habitat needs and the enhancement of the biological sustainability of anadromous species. NRCS interpreted this clause to include habitat for salmon and other salmonid species such as steelhead trout, which were present in the creek.

The purpose of the day-use park on Agency Creek is to educate Tribal members, the general public and fishermen about how the riparian zone, the stream channel and the associated watershed uplands are related to and directly affect the health of salmon and steelhead in the creek. In order to improve the salmonid resource in this area, the grant review team felt it was important to provide an example of a healthy stream for salmon. The site of the day use park on Agency Creek has most of the components of a healthy stream. It has large conifers, multiple channels in the stream with scattered small log-jams, connected back water channels providing high water shelter for fish and some adjacent mature forested uplands. Visitors will have an opportunity to take a self-guided walking tour with strategically placed signs offering explanations of the importance of habitat to anadromous species.

We note that the fishermen on this project learned about the importance of planting trees, instream structures and riparian zones in restoring critical salmon habitat. In building the park, the fishermen helped design the foot bridges, the picnic tables and built these structures from scratch. Those are skills that can easily be transferred to other jobs in construction, tree planting crews, and park/trail construction and maintenance.

Public Outreach and Education Projects in Humboldt, Del Norte and Mendocino Counties --

The other finding contained in the OIG report involving the habitat restoration jobs program concerns the funding of three public outreach and education projects located in Humboldt, Del Norte, and Mendocino Counties. The total cost of these projects was \$75,600. The finding is that the three projects are duplicative and excessive.

NOAA believes all three projects were worthwhile and necessary to conduct the outreach activities vital to NEAP's conservation goals. The primary purpose of the landowner outreach effort is to educate landowners on the causes for the decline of salmon habitat, the resulting loss of fisheries values, and most

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important, what can be done to protect and restore these habitats. This activity is of critical importance since many landowners do not fully understand the needs of salmon and how habitat values are directly related in many cases to the land uses occurring within the watershed. The three counties in which the programs were Focated involve many small towns, disparate fighing populations, and diverse habitat restoration projects. The funds spent were not excessive; rather, they enabled NOAA to reach as many affected salmon fishermen as possible, and facilitated efficient management and completion of the projects.

#### 2. DATA COLLECTION JOBS PROGRAM

To date, it is estimated that the Data Collection Jobs Program, which is administered throughout the region by the Pacific States Marine Fisheries Commission (PSMFC), is expected to create 312 jobs. The OIG report identifies 2 of 14 projects, totaling \$276,000, under this program which did not benefit the salmon fishery resource. NOAA believes that both projects met the NEAP criteria.

Columbia River Sturgeon Tagging Study --

In response to the OIG comments questioning this study, we note that the entire Northwest commercial sturgeon fishery occurs as a companion catch in the Columbia River and Willapa Bay Salmon Gillnet fisheries. The two relevant fishery management plans consider these two species as a single management unit. The Columbia River fishery predominates over Willapa Bay and Grays Harbor, Washington fisheries. The Salmon Gillnet fishery and its companion sturgeon catch in the Columbia River are managed by the Columbia River Interstate Compact and the Washington fisheries by WDFW.

The Columbia River Compact sets both tribal and non-tribal fisheries for salmon and sturgeon on the Columbia River. The Compact includes the states of Washington and Oregon who set the fishery. The Compact has a Technical Advisory Committee (TAC) that makes recommendations to the Compact regarding seasons and harvest quotas. The TAC includes scientists from the Columbia River Tribes and Idaho Department of Fish and Game as well as biologists from Washington and Oregon Fish and Wildlife Departments.

The salmon fishery and gear regulations (related to mesh size of the nets) is directly related to the allowable sturgeon harvest determined from population studies from sturgeon tagging and recoveries. As an extreme, if there are uncertainties relating to the sturgeon populations size and age class structure, there is either a very restricted salmon fishery or no fishery or the

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salmon fishery may be closed prematurely. The sturgeon and salmon in the Columbia River are managed as a unit. Good population data is needed from both species for the fishery to be well managed and stocks of both protected. Extensive tagging of salmon is an ongoing task along the entire Pacific coast including Canada. -However, limited tagging has been undertaken the last couple of years on sturgeon.

This study provided additional sturgeon tagging information to support better management and stock rebuilding of salmon and protection for sturgeon for more viable fisheries in the future. The opportunity to fund this needed research on the Columbia using salmon gillnet fishermen and their gillnet gear provided economic relief to the greatly impacted Salmon Gillnet fishermen of the Columbia River. Gillnets are the only viable method to collect large quantities of live sturgeon for tagging in an efficient manner. No other planned studies necessitates this type of gear to do needed stock research. In addition, it provides important scientific data for better management and protection of their fishery and fish stocks. For these reasons, this project directly meets the criteria of the NEAP and provides the only opportunity for relief to the Gillnet fishermen that allows them to use their boats and gear in one of the Data Collection Projects.

Nearshore Rockfish and Lingcod Study --

The salmon charterboat industry can impact the health of rockfish stocks, particularly nearshore rockfish. Curtailments in salmon harvest and/or availability, or lack of fishing success for salmon on a particular trip can result in increased effort on rockfish stocks. When salmon seasons are closed, rockfish charterboat trips provide some income for salmon charterboats, but they may also result in increased effort on and catch of these rockfish stocks. Private boat effort also impacts rockfish stocks for this large complex of long-lived species.

This nearshore rockfish and lingcod study provided opportunities for salmon fishermen to work with the state of California Department of Fish and Game in tagging nearshore rockfish to provide better information on rockfish population sized, age class structure and recruitment to the fishery. This information is important in determining the economic impact to salmon fishermen and coastal communities when setting salmon seasons, size limits and bag limits.

The actions in the salmon fishery can be tempered by opportunities for rockfish catch by sport anglers or may also be detrimental to rockfish from increased effort on depressed stocks. This study was designed to assist the state in gathering

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this needed data on rockfish with a planned five-year study that will be funded in the last three years by the state. Salmon fishermen trained in performing this work may have opportunities to continue with work after the current NEAP program. This project was also selected in order to provide work opportunities in California.

With the limited funds made available to California, larger atsea studies were too expensive to be undertaken. In addition, the Pacific Coast salmon resources are comprised of multiple intermixed stocks that range from California to Alaska. The fisheries and problems are regional in nature and not just restricted to state boundaries. The Pacific States Marine Fisheries Commission (PSMFS) approach to the Data Collection Jobs Program was regional and tempered with a desire to not duplicate projects off each state waters, especially when the study findings would be applicable coastwide. PSMFC also did not want to incur the large cost for duplicative studies as to gear and platforms if there would not be differences in the data collected in different areas.

Thus, the rockfish studies off Northern California are related to salmon fisheries and the impacts of salmon management. In addition, they provide opportunities locally for employment of salmon fishermen in affordable projects that directed a majority of the money to salmon fishermen and did not try to unnecessarily duplicate studies being conducted just north off the Oregon coast.

#### OIG Recommendation:

That the Deputy Under Secretary for Oceans and Atmosphere require NOAA to revise project funding criteria to ensure that habitat and data collection projects comply with the requirements of the Interjurisdictional Fisheries Act and the Secretary's Disaster Declaration.

NOAA Action: While NOAA recognizes and appreciates the questions raised by the OIG with respect to these projects, the Agency relies upon the expertise of local officials in the selection of projects to determine whether projects are within the guidelines established for the Program. NOAA is satisfied that the specified projects identified in the OIG report are consistent with the NEAP guidelines. However, if there are future NEAP Programs, NOAA will be careful to monitor these programs. to

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ensure consistency with NEAP goals. In addition, should future funding be made available for these programs, NOAA will take special care, in light of the concerns expressed in the OIG report, to ensure that the programs are in compliance with the appropriate statutory authority and the Secretary's Disaster Declaration.

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U.S. DEPARTMENT OF COMMERCE Office of Inspector General



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# **BUREAU OF INDUSTRY AND SECURITY**

## Annual Follow-Up Report on Previous Export Control Recommendations, as Mandated by the National Defense Authorization Act for Fiscal Year 2000

Final Inspection Report No. IPE-17361/March 2005

Office of Inspections and Program Evaluations



UNITED STATES DEPARTMENT OF COMMERCE The Inspector General Washington, D.C. 20230

March 30, 2005

## FOR OFFICIAL USE ONLY (With Attachment)

## **MEMORANDUM FOR:**

Peter Lichtenbaum Acting Under Secretary for Industry and Security

Mark Foulon Deputy Under Secretary for Industry and Security

FROM:

Johnnie E. Frazier Annual Follow-Up Report on Previous Export Contr

Annual Follow-Up Report on Previous-Export Control Recommendations, as Mandated by the National Defense Authorization Act for Fiscal Year 2000, as Amended (IPE-17361)

This is our annual report on the status of open recommendations from our prior reviews conducted in accordance with the National Defense Authorization Act (NDAA) for Fiscal Year 2000, as amended. As such, this report covers the (1) March 2001 report, *Management of the Commerce Control List and Related Processes Should be Improved* (IPE-13744), (2) February 2002 report, *BXA Needs to Strengthen its ECASS Modernization Efforts to Ensure Long-Term Success of the Project* (IPE-14270), (3) March 2003 report, *Improvements Are Needed to Better Enforce Dual-Use Export Control Laws* (IPE-15155), and (4) March 2004 report, *Deemed Export Controls May Not Stop the Transfer of Sensitive Technology to Foreign Nationals in the U.S.* (IPE-16176). A summary of the observations and conclusions from all of our NDAA reports, including those listed above, is outlined in the attachment to this report.

While the Bureau of Industry and Security<sup>1</sup> has taken corrective actions on some of the recommendations from our March 2004 report, many key recommendations remain open from that report as well as from our February 2002 report (and subsequent March 2002 interagency report on the same topic).<sup>2</sup> In addition, a few recommendations from our March 2003 and March 2001 reports still remain open. All recommendations from our March 2000 report are closed. Please note that the attachment discusses in detail the actions BIS has taken to implement our recommendations from these reports since the issuance of our last annual follow-up report.

We are encouraged by the level of commitment BIS has recently placed on the administration of deemed export controls. We believe the attention this topic has received from all parties involved—including the academic and federal research communities—since issuance of our 2004 deemed exports report will enable BIS to better focus on how to more effectively prevent the transfer of sensitive technology to foreign nationals from countries or entities of concern while they are in the United States.



The Bureau of Industry and Security was formerly known as the Bureau of Export Administration.

**SUBJECT:** 

<sup>&</sup>lt;sup>2</sup> Interagency Review of Federal Automated Export Licensing Systems, Report No. D-2002-074, March 2002. TOF COMMERC

We request that BIS officials provide an updated response and action plan within 60 calendar days for those recommendations that we still consider to be open. If you would like to discuss this report, please call me at (202) 482-4661, or Jill Gross, Assistant Inspector General for Inspections and Program Evaluations, at (202) 482-2754.

#### BACKGROUND

The House and Senate Armed Services Committees, through the NDAA for FY 2000, as amended, directed the Inspectors General of the Departments of Commerce, Defense, Energy, and State, in consultation with the Director of Central Intelligence and the Director of the Federal Bureau of Investigation, to conduct an annual assessment of the adequacy of current export controls and counterintelligence measures to prevent the acquisition of sensitive U.S. technology and technical information by countries and entities of concern.<sup>3</sup> The Offices of Inspector General (OIGs) are required to report to the Congress no later than March 30 of each year from 2000 to 2007. In addition, the legislation requires the OIGs to include in their annual report the status or disposition of recommendations made in earlier reports submitted in accordance with the act.

The United States controls the export of dual-use commodities—equipment and technologies that have both military and civilian applications—for reasons of national security and foreign policy (including antiterrorism) under the authority of several different laws. The primary legislative authority for controlling the export of dual-use commodities is the Export Administration Act of 1979, as amended.<sup>4</sup> Under the act, BIS administers the Export Administration Regulations (EAR) by developing export control policies, issuing export licenses, and enforcing the laws and regulations for dual-use exports.

To comply with the first-year requirement of the NDAA for FY 2000, the OIGs agreed to conduct an interagency review of selected aspects of (1) federal agencies' (including research facilities') compliance with the "deemed export"<sup>5</sup> regulations and (2) U.S. government efforts to help prevent the illicit transfer of U.S. technology and technical information through select intelligence, counterintelligence, foreign investment reporting, and enforcement activities.<sup>6</sup> To meet the act's

<sup>&</sup>lt;sup>3</sup> Public Law 106-65, October 5, 1999.

<sup>&</sup>lt;sup>4</sup> Export Administration Act of 1979, as amended, sec. 3; 50 U.S.C app. sec. 2402(2). Although the Act expired on August 20, 2001, the Congress agreed to the President's request to extend existing export regulations under Executive Order 13222, dated August 17, 2001, thereby invoking emergency authority under the International Emergency Economic Powers Act.

<sup>&</sup>lt;sup>5</sup>According to the EAR, any release to a foreign national of technology or software subject to the regulations is deemed to be an export to the home country of the foreign national. These exports are commonly referred to as "deemed exports," and may involve the transfer of sensitive technology to foreign visitors or workers at U.S. research laboratories and private companies.

<sup>&</sup>lt;sup>6</sup>Because the NDAA was not enacted until October 1999, we were not able to conduct a comprehensive assessment of BIS' export enforcement activities by the March 30, 2000, deadline. However, as part of the 2003 interagency OIG review, we reviewed BIS' export enforcement activities.

| U.S. Department of Commerce | Final Report IPE-17361 |
|-----------------------------|------------------------|
| Office of Inspector General | March 2005             |

second-year requirement, the OIGs focused on the Commerce Control List,<sup>7</sup> which is maintained by BIS, and the U.S. Munitions List, which is maintained by the State Department. The Commerce review looked at BIS' policies and procedures for the design, maintenance, and application of the Commerce Control List.

For 2002, the OIGs agreed to conduct an interagency review of the various automated export licensing systems maintained or under development by the federal licensing agencies—to determine how the systems interact and whether it is feasible to develop a single federal automated export licensing network or other alternatives to facilitate systems integration. Each OIG also looked at its own agency's efforts to modernize its export licensing system. Our focus at the Commerce Department was to assess BIS' efforts to modernize its Export Control Automated Support System (ECASS).

For 2003, the Inspectors General agreed to conduct an interagency review of the federal government's enforcement of export controls for both dual-use items and munitions. Each OIG also examined its own agency's efforts to enforce these controls. Our review at Commerce focused on BIS' export enforcement program, including its efforts to prevent the illegal export of dual-use items and to investigate and assist in the prosecution of violators of the EAR.

To meet the act's fifth-year requirement, the OIGs agreed to conduct an interagency review of the federal government's deemed export control laws and regulations. Each OIG also examined its own agency's efforts to prevent the transfer of controlled U.S. technologies and technical information to foreign nationals from countries and entities and concern. The Commerce review assessed how effectively the dual-use deemed export regulations and policies, as implemented by BIS, prevent such transfer, and whether U.S. industry and academic institutions are complying with the regulations. As a part of this effort, we followed up on prior OIG recommendations related to deemed exports at two of Commerce's scientific agencies—the National Institute of Standards and Technology (NIST) and the National Oceanic and Atmospheric Administration (NOAA). We also worked with the Department's Office of Security (OSY) regarding potential security vulnerabilities associated with foreign national access to departmental facilities.

<sup>&</sup>lt;sup>7</sup> The Commerce Control List contains items subject to control under the EAR. The list specifies the commodities, software, and technology that are subject to the regulations, as well as what controls are placed on these items, depending on the country to which the items are to be exported.

### **OBJECTIVES, SCOPE, AND METHODOLOGY**

The primary objective of our review was to follow up on actions taken by BIS, and other applicable Commerce bureaus, to implement the open recommendations contained in our 2001, 2002, 2003, and 2004 export control reports. To meet our objective, we spoke with various BIS officials, including senior managers, licensing and enforcement officials, as well as officials from Commerce's NIST, NOAA, and OSY. We also reviewed supporting documentation to verify that the actions reportedly taken by these agencies were sufficient to implement our recommendations.

#### **OBSERVATIONS AND CONCLUSIONS**

Table one summarizes the number of remaining open recommendations from each of the individual inspection reports. The attachment to this report includes a detailed description of the individual open recommendations and the OIG status report on them.

| Report Title                            | Action<br>Agency | Total # of<br>Recommendations | # Closed<br>Prior to this<br>Reporting<br>Period | # Closed<br>During this<br>Reporting<br>Period | # Open |
|---|------------------|-------------------------------|--|--|--------|
| Deemed Export                           | BIS              | 7                             | 0  | 2  | 5      |
| Controls May Not                        | NIST             | 7                             | 0  | 3  | 4      |
| Stop the Transfer                       | NOAA             | 5                             | 0  | 0  | 5      |
| of Sensitive                            | OSY              | 1                             | 0  | 0  | 1      |
| Technology to                           |                  |                               |  |  |        |
| Foreign Nationals                       |                  |                               |  |  |        |
| <i>in the U.S.</i><br>(IPE-16176, March |                  |                               |  |  |        |
| 2004)                                   |                  |                               |  |  |        |
| Improvements Are                        | BIS              | 55                            | 36   | 13   | 6      |
| Needed to Better                        | ITA              | 4                             | 4  | 0  | 0      |
| Enforce Dual-Use                        |                  | -                             |  |  |        |
| Export Control                          |                  |                               |  |  |        |
| Laws                                    |                  |                               |  |  |        |
| (IPE-15155,                             |                  |                               |  |  |        |
| March 2003)                             |                  | 10                            |  |  |        |
| BXA Needs to                            | BIS              | 13                            | 8*   | 1  | 4      |
| Strengthen Its                          |                  |                               |  |  |        |
| ECASS<br>Modernization                  |                  |                               |  |  |        |
| Modernization<br>Efforts to Ensure      |                  |                               |  |  |        |
| Lijoris to Ensure<br>Long-Term          |                  |                               |  |  |        |
| Success of the                          |                  |                               |  |  |        |
| Project                                 |                  |                               |  |  |        |
| (IPE-14270,                             |                  |                               |  |  |        |
| February 2002)                          |                  |                               |  |  |        |
| Interagency Review                      | BIS              | 4                             | 1  | 0  | 3      |
| of Federal                              |                  |                               |  |  |        |
| Automated Export                        |                  |                               |  |  |        |
| Licensing Systems                       |                  |                               |  |  |        |
| (D-2002-074,<br>March 2002)             |                  | <i>i</i>                      |  |  |        |
| Management of                           | BIS              | 14                            | 10   | 2  | 2      |
| Commerce Control                        | 610              | 14                            | 10   | 2  | 2      |
| List and Related                        |                  |                               |  |  |        |
| Processes Should                        |                  |                               |  |  |        |
| be Improved                             |                  |                               |  |  |        |
| (IPE-13744,                             |                  |                               |  |  |        |
| March 2001)                             |                  |                               |  |  |        |
|   |                  |                               |  |  |        |

## Table 1: Status of Open Recommendations in OIG 2000-2004 Reports on Export Controls

| Improvements Are           | BIS  | 22 | 22** | 0 | 0 |
|----------------------------|------|----|------|---|---|
| Needed in                  | ITA  | 1  | 1    | 0 | 0 |
| Programs                   | NIST | 6  | 6    | 0 | 0 |
| <b>Designed to Protect</b> | NOAA | 5  | 5**  | 0 | 0 |
| Against the                |      | -  | -    |   |   |
| Transfer of                |      |    |      |   |   |
| Sensitive                  |      |    |      |   |   |
| Technologies to            |      |    |      |   |   |
| Countries of               |      |    |      |   |   |
| Concern                    |      |    |      |   |   |
| (IPE-12454-1,              |      |    |      |   |   |
| March 2000)                |      |    |      |   |   |

\*Three of the recommendations were incorporated as part of the recommendations in the March 2002 interagency report. As such, we closed these recommendations from this report.

\*\*While BIS' and NOAA's actions for two of the recommendations did not fully meet the intent of our recommendations, our 2004 report readdresses these issues. As such, we closed these recommendations from the 2000 report.

#### Attachment

cc: Otto J. Wolff, Chief Financial Officer and Assistant Secretary for Administration Dr. Hratch G. Semerjian, Acting Director, National Institute of Standards and Technology Vice Admiral Conrad C. Lautenbacher, Jr, Under Secretary for Oceans and Atmosphere

#### ATTACHMENT

## SUMMARY AND STATUS OF OPEN RECOMMENDATIONS IN OIG REPORTS ON EXPORT CONTROLS ISSUED PURSUANT TO THE NATIONAL DEFENSE AUTHORIZATION ACT FOR FISCAL YEAR 2000, AS AMENDED

### (FISCAL YEARS 2000-2004)

### DEEMED EXPORT CONTROLS MAY NOT STOP THE TRANSFER OF SENSITIVE TECHNOLOGY TO FOREIGN NATIONALS IN THE U.S., IPE-16176, MARCH 2004

#### A. Summary of OIG Findings and Recommendations

During the 2004 reporting period, we conducted a review to determine whether deemed export control laws and regulations prevent the transfer of controlled U.S. technologies and technical information to foreign nationals from countries or entities of concern. We assessed how effectively the dual-use deemed export regulations and policies, as implemented by BIS, prevent such transfer, and whether U.S. industry and academic institutions are complying with the regulations. We also looked at compliance by Commerce's National Institute of Standards and Technology (NIST), National Oceanic and Atmospheric Administration (NOAA), and the Office of Security (OSY). Some of our observations from the March 2004 review were as follows:

Regulations and policies could enable foreign nationals from countries and entities of concern to access otherwise controlled technology. Some of the deemed export licensing exemptions in the Export Administration Regulations (EAR) as well as BIS' deemed export licensing policies may inadvertently affect national security, and require further examination.

**EAR exemptions eliminate a large number of foreign nationals from dual-use export controls.** As we noted in our 1999<sup>1</sup> and 2000<sup>2</sup> reports on export controls, the EAR does not require licenses for foreign nationals working with publicly available technology and software, that (1) are already published or will be published, (2) arise during or result from fundamental research, (3) are educational, or (4) are included in certain patent applications. As such, many foreign students or researchers at U.S. academic institutions and many federal research facilities are exempt from the regulations, as are foreign nationals who are permanent U.S. residents. We previously recommended that BIS work with the National

<sup>&</sup>lt;sup>1</sup> Improvements Are Needed to Meet the Export Licensing Requirements of the 21st Century, U.S. Department of Commerce Office of Inspector General, IPE-11488, June 1999.

<sup>&</sup>lt;sup>2</sup> Improvements Are Needed in Programs Designed to Protect Against the Transfer of Sensitive Technologies to Countries of Concern, U.S. Department of Commerce Office of Inspector General, IPE-12454-1, March 2000.

Security Council (NSC) to ensure that deemed export control policies and regulations are clear and devoid of any loopholes that would permit countries or entities of concern to obtain controlled U.S. equipment or technology. BIS raised this issue with the NSC in 2000, but no action has been taken.

**Confusion exists over the "use" of controlled equipment.** Confusion over the definition and implementation of controls associated with the "use" of EAR-controlled equipment by foreign nationals creates opportunities for inappropriate transfers. The EAR defines "use" as "operation, installation (including on-site installation), maintenance (checking), repair, overhaul, and refurbishing" and some BIS' licensing officials maintained that all of these activities must occur to constitute "use." While BIS normally grants approval for a foreign entity to operate, install, maintain, repair, overhaul, and refurbish a piece of controlled equipment exported from the United States in order to permit the full range of uses for an export, the same definition of use does not seem to apply to deemed exports. It is unlikely that one individual would accomplish all these tasks in most situations. In addition, two of the four multilateral control regimes<sup>3</sup> define the term either with an "or," or without any connector word (i.e., a bullet listing of the activities). The Defense Technology Security Administration notes each of the listed activities with the compound conjunction "and/or."

This difference in interpretation is critical in determining how to implement and enforce the deemed export provisions in the EAR. For instance, the U.S. academic and federal research community generally use the EAR's fundamental research exemption for most of its research. However, when controlled equipment is used by foreign nationals at a U.S. university or federal research facility it may be accompanied by a transfer of technology. Some academics believe such equipment use is exempt from export licensing requirements if the use occurs when working on fundamental research. But according to BIS, the technology for the "use" of controlled equipment is subject to the deemed export provisions regardless of whether the associated research is fundamental. This means that academic and federal laboratories might need to seek deemed export licenses for some foreign nationals working with controlled equipment or otherwise restrict their access to such equipment. We recommended that BIS modify the definition of "use" in the EAR and then inform the U.S. academic community, industry, and federal agencies on the deemed export controls associated with the technology for the use of the EAR-controlled equipment by foreign nationals.

Citizenship/residency requirements could permit unintended access. BIS' deemed export licensing policy, in contrast to State Department's, only recognizes a foreign national's most recent citizenship or permanent residency, and thus allows foreign nationals

<sup>3</sup> The United States is a member of several multilateral regimes concerned with the export of dual-use and munitions items to countries of concern. Those organizations include the Australia Group (concerned with the proliferation of chemical and biological weapons), the Missile Technology Control Regime (concerned with the proliferation of missiles capable of delivering weapons of mass destruction), the Nuclear Suppliers Group (concerned with nuclear weapons proliferation), and the Wassenaar Arrangement (concerned mainly with the transfer of conventional weapons).

originally from countries of concern to obtain access to controlled dual-use technology without scrutiny if their current citizenship or permanent resident status is with a country not subject to the controls. We recommended that BIS amend its policy to require U.S. entities to apply for a deemed export license for employees or visitors who are foreign nationals and have access to dual-use controlled technology if they were born in a country where the technology transfer in question is EAR-controlled regardless of their most recent citizenship or permanent resident status (unless they are U.S. citizens or permanent residents).

**BIS' approval of licenses is inconsistent with EAR policies**. Despite a general policy of denial for exports to certain terrorist-supporting countries, BIS approved 78 of 107 deemed export license applications (73 percent) involving foreign nationals from Iran (76) and Iraq (2)<sup>4</sup> between FYs 2000-2003. BIS officials informed us that its justification for approving such licenses was based on a 1997 BIS legal opinion stating that deemed export licenses are permissible for foreign nationals from Iran and Iraq because the laws prohibiting "exports" to those two countries did not apply to their respective nationals. However, we were concerned that BIS' legal opinion did not specifically address the concept of deemed export controls and recommended that BIS reevaluate its approval of deemed export licenses for foreign nationals from Iran and Iraq to ensure such approvals are consistent with current deemed export control licensing policies and procedures.

- BIS could further raise awareness of deemed export control regulations by refocusing outreach and clarifying web site information. Our review found that BIS had greatly expanded its efforts to raise awareness of deemed export controls since our March 2000 report. But expanded activities in FY 2003 mainly focused on companies and industry sectors that already apply for deemed export licenses rather than those that do not. We determined that BIS needed a strategic outreach plan that targets priority industries, federal agencies, and academic institutions not currently applying for licenses. The bureau also needed to clarify and periodically update some of the EAR information available on its web site to help exporters better evaluate applicability of the regulations to their particular situation.
- BIS needs a deemed export compliance program. The EAR allows BIS to further limit a transaction authorized under an export license by placing conditions on the license itself. For instance, deemed export license conditions might state "no exposure to [Defense] contracts will be allowed" or "use of computers [above a certain threshold] must be controlled and monitored to ensure that only job-related work is performed." Placing conditions on a license provides the bureau with an additional means of monitoring certain transactions. However, BIS stated that it lacked the resources needed to adequately monitor compliance. Monitoring license conditions is an important component of ensuring that

<sup>&</sup>lt;sup>4</sup> On May 22, 2003, the United Nations Security Council issued Resolution 1483 that lifted the comprehensive United Nations trade sanctions on Iraq, while retaining restrictions on the sale or supply to Iraq of arms related material. BIS is currently in the process of preparing an amendment to the EAR to reflect Iraq's significantly changed status.

licenses are used as authorized. A company's failure to comply with license conditions should be a factor in the interagency review of future license applications for that company.

Deemed export control compliance by Commerce Bureaus is mixed. As part of our review, we followed up on recommendations made to the National Institute of Standards and Technology (NIST) and the National Oceanic and Atmospheric Administration (NOAA) in our March 2000 review regarding their compliance with deemed export control licensing for foreign national visitors.

### <u>NIST</u>

NIST had instituted a policy to regulate foreign national access to controlled technologies after our March 2000 review, and provided deemed export control training to employees. Though NIST maintained that the majority of its research was fundamental and, therefore, exempted from deemed export controls, we learned that agency officials were unaware that technology for the "use" of controlled equipment during the conduct of fundamental research by foreign nationals was still subject to the EAR.

During our 2004 survey work, we identified at least one EAR-controlled commodity at a NIST facility that may have been accessible to foreign nationals. Because NIST was unsure of what other EAR-controlled equipment may be housed at its facilities, we recommended that NIST (1) review the equipment on hand in the labs to identify EAR-controlled equipment, (2) interview managers of labs that have controlled equipment to establish what foreign nationals (if any) use or have access to the equipment, and (3) work with BIS to develop an effective means to identify when a deemed export license might be required. In addition, NIST should provide periodic training on deemed export requirements to its employees who work with EAR-controlled technology or equipment. Finally, we noted that NIST's Editorial Review Board process—which requires a prepublication clearance for all materials to identify sensitive material—might have disqualified them from using the fundamental research exemption in the EAR. As such, we recommended that NIST work with BIS to determine if its Editorial Review Board process voids the fundamental research exemption in the EAR.

#### <u>NOAA</u>

NOAA lacked an overall deemed export control policy to effectively monitor foreign national access to controlled technology despite OIG recommendations to this effect in our March 2000 report and subsequent follow up work in this area. NOAA believed that deemed export controls for the most part did not apply to the work of its line offices because their research was primarily fundamental. Like their counterparts at NIST, however, NOAA officials were unaware that the technology for the "use" of controlled equipment during the conduct of fundamental research by foreign nationals was subject to the EAR, and the agency has since indicated that some of NOAA facilities might contain controlled equipment which foreign visitors or guest researchers might have access to. In response to our past and present concerns, NOAA began developing deemed export control policies and procedures. Like NIST, we recommended that NOAA (1) establish an employee- training program that effectively disseminates its deemed export policies and procedures, (2) review its equipment inventory to determine commodities that are EARcontrolled, (3) identify foreign nationals who have access to them, and (3) work with BIS to develop any needed controls and determine when a deemed export license may be required. Finally, we recommended that NOAA review its research and NOAA-sponsored research to determine the applicability of deemed export controls.

In addition, given the potential security vulnerabilities identified at these two Commerce bureaus, we recommended that the Department's Office of Security enforce—including conducting periodic on-site security reviews—its security policies related to foreign national visitors or guest researchers in Commerce facilities and hold these bureaus accountable.

## B. Status of OIG Recommendations

### **Recommendations for BIS**

1. Modify the definition of "use" in the EAR in order to help licensing and enforcement officials better implement and enforce deemed export controls associated with the technology for the use of controlled equipment.

**Status: Open.** In its February 2005 action plan, BIS stated that it would circulate a draft proposed rule to the Departments of Defense and State in March 2005 for their review and clearance. During this same timeframe, BIS also intends to seek public comment on the draft proposed rule change. According to BIS, the draft proposed rule would clarify the definition of "use" technology by replacing the word "and" with the word "or." BIS anticipates having a new definition in place by the end of the calendar year. Until the definition has been officially modified, this recommendation will remain open.

# 2. Inform the U.S. academic community, industry, and federal agencies of the deemed export controls associated with the technology for the use of EAR-controlled equipment by foreign nationals.

Status: Closed. BIS created a new presentation addressing the issue of technology associated with equipment used to conduct research (including fundamental research). In addition, since issuance of our March 2004 report, BIS has held a number of meetings with government (including federal laboratory) and academic officials as well as conducted site visits at four leading U.S. academic institutions to discuss this issue. BIS officials have also reportedly participated in various academic association meetings and conducted telephone reviews of research technology with various academic and federal laboratory officials. While we believe BIS has met the intent of our recommendation, we encourage it to continue its outreach efforts in the area. Accordingly, this recommendation is closed.

# 3. Amend BIS' current policy to require U.S. entities to apply for a deemed export license when a foreign national employee or visitor was born in a country where the technology transfer in question is EAR-controlled.

**Status: Open.** According to its February 2005 action plan, BIS has been conducting an internal review with the Office of the Chief Counsel for Industry and Security and the Regulations Policy Division to determine whether there are any legal impediments or any inappropriate policy outcomes that should be considered if it were to modify the current deemed export policy which exempts foreign nationals from deemed export licensing requirements based on the country of their most recent citizenship or legal permanent residence. In addition, BIS stated that it has initiated discussions with representatives of the Technical Advisory Committees<sup>5</sup> to determine what if any impact there would be on industry if it modified the current policy. While BIS originally indicated it would have a decision on this matter by March 2005, the current Acting Under Secretary for Industry and Security informed us that it would take additional time to make a decision. As such, this recommendation will remain open until BIS completes its review and amends the current policy or provides justification as to why a policy change is not warranted for dual-use export controls.

# 4. Reevaluate its approval of deemed export licenses for foreign nationals from Iran and Iraq to ensure such approvals are consistent with current law and deemed export control licensing policies and procedures.

**Status: Open.** As set forth in the July 30, 2004 amendment of the EAR regarding exports to Iraq, there is no longer a general policy of denial for exports to Iraq. Therefore, our recommendation concerning BIS' deemed export licensing policy for Iraqi nationals is no longer valid. With regard to BIS' deemed export licensing policy for Iranian nationals, BIS stated in its February 2005 action plan that no amendment to the EAR is warranted. However, based on a follow-up meeting in late February 2005 with the current Acting Under Secretary for Industry and Security, BIS has agreed to update the regulations to ensure consistency with BIS' current deemed export licensing policies and procedures for Iranian nationals. Until the regulations have been amended to reflect this change, this recommendation will remain open.

<sup>&</sup>lt;sup>5</sup> The Technical Advisory Committees advise the Department of Commerce on the technical parameters for export controls applicable to dual-use commodities and technology and on the administration of those controls. The committees are composed of representatives from industry and government representing diverse points of view on the concerns of the exporting community.

# 5. Establish and implement a strategic outreach plan for deemed exports that has annual goals and identifies priority industries, federal agencies, and academic institutions that are not currently applying for deemed export licenses.

**Status:** Closed. BIS established a strategic outreach plan outlining its deemed export outreach objectives for FY 2005. While BIS plans to continue to conduct outreach to industry, federal research facilities, and the academic community, one of its main outreach efforts for FY 2005 is a cooperative effort with the Department of Homeland Security's U.S. Citizenship and Immigration Services (CIS). According to BIS, CIS is planning to require applicants for an H-1 visa<sup>6</sup> to validate they are in compliance with the deemed export rule beginning in April 2005. BIS also reported that CIS reviewed 300,000 H-1 visa petitions in FY 2004. Based on these numbers, BIS believes this effort will result in a significant increase in both outreach and compliance with the deemed export program.

In addition, BIS plans to develop a new link within the BIS website to specifically target universities. Some of the items to be included are (1) BIS' general deemed export presentations, (2) OIG recommendations in this area and BIS' responses, (3) a template example with a step-by-step analysis to evaluate controlled equipment and technology, and (4) questions and answers addressing specific concerns raised in letters to BIS from the academic and research community. Other deemed export outreach objectives include (1) creating two special export control training sessions in Washington, D.C. targeted at universities, (2) establishing an ongoing dialogue with the key academic associations (e.g., Council of Governmental Relations, Association of American Universities, and the National Council of University Research Administrators), and (3) visiting many of the university campuses where the Office of Inspector General visited during its review. Accordingly, BIS' actions and/or proposed actions meet the intent of our recommendation.

# 6. Clarify and periodically update the deemed export "Questions and Answers" in Supplement No. 1 to Part 734 of the EAR.

**Status: Open.** According to its February 2005 action plan, BIS plans to revise the relevant "Questions and Answers" in Supplement No. 1 to Part 734 of the EAR once it completes its review of the policy issues discussed in recommendations one and three above. Until BIS updates the deemed export Questions and Answers, this recommendation will remain open.

<sup>&</sup>lt;sup>6</sup> The H-1 Work Visa is a temporary permit for an alien to work in the United States. The H-1 is initially granted for a period of up to three years, with subsequent renewals possible. The total time that an alien can remain employed under an H-1 Visa is restricted to a maximum of six years.

- 7. Develop a compliance program that effectively evaluates deemed export license holders' compliance with license conditions. At a minimum, the review should determine whether:
  - a. All research, including access to technology, is being performed in accordance with license conditions;
  - b. Deviations to the foreign national's job responsibilities stay within the technical parameters of the license; and,
  - c. The technology control plan used by the subject U.S. entity accurately and fully reflects its practices.

**Status: Open.** According to its February 2005 action plan, BIS has identified four end-use checks to be conducted during FY 2005. Two are to be conducted in the Washington, D.C. metropolitan area by May 31, 2005. The other two end-use checks are to be conducted on the west coast during the third quarter of FY 2005. According to BIS officials, the checks will be conducted by both export enforcement agents and licensing officers. While we are encouraged that BIS is preparing to pilot an end-use check program for deemed exports, this recommendation will remain open until BIS fully implements a deemed export compliance program.

#### **Recommendations for NIST**

1. Review NIST's equipment on hand in the labs to identify EAR-controlled equipment, interview managers of labs that have controlled equipment to establish what foreign nationals (if any) use or have access to the equipment, and work with BIS to develop an effective means to identify when a deemed export license might be required.

**Status: Open.** According to its January 2005 action plan, the NIST Operations Board, comprising the NIST Operating Unit Deputy Directors, and with support of the NIST Counsel, held a series of meetings to fully understand the deemed export licensing requirements. Subsequent to these meetings, NIST reported that each Operating Unit (1) conducted a review of all equipment on hand in the laboratories to identify all EAR-controlled equipment, (2) inventoried all EAR-controlled equipment, and (3) implemented appropriate documentation and controls. As a result, NIST reportedly identified 120 pieces of EAR-controlled equipment. Furthermore, the NIST Counsel worked with BIS to develop means to identify when an export license is required. Subsequent guidance was developed from these discussions and the NIST Operations Board approved it on January 18, 2005.

As a part of this effort, NIST developed an "Export Control Procedures" form to be used for each piece of EAR-controlled equipment. The form contains fields to describe: (1) what is the type and description of the equipment, (2) location of the equipment, (3) name(s) of individual(s) who is responsible for the equipment, (4) who is allowed access to the equipment, (5) what EAR controls and restrictions exist for the equipment, (6) what type of physical security is in place for the equipment, and (7) what type of export control awareness and/or training have the operators of the equipment been given, among other things. Once the form is completed, the Chief, Emergency Services Division, is required to inspect each piece of equipment and verify the information on the form.

We are pleased with the actions NIST has taken to date to implement this recommendation. While NIST informed us that it has inspected most of the EAR-controlled equipment at its Gaithersburg, Maryland, facility, none of the EAR- controlled equipment has been inspected at its Boulder, Colorado, facility. NIST anticipates completing all of its inspections in April 2005. Until NIST has completed its security inspection of the identified EAR-controlled equipment to ensure that access controls are in place, this recommendation will remain open.

# 2. Conduct periodic deemed export control training, including coverage of the transfer of technology associated with the "use" of controlled equipment, for all NIST employees that work with EAR-controlled technology and/or equipment.

**Status: Closed.** According to its January 2005 action plan, the NIST Counsel conducted training sessions for Group Leaders and Division Chiefs at both Gaithersburg and Boulder (via video conferencing) facilities in the summer of 2004 that included a detailed explanation of the EAR and deemed exports. Four additional training sessions were conducted in March 2005 to reiterate deemed export controls as well as to discuss NIST's new "upfront" review procedures to determine if individual research projects fall under deemed export control regulations or contain sensitive homeland security information (see discussion in recommendation three below for more detail). In addition, and as mentioned above, each employee that has access to EAR-controlled equipment is required to understand what the deemed export control training sessions NIST has held to date and encourage NIST to continue periodic deemed export control training in the future. NIST's actions meet the intent of our recommendation.

# 3. Ensure that NIST management reviews the subject of NIST research "upfront" to determine its sensitivity and applicability to deemed export controls.

**Status: Open.** NIST has developed a policy calling for management review of all research projects on at least an annual basis to determine whether the research may be freely published or should be controlled for export control and/or homeland security purposes. Specifically, NIST's January 2005 policy calls for up-front reviews to be included as part of the performance planning and review process for each researcher. According to NIST's Counsel, supervisor's decisions are to be documented in each employee's performance management record at the beginning of the year, at the midpoint review, and at the end of year review. The new process calls for supervisors to make case-by-case decisions about the research being conducted in their group or division. NIST officials informed us that this process has been fully implemented by NIST, this recommendation will remain open.

# 4. Work with BIS to determine if NIST's Editorial Review Board process voids the fundamental research exemption in the EAR and seek appropriate deemed export licenses, as necessary.

Status: Closed. This recommendation is superseded by the action discussed in recommendation three above. Accordingly, this recommendation is closed.

# 5. Adhere to departmental policy regarding vetting foreign national visitors and guest researchers before allowing them access to its facilities.

**Status: Open.** NIST officials informed us that NIST would comply with the new departmental policy relating to foreign national access once it is finalized. In the interim, NIST continues to submit names of its long-term foreign national visitors and guest researchers to OSY for background checks. However, it is currently not submitting the names of its short-term visitors. While we acknowledge that OSY is currently in the process of revising its guidance in this area, we want to remind NIST that all Commerce bureaus should continue to abide by the current departmental policy. Specifically, with the exception of foreign nationals attending public conferences, departmental policy states that foreign nationals may not be cleared to visit or work at a departmental facility without the approval of the servicing security officer.<sup>7</sup> Until NIST begins to vet all such foreign national visitors, this recommendation will remain open.

# 6. Install card readers between different laboratories to prevent foreign national guest researchers assigned to one lab from entering laboratories to which they are not assigned.

**Status: Open.** Since issuance of our March 2004 report, NIST has upgraded various security features at its Gaithersburg, Maryland, facility (e.g., a key card is now required to access all floors higher than the main level in the administration building via the elevator or the two applicable stairwells). With the exception of NIST's newest facility—the Advanced Measurement Laboratory—all of NIST's buildings are reportedly controlled from the outside via card readers. According to NIST's Chief of Emergency Services Division, there is only one building on the "spine" that interconnects NIST's 15 general-purpose lab buildings (including the Administration building) that is also protected via card readers within the tunnel system. Essentially, NIST officials indicated that (1) they have secured EAR-controlled equipment by other means (see recommendation seven below for more detail) and (2) it would be cost prohibitive to install card readers between every laboratory.

With regard to the Advanced Measurement Laboratory, we want to note that while the outside doors to the main entrance currently do not have any type of security controls (e.g. locks, key card readers) due to their design, NIST is currently in the process of

<sup>&</sup>lt;sup>7</sup> U.S. Department of Commerce, Manual of Security Policies and Procedures, Section II – Personnel Security, Chapter 16: Foreign National Visitor Access to Departmental Facilities and Activities, April 4, 2003: 16.1.

replacing these doors and installing card readers. In addition, while the side doors to this facility have a regular key lock on them, NIST does not lock them because the researchers who work in this facility do not have keys. However, NIST reports that card readers are currently being installed on all outside doors to this facility and the anticipated completion date for this activity is scheduled for April 2005. While NIST's actions partially meet the intent of our recommendation, this recommendation will remain open until the Advanced Measurement Laboratory is secure from the outside.

# 7. Consider installing additional card readers within laboratories, as appropriate, to safeguard EAR-controlled equipment.

**Status: Closed.** Since issuance of our March 2004 report, NIST reportedly identified and inventoried its EAR-controlled equipment. Based on this inventory, NIST's Security Officer worked with the equipment's "owners" to identify appropriate and cost-effective physical security safeguards to meet all legal and regulatory requirements. As a result, NIST installed additional card readers at some appropriate locations. In those areas that NIST determined it was cost prohibitive to install card readers, it installed regular or cipher locks or vibration controls to safeguard EAR-controlled equipment from unauthorized foreign national access. NIST's actions meet the intent of our recommendations. Accordingly, this recommendation is closed.

### **Recommendations for NOAA**

# 1. Create and implement agency-wide export control policies and procedures relating to foreign national access to EAR-controlled technology.

**Status: Open.** Since issuance of our March 2004 report, NOAA has developed a draft NOAA Administrative Order (NAO) on Foreign National Access. While the current draft NAO addresses deemed export control matters and access thereto, NOAA recognizes that more work remains to be done on the more complex deemed export control issues. NOAA reported that the draft NAO incorporates comments from the department's Office of Security as well as informal comments from the OIG, however, comments have not been received from its line offices. While NOAA's March 2005 action plan stated that the final NAO would be issued in April 2005, a subsequent discussion with NOAA's Chief Administrative Officer indicated that issuance would most likely be delayed. Once NOAA issues its NAO, it will need to develop some type of mechanism and/or process for implementing it. Towards that end, the Chief Administrative Officer also informed us that he is currently trying to identify an official to be in charge of overseeing the implementation of the NAO. While NOAA's actions partially meet the intent of our recommendation, this recommendation will remain open until the NAO is finalized and a process has been established to implement it.

### 2. Review its equipment inventory to determine:

- a. What commodities are EAR-controlled.
- b. What foreign nationals have access to those commodities and whether improved access controls are needed.
- c. Whether a deemed export license may be required.

**Status: Open.** While NOAA's March 2005 action plan stated that it is waiting for additional guidance from BIS on EAR-controlled items before reviewing its personal property portfolio to ascertain what equipment may be considered EAR-controlled, NOAA's Chief Administrative Officer was not clear on what specific guidance NOAA was seeking from BIS. Towards that end, NOAA reported that insufficient staff resources and other priorities in the personal property program have prevented NOAA from making further progress on this issue. Given a year has passed since this recommendation was first made, we urge NOAA to work with BIS as well as NIST to identify an effective means for reviewing its equipment inventory to determine what commodities are EAR-controlled, what foreign nationals have access to those commodities, and whether a deemed export license may be required. Until NOAA completes its inventory review for EAR-controlled equipment, this recommendation will remain open.

## 3. Establish an employee training program that effectively disseminates the necessary deemed export control provisions to all NOAA employees that work with EAR-controlled technology and/or equipment.

**Status: Open.** According to its March 2005 action plan, NOAA stated that it would initiate a training program to ensure all stakeholders are cognizant of the responsibilities following the issuance of the NAO on foreign nationals. NOAA anticipates that the training will be completed by September 2005. Accordingly, this recommendation will remain open until NOAA establishes and implements a deemed export control training program.

## 4. Review NOAA research and NOAA-sponsored research to determine the applicability of deemed export controls.

**Status: Open.** During our meeting with NOAA's Chief Administrative Officer in March 2005, we were told that NOAA has not begun to implement this recommendation due to insufficient staff resources. As such, this recommendation will remain open until NOAA reviews its research as well as NOAA-sponsored research to determine the applicability of deemed export controls.

## 5. NOAA should formulate adequate security procedures governing visits by foreign nationals to its facilities that adhere to departmental security policy.

**Status: Open.** NOAA's draft NAO on foreign nationals includes security procedures governing visits by foreign nationals to its facilities. These draft procedures appear to be in line with pending departmental security policies covering foreign national access to Commerce facilities. As stated previously, NOAA anticipates issuance of the NAO on foreign nationals by April 2005. Until the NAO on foreign nationals is issued and implemented, this recommendation will remain open.

### **Recommendation for the Chief Financial Officer and Assistant Secretary for Administration**

# 1. Enforce—including conducting periodic on-site security reviews—the Department's security policies related to foreign national visitors or guest researchers and hold Commerce bureaus accountable for compliance with those policies.

**Status: Open**. Commerce's Office of the Chief Financial Officer and Assistant Secretary for Administration, through the Office of Security, has completed a draft Department Administrative Order (DAO) related to foreign national visitors and guest researchers. At the time of this writing, the order was with the Office of General Counsel for final review. In addition, OSY is currently developing a risk assessment program, which will include onsite assessments to mitigate risks associated with espionage. To date, OSY has conducted two pilot risk assessments but the main assessments are not scheduled to begin until June 2005. Until the DAO is finalized and OSY begins to enforce it, this recommendation will remain open.

## *IMPROVEMENTS ARE NEEDED TO BETTER ENFORCE DUAL-USE EXPORT CONTROL LAWS*, IPE-15155, MARCH 2003

### A. Summary of OIG Findings and Recommendations

During the 2003 reporting period, we completed a review of BIS' efforts to enforce export control laws. Specifically, we reviewed BIS' activities related to its (1) conduct of investigations (including agent training and the administrative remedy process); (2) interactions with the law enforcement community (e.g., U.S. Customs Service<sup>8</sup> and Federal Bureau of Investigation), the intelligence community, U.S. Postal Service, and U.S. Attorneys' Offices; (3) monitoring of license conditions; (4) outreach; and (5) end-use checks. Our report identified a number of deficiencies, several of which we had identified in our 1999 export license review. Some of our observations and conclusions from the February 2003 review were as follows:

<sup>&</sup>lt;sup>8</sup> The U.S. Customs Service transferred from the Department of the Treasury to the Department of Homeland Security in 2003. Most of its responsibilities, including those related to enforcement of export control laws, now reside in the Bureau of Immigration and Customs Enforcement.

- \* Investigative process needs greater management attention to increase criminal prosecutions and administrative sanctions. The Office of Export Enforcement (OEE) endeavors to identify, investigate, and apprehend violators of the EAR and to obtain criminal and administrative sanctions against them. We uncovered systemic weaknesses at key points in the investigative process that, cumulatively, have negatively impacted Export Enforcement's ability to achieve its mission. In FY 2002, for example, just 3 of an average yearly caseload of 1,038 cases resulted in convictions, 25 closed with administrative sanctions, and 208 were closed with warning letters-an informal action that imposes neither fines nor restrictions on export privileges but advises exporters that the warning may affect how OEE pursues any future violations. Some of the investigative weaknesses were the result of factors outside of BIS' control. For example, the bureau must rely on U.S. Attorneys to criminally prosecute its cases. We were told that some of them are reluctant to accept these cases because of their complexity, lack of jury appeal, and difficult enforceability in the absence of strong export control legislation. Regardless, we noted deficiencies in the following areas that warranted BIS' attention and improvement:
  - Case management and guidance;
  - Management oversight of the investigatory process
  - Processing of license determinations
  - The administrative remedy process
  - Collection of delinquent administrative penalties
  - Agent training, and
  - Cooperation with other federal law enforcement and intelligence agencies.
- BIS was not adequately monitoring licenses or strategically conducting outreach to U.S. exporters. The EAR allows BIS to further limit transactions and monitor shipments authorized under an export license by placing conditions on the license itself. There are 54 possible conditions, 7 of which have reporting requirements (i.e., the licensee must provide BIS with various types of documentation concerning the shipment). We found that BIS was not adequately monitoring licenses with reporting conditions—a problem we identified in our 1999 export licensing report. When license conditions are not carefully monitored, BIS cannot be certain that goods were not diverted to unauthorized end users or that exporters who fail to comply with conditions are denied subsequent licenses. In addition, we found that while BIS may contact U.S. exporters to educate them about export controls, OEE did not have a national plan for proactively identifying and conducting outreach to manufacturers and exporters of critical commodities.
- BIS should continue to improve the end-use check process. End-use checks, an important part of both the license evaluation process and enforcement process, verify the legitimacy of dual-use export transactions controlled by BIS. While our evaluation found that end-use checks are a valuable tool, we found a number of problems we identified in 1999 remain unresolved. Specifically, US&FCS officers, who conduct most of the pre-

license checks, had not received training needed to conduct effective checks—a problem made worse by BIS' failure to sometimes provide adequate product information in its formal requests for end-use checks. In addition, the end-use check handbook needed to be revised to include instructions for coordinating checks with other U.S. agencies at a particular overseas post and made available on-line to ensure that officers at post have easy access to the most recent guidance. We also found that the Safeguards Verification Program was working reasonably well. However, improvements in several areas—such as the writing and dissemination of trip reports and coordination with other U.S. agencies at a particular overseas post—would likely make the program more effective.

Export Administration's processing of license determinations for the U.S. Customs Service was untimely. The Export Administration Act allows Customs to detain a shipment for up to 20 days, after which it must formally seize or release the goods. Within this 20-day window, Customs must ascertain whether the commodity requires a valid license for export. To do this for dual-use exports, it must request a license determination from BIS. As in 1999, we found that BIS was slow to process these requests: less than 50 percent of the FY 2002 requests we examined were processed within 20 days. We also found that the determination referral process was not automated and that the two agencies had insufficient guidance on the standard procedures and format for (1) submitting license determinations requests, (2) processing them in a timely manner, and (3) providing recourse when they are late.

### **B.** Status of OIG Recommendations

### **Recommendations for BIS**

### (Case Development)

### 1. Improve case development by:

### a. Creating a task force to identify and dispose of export enforcement cases currently pending in OEE field offices that have no potential for criminal or administrative prosecution.

**Status: Closed.** Rather than a task force, the former Deputy Assistant Secretary for Export Enforcement and the applicable Special Agents-in-Charge (SAC) reportedly undertook full caseload reviews of each OEE field office to identify and dispose of export enforcement cases that had no potential for criminal or administration action. According to BIS, reviews were conducted with a view toward prioritization consonant with law enforcement policy and likelihood of prosecution. Cases opened three or more years ago were reviewed with a presumption toward closure unless they were pending for administrative or criminal enforcement. Towards this end, in FY 2004, OEE reportedly created the Export Case Emphasis List to help it prioritize its caseload to focus on the most critical cases. The list offers OEE managers the

ability to ensure agents are focusing their efforts and resources on cases involving items with potential use in chemical, biological, and/or nuclear weapons, and cases involving violations where the end-users were from nations or organizations of greatest concern. At the beginning of FY 2004, OEE had 1108 cases open. Between October 1, 2003 and June 1, 2004, OEE opened an additional 204 cases while closing 386 cases. BIS' actions meet the intent of our recommendation.

### (Case Leads)

2. Review each headquarters program

(b) (7)(E)

(b) (7)(E) designed to provide export enforcement leads in an effort to measure their success and adjust resources dedicated to these programs accordingly. This assessment should identify successful criminal and administrative cases and other outcomes, such as the issuance of warning letters and any detentions and seizures resulting from OEE investigations.

Status: Closed. BIS provided a copy of its (b)(7)(E) program assessment in August 2004. We also received a copy of Export Enforcement's assessment of its enforcement leads in October 2004. Both reviews were initiated at the end of FY 2003 and cover the two-year time period between FYs 2002 and 2003. We hope these assessments will be useful to Export Enforcement in measuring the success of these programs. BIS' actions meet the intent of our recommendation.

### (Administrative Case Processing)

5. Improve administrative case processing by:

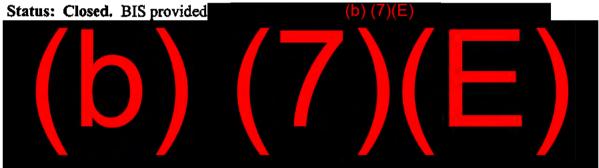
## b. Establishing a written agreement that specifies internal target dates for processing administrative cases.

Status: Closed. BIS established new administrative case procedures that were provided to the Office of Inspector General in June 2004. The new procedures include a more streamlined approach to processing administrative cases. For instance, the new guidance includes "fast track" procedures for self-disclosures as well as strict time lines for more complex cases. BIS' action meets the intent of our recommendation. 6. Strengthen OEE's up-front review procedures to ensure that administrative case reports, submitted to the Office of Chief Counsel for administrative action, comply with Special Agent Manual requirements.

Status: Closed. Export Enforcement revised its case report format and a copy was provided to the Office of Inspector General in June 2004. BIS' action meets the intent of our recommendation.

### (Collection of Administrative Penalty Payments)

7. Formulate and implement procedures for ensuring that actions are promptly taken against companies and individuals who are delinquent in paying the penalties imposed against them.



BIS' action meets the intent of our recommendation.

### (Special Agent Manual & Agent Training)

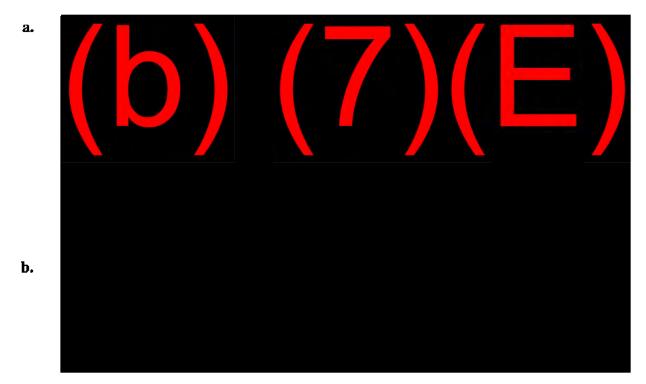
8. Strengthen the 2002 Special Agent Manual by:

## Addressing the additional weaknesses identified in the Special Agent Manual that are noted in Appendix B of this report.

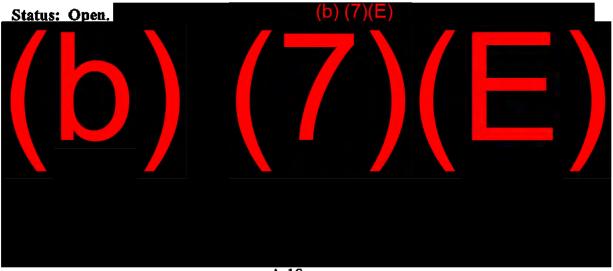
**Status:** Closed. BIS has addressed the weaknesses identified in Appendix B of the National Defense Authorization Act report on export enforcement. However, it should be noted that while Export Enforcement established written procedures for the License Determination (LD) process, we are concerned that it does not specifically explain what an LD is or how to fill one out (information which might be useful to new agents). The current Deputy Assistant Secretary for Export Enforcement believes that these procedures are sufficient given that (1) LDs are a subject area covered at Export Enforcement's annual agent training and (2) no new or junior agents are left on their own when they are first hired and that they would learn about LDs through hands on experience. Given these supplemental activities, this recommendation is closed.

### (Interagency Relationships)

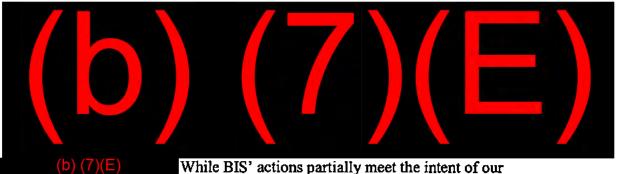
13. Improve Export Enforcement's relationship with the Central Intelligence Agency (CIA) by:



15. Work with the U.S. Postal Service to clarify the latter's appropriate role in helping prevent individuals from circumventing U.S. export control laws through the U.S. mail. As a part of that effort, increase interagency cooperation and coordination in identifying potential violations of dual-use export control laws.



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recommendation, we again reiterate our recommendation for Export Enforcement to pursue a stronger relationship with the Postal Service to increase interagency cooperation and coordination in identifying potential violations of dual-use export control laws. Accordingly, this recommendation will remain open.

### (Monitoring of License Conditions)

### 16. Improve BIS' monitoring of license conditions by taking the following actions:

a. Review Export Administration's follow-up procedures and modify, as necessary, to ensure that open licenses with reporting conditions are effectively monitored and followed up to the maximum extent practicable.

Status: Closed. To help prevent and detect the illegal export of controlled U.S. technology, BIS is charged with monitoring export licenses to ensure that license holders comply with all license conditions. As previously reported, on May 29, 2003 (amended July 8, 2003), Export Administration issued step-by-step procedures for following up on license conditions. While we support BIS' effort to issue new license condition follow-up procedures, we are concerned that the number of resources currently devoted to this activity remains constant. BIS previously stated that these resources were not sufficient to perform this follow-up work and it planned to develop a "license condition enforcement program" in FY 2005. In the interim, Export Administration assigned an additional staff member to update the current condition follow-up system. However, according to BIS' February 2005 action plan, the Congress did not approve funding for Export Enforcement's license condition unit in FY 2005. As such, Export Administration informed us that it still has two staff members assigned to work on the follow-up system. While we encourage BIS to continue with its efforts to develop a license condition enforcement program, this recommendation is closed.

<sup>&</sup>lt;sup>9</sup> The U.S. Customs Service transferred from the Department of the Treasury to the Department of Homeland Security in 2003. Most of its responsibilities, including those related to the enforcement of export control laws, now reside in the Bureau of Immigration and Customs.

### c. Ensure that licensing officers thoroughly review a company's license compliance history when processing new licenses to ensure that noncompliant exporters are not issued additional licenses.

**Status: Open.** On July 8, 2003, BIS issued a memorandum to all licensing officers, which in part, advised each officer of his/her individual responsibility for reviewing a company's prior compliance history and verifying that the exporter is in compliance with conditions on previous licenses. The guidance also outlines procedures for conducting a review of prior compliance history. In addition, according to BIS' June 2004 action plan, licensing officers notes show that licenses have not been issued because of a prior history of noncompliance. However, as a part of our current National Defense Authorization Act review of the export licensing process for chemical and biological commodities, licensing officers informed us that they were not reviewing previous license histories to determine compliance with license conditions. While BIS' actions partially meet the intent of our recommendation, this recommendation will remain open until BIS follows up to ensure that licenses are not being issued to noncompliant exporters.

d. Take the necessary actions to follow-up on open licenses with Condition 14 at least one year after they are issued to verify whether a shipment was made and initiate a Post Shipment Verification, if needed. In addition, the Office of Enforcement Analysis should ensure that expired Condition 14 licenses receive adequate monthly follow-up.

Status: Closed. The Office of Enforcement Analysis implemented procedures in October 2003 to ensure all licenses with Condition 14 are followed up on at least one year after issuance. These procedures also require follow up on all expired licenses with Condition 14 within 30 days of the date of expiration. Finally, all of the employees in the Office of Enforcement Analysis are required to recommend denial of any subsequent license application involving a party who has not complied with a previous license condition requiring the submission of shipping documents within 30 days. According to BIS, all of these matters will be referred to OEE as an investigative lead. Absent good cause and until OEE resolves all concerns about the suitability of the party to receive further valid licenses, Export Enforcement will not remove its objection to the issuance of the license. According to BIS, the Office of Enforcement Analysis has made several recommendations to deny license applications based on a company's noncompliance with licenses issued with Condition 14. As such, approval of these licenses was reportedly held up until proper documentation was received. BIS' actions meet the intent of our recommendation.

### (Outreach)

- 17. Make outreach to industry a more proactive and strategic tool by:
  - a. Establishing a national outreach plan that has annual goals and identifies priority industries to be visited across the country.

**Status: Open.** According to BIS' February 2005 action plan, Export Enforcement has redesigned its outreach program to work with Export Administration's seminars program in order to reach a broader audience. However, based on discussions with the current Deputy Assistant Secretary for Export Enforcement, export enforcement agents will also continue to conduct their own outreach visits to U.S. entities. To date, Export Enforcement does not have a written national outreach plan to guide its agents on the priority industries to be targeted for outreach. Therefore, this recommendation will remain open until Export Enforcement establishes a written national outreach plan that has annual goals and identifies priority industries to be visited across the country.

### (End-Use Checks)

- 19. Revise the guidance for the Safeguards Verification Program<sup>10</sup> and enhance the quality and timeliness of Safeguards checks conducted by agents by:
  - e. Disseminating trip reports, and any relevant analyses, in an appropriate and secure electronic format to U.S. and Foreign Commercial Service (US&FCS) posts where the Safeguards visits occurred.

**Status: Closed.** BIS updated the Safeguards Verification Program section in its *Special Agent Manual* to require Safeguards teams to submit a copy of their trip reports to the Office of Enforcement Analysis Safeguards Coordinator who will then forward a copy of the report to the pertinent US&FCS post where the visit took place. BIS previously informed us that, given the sensitive law enforcement nature of the information contained in each report, a hard copy of the report is mailed to the pertinent US&FCS post. BIS recently verified that all of the posts involved with Safeguards visit from October to December 2003 received copies of the applicable reports. In addition, all but one US&FCS post verified receiving the reports, although in two instances the posts reported that they just received them. Accordingly, this recommendation is closed.

<sup>&</sup>lt;sup>10</sup> The Safeguards Verification Program was recently renamed to the Sentinel Program.

### (Status of Unfavorable Pre-license Checks)

### 21. Institute appropriate internal controls in the Export Control Automated Support System (ECASS) to ensure that a license application cannot be returned without action over an Export Enforcement recommendation to reject.

Status: Closed. In July 2004, BIS established an internal process to be followed to reach a unified BIS position on a license application. In addition, according to its February 2005 action plan, an enhancement in ECASS has been completed so that no BIS license application with a final licensing officer determination of "return without action" and an Export Enforcement final recommendation of "reject" will be immediately validated. Instead, the system will escalate the case to the Director of the Office of Export Enforcement for subsequent resolution with Export Administration. BIS' actions meet the intent of our recommendation.

### 22. Reevaluate the guidance in the 1996 MOU concerning the return of license applications without action.

**Status:** Closed. As mentioned above, in July 2004, BIS established new procedures to be followed in reaching a unified BIS position on license applications. Specifically, if Export Administration disagrees with an Export Enforcement recommendation, Export Administration will escalate the issue for Office Director review within one business day. Export Administration and Export Enforcement Office Directors will then have two days to reach an agreed BIS position. Recommendations that are not reconciled at this level within two days will be escalated to the Deputy Assistant Secretary/Assistant Secretary level for resolution. If they cannot reach agreement, the recommendations will then be promptly escalated to the Under Secretary for final resolution. BIS' action meets the intent of our recommendation.

## 23. Notify the licensing referral agencies of all unfavorable pre-license check results and any subsequent BIS recommendation to return the relevant license application without action.

**Status: Open.** According to its February 2005 action plan, BIS is working to provide access to all interagency partners to the secure BIS network. On this network is a searchable database of scanned pre-license check cables, which will allow interagency representatives to access negative results. Until this access is provided to the interagency partners, the Office of Enforcement Analysis implemented a procedure in January 2005 whereby its analysts forward a copy of all unfavorable pre-license check cables to the licensing officer handling the related application. The licensing officer can then forward the cable to the interagency representative. However, it is our understanding that licensing officers have not been given specific instructions on forwarding unfavorable pre-license check cables to the interagency partners. Until interagency representatives are notified of

all unfavorable pre-license check results prior to BIS returning the relevant license application without action, this recommendation will remain open.

### (License Determinations for Customs)

### 24. Ensure that Export Administration works with Customs<sup>11</sup> in the following areas:

a. Develop and issue guidance to Customs agents and inspectors that sets forth procedures and a standard format for (1) submitting LD requests, (2) processing them in a timely manner, and (3) providing recourse when they are late.

**Status: Open.** According to BIS' February 2005 action plan, Export Administration has established LD procedures for export enforcement agents and has adapted them to outside agencies, including Customs. However, we question the suggested guidelines BIS provided us for processing Customs cases. Specifically, while the title indicates that the guidelines are for Customs, the body of the guidance talks only of Export Enforcement. In addition, the timeframes established in the guidance are not consistent with the timeframes Customs is required to work with according to the Export Administration Act of 1979, as amended (e.g., the guidance talks of processing LDs in 25 days while the law only allows Customs to detain a shipment for 20 days before it must formally seize or release the goods). As such, this recommendation will remain open until BIS develops and issues guidance to Customs on the LD process.

### b. Automate the license determination referral process as part of BIS' modernization of ECASS.

**Status: Open.** No action has been taken on this recommendation since our March 2004 report. Until the Customs license determination process is automated, this recommendation will remain open.

### **BXA NEEDS TO STRENGTHEN ITS ECASS MODERNIZATION EFFORTS TO ENSURE** LONG-TERM SUCCESS OF THE PROJECT, IPE-13744, FEBRUARY 2002.

### A. <u>Summary of OIG Findings and Recommendations</u>

During the 2002 reporting period, we completed a review of BIS' efforts to upgrade its automated licensing and enforcement systems. In particular, we sought to determine whether BIS had (1)

<sup>&</sup>lt;sup>11</sup> The U.S. Customs Service transferred from the Department of the Treasury to the Department of Homeland Security in 2003. Most of its responsibilities, including those related to enforcement of export controls, now reside in the Bureau of Immigration and Customs Enforcement.

adequately considered business process changes and appropriate resources for the life of the project; (2) established an infrastructure capable of monitoring project costs, schedule, and deliverables; (3) developed a realistic, achievable system-design schedule; and (4) implemented previous OIG recommendations pertaining to modernization of the export licensing system and other internal control issues. While our review found that BIS made some progress on its redesign effort, it also highlighted several areas needing improvement to ensure long-term success of the project. Some of our observations and conclusions from the February 2002 review were as follows:

- BIS made some progress on its redesign effort. Specifically, BIS was developing, in conjunction with Defense, a "front-end" licensing subsystem, known as the Simplified Network Application Processing (SNAP) system, that would allow exporters to submit all types of license applications as well as the corresponding supporting documentation on-line. In addition, BIS implemented its new Export Enforcement system, known as the Investigative Management System.
- BIS needed better planning to ensure long-term success of the project. Specifically, BIS needed to determine what business process reengineering recommendations needed to be implemented, prepare a revised cost estimate for its system redesign, and determine all of the ECASS 2000+ requirements, including user and security requirements.
- BIS needed to strengthen its modernization effort by implementing established information technology management best practices. Specifically, at the time our fieldwork was completed, the ECASS 2000+ project lacked adequate management tools, including (1) a project management plan, (2) target architecture, (3) a software acquisition training program, and (4) configuration and risk management processes.

Our report also noted that interagency cooperation on planning, design, and development of a dualuse export licensing system had been mixed because BIS has not involved the other licensing agencies in its own redesign effort beyond SNAP. For example, BIS was developing ECASS licensing requirements without input or validation from the current review agency users (State and Justice) or potential review agency users (Defense). Both State and Justice currently use ECASS to process license applications referred to them, and Defense could have used ECASS in the future. As such, we recommended that the other licensing agencies should be included in the development of licensing requirements for any new system.

#### B. Status of OIG Recommendations

#### **Recommendations for BIS**

### 2. Determine what resources are needed for ECASS 2000+ in the short-term (FYs 2002 and 2003) and long-term (FYs 2004 through 2006), how to secure adequate funding levels, and whether it is necessary to extend the project timeframe.

**Status: Open**. BIS hired a new Chief Information Officer (CIO) in August 2004 and a new ECASS program manager in December 2004. At that time the CIO reportedly completed a preliminary assessment of the project based on documented independent verification and validation findings as well as findings from the Commerce Information Technology Review Board. According to BIS, based on this assessment as well as an assessment of the risk associated with the current ECASS legacy system's maintainability, a project strategy was developed and briefed to the BIS Information Technology Steering Committee in December 2004 and the Commerce Information Technology Review Board in February 2005. It should be noted that the revised project and strategy are now identified as the "ECASS Redesign" project (which distinguishes its from the previously titled "ECASS 2000+").

BIS' February 2005 response states the final detailed assessment and project rebaselining will be completed in the third quarter of FY 2005. According to BIS, the project baseline is dependent on the completion of a "To Be" concept of operations, detailed specifications, and the high level architecture to be delivered in the requirements and concept definition phase. Until BIS completes its rebaselining activity and prepares a plan to secure adequate funding levels this recommendation will remain open.

### 3. Ensure that appropriate users, including those from referral agencies, validate the systems requirements for the licensing subsystem.

**Status: Open.** According to its February 2005 action plan, the BIS CIO's office is in the process of implementing this action. Specifically, as part of the FY 2004 CIO's office reorganization and the ECASS Redesign project, BIS is implementing a life cycle management approach, which includes a detailed concept of operations and a verified requirements baseline as deliverables in the ECASS Redesign concept and requirements definition phase. According to BIS, this process will occur at the system level for the ECASS core system, and include requirements validation through user acceptance testing, as well as verification through an independent verification and validation contractor. The same life cycle management process will be applied to each ECASS subsystem throughout the incremental implementation. While we are encouraged by BIS' stated objectives in the ECASS Redesign concept and requirements definition phase, until BIS fully engages both BIS and interagency licensing officials in the definition and validation of systems requirements for the licensing subsystem, this recommendation will remain open.

# 4. Document security requirements as soon as possible and determine how to fund them, including whether BIS should reallocate existing resources or make them a high funding priority.

**Status: Open.** According to BIS' February 2005 response, this action is being implemented as part of the requirements verification and validation process. In addition, BIS stated it will also be addressed as part of the BIS life cycle management deliverables and activities, including the (1) security plan, (2) security requirements specification, (3) allocation of security requirements to the ECASS application as well as the BIS security infrastructure design, (4) BIS security management plan and process led by the BIS Information Technology Security Officer, (5) implementation and validation by the individual system and infrastructure information system security officers, and (6) validation through the BIS system certification and accreditation process. However, until BIS fully documents its security requirements and associated costs for the ECASS Redesign project and determines how to fund them, this recommendation will remain open.

### 9. Revise and approve the project management plan during the second quarter of FY 2002.

Status: Closed. According to BIS, the project management plan for the ECASS Redesign has been completed and approved by the current CIO, although it is anticipated that it will be updated and augmented periodically. Accordingly, BIS has met the intent of our recommendation.

## 10. Complete the target architecture and select a location to house BIS' new export licensing automation system during the second quarter of FY 2002.

**Status: Open.** According to its February 2005 action plan, BIS stated that this action would be completed as part of the ECASS Redesign project in the third quarter of FY 2005. Specifically, the explicit deliverables will include the ECASS high level architecture and related technology assessments as well as the data, technical reference and service component reference models. However, until BIS has determined its system direction and final target architecture, this recommendation will remain open.

### MARCH 2002 INTERAGENCY OIG REPORT: INTERAGENCY REVIEW OF FEDERAL AUTOMATED EXPORT LICENSING SYSTEMS (D-2002-074)

### A. Summary of Interagency OIG Findings and Recommendations

In addition to our assessment of Commerce's system (see February 2002 report above), the interagency OIG review team looked at the various automated dual-use and munitions export licensing systems maintained by Commerce, Defense, Energy, and State to determine whether the systems could better interact and whether system modernization initiatives were in accordance with

federal policies and regulations. The review found that dual-use export licensing involves multiple automated systems owned and operated independently by the licensing and review agencies. Many of these systems were developed prior to some of today's information-sharing technologies and are not optimally effective given present-day information-processing capabilities. Current systems limitations include (1) differing security standards among agencies, (2) cumbersome manual and paper-based processes, and (3) lack of a comprehensive export-information database that can be used to assess cumulative effect of multiple exports. Improvement alternatives, beyond enhancing existing system interfaces, were not adequately considered.

### B. Status of Interagency OIG Recommendations

### **Recommendations for BIS**

### 1. Create a charter outlining the responsibilities of each agency in the design, development, and operation of a dual-use licensing system and how each agency will coordinate its automation efforts.

Status: Open. According to BIS' February 2005 action plan, a limited subset of this recommendation will be completed as part of the ECASS Redesign project with respect to replacement of current interagency interfaces, and the associated concept of operations, requirements specifications, and interface control documents. However, BIS also stated that the current ECASS funding profile will only address core BIS functionality. In addition, BIS stated that given the urgency of risk mitigation to minimize dependency on the twenty year-old mission critical ECASS legacy system and ensure the ability to migrate ECASS data, BIS has defined the initial and highest priority ECASS Redesign scope to be replacement of existing functionality with process productivity improvements and data migration.

While we understand BIS' urgency in replacing the ECASS Legacy system, we believe that some process productivity improvements may be able to be made through coordination of the various dual-use export licensing agencies' automation efforts. Again, we are concerned that there has been no recent interaction between the dual-use export licensing agencies and consequently none of these agencies has a clear plan of how they will continue to work together to coordinate its automation efforts. While it appears that each export licensing agency is currently or planning to develop its own in-house dual-use export licensing system, we believe it is still important for BIS, and the other licensing agencies, to establish some type of mechanism (via a charter or a written agreement) outlining how each agency will coordinate its efforts. Accordingly, this recommendation will remain open.

## 3. Develop a common central repository for all unclassified data records that pertain to the review and approval of an export license.

**Status: Open.** BIS previously reported that through the implementation of SNAP (Simplified Network Application Process), there would be a central repository for all

supporting documentation for a license application, which would be available to all referral agencies to use. However, BIS' February 2005 action plan reported that, within BIS, a central repository would be addressed as part of the ECASS Redesign project<sup>12</sup> but, with respect to a shared interagency repository, BIS stated that its funding profile does not support a requirement for a shared inventory at this time. Regardless, BIS believes that data sharing will be improved, to the extent practical within ECASS program funding constraints, by data migration to a new platform versus the current legacy point-to-point interfaces. In addition, BIS stated that the technology infrastructure used for the new ECASS core system would provide a platform to broaden the concept of a central repository to whatever implementation is desired by the participating federal agencies in the future.

Given that BIS has not fully defined its requirements or costs for the ECASS Redesign project, it is not clear why BIS is reporting that its ECASS funding profile prohibits development of a common central repository to be used by the dual-use export licensing agencies. As such, we encourage BIS to reconsider development of a common central repository for all unclassified data records that pertain to the review and approval of an export license as part of its current ECASS Redesign project. Accordingly, this recommendation will remain open.

# 4. Establish performance goals and metrics to track the progress of the system development efforts and report on the interagency entity's activities on a semiannual basis to the respective Secretaries.

**Status: Open.** According to its February 2005 action plan, BIS reported that revised performance goals and metrics will be defined as part of the ECASS Redesign project, in accordance with the incremental implementation of the system during FYs 2005 through 2009. In addition, BIS reported that performance measures will be documented as part of the BIS performance reference model, and captured as defined in the BIS requirements baseline for business processes, and service level agreements for information technology related performance. Until these goals and metrics have been identified and implemented, this recommendation will remain open.

### MANAGEMENT OF COMMERCE CONTROL LIST AND RELATED PROCESSES SHOULD BE IMPROVED, IPE-13744, MARCH 2001.

### A. <u>Summary of OIG Findings and Recommendations</u>

During the 2001 reporting period, we completed a review of the Commerce Control List (CCL). The CCL, which is maintained by BIS, specifies the commodities, software, and technology that are subject to the EAR, as well as those controls that are placed on these items, depending on the

<sup>&</sup>lt;sup>12</sup> The implementation date for this central repository will be defined as part of the ECASS Redesign rebaseline activity in the third quarter of FY 2005.

country to which they are to be exported. Each item on the CCL is grouped by type of commodity and assigned an Export Control Classification Number. The U.S. Munitions List, administered by State, specifies items subject to the International Traffic in Arms Regulations. Businesses use both lists to determine whether they need to apply for an export license for items they want to export.

Our review examined how the Control List was managed and determined whether there was a need for greater transparency in BIS' commodity classification process and State's commodity jurisdiction process. Some of our observations and conclusions from the March 2001 review were as follows:

- Improvements were needed in BIS' management of the CCL. Exporters generally thought the CCL was easier to understand than the U.S. Munitions List. However, some improvements were needed in the management of the CCL, including (1) exploring additional ways to make the list more user-friendly (2) improving the timeliness of implementing agreed-upon multilateral changes to the list, and (3) correcting the inappropriate use of national security controls on some items.
- There was a continuing need for improvements in the commodity classification process. Again, we found that the processing of commodity classifications was untimely, resulting in unnecessary delays for exporters. More importantly, we determined that the commodity classification process was not transparent because BIS was still not referring all munitions-related classifications to Defense and State for review, as directed by the 1996 National Security Council guidelines. This created the potential for incorrect classifications.
- The commodity jurisdiction (CJ) process needed improvement. CJ determination requests were not being processed in a timely manner by any of the involved agencies, including Commerce, Defense, and State. In addition, determination requests were currently being processed manually. Under such a manual system, documents can be lost, misplaced, or misdirected resulting in unnecessary delays. Furthermore, none of the agencies involved in the process were always fully informed about the jurisdiction opinions provided by the other agencies. Finally, there were concerns that State may be making incorrect CJ determinations because it did not always consult with BIS or Defense. We found two instances where this had occurred, causing inconvenience and expense to the exporters involved.
- Other OIG concerns related to the CCL. There was a breakdown in the interagency process for resolving jurisdictional disputes between Commerce, Defense, and State licensing offices (also called government jurisdictions) with regard to both night vision technology and space-qualified items.

#### B. <u>Status of OIG Recommendations</u>

#### **Recommendations for BIS**

### (Commerce Control List)

2. In conjunction with Defense and State, review the national security controlled items that have been decontrolled by the Wassenaar Arrangement to determine (a) whether the national security controls for these items should be removed and (b) whether these items should continue to be controlled for foreign policy reasons under the CCL.

Status: Closed. A rule entitled "Removal of National Security Controls from and Imposition of Regional Stability Controls on Certain Items on the Commerce Control List" was published in the *Federal Register* on March 29, 2004. Accordingly, this recommendation is closed.

3. Convene a working group of business and government representatives, under the auspices of the Regulations and Procedures Technical Advisory Committee, to improve the user-friendliness of the CCL. In addition, work with State to (1) eliminate the current overlap of items and make sure that it is very clear on which list an item falls, and (2) create a user-friendly consolidated index of the items on the CCL and the U.S. Munitions List (USML). To ensure that this happens, work with the applicable congressional committees, that are considering new legislation for dual-use exports, to ensure that any new Export Administration Act or similar legislation includes a requirement that the agencies eliminate the overlap and create such an index for both the CCL and the USML. Finally, ensure that the annual scrubs of the CCL also take into account any corrections or changes that would help to make the CCL easier for exporters to use.

**Status: Closed.** As reported previously, BIS implemented some of the recommendations from the Regulations and Procedures Technical Advisory Committee's 2001 study on how BIS can improve the CCL. In addition, BIS reported that the ongoing review of the USML under the Defense Trade Security Initiative Number 17 will address whatever overlap may exist between the CCL and USML. For example, BIS reported that regulations have been issued which have added pepper spray and some additional oxidizers to the CCL.

However, BIS still maintains that the current index to the CCL is sufficient for exporters. As such, it does not agree with our recommendation to create a consolidated index. We still maintain that the CCL can be confusing for exporters, and they may make errors in determining whether their item is covered by the CCL. As a result, they may not apply for a license when one is required. As noted in our report, many users told us that having a consolidated index of items on the CCL and USML would greatly help in navigating the two lists and understanding which agency has jurisdiction for a particular item. In its June 2004 action plan, BIS stated that it would welcome the availability of a USML item-specific index or indices which could be made available with the CCL indices. However, it stated that the development of such indices is outside of it purview as the State Department is responsible for and in control of the USML.

Again, to encourage greater compliance with U.S. export control laws, BIS should take the initiative to make the CCL as user-friendly as possible. Thus, we urge BIS to begin work with State immediately on the index or come up with another alternative to make the CCL easier to navigate in conjunction with the USML. However, at this time, we agree to close this recommendation.

### (Commodity Classifications)

7. Request that National Security Council (NSC) form a working group (including Commerce, Defense and State) to (a) review the 1996 commodity classification guidance, (b) revise it if necessary, and (c) develop specific criteria and procedures to ensure that the referral of munitions-related commodity classifications to Defense and State is handled in a timely, transparent, and appropriate manner by all agencies involved.

**Status: Open.** According to its February 2005 action plan, BIS stated that the review of the commodity jurisdiction and commodity classification processes is covered under the National Security Policy Directive 19. Once the directive is finalized, agencies will be tasked with developing criteria for improving the process. Again, we are pleased that high-level discussions are taking place about the review of commodity classifications. As such, BIS' actions partially meet the intent of our recommendation. This recommendation will remain open until the NSC/Commerce/Defense/State review of the 1996 commodity classification guidance is completed and specific criteria and procedures are developed to ensure that the referral of munitions-related commodity classifications to Defense and State is handled in a timely, transparent, and appropriate manner.

### 8. Provide State with a copy of the final determinations for any CCATS it reviews.

.

Status: Open. No additional action has been taken on this recommendation since our September 2002 follow-up report. BIS previously informed us that it was not practical to implement our recommendation under the current export licensing system. According to BIS' February 2005 action plan, the modernization effort will resume in FY 2006 with this recommendation as a discussion item. Until BIS provides State copies of the final determinations for CCATS it reviews, this recommendation will remain open.

# *IMPROVEMENTS ARE NEEDED IN PROGRAMS DESIGNED TO PROTECT AGAINST THE TRANSFER OF SENSITIVE TECHNOLOGIES TO COUNTRIES OF CONCERN*, IPE-12454-1, MARCH 2000.

### A. <u>Summary of OIG Findings and Recommendations</u>

During the 2000 reporting period, we focused on three activities that the Department of Commerce, principally through BIS, carries out or participates in to help prevent the illicit transfer of sensitive technology: (1) deemed export control activities, (2) the Visa Application Review Program, and (3) efforts in support of the Committee on Foreign Investment in the United States (CFIUS). The specific objectives of the review were to (1) examine the deemed export regulations, including their implementation and enforcement by BIS, as well as compliance with the regulations by industry and other federal agencies; (2) determine the effectiveness of BIS's Visa Application Review Program in preventing the illicit transfer of U.S. technology to countries and entities of concern; and (3) survey selected aspects of CFIUS' efforts. Our specific observations and conclusions from the March 2000 review were as follows:

- Deemed export control regulations and compliance needed to be reviewed. Export control policy and regulations for foreign nationals needed to be clarified. In addition, BIS needed to provide more outreach to industry and federal agencies to improve compliance with the regulations (only two federal agencies had applied for a total of five deemed export licenses in 1999).
- BIS' visa application review program showed potential for helping achieve the agency's export enforcement mission. However, we recommended some improvements in the way BIS handles the review of visa applications and in the coordination between the various agencies involved in the overall Visas Mantis program run by the State Department.
- Federal efforts to monitor foreign investment needed to be reviewed. Specifically, we raised concerns about the overall effectiveness of CFIUS, including (1) the lack of mandatory foreign investment reporting, (2) the low number of investigations conducted on company filings, (3) the role of Treasury in overseeing the program, and (4) the division of responsibilities between BIS and the International Trade Administration for the program within Commerce.

### B. Status of OIG Recommendations

With the exception of two OIG recommendations made to BIS and NOAA regarding deemed export controls, BIS' actions on recommendations related to its visa application review program and efforts in support of CFIUS met the intent of our recommendations. While BIS' and NOAA's actions for two of the recommendations did not fully meet the intent of our recommendations, our 2004 report readdresses these issues. As such, we closed these recommendations from the 2000 report.



### **U.S. DEPARTMENT OF COMMERCE**

Office of Inspector General Room 7898C, HCHB 14th Street & Constitution Avenue, NW Washington, DC 20230

Internet Web site:

www.oig.doc.gov

From: OIG FOIA Date: Jun 23, 2016 5:11:49 PM Subject: RE: FOIA Request 2016-001211

### Greetings-

As an update, we're still awaiting consult responses from other bureaus for some of the reports before we can release them. In the meantime, please see the following the links for a few documents that you requested as we posted them online after we conducted our search.

https://www.oig.doc.gov/OIGPublications/IPE-15155.pdf, https://www.oig.doc.gov/OIGPublications/IPE-15155-2.pdf, https://www.oig.doc.gov/OIGPublications/NOAA-ENT-8749-03-1997.pdf, and https://www.oig.doc.gov/OIGPublications/FY%201996%20Superfund%20Charg es%20to%20EPA%20NIST-EDAD-10062-7-0001-08-1997.pdf

Let me know if you would like to continue to include these as part of your FOIA request. Thanks.

Raman

[Note: these have been downloaded and are included herein]



UNITED STATES DEPARTMENT OF COMMERCE The Inspector General Washington, D.C. 20230

March 31, 2003

### FOR OFFICIAL USE ONLY

**MEMORANDUM FOR:** 

Kenneth I. Juster Under Secretary for Industry and Security

FROM:

Johnnie E. Frazier

SUBJECT:

Final Inspection Report: Improvements Are Needled To Better Enforce Dual-Use Export Control Laws (IPE-15155)

As a follow up to our March 4, 2003, draft report, attached is our final report on export enforcement, the fourth report required by the National Defense Authorization Act for Fiscal Year 2000. As you know, this legislation mandates that by March 30 of each year through 2007, we issue a report to the Congress on the policies and procedures of the U.S. government with respect to the export of technologies and technical information to countries and entities of concern. This fourth report focuses on BIS's export enforcement program, including its efforts to prevent the illegal export of dual-use items and to investigate and assist in the prosecution of violators of the Export Administration Regulations. The report includes comments from your March 25, 2003, written response to our draft report. A copy of your entire response is included as an appendix to this report. This report will also be issued as part of an interagency OIG report on federal export enforcement efforts.

The report highlights our major concern that Export Enforcement's investigative process produces few criminal prosecutions and administrative sanctions. It also outlines specific areas that need attention and improvement to strengthen BIS' export enforcement program, including (1) management of the investigative process and cases, (2) internal coordination between Export Enforcement and Export Administration (3) cooperation with other federal agencies involved in export enforcement, (4) monitoring of license conditions, (5) outreach efforts, and (6) end-use checks. The report offers a number of recommendations that we believe, if implemented, will help BIS' and the U.S. government's efforts to enforce export controls.

We are pleased to note that BIS, in its written response to our draft report, indicated that it has already taken or plans to take action on many of our recommendations. In addition, after carefully considering your response, we have made some adjustments in our final report, as appropriate. We request that you provide an action plan within 60 calendar days for those recommendations that we still consider open.

We would like to thank you and your staff for the assistance and courtesies extended to us during our evaluation. If you would like to discuss this report or the requested action plan, please call me at (202) 482-4661 or Jill Gross, Assistant Inspector General for Inspections and Program Evaluations, at (202) 482-2754.

Attachment

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U.S. Department of Commerce Office of Inspector General FOR OFFICIAL USE ONLY

### **EXECUTIVE SUMMARY**

The National Defense Authorization Act for Fiscal Year 2000 directs the Inspectors General of the Departments of Commerce, Defense, Energy, and State, in consultation with the Directors of Central Intelligence and the Federal Bureau of Investigation, to assess the adequacy of export controls and counterintelligence measures for preventing countries and entities of concern from acquiring militarily sensitive U.S. technology and technical information.<sup>1</sup> The legislation further mandates that the Inspectors General report their findings to Congress by March 30 of each year until 2007.

For 2003, the Inspectors General agreed to conduct an interagency review of the federal government's enforcement of export controls.<sup>2</sup> Each OIG also examined its own agency's efforts to enforce these controls. Our review at Commerce focused on the Bureau of Industry and Security's (BIS) export enforcement program, including its efforts to prevent the illegal export of dual-use items (goods and technologies that have both civilian and military applications) and to investigate and assist in the prosecution of violators of the Export Administration Regulations. Specifically, we reviewed BIS' activities related to its (I) conduct of investigations (including agent training and the administrative remedy process); (2) interactions with the law enforcement community (e.g., U.S. Customs Service and Federal Bureau of Investigation), the intelligence community, U.S. Postal Service, and U.S. Attorneys' Offices; (3) monitoring of license conditions; (4) outreach; and (5) end-use checks.

The Under Secretary of Commerce for Industry and Security has addressed the importance of export controls on numerous occasions. In particular, at the BIS Update West 2002 Conference,<sup>3</sup> he said:

"The terrorist attacks of September 11 simply reinforced the importance of our mission. We will vigorously administer and enforce export controls to stem the proliferation of weapons of mass destruction and the missiles to deliver them, to halt the spread of advanced conventional weapons to terrorists or countries of concern, and to further important U.S. foreign policy objectives. Where there is real and credible evidence suggesting that the export of a dual-use item threatens our national security, we must act to combat that threat."<sup>4</sup>

To be effective, export controls must be enforced, and companies or individuals who conspire to evade those controls or commit illegal exporting must be detected and prosecuted accordingly. However, our evaluation disclosed deficiencies within several key areas of BIS' export

<sup>&</sup>lt;sup>4</sup>Keynote Address by Kenneth I. Juster, Under Secretary of Commerce for Industry and Security, at Update West 2002 in Pasadena, CA, on April 16, 2002.



<sup>&</sup>lt;sup>1</sup>Public Law 106-65, October 5, 1999.

<sup>&</sup>lt;sup>2</sup>Because the Department of the Treasury's U.S. Customs Service is a key player in the enforcement of export controls, Treasury's OIG participated in this year's review. In addition, the U.S. Postal Service's OIG joined the review to assess the Postal Service's efforts to assure that users of the U.S. mail service comply with the export control laws and regulations.

<sup>&</sup>lt;sup>3</sup>BIS' Update West Conference is an annual meeting held in California that brings together representatives of industry and government to discuss current and upcoming export control issues.

enforcement program, which hinder its ability to achieve these goals. Our specific observations are as follows:

## Export Enforcement's Investigative Process Produces Few Criminal Prosecutions and Administrative Sanctions

Export Enforcement's mission is to advance U.S. national security, foreign policy, and economic interests by enforcing the export control provisions of the Export Administration Regulations. To this end, it endeavors to identify, investigate, and apprehend violators, and seeks criminal and administrative sanctions against them. We examined in detail Export Enforcement's investigative process and identified weaknesses in several critical areas, which negatively impact its ability to achieve its mission and need to be addressed:

- Stronger management oversight of the investigatory process is needed. Neither case development nor case leads are consistently monitored or evaluated by Export Enforcement managers.
- The processing of license determinations needs to be improved. Inconsistent and untimely determinations sometimes terminate or postpone investigations.
- The administrative remedy process needs to be more transparent and timely. The rationale with regard to how administrative penalties are determined is not transparent. In addition, the Office of Chief Counsel's processing of cases can be untimely.
- Delinquent administrative penalty accounts need to be followed up. The Office of Export Enforcement does not take enforcement action against companies and individuals who fail to pay monetary penalties.
- Better case management guidance and agent training should improve enforcement capabilities. The new Special Agent Manual lacks sufficient policies and procedures to guide agents in conducting investigations, and training is not consistently provided.
- Better cooperation with other federal law enforcement and intelligence agencies could strengthen its investigative process. Export Enforcement's cooperation with U.S. Attorneys, U.S. Customs Service, Federal Bureau of Investigation, Central Intelligence Agency, and U.S. Postal Service could be enhanced to help it better prevent, detect, and assist in prosecuting illegal export transactions.

We recognize that some of these weaknesses are partly dependent upon external factors. For example, BIS must rely on the Department of Justice's U.S. Attorneys to criminally prosecute its cases. However, we were told that some U.S. Attorneys, or their Assistant U.S. Attorneys (AUSAs), are sometimes reluctant to accept these cases because (1) dual-use export control cases can be very complex, (2) there is currently no strong export control legislation, and (3) these cases can lack jury appeal. Some AUSAs stated that it is difficult for a jury to grasp the importance of export controls because new legislation has not been approved by the Congress to

replace the lapsed Export Administration Act. We have noted that, in an effort to increase AUSA interest in pursuing these cases and to better educate them on dual-use export control laws and regulations, senior BIS Export Enforcement officials have, on occasion, conducted outreach visits with AUSAs.

BIS managers agree that their enforcement priorities are to increase criminal prosecutions and administrative sanctions. However, we found that, cumulatively, the weaknesses listed above have hampered the investigative process, in that it produces few cases, which result in successful prosecutions. Out of an average yearly caseload of 1,038 cases, for example, just 3 criminal cases were successfully prosecuted (i.e., convictions) and 25 administrative enforcement cases were closed with sanctions in FY 2002.



### BIS' Other Enforcement Efforts Need Improvements

To help prevent and detect illegal exports, BIS (1) monitors export licenses to ensure that companies comply with all license conditions, and (2) conducts outreach to help educate industry about dual-use export controls as well as encourage reporting of potential control violations. Both endeavors require the combined efforts of BIS' two principal operating units – Export Administration and Export Enforcement.

Of the 54 standard license conditions, only 7 require the licensee to submit export documentation to BIS regarding the shipment of a controlled commodity. Export Administration is responsible for monitoring 6 of these conditions, and Export Enforcement the remaining one. We found that Export Administration and Export Enforcement are not adequately monitoring licenses with reporting conditions—a problem we previously identified in our 1999 export licensing report.<sup>5</sup> When license conditions are not carefully monitored, BIS cannot be certain that goods were not diverted to unauthorized end users or that exporters who fail to comply with conditions are being denied subsequent licenses. Therefore, we recommend that BIS (1) take the necessary actions to ensure that license conditions are monitored and followed up consistently, and (2) require licensing officers to thoroughly review a company's compliance history when processing new licenses.

<sup>&</sup>lt;sup>5</sup>Improvements Are Needed to Meet the Export Licensing Requirements of the 21<sup>st</sup> Century, U.S. Department of Commerce Office of Inspector General, IPE-11488, June 1999.

Our review also disclosed that Export Enforcement does not have an established national plan for proactively identifying manufacturers and exporters of critical commodities to target for outreach, nor does it have formal guidance to help its agents strategically identify these firms. It should be noted, however, that Export Enforcement did employ a nationwide strategic approach to outreach with respect to chemical manufacturers in the months immediately following the terrorist attacks of September 11, 2001. Nonetheless, without an established, proactive program, BIS lacks a key mechanism for preventing export violations through education and for detecting violations via company leads. Therefore, we recommend that Export Enforcement establish a national outreach plan that has annual goals and identifies priority industries to be visited (see page 50).

### BIS Should Continue to Improve the End-Use Check Process

End-use checks, an important part of the license evaluation and enforcement process, verify the legitimacy of dual-use export transactions controlled by BIS. A pre-license check (PLC) is used to validate information on export license applications by determining if an overseas person or firm is a suitable party to a transaction involving controlled U.S.-origin goods or technical data. Post shipment verifications (PSVs) strengthen assurances that exporters, shippers, consignees, and end users comply with the terms of export licenses, by determining whether goods exported from the U.S. were actually received by the party named on the license and are being used in accordance with the license provisions. (b) (7)(E)

BIS export control attachés,

stationed at three overseas posts, also conduct end-use checks."

While we continue to find that the end-use check process is a valuable tool, as we discuss in the following sections, we found that many of the problems with end-use checks discussed in our 1999 export licensing report persist.



### (b) (5), (b) (7)(E)

<sup>6</sup>Export control attaches are currently stationed in Abu Dhabi, United Arab Emirates; Beijing, China; and Moscow, Russia. BIS plans to station four additional attachés in Cairo, Egypt; New Delhi, India; Shanghai, China; and Singapore, by the end of FY 2003.



Safeguards team checks. (b) (7)(F)

. In

addition to conducting most PSVs and some PLCs, Safeguard teams also conduct outreach visits to foreign firms and provide guidance and support on preventive enforcement matters to the American Embassy personnel and/or host government export control officials. During FY 2001, BIS conducted Safeguard Verification trips to 15 countries.

Overall, we believe the Safeguards Verification Program is working reasonably well. However, we have identified several areas, such as the writing and dissemination of trip reports and coordination with other U.S. government agencies at post, where we believe improvements would make this program more effective. Therefore, we recommend that BIS (1) ensure that its agents submit timely trip reports, (2) make improvements to the Safeguards report format, (3) (b) (5), (b) (7)(E) and (4) instruct Safeguards teams to brief U.S. agencies at post about the end-use visits and endeavor to share relevant law enforcement or intelligence information (see page 59).

Unfavorable pre-license checks. BIS and licensing referral agencies rely on the results of PLCs to determine the ultimate disposition of a license application. Of the 373 PLCs conducted in FY 2001, 27 received an unfavorable determination. License applications for 15 of these were "returned without action", 9 were rejected, and 3 were approved with conditions after BIS took action to ensure that the concerns raised during the check were corrected or addressed. However, we identified seven cases in which Export Enforcement recommended rejection of a license application, but Export Administration returned them without action. This, in our opinion, violates the spirit of the 1996 memorandum of understanding (MOU) between Export Administration and Export Enforcement.<sup>7</sup> Specifically, the MOU indicates that if Export Administration disagrees with a licensing recommendation made by Export Enforcement, the offices must resolve the dispute, via the dispute resolution process, before the application can be processed further. However, for these seven cases, there was no indication that the dispute resolution process was actually used. Complicating the resolution process is the lack of internal controls in ECASS, BIS' automated licensing system, for ensuring that export license applications are not returned without action by Export Administration over a rejection by Export Enforcement.

BIS should remind Export Administration directors and licensing officers to adhere to the dispute resolution process outlined in the 1996 MOU and hold them accountable for

<sup>&</sup>lt;sup>7</sup>Export Administration and Export Enforcement entered into an MOU in 1996 regarding Export Enforcement's recommendations on export license applications. The MOU includes a dispute resolution process to be used by both organizations.

implementing it. In addition, BIS should (b) (5), (b) (7)(E) (b) (5), (b) (7)(E) (b) (5), (b) (7)(E) BIS should also revaluate the guidance provided in the 1996 MOU

concerning the return of license applications without action, and—as we recommended in 1999—disseminate negative PLC results to all referral agencies (see page 59).

### Export Administration's Processing of License Determinations for Customs is Untimely

Export Administration is not processing license determinations (LDs) requested by the U.S. Customs Service in a timely manner. LDs are needed to determine (1) whether an item is subject to the Export Administration Regulations; (2) the reason(s) for control, if any; (3) the item's export control commodity number; and (4) the licensing policy for the export of the item to the specified destination.

As stated in the Export Administration Act<sup>9</sup>, Customs can detain a shipment for only 20 days. If Customs does not receive a determination within 20 days from Export Administration, it has three options: it can (1) continue to detain the shipment in violation of the Act, (2) formally seize the shipment, or (3) release the shipment. Each option is potentially problematic. If Customs chooses option 1 or 2, it may unnecessarily delay legitimate trade if the licensing officer determines that the item does not require a license. If Customs chooses option 3, it could allow sensitive dual-use commodities to leave the United States that should not be shipped without a valid export license or, possibly, should not be exported at all. Because of this, Customs needs to receive the LD within a 20-day window in order to make an appropriate decision regarding disposition of the shipment. However, during our review, we found that less than 50 percent of the LDs requested in FY 2002 were processed in 20 days or less.

We also examined this issue in our 1999 export licensing report, and recommended that BIS work with Customs to (1) automate the referral of Customs' LD requests and (2) formulate a written agreement outlining the responsibilities of each party involved in the process. Although BIS agreed with our recommendations, it has not initiated efforts in either area. We remain concerned that, without an automated system and written guidelines, neither BIS nor Customs can be assured that LDs will be processed in a timely manner. As such, we recommend that (b) (5), (b) (7)(E)

(see page 74).

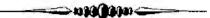
On page 77, we list all of our recommendations to address the concerns raised in this report.

<sup>&</sup>lt;sup>8</sup> Export Control Automated Support System.

<sup>&</sup>lt;sup>9</sup>See section 12(2)(a) of the EAA. Although the EAA is expired, the President's executive order invoking emergency authority under the International Emergency Economic Powers Act directs the executive branch to continue to comply with the provisions of the EAA to the extent possible.

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In its March 25, 2003, written response to our draft report, BIS indicated that many of the issues raised in our report had already been identified by BIS management, and these items already have or are in the process of being addressed. We discussed many of our findings and recommendations with senior Export Enforcement officials throughout the course of our review. They were consistently candid about and receptive to our concerns and recommendations and began many corrective actions before completion of our review. We are pleased that BIS management is committed to taking vigorous action to enforce the U.S. government's dual-use export control laws.

However, BIS' response also raised several concerns about our report's conclusions. First, the response took issue with the fact that our report focuses on case prosecutions versus preventive enforcement matters. Specifically, the response stated that "... attempting to police on a case-bycase basis the millions of export transactions that occur annually in the contemporary globalized economy with a force of slightly more than 100 agents is effectively impossible. Rather, enforcement is most effectively promoted through deterrence, preventive action, and the targeting of limited resources on major 'chokepoints' in global strategic trade flows, where they will have the most impact." We completely agree with BIS that preventive efforts and deterrence are an integral part of any enforcement program. Accordingly, we did review many of BIS' preventive programs, including its outreach to industry, (b) (7)(E) . end-use checks, and follow-up on license conditions. Our draft report offered a number of recommendations that address actions Export Enforcement could take to improve those preventive efforts, including its outreach efforts to U.S. exporters as well as exporter compliance with license conditions. While the draft report also acknowledged BIS' recently established Transshipment Country Export Control Initiative, which is a cooperative endeavor that seeks to strengthen the trade compliance and export control practices of governments and industry in the major transshipment hubs, this effort was too new for us to evaluate its impact at this point.

In addition, BIS took exception to our conclusion that it produces "few" criminal prosecutions (3 in FY 2002) and administrative sanctions (25 in FY 2002). Specifically, it questions how we judged these statistics and whether we compared them to those of other law enforcement agencies, such as the U.S. Customs Service which has concurrent jurisdiction over export controls or the FBI which enforces white collar criminal laws in addition to other laws. BIS' response compares 1015 cases opened by it to a *National Journal* citation of 80 investigations launched by Customs last year, but does not note that BIS' "cases" include both case leads and investigations. While we were unable to obtain comparable data from either Customs or the FBI, we were told, by the Acting Assistant Secretary for Export Enforcement, that comparing BIS statistics with FBI statistics on its white collar crime cases would probably not be appropriate given the nature and complexity of BIS cases. Our conclusion about BIS' record on criminal prosecutions and administrative sanctions was based on consideration of a number of factors. First, we note that repeatedly throughout our review, senior Export Enforcement managers were candid in acknowledging that they thought there was considerable room for improvement in increasing the number of criminal convictions and administrative sanctions. Second, according





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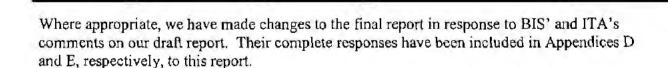
to its FY 2003 Performance Plan, BIS states that it will devote its current level of enforcement resources to investigations that have the highest probability of leading to the prosecution of export violators.

Although we did not compare BIS' criminal prosecutions and administrative sanctions with other law enforcement agencies, we did compare BIS' 2002 statistics with its performance data from prior years. As a result, we learned that since 1998, BIS' prosecutions, sanctions, and warning letters issued have steadily decreased. Specifically, as our draft report cites, in FY 1998 BIS had 10 criminal prosecutions, 44 administrative sanctions, and 266 warning letters as compared to FY 2002 in which BIS had 3 criminal prosecutions, 25 administrative sanctions, and 132 warning letters. During the course of our review, export enforcement officials were unable to explain this decrease.

Finally, BIS' written response questions the linkage between few criminal prosecutions and administrative sanctions and inadequate case management and license determinations. Our discussion of case management principally highlights the fact that not all of OEE's special-agents-in-charge or headquarters managers are adequately monitoring case activity. We found that not all SACs were conducting quarterly case reviews to ensure that the agents were adequately working cases and expending their resources on the most viable cases. Without sufficient supervisory attention, the agents may not be pursuing the best case strategy or leads or working the highest priority cases. In addition, failure to conduct timely preliminary investigations often resulted in the unnecessary upgrade of some case leads to full-scale investigations and potentially solid investigations just languished in agents' queue because of the increasingly large caseloads. The ultimate effect of this action is that agents are not able to fully focus their attention on those cases that may be most likely to result in prosecutions or sanctions.

While our report discusses just two examples of problem license determinations, we identified several other inaccurate, inconsistent, and untimely license determinations during our review. We chose to highlight two of the more egregious examples to demonstrate the adverse impact that problem license determinations have on the export enforcement investigative process.

In its March 28, 2003, written response to our draft report, ITA (b) (5), (b) (7)(E)



### INTRODUCTION

The Inspectors General of the Departments of Commerce, Defense, Energy, State, in consultation with the Directors of Central Intelligence and the Federal Bureau of Investigation (FBI), are required by the National Defense Authorization Act for Fiscal Year 2000 to annually assess — for a period of 8 years — the adequacy of export controls and counterintelligence measures for preventing the acquisition of sensitive U.S. technology and technical information by countries and entities of concern.<sup>10</sup>



To meet the act's 2001 requirement, the OIGs conducted an interagency review of the Commerce Control List and the U.S. Munitions List. Our review looked at BIS' policies and procedures for the design, maintenance, and application of the Commerce Control List.<sup>14</sup> For 2002, the interagency review examined the various automated export licensing systems maintained by federal licensing agencies to determine how the systems interact and whether it is feasible to develop a single federal automated export licensing network or other alternatives. We conducted a program evaluation that focused on BIS' efforts to modernize its aging Export Control Automated Support System (ECASS).<sup>15</sup>

To comply with the 2003 requirement, the OIGs agreed to conduct an interagency review of the federal government's export enforcement efforts. We focused on evaluating the adequacy and effectiveness of BIS' export enforcement program for dual-use commodities (goods and technologies that have both civilian and military applications).

<sup>&</sup>lt;sup>10</sup>Because the Department of the Treasury's U.S. Customs Service is a key player in the enforcement of export controls, the Treasury's OIG participated in this year's review. In addition, the U.S. Postal Service's OIG joined the review to assess the Postal Service's efforts to assure that users of the U.S. mail service comply with the export control laws and regulations.

<sup>&</sup>lt;sup>11</sup>On April 18, 2002, the Bureau of Export Administration (BXA) was renamed the Bureau of Industry and Security (BIS) to reflect more accurately the broad scope of the agency's responsibilities. <sup>12</sup>Improvements Are Needed in Programs Designed to Protect Against the Transfer of Sensitive

<sup>&</sup>lt;sup>12</sup>Improvements Are Needed in Programs Designed to Protect Against the Transfer of Sensitive Technologies to Countries of Concern, U.S. Department of Commerce Office of Inspector General, IPE-12454-1, March 2000.

<sup>&</sup>lt;sup>13</sup>According to the Export Administration Regulations, any release to a foreign national of technology or software subject to the regulations is deemed to be an export to the home country of the foreign national.

<sup>&</sup>lt;sup>14</sup>Management of Commerce Control List and Related Processes Should be Improved, U.S. Department of Commerce Office of Inspector General, IPE-13744, March 2001.

<sup>&</sup>lt;sup>15</sup>BXA Needs to Strengthen Its ECASS Modernization Efforts to Ensure Long-Term Success of the Project, U.S. Department of Commerce Office of Inspector General, IPE-14270, February 2002.

Program evaluations are special reviews that the OIG undertakes to give agency managers timely information about operations, including current and foreseeable problems. One of the main goals of a program evaluation is to eliminate waste in federal government programs by encouraging effective and efficient operations. By asking questions, identifying problems, and suggesting solutions, the OIG hopes to help managers move quickly to address program weaknesses and to prevent similar ones in the future. Program evaluations may also highlight effective programs or operations, particularly if they may be useful or adaptable for agency managers or program operations elsewhere.

We conducted our evaluation from late April through early December 2002, under the authority of the Inspector General Act of 1978, as amended, and in accordance with the *Quality Standards for Inspections* issued by the President's Council on Integrity and Efficiency. Throughout the course of our review and at the end, we discussed our findings and conclusions with BIS' Under Secretary, Deputy Under Secretary, Acting Assistant Secretary for Export Enforcement, Deputy Assistant Secretary for Export Administration, and other senior BIS officials.

### **OBJECTIVES, SCOPE, AND METHODOLOGY**

We sought to assess the adequacy and effectiveness of BIS' export enforcement program in preventing the illegal export of dual-use items and investigating and prosecuting violators of the Export Administration Regulations (EAR). Specifically, we reviewed the following BIS activities:

- Conduct of investigations (including the adequacy of case leads and case management, administrative enforcement proceedings, and its training of agents).
- Interactions with the export licensing, law enforcement, and intelligence communities, and with U.S. Attorneys' Offices.
- Monitoring of license conditions by both Export Enforcement and Export Administration.
- Outreach and education to provide U.S. companies with export control guidance and obtain investigative leads.
- End-use checks, including pre-license checks (PLCs), post shipment verifications (PSVs), and the Safeguards Verification Program.

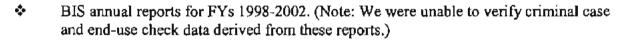
We used the following methodology to conduct our inspection:

**Interviews.** Within Export Enforcement, we interviewed the Acting Assistant Secretary; the directors of the Office of Export Enforcement (OEE), Office of Enforcement Analysis, and Office of Antiboycott Compliance; Export Enforcement agents, including all special agents-incharge (SACs), and analysts. Within Export Administration we met with the Deputy Assistant Secretary; directors of the Office of Strategic Trade and Foreign Policy Controls and the Office of Exporter Services; directors of the Chemical and Biological Controls Division, Nuclear and Missile Technology Controls Division, and Strategic Trade Division; and other licensing officials. We also met with the Chief Counsel for Industry and Security and staff attorneys, and with officials from the Office of Administration.

Within Commerce, we also met with officials from the International Trade Administration, including the United States and Foreign Commercial Service's (US&FCS) Deputy Assistant Secretary for International Operations.

Externally, we met with officials from the Departments of Defense (Defense Intelligence Agency and U.S. Air Force), Justice (FBI and U.S. Attorneys' Offices), State, and the Treasury (U.S. Customs Service (Customs)); the Central Intelligence Agency (CIA); the U.S. Postal Service; and the U.S. General Accounting Office. We also met with representatives of a shipping company and a freight forwarder located in Baltimore, and with officials from the Port of Baltimore. (For information on overseas contacts, see the following page.)

Review of export control laws and regulations, relevant BIS guidance, and other documents. We examined current and prior legislation, executive orders, and related regulations, including the Export Administration Act (EAA) of 1979, the EAR, and the International Emergency Economic Powers Act (IEEPA), as well as the following:



- Presidential Budget Submissions for FYs 1999-2002 and the Office of Management and Budget's FY 2003 budget submission for BIS.
- The 1993 Export Enforcement Coordination Procedures between the Office of Export Enforcement and the United States Customs Service (the 1993 MOU), and the 1996 memorandum of understanding between Export Enforcement and Export Administration regarding export license recommendations.
- Customs' shipment seizure data for FYs 2001 and 2002, data regarding the inspectors assigned to the Outbound inspection program, and literature on Project Shield America.
- The Department of Justice's manual on the export control laws.

We also examined closed investigatory case files for FYs 2001 and 2002 from the four Office of Export Enforcement (OEE) field offices we visited, a chronology of training completed by OEE agents over the prior 5 years, OEE's 1989 and 2002 *Special Agent Manual* (SAM) and Office of the Director Memoranda (ODMs). We also reviewed BIS guidance on end-use checks (both for (b) (7)(E) and OEE's Safeguards Verification Teams), (b) (7)(E), and OEE's export control attaché work plan. We reviewed the (b) (7)(E)



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(b) (7)(E) and 4 PLCs and 25 PSVs from Safeguards teams,<sup>16</sup> as well as information (including 532 end-use checks) from 10 Safeguards team reports on trips conducted in FY 2001.

In preparation for an overseas trip to Asia, we also examined PLCs and PSVs conducted in Hong Kong and Singapore (b) (7)(E) during FYs 2001 and 2002, in addition to reviewing reports on Safeguards team trips to both countries during that same period. Furthermore, we reviewed the license outcomes associated with the 28 unfavorable PLCs for FY 2001.

In addition, we reviewed BIS directives and data relating to license monitoring. Specifically, we analyzed information derived from a sample of 90 export licenses monitored by Export Administration and from a sample of 33 export licenses monitored by Export Enforcement. We also examined Export Administration's processing of license determinations (LDs) requested by both OEE and Customs during FYs 2001 and 2002. In doing so, we reviewed internal BIS directives on the LD process, particularly the August 2002 License Determination Work Plan and performance evaluations for division directors and licensing officers. With regard to BIS' administrative remedy process, we reviewed the charter for the Administrative Case Review Board (ACRB), along with cases closed with administrative sanctions in FYs 2001 and 2002, and observed an ACRB meeting. We requested information on the processing of administrative cases by the Office of Chief Counsel for Industry and Security (OCC), which were presented to the ACRB; however, we were unable to obtain such data.

**OEE** Field Office visits. In addition to our work at OEE headquarters, we visited four of OEE's 8 field offices, including those in Herndon, Virginia (Washington Field Office); New York, New York; Irvine (Los Angeles Field Office, including its satellite office located at Los Angeles International Airport), and San Jose, California.

**Overseas visits.** We met with various officials stationed at the U.S. consulate in Hong Kong and the U.S. embassy in Singapore, including those with the US&FCS, State's Economic and Political Section, Customs, FBI, Defense, and officials of other relevant agencies. We spoke with the U.S. Consul General in Hong Kong and both the Ambassador and Deputy Chief of Mission in Singapore, as well as with officials of Hong Kong's Trade and Industry Department, Customs and Excise Department, and the Commerce, Industry and Technology Bureau. In addition, we participated in a PSV conducted by US&FCS personnel in Singapore.

Surveys. We conducted two electronic surveys during the course of our review. One questionnaire was sent to 76 OEE agents in the field and at headquarters, and 8 SACs to solicit their input on the adequacy of BIS' export enforcement program. We received responses from 33 agents (43 percent) and 7 SACs (88 percent). The other questionnaire was delivered to (()(1)(1))

#### (b) (7)(E)

<sup>16</sup>(b) (7)(l

#### BACKGROUND

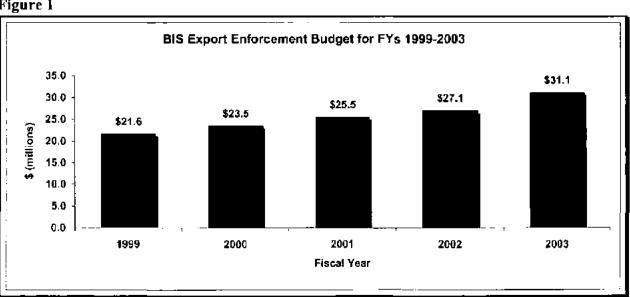
The United States controls the export of dual-use commodities for national security, foreign policy, antiterrorism, and nonproliferation reasons under the authority of several different laws, but the primary legislative authority is the EAA. Under the act, BIS administers the EAR by developing export control policies, issuing export licenses, and enforcing the laws and regulations for dual-use exports. Although the act last expired on August 21, 2001, the President extended existing export regulations under Executive Order 13222, dated August 17, 2001, invoking emergency authority under the IEEPA.

#### I. **BIS' Organizational Structure**

BIS has two principal operating units, Export Enforcement and Export Administration that are involved in export controls. BIS' Office of Chief Counsel and Office of Administration are also involved in some aspects of export enforcement as well as export licensing.

#### Export Enforcement

Export Enforcement's budget for FY 2002 was \$27.1 million, an increase of \$1.6 million over FY 2001. For FY 2003, Export Enforcement's budget increased nearly 15 percent to \$31.1 million (see figure 1). In FY 2001, the unit had a staff of 152, including 95 special agents.





Source: Budget of the United States of America for FYs 1999-2002, and House Conference Report 108-10 accompanying House Joint Resolution 2, U.S. House of Representatives.

Export Enforcement comprises three offices: (1) the Office of Export Enforcement, (2) the Office of Enforcement Analysis (OEA), and (3) the Office of Antiboycott Compliance (OAC).

#### Office of Export Enforcement

OEE investigates alleged export control violations and coordinates its enforcement activities with other federal agencies, including Customs, the FBI, and U.S. Attorneys' Offices. OEE agents are empowered to make arrests, carry firearms, execute search warrants, and seize goods about to be exported illegally. They also travel overseas to conduct end-use checks under the Safeguards Verification Program (see page 59 for further discussion).

OEE is headquartered in Washington, D.C., and has eight field offices and one satellite office that provide coverage for all 50 states (see figure 2). Export control attachés are stationed in Abu Dhabi, United Arab Emirates; Beijing, China; and Moscow, Russia. By the end of FY 2003, BIS intends to open a field office in Seattle, Washington; a satellite office in Houston, Texas; and have additional attachés in place in Cairo, Egypt; New Delhi, India; Shanghai, China; and Singapore.

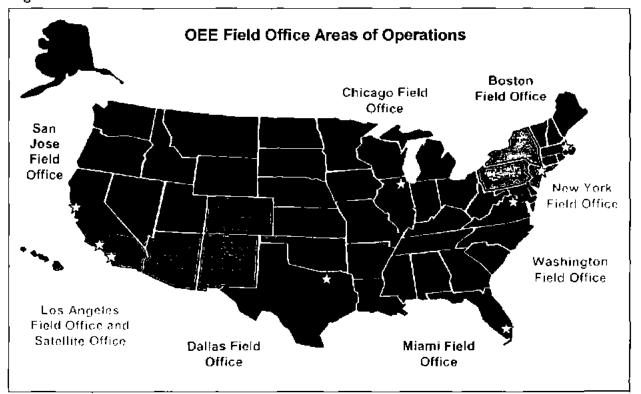


Figure 2

Source: Office of Export Enforcement, Bureau of Industry and Security.

Finally, OEE's Intelligence and Field Support Division (IFSD), located at headquarters, is also staffed by agents and serves as a liaison with the U.S. intelligence community and OEE's field offices.

#### Office of Enforcement Analysis

OEA is the central point for the collection, research, and analysis of classified and unclassified information on end users who are of export control concern. OEA analysts review license applications, (b) (7)(E) the second sec

#### Office of Antiboycott Compliance

OAC enforces the antiboycott provisions of the EAA and the EAR, assists the public in complying with these provisions, and compiles and analyzes information regarding international boycotts.

#### **Export Administration**



Export Administration is composed of four offices. The Office of Exporter Services (OExS) is responsible for outreach (e.g., educational seminars and conferences) and counseling efforts to help ensure exporters' compliance with the EAR and coordination of policy within Export Administration. OExS is also responsible for following up on license conditions to determine exporters' compliance with them. The Office of Nonproliferation Controls and Treaty Compliance and the Office of Strategic Trade and Foreign Policy Controls each have a full range of responsibilities associated with the licensing of exports, including processing license determinations for OEE and Customs. Finally, the Office of Strategic Industry and Economic Security oversees issues related to U.S. defense industry competitiveness.

With regard to outreach efforts, in FY 2002, 37 educational seminars were held in 16 states that attracted 2,273 participants. BIS also held its two annual Update Conference events to bring high-level government officials and industry representatives together to discuss new export control policies, regulations, and procedures.

#### Office of Chief Counsel

OCC provides BIS with legal advice and policy support. OCC attorneys represent BIS in administrative enforcement cases, advise criminal investigators in their investigations, and assist Assistant U.S. Attorneys (AUSAs) in prosecuting criminal export control cases. OCC also provides guidance on legal and policy issues related to export licensing and antiboycott compliance and helps draft and review proposed export control regulations and interpret existing ones.



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#### Office of Administration

The Office of Administration handles BIS' overall administrative management. It includes the Office of the Comptroller, which monitors payments of administrative penalties assessed by Export Enforcement.

#### II. BIS' Export Enforcement Program

BIS uses a number of tools to carry out its Export Enforcement program that is designed to (1) investigate and assist in the prosecution of violators of the EAR and (2) prevent the illegal export of dual-use items.

#### **Investigative and Prosecutorial Efforts**

During FY 2001, OEE conducted numerous investigations, some of which led to criminal and/or administrative sanctions. OEE also closed 208 cases involving minor violations with warning letters.<sup>17</sup> Export Enforcement's staff works closely with OCC and AUSAs to prosecute companies and individuals who violate export control laws. Violators can face criminal penalties (fines and possible imprisonment) and/or administrative sanctions.<sup>18</sup> In FY 2001, \$2.4 million in administrative penalties and \$1.01 million in criminal fines were imposed for export control violations. Corresponding amounts for FY 2002 were \$5.2 million in administrative penalties and \$15,000 in criminal fines.

BIS employs an internal administrative remedy process to sanction those companies or individuals who violate the export control laws. If there is sufficient evidence to pursue an administrative sanction, the SAC presents the agent's administrative case report to the Director of OEE, who evaluates the justification for an administrative action. If there is insufficient evidence, the case report is returned to the SAC for additional field investigation or issuance of a warning letter. If the report is complete, the OEE Director submits it to OCC to begin the administrative case processing. OCC determines the number of violations committed under the regulations and then presents an administrative case package to the ACRB for review.

The ACRB, an internal BIS committee created in February 2002, advises the Assistant Secretary for Export Enforcement at the important stages of the administrative remedy process. If the ACRB agrees with the charges proposed by OCC, a pre-charging letter<sup>19</sup> is issued to the respondent (i.e., company or individual). If the respondent wishes to settle the charges, negotiations with OCC then commence. A settlement may include a monetary penalty and/or a denial of export privileges. In some cases, the denial of export privileges may be suspended for

<sup>&</sup>lt;sup>17</sup>A warning letter is an informal action by OEE that imposes neither fines nor restrictions on export privileges. It describes the alleged violations and possible sanctions. It further states that while no sanction will be imposed, BIS will consider any future violations in light of the warning.

<sup>&</sup>lt;sup>18</sup>An administrative sanction is a monetary penalty and/or denial of export privileges.

<sup>&</sup>lt;sup>19</sup>A pre-charging letter, signed by the Director of OEE, constitutes a formal complaint against a company and indicates BIS' reason(s) for believing that a violation of the export control laws has occurred.

the duration of the denial period, provided that the respondent complies with the terms of the order, which would include payment of administrative penalties. Failure to pay or committing any other violation might result in the imposition of a full denial of export privileges. After a settlement is reached, an order is drafted and signed by the Assistant Secretary for Export Enforcement. Cases that are settled may not be reopened or appealed.

Conversely, if the company or individual fails to respond to the pre-charging letter or contests the charges, a formal charging letter is issued and the case is referred to the administrative law judge (ALJ) for adjudication. In the case of the respondent's failure to respond to the charging letter, BIS files a motion of default action against the company or individual.<sup>20</sup> Based on the evidence presented, the ALJ submits a recommended decision and order to the Under Secretary of Commerce for Industry and Security who then issues a written order approving, modifying, or vacating the recommended decision and order of the ALJ. The charged party may appeal the Under Secretary's written order to the U.S. Court of Appeals for the District of Columbia.

#### Preventive Enforcement Measures

End-use checks. As an important component of the export control process, end-use checks help determine if the overseas parties or representatives of U.S. exporters are suitable for receiving sensitive U.S. items and technology and will likely comply with appropriate end-use conditions and retransfer restrictions. End-use checks consist of pre-license checks (PLCs) and post shipment verifications (PSVs). A PLC is conducted before approval of a license application to obtain information about a foreign end user or intermediary consignee, which helps validate information on export license applications. The results of PLCs are factored into Export Enforcement's licensing recommendations to Export Administration's licensing officials. In contrast, a PSV is conducted after goods have been shipped, to determine whether the licensed item or technology was received and is being used in accordance with the provisions of the license. PSVs help assure that all parties involved in the transaction—exporters, shippers, consignees, and end users—comply with the terms of export licenses.

## (b) (7)(E)

(b) (7)(E) most PSVs and some PLCs are conducted by OEE's agents under the Safeguards Verification Program. In FY 2001, 373 PLCs and 689 PSVs were conducted. End-use checks may be initiated or requested by any of the parties involved in the license review process, including BIS' licensing or enforcement personnel, or export licensing referral agencies.

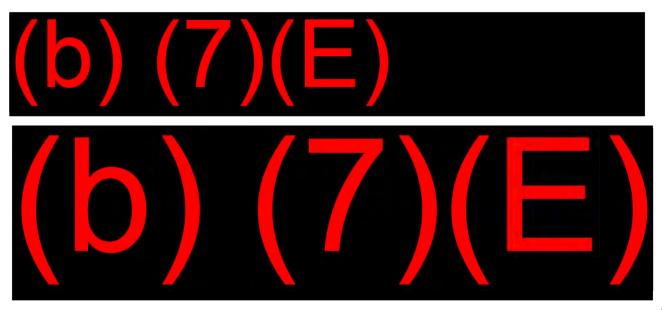
**Project Outreach.** OEE's agents conduct outreach visits with companies to educate them about the export control laws and seek their cooperation in identifying illegal export activity within their respective industry. Agents also conduct outreach visits to follow-up on certain types of investigative leads, such as (b) (7)(E). In addition (b) (7)(E)



<sup>&</sup>lt;sup>20</sup>Failure to respond constitutes a waiver of the respondent's rights to appear and contest the allegations in the formal charging letter.

# ) (7)(E)

(b) (7)(E) across the country; 4 of which were held in conjunction with seminars sponsored by the Office of Exporter Services (OExS), an office within BIS' Export Administration.



**Export Enforcement International Outreach.** BIS officials provide advice and information on methods to enforce export control laws and regulations to other countries through international export control seminars and workshops. In FY 2002, BIS conducted a number of outreach programs with a particular emphasis on countries with transshipment hubs<sup>21</sup> to achieve more effective export control enforcement. For example, in March 2002, the Under Secretary of Commerce for Industry and Security and the Assistant Secretary for Export Enforcement led an interagency delegation to Hong Kong for the seventh round of the U.S.–Hong Kong Interagency Export Control Discussions. Export Enforcement officials also conducted training and technical workshops in Cyprus, the Czech Republic, Hungary, Malta, Romania, Slovakia, and the United Arab Emirates. In addition, BIS officials participated in international nonproliferation regimes, including the Missile Technology Control Regime, the Nuclear Suppliers Group, the Australia Group (for chemical and biological weapons), and the Wassenaar Arrangement (conventional weapons).

For FY 2003, BIS is focused on enhancing trade security by working in partnership with transshipment countries and the trade community to highlight the danger of illicit diversion of sensitive items through the major transshipment ports. In October 2002, BIS announced its Transshipment Country Export Control Initiative (TECI), which is a cooperative endeavor that seeks to strengthen the trade compliance and export control practices of government and industry in the major transshipment hubs. Towards that end, the Deputy Under Secretary of Commerce

<sup>&</sup>lt;sup>21</sup>A transshipment hub is a global commerce port which processes large volumes of shipments. Most transshipment hubs are located near countries of concern. The proximity of transshipment hubs to destinations of concern increases the risk of sensitive technologies being diverted or illicitly re-exported to those destinations. Transshipment hubs include Hong Kong, Singapore, and the United Arab Emirates.

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for Industry and Security promoted the goals of TECI to U.S. trade partners at the Southeast Asian Conference on Trade Security in Thailand during December 2002.

#### **Other Preventive Enforcement Efforts**

BIS first published its list of "unverified" foreign entities in June 2002. The list essentially advises U.S. exporters about foreign companies on which the United States has been unable to conduct requested PLCs or PSVs and warns U.S. exporters to perform enhanced due diligence before exporting any items to the listed entities. The list does not impose a new licensing requirement for exports to these entities. Exporters are required to seek a license only if, upon completion of their due diligence, they believe that the transaction involves a proliferation activity or is in violation of the Export Administration.

In addition, Export Enforcement maintains the (1) "Entity List," which indicates those end users determined to present an unacceptable risk of diversion because of their link to the development of weapons of mass destruction or the missiles used to deliver those weapons and puts exporters on notice of export license requirements that apply to exports to these parties, and (2) "List of Denied Persons," which contains the names and addresses of those firms and individuals denied access to U.S. goods, and advises U.S. companies to avoid doing business with these entities.





#### **OBSERVATIONS AND CONCLUSIONS**

#### I. Export Enforcement's Investigative Process Produces Few Criminal Prosecutions and Administrative Sanctions

A key BIS performance goal for Export Enforcement is to detect illegal export transactions and penalize violators.<sup>22</sup> Towards that end, in its FY 2003 Annual Performance Plan, BIS states that it, "...will devote its current level of enforcement resources to investigations that have the highest probability of leading to prosecution of export violators." As such, we examined Export Enforcement's investigative process for preventing and detecting illegal export transactions and for prosecuting violators of U.S export control laws. We found a number of systemic weaknesses that warrant BIS' attention and improvement:

- Stronger case management oversight is needed. Neither case development nor case leads are consistently monitored or evaluated by management.
- The processing of license determinations needs to be improved. Inconsistent and untimely determinations sometimes terminate or postpone investigations conducted by the Office of Export Enforcement (OEE).
- The administrative remedy process needs to be more transparent and timely. The rationale with regard to how administrative penalties are determined is not transparent. In addition, the Office of Chief Counsel's processing of cases can be untimely.
- Delinquent administrative penalty accounts need to be followed up. OEE does not take enforcement action against companies and individuals who fail to pay monetary penalties.
- Better case management guidance and agent training should improve enforcement capabilities. The new Special Agent Manual (SAM) lacks sufficient policies and procedures to guide agents in conducting investigations, and training is not consistently provided.
- Better cooperation with other federal law enforcement and intelligence agencies could strengthen its investigative process. Export Enforcement's relations with other federal law enforcement and intelligence agencies should be improved to help it better meet its goal of preventing, detecting, and prosecuting illegal export transactions.

(Figure 3 on page 14 illustrates the entire investigative process and identifies, by color code, the steps in the process that are impacted by these weaknesses.)

We would like to point out that some of these weaknesses are partly dependent upon external factors. For example, BIS must rely on the Department of Justice's U.S. Attorneys Office to

<sup>&</sup>lt;sup>22</sup> BIS' FY 2003 Annual Performance Plan.

criminally prosecute its cases. However, Assistant U.S. Attorneys (AUSAs) with whom we spoke informed us that dual-use export control cases can be very complex and without strong export control legislation, these cases can lack jury appeal. For instance, some AUSAs stated that it is difficult for a jury to grasp the importance of export controls when new export control legislation has not been approved by the Congress. As a result, AUSAs are sometimes reluctant to accept an export enforcement case for prosecution. In an effort to better educate AUSAs on dual-use export control laws and regulations, we noted that, on occasion, the former Assistant Secretary for Export Enforcement, the Acting Assistant Secretary for Export Enforcement, and the Director of OEE have conducted outreach visits with AUSAs in an effort to "sell" OEE cases to them.

However, the cumulative effect of these inadequacies in the investigative process results in few criminal convictions and administrative sanctions from the many cases opened by Export Enforcement. In FY 2001 and FY 2002, for example, Export Enforcement obtained criminal convictions in 6 cases in FY 2001 and 3 in FY 2002. In addition, 25 administrative enforcement actions were taken in each of these two years.<sup>23</sup> (Table 1 provides a comparison of case data from FYs 1998 thru 2002.)

|  | 1998             | 1999             | 2000             | 2001              | 2002             |
|--|------------------|------------------|------------------|-------------------|------------------|
| Total Cases Opened   | N/A <sup>b</sup> | N/A <sup>b</sup> | N/A <sup>b</sup> | 1060 <sup>e</sup> | 1015°            |
| Cases Yielding Criminal Convictions                              | 10               | 11               | 6                | 6                 | 3                |
| Administrative Sanctions Imposed                                 | 44               | 26               | 29               | 25                | 25               |
| Warning Letter Issued  | 266              | 263              | 192              | 208 <sup>d</sup>  | 132 <sup>d</sup> |
| Cases Yielding Criminal<br>Indictments/Informations <sup>e</sup> | N/A <sup>b</sup> | 11               | 6                | 8                 | 6                |
| Total Cases Closed   | N/A <sup>b</sup> | N/A <sup>b</sup> | N/A <sup>b</sup> | 1227 <sup>c</sup> | 941 <sup>c</sup> |

#### Table 1: Export Enforcement Case Data, FYs 1998-2002\*

Notes:

<sup>3</sup>Unless noted otherwise, data derived from BIS Annual Reports (FYs 1998-2002).

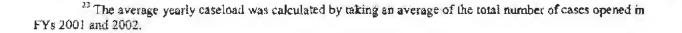
<sup>b</sup>Data not readily available from BIS.

<sup>s</sup>Data provided by Expert Enforcement,

<sup>4</sup>Data provided by Export Enforcement and reflect cases closed with warning letters.

"Includes indictments and informations that led to convictions in the same fiscal year. An "information" is an accusation or criminal charge brought by the prosecutor without a grand jury indictment.

Sources: Bureau of Industry and Security.



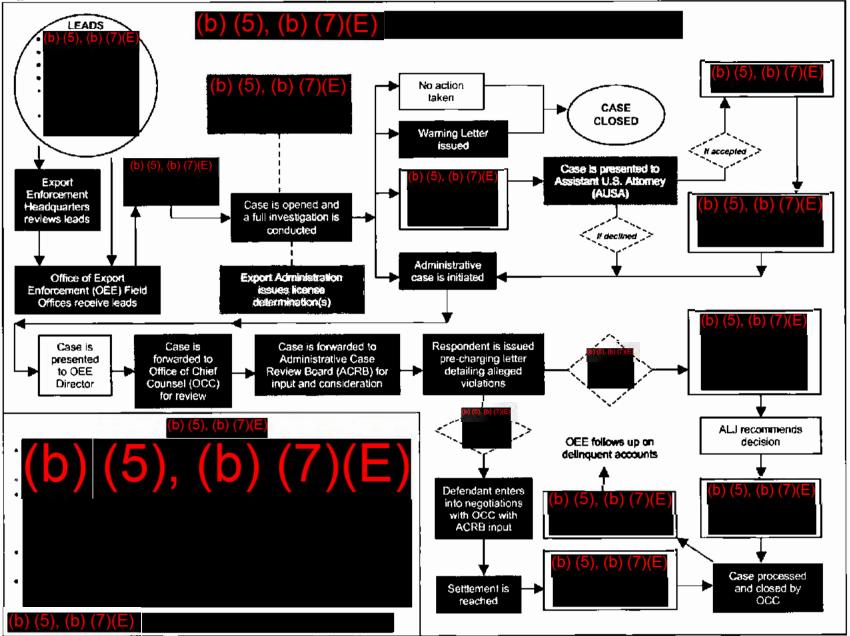






#### Figure 3

14



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#### A. The investigative process needs better management oversight

OEE management is responsible for designing standard investigative operating procedures for its staff, and regularly monitoring compliance with them. However, we found this oversight (at both the headquarters and field office levels) was inadequate in the following areas: (1) case development was not consistently monitored and (2) case leads were not being adequately assessed and prioritized. It should be noted that during the course of our review, OEE hired new SACs for its Boston, Los Angeles, and Washington Field Offices and is currently trying to fill two management positions at headquarters (including the Assistant Director for Investigations and the Assistant Director for the Intelligence and Field Support Division).

#### Case development should be better monitored

Not all of OEE's SACs or headquarters officials are adequately monitoring case activity. Specifically, we found that the majority of cases from our sample<sup>24</sup> (b) (7)(E)

In addition, we determined that the majority of SACs were not conducting quarterly case reviews for all cases, as required.<sup>25</sup> As a result, full-scale investigations are being launched regardless of merit, increasing agents' caseloads with cases that may not warrant attention and are ultimately closed because of no violation or insufficient evidence of a violation. The larger caseloads tend to slow overall case processing.

**Preliminary Investigations.** According to the SAM, the SAC is responsible for case control. When a lead is received at the field office, the SAC assigns it to an agent, for a preliminary investigation. The purpose of a preliminary investigation is to conduct an initial inquiry on all credible leads received. If the investigation is not completed within 90 days,<sup>26</sup> the SAC must request an extension from the Director of OEE. At that time, a full-scale investigation is opened. However, we found that OEE's former export enforcement information system (b) (7)(E)



Our review of 87 closed case files obtained from the four OEE field offices we visited—all of which had been upgraded to headquarters cases—found that 80 (92 percent) were closed without criminal or administrative action. In some of these cases, we found minimal investigative work

<sup>&</sup>lt;sup>24</sup>Our review predominantly focused on 87 cases closed in FY 2001. Our sample included all of the closed criminal and/or administrative cases from the four field offices that we visited. We were not given access to open criminal or administrative cases.

<sup>&</sup>lt;sup>25</sup>Although the 1989 SAM only required SACs to review cases every 6 months, the Director of OEE informed us that he subsequently issued an ODM requiring quarterly case reviews, and this requirement has been incorporated into the 2002 SAM

<sup>&</sup>lt;sup>26</sup>The 2002 manual stipulates that a field office investigation must be completed within 120 days.

had been conducted and others where no investigative work had been conducted before they were upgraded to a headquarters case.

While we understand that many OEE agents have heavy caseloads (e.g., in July 2002, agents in New York were handling between 30 and 40 cases each), failure to thoroughly evaluate leads up-front could negatively impact a case later on. For example, in several visa referral cases that we reviewed,  $^{27}$  (b) (7)(E)

In such instances, agents informed us that they must trust the company's assertion that U.S.-controlled technology was not transferred illegally. In addition, export control regulations may change during the course of an investigation forcing OEE to decide whether to pursue a situation that was a potential violation (under the old regulations), but may no longer be so. For example, OEE received a number of allegations involving violations of export control laws enacted in 1998 that prohibited certain exports to India and Pakistan, but when the laws were rescinded in 2001, these cases became more difficult to pursue. In general, as one SAC stated, "leads may simply go cold" if not followed up early. When leads are vetted early during preliminary investigations, SACs can better ensure that agents dedicate their efforts to those cases with the greatest potential.

Quarterly Case Reviews. Once a preliminary investigation is upgraded to a full-scale investigation, SACs are required to conduct quarterly case reviews. Quarterly case reviews help the SACs ensure that agents are expending their resources on viable cases and adequately working them. SACs can also help an agent determine a strategy for pursuing a case during these reviews. While many SACs indicated that they conduct quarterly case reviews on "select" cases, not all conduct quarterly case reviews on all cases.

However, we would like to point out two best practices we noted during our visits to OEE's San Jose and New York field offices. First, the SAC in San Jose, on a quarterly basis, requires her agents to summarize any actions taken to date for each case so that she can walk through the actions with them. This information is updated each quarter and is incorporated into the official case file. In addition, during our visit to OEE's New York field office in July 2002, the SAC showed us a recently created quarterly case review form that each of his agents is required to complete. The form requires an update on all cases and if an agent has not taken any action on a case in a few months, the SAC requires an explanation.

Because not all of OEE's SACs conduct quarterly case reviews on all cases, we found that many cases languished in an agent's queue with little or no action.<sup>28</sup> Again, as stated earlier, we found some cases where partial investigative work had been conducted and others where no investigative work had taken place. Our review of the 87 case histories revealed the following:

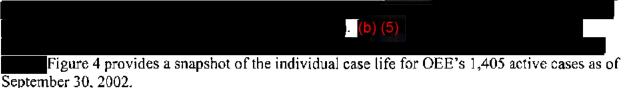


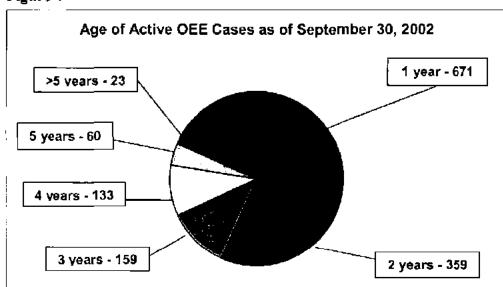
<sup>28</sup>Please note that while our case review focused on cases closed in FY 2001, some of them were opened years ago under former SACs.

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- Seven cases were closed with administrative action, with an average time to case completion of 1404 days (or 4 years).<sup>29</sup>
- Twenty-nine cases were closed with a warning letter, with an average time to case completion of 664 days (or 1.8 years).
- Fifty-one cases were closed due to insufficient evidence or no evidence of a violation, with an average time to completion of 1,044 days (or 2.9 years).

Based on our discussions with various law enforcement agents (from OEE, Customs, and FBI), we understand that agents may require several years to investigate potential criminal or administrative cases. However, the majority of OEE's investigations close with no violation after many months of being in an active case status. In addition, in FYs 2001 and 2002, 15 and 10 cases were closed, respectively, because the 5-year statute of limitations had expired. We would like to point out that the Acting Assistant Secretary for Export Enforcement visited the Los Angeles Field Office after we completed our fieldwork there to provide the office with guidance and direction on "cleaning up" their old cases. Specifically, we were told that she instructed the agents to close all cases that were over four years old that had no merit. We believe this was a positive effort and that OEE headquarters (b) (5)





#### Figure 4

Source: Export Enforcement, Bureau of Industry and Security.

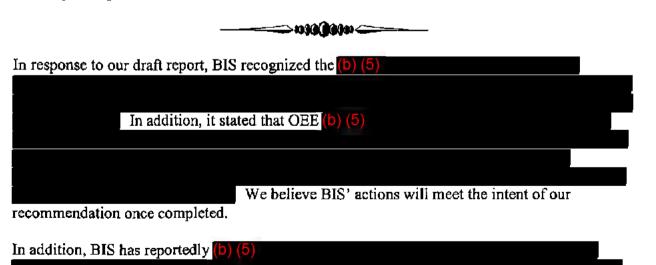
<sup>&</sup>lt;sup>29</sup>Some of these were also untimely due to, among other things, OEE's investigative process and the administrative review process (see section C).

During the course of our review, we also noted that OEE headquarters does not monitor warning letters issued by SACs. In FYs 2001 and 2002, 208 and 132 cases, respectively, were closed with warning letters. The SAM provides guidance on issuing a warning letter; however, most SACs we spoke with stated that they rely on their own experience in deciding to issue these letters rather than on the guidance. There is currently no requirement for a SAC to seek headquarters' clearance for issuance of a warning letter. (b) (5)

**RECOMMENDATIONS.** OEE headquarters should do the following:

| * | (b) (5) |
|---|---------|
| * | (b) (5) |
| * | (b) (5) |

Require SACs to provide quarterly reports to OEE headquarters on the status of their quarterly case reviews. Such reports should include the total number of cases open in their field office, the number of cases opened and closed during a particular quarter, as well as warning letters, indictments, convictions, and the number of administrative cases pending at headquarters.



| (b) (5)<br>this end, BIS' (b) (5)                | ,. Towards<br>1. |
|--|------------------|
| With regard to our recommendation that (b) (5)   |                  |
| In the interim, as stated above, the Acting Assi | stant Secretary  |
| for Export Enforcement will (b) (5)              |                  |
|  |                  |
|  |                  |
|  |                  |

Finally, according to BIS' written response, in February 2003, OEE instituted a policy that requires the SACs to conduct case reviews twice a year, not quarterly. The SACs are required to report to the Director and Assistant Director for Investigations every six months that they have completed reviews of all their field office cases. As such, OEE stated that it will amend the SAM accordingly.

#### Headquarters case leads need to be evaluated

Export Enforcement does not routinely track the outcome of headquarters leads, such as (b) (7)(E) (7

### (b) (7)(E) . We found that many agents and SACs dislike

headquarters leads because they take up a lot of their time but typically do not result in criminal or administrative cases.

We could not fully evaluate these issues since neither OEA nor IFSD tracks the number or disposition of their referrals. However, our review of the 87 closed cases supported some of the SACs' and agents' concerns (see table 2).



#### Table 2: Disposition of Headquarters Leads from Select Closed OEE Cases

| Type of Lead  | Administrative | Warning Letter | No Violation or                       |  |
|---|----------------|----------------|---------------------------------------|--|
|   | Action         |                | , , , , , , , , , , , , , , , , , , , |  |
|   |                |                | Evidence                              |  |
| Project Outreach  | 0              | 0              | 5                                     |  |
| Intelligence  | 1              | 2              | 3                                     |  |
| (b) (7)(E)  | 0              | 0              | 11                                    |  |
| (b) (7)(E)  | 0              | .7             | 4                                     |  |
| * The leads from the remaining 54 cases in our sample were generated from self-disclosures, informants, |                |                |                                       |  |
| spin-offs from other cases, and end-use checks.   |                |                |                                       |  |

Source: OEE's Washington, New York, Los Angeles, and San Jose Field Offices.

In our March 2000 export control review, we recommended that BIS periodically assess its Visa Application Review Program to determine whether the resources dedicated to it justify the results. Currently, there are approximately 2.75 full-time equivalents (ranging in grades from a GS-12 to a GS-14) devoted to this program. The Director of OEA informed us that BIS' FY 2003 budget request also includes an additional full-time equivalent to be applied to this



Given that the assessment was not completed until the end of our review, we were unable to fully assess all of the information contained in the report.<sup>30</sup> However, we would like to note some highlights from the assessment and offer a few general comments. (b) (7)(E)







(b) (7)(E) was incorporated into existing investigations. As we discussed in the first part of this section, the fact that there are open investigations stemming (b) (7)(E) does not, in our opinion, indicate whether the resources dedicated to the program justify the results. Again, our review indicates that investigations can remain open without any investigative work being done on them. A more appropriate measure of the usefulness of this program and its leads would

<sup>&</sup>lt;sup>30</sup> The visa application review assessment was not provided to the OIG until January 28, 2003.

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be a measure of the outcome of these referrals as they relate to the enforcement of export controls, e.g., visa referrals that resulted in warning letters issued, criminal convictions, or administrative sanctions.

The BIS 2003 assessment also indicates that, as a result of the visa review program, (1) 28 visa denial recommendations have been submitted to the State Department, (2) (b) (7)(E) (b) (7)(E),  $^{31}$  and (3) 3 warning letters were issued. In addition, the assessment highlights the fact that there have been significant intelligence benefits resulting from this program.

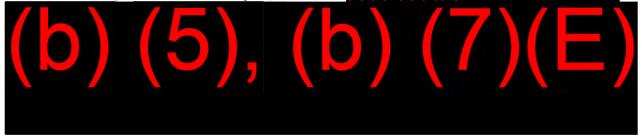
While we do not question (b) (7)(E)

-according to its FY 2003 Performance Plan, BIS states that it will devote its current level of enforcement resources to investigations that have the highest probability of leading to the prosecution of export violators. Accordingly, it follows that Export Enforcement's involvement in the program (i.e., the number of resources dedicated to this program and the scope of the program), as well as the **DIFFE** and intelligence research programs, should focus on its mission of identifying and following up on the most effective leads for developing criminal and/or administrative export enforcement cases.

**RECOMMENDATION.** Export Enforcement (b) (5)



In its written response to our draft report, BIS stated (b) (5), (b) (7)(E



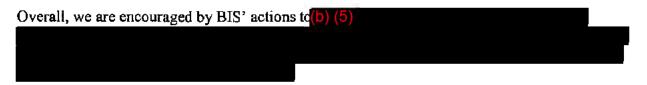
However, BIS' written response also noted (b) (5), (b) (7)(E)

<sup>31</sup> (b) (7)(E)

#### (b) (5), (b) (7)(E)

. While we were not provided a copy of the actual survey results, only four of the cases cited in the assessment appear to be highly active export enforcement criminal investigations (involving search warrants and detentions, as well as, two indictments in one case). An additional case was apparently accepted by an AUSA for criminal prosecution but later declined due to insufficient evidence and a warning letter was issued instead.

Our report highlighted three specific types of headquarters leads that, according to many QEE agents and SACs, resulted in few criminal or administrative cases. Again, our report notes that we were unable to fully evaluate these issues since neither OEA nor IFSD tracked the number or disposition of their referrals. However, as discussed in our draft report, our review of 87 closed cases supported some of the SACs' and agents' concerns (see table 2).



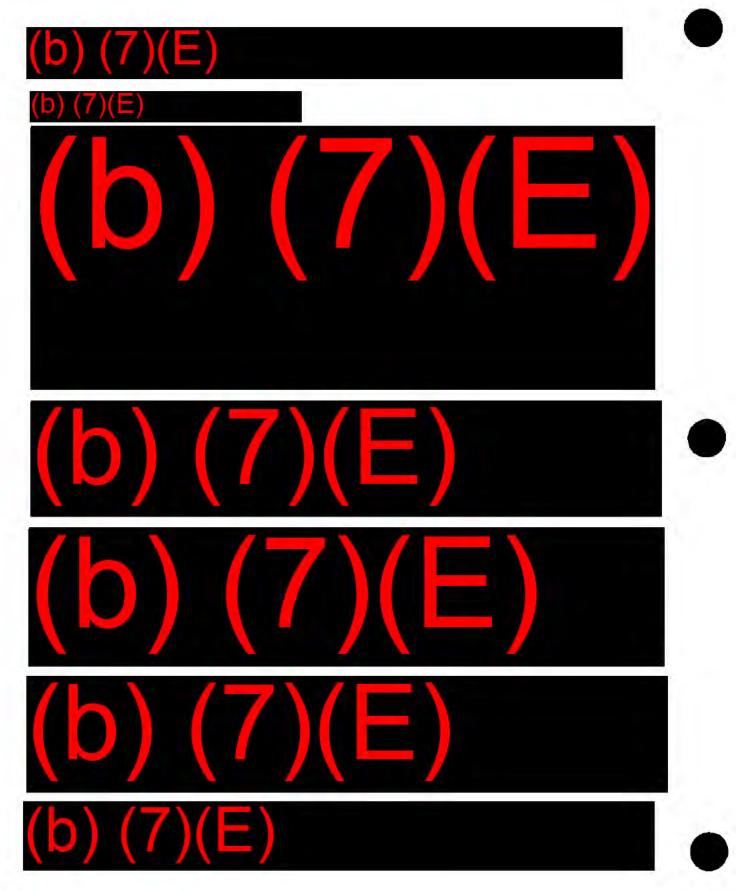
#### **B**. License determinations are problematic

In the early stages of an investigation, OEE requests a license determination (LD) to help it decide whether a company or individual has violated, or attempted to violate, the EAR and thus whether enforcement action is warranted. An LD, completed by a licensing officer, is an official finding by Export Administration that indicates (1) whether the item is subject to the EAR, (2) the reason for control, if any, (3) the export control commodity number for the item, and (4) the licensing policy for the export of the item to the specified destination (i.e., a presumption of approval or denial of an export license application for the commodity and destination in question). OEE reported requesting 441 LDs from Export Administration during FY 2001.

If an LD indicates that the export of a product requires a validated license, and the company or individual made, or attempted to make, unlicensed shipments, then OEE is justified in pursuing criminal or administrative action. A determination must be certified to enable agents to obtain a search warrant or charging letter.<sup>32</sup> A certified LD is a notarized document that is signed by the appropriate Export Administration division director and becomes evidence in the criminal or administrative proceeding.



<sup>&</sup>lt;sup>32</sup>A charging letter is a formal complaint against a company, which indicates BIS' reasons for believing that a violation(s) of the export control laws has occurred.

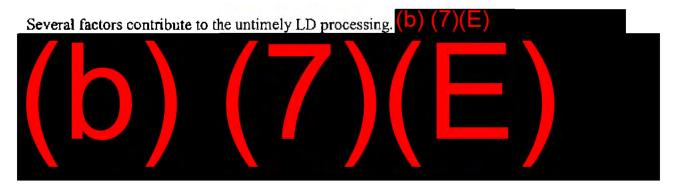




#### LDs need to be more timely

During our period of review, the target for LD processing was 30 days. However, in FY 2001, the average processing time was 73 days, and in several instances, LDs remained pending more than a year after they were requested. For example, as of September 30, 2002, two certified LDs requested on March 8, 2001, had not been completed (a delay of approximately 562 days).

Untimely LDs undermine OEE's ability to fulfill its mission. Late determinations can have serious consequences: (1) investigations may be placed on hold, charges dropped, or cases terminated; (2) case presentations to AUSAs may be postponed; and (3) issuance of charging letters delayed.



To improve the quality and timeliness of LDs, Export Administration and Export Enforcement drafted a License Determination Work Plan in August 2002, and established a working group comprised of staff from both offices. The working group, known as the Tiger Team, is expected to meet bimonthly to conduct an up-front review of LD requests, resolve issues on pending LDs, and foster greater communication between Export Administration and Export Enforcement.

Under the plan, Export Administration has agreed to a 25 working day target for processing LDs. We note that the Tiger Team is making progress toward achieving this goal. During November 2002, 38 determinations were completed in an average processing time of 25 days.

The work plan also calls for all determinations to be certified as part of the LD process. To facilitate certification, Export Enforcement has added (b) (7)(E) Given that LDs are a

critical element in export control enforcement, we support Export Enforcement's efforts to certify all determinations before issuance.

**RECOMMENDATIONS.** To ensure that the objectives of the License Determination Work Plan are achieved, Export Administration and Export Enforcement should monitor the implementation and progress of the plan. We also recommend that Export Administration ensure that division directors and licensing officers complete "accurate and timely" LDs, as required in their respective performance plans.

In addition, Export Administration should (1) provide more instruction and guidance to OEE agents on the information needed to complete a determination accurately and in a timely manner; and (2)(b) (5)

In its written response to our draft report, BIS stated that the Tiger Team, which now reportedly meets weekly to review new and pending LD requests, is ensuring that LDs are completed in an accurately and timely manner. BIS indicated that the average processing time for LDs closed in February 2003 was 27 days as compared to 64 days for LDs closed in October 2002. BIS also stated that to ensure the accuracy of LDs, it has clarified its internal policies to require the licensing division with the strictest controls (e.g., (b) (7)(E)

Additionally, to ensure that LDs are not issued with clerical errors, BIS has instituted an additional review of certified LDs. (b)(7)(E)

We believe that BIS actions'

meet the intent of our recommendations to ensure that the objectives of the License Determination Plan are meet and that division directors and licensing officers complete accurate and timely LDs.

In response to our recommendation that Export Administration provide more instruction and guidance to OEE agents on information needed to complete LDs, BIS indicated that it has initiated training at OEE's field offices. As of March 25, 2003, five of the eight field offices received LD training during FY 2003, and the remaining offices will receive the same training by May 2003. BIS stated that additional LD guidelines are being prepared for licensing officers and agents. We support these instructional efforts and request that a copy of the additional LD guidelines be provided to us as part of the action plan.





Finally, in its response, BIS stated that we identified problems based on only a handful of LDs completed in FY 2002. In addition to the problems we identified concerning LDs in our 1999 export licensing report, our current review identified many inaccurate, inconsistent, and untimely LDs and certified LDs. For purposes of this report, we discussed only the most egregious LDs cases identified in order to highlight the adverse impact that problem LDs have on Export Enforcement's investigative process.

#### C. Administrative case processing and the collection of penalties could be improved

Export Enforcement pursues administrative action against a company (or individual) under any of four scenarios: (1) the investigation demonstrates no criminal intent on the part of the subject in committing the export control violation; (2) the U.S. Attorney's Office declines to criminally prosecute the case; (3) Export Enforcement decides to supplement a criminal punishment with a civil sanction (i.e., a monetary fine and/or denial of export privileges); or (4) the violators are not subject to U.S. criminal jurisdiction. Regardless of the reason for pursuing an administrative remedy, the case flows through BIS' administrative process in the same manner.

The Office of Chief Counsel for Industry and Security (OCC) represents Export Enforcement in all administrative enforcement proceedings. In both FY 2001 and FY 2002, OCC closed 25 administrative enforcement cases (see table 3).<sup>33</sup> As a result, civil penalties totaling \$2,392,000 and \$5,198,500, respectively, were imposed.



#### Table 3: Results of Administrative Enforcement Cases (FYs 2001-2002)

| Results  | FY 2001 | FY 2002 |
|--|---------|---------|
| <b>Civil Penalties (including denial of export privileges)</b> | 13 (5)  | 18 (5)  |
| Denial of Export Privileges Only                               | 6       | 3       |
| Section 11(h) Denial*  | 4       | 1       |
| Temporary Denial Order   | 1       | 3**     |
| Other  | ***     | 0       |

\*Section 11(h) of the EAA authorizes the Secretary of Commerce to impose a denial of export privileges for up to 10 years upon anyone convicted of specific violations, such as espionage.

\*\*Includes renewals of existing temporary denial orders.

\*\*\* An existing order was amended.

Source: BIS' FY 2001 Annual Report (Appendix A - Table 5-2) and FY 2002 Annual Report (Appendix D -Table 1).

Our review of the administrative remedy process revealed (1) a lack of transparency with regard to how administrative penalties are determined, and (2) untimely handling of some cases by OCC. We also found that OEE is not taking follow-up enforcement action against companies and individuals who fail to pay administrative penalties.



<sup>&</sup>lt;sup>10</sup>A case is considered closed by OCC on the date the order is signed.

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#### Determination of penalties needs to be more transparent

According to its charter, BIS established the Administrative Case Review Board (ACRB) in February 2002 to ensure that export enforcement cases are processed consistently, fairly, and in accordance with best legal practices. The ACRB reviews and decides upon administrative charges (set forth in pre-charging and charging letters), settlement offers, settlements, dismissal of charges, and other key decisions (e.g., litigation strategy). The charter also stipulates that the ACRB receives recommendations with respect to these issues from OEE or the Office of Antiboycott Compliance (OAC), as appropriate.

The ACRB advises the Assistant Secretary for Export Enforcement at the important stages of administrative cases and assists in determining Export Enforcement's positions related to the prosecution of cases. The Assistant Secretary has the authority to affirm, reject, remand, or modify the ACRB's recommendations. According to its charter, the ACRB is composed of three members—(1) the Deputy Assistant Secretary for Export Enforcement, who presides over board meetings, (2) the Chief Counsel for Industry and Security, and (3) either the Director of OAC for an export control case or the Director of OEE for an antiboycott case.

Prior to the creation of the ACRB, the shaping of legal strategy, negotiation, and resolution of cases were primarily handled at a lower level of management involving the Director of OEE and OCC attorneys. The Deputy Under Secretary of Commerce for Industry and Security, who participated in the creation of the Board, informed us that, while there were no major problems with the pre-ACRB administrative process, the purpose of designing the ACRB was to ensure best legal practices and that the positions taken by Export Enforcement in cases reflect the policy goals of BIS, as set by senior managers.

Of the 25 administrative enforcement cases closed in FY 2002, the ACRB deliberated 5 of them. Because the ACRB reviewed few of the administrative cases closed during FY 2002, we were unable to fully analyze its impact on the processing and resolution of administrative cases. However, we did find that the ACRB's administrative penalty decisions are not always transparent.

Specifically, no guidelines or table of penalties exists for determining appropriate fees or number of years to deny export privileges. Without formal guidelines, penalties may appear arbitrary or inconsistent and future board members could have a difficult time deciding cases without a source of guidance to consult. BIS' Chief Counsel stated (b) (5)

A table of penalties could work better under any of the proposals for a new Export Administration Act which would have a higher range of penalties.

**RECOMMENDATION.** Export Enforcement and OCC (b) (5)

In its response to our draft report, BIS disagreed with a recommendation we had in the draft report (b) (5)

BIS stated that the ACRB is an advisory and review body, not the final decision-making authority in the administrative resolution of cases – as they contend we imply in stating the "ACRB reviews and decides upon administrative charges" (see page 27). We want to point out that the language in our report describing the role of the ACRB was taken directly from BIS" "Export Enforcement Administrative Case Board" charter, dated February 19, 2002, which was provided to us by Export Enforcement. If the ACRB is in fact only an advisory board, BIS should revise the charter to reflect the actual intent of the board.

In addition, although we recommended that BIS (b) (5)

As such, we believe BIS' alternative is reasonable and will

address the problem.

Processing of administrative cases should be more timely

Export Enforcement relies on OCC to initiate timely action against individuals and companies that violate the export control laws. From our sample of 87 cases, we reviewed the 7 cases closed with administrative sanctions and found that OCC's processing of these cases was sometimes slow, for example:

An OEE investigation of a Pakistani company ("Company M"), initiated in June 1992, revealed that the firm was a fictitious front company. OEE sought an administrative sanction in the form of an indefinite denial order to preclude U.S. firms from making future shipments to the company. On June 23, 1994, OCC accepted the case, but did not issue a charging letter until April 1, 1997, after the statute of limitations began to expire.<sup>34</sup> A year later, and with no response from Company M to the charging letter, OEE requested that default action be taken. However, OCC did not file the default motion until August 2000, which resulted in a final order on December 14, 2000, denying Company M's export privileges for 10 years. The untimeliness in this case was partly due to OCC's concerns about initiating the default action without knowing whether the firm had received the charging letter. However, OCC knew, upon accepting the case and issuing the charging letter, that Company M was fictitious and, therefore, unlikely to respond to the letter.

<sup>&</sup>lt;sup>34</sup>There were multiple violations committed. The date of the oldest violation for statute of limitations purposes was January 29, 1992.

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- A self-disclosure case<sup>35</sup> was accepted by OCC on January 20, 2000. The proposed charging letter was issued on February 24, 2000, but the final order was not signed until May 22, 2001, despite the fact that the company was cooperative in the settlement. OCC closed the case on July 16, 2001.
- OCC was also slow to initiate action in a Section 11(h) denial case. Though the case was accepted on June 9, 1999, OCC did not take any action until March 24, 2000. OCC closed the case on September 28, 2000.

Some agents also informed us that since the ACRB's creation, the processing time for administrative cases remains slow. For example, a case accepted by OCC in September 2001, had yet to be presented to the ACRB for a proposed charging letter as of January 3, 2003. As of early December 2002, 34 export control cases were on the ACRB's schedule, but Export Enforcement was unable to provide us with the chronologies of these cases so that we could evaluate the case processing times.<sup>36</sup>

Several factors contribute to OCC's slow case processing:

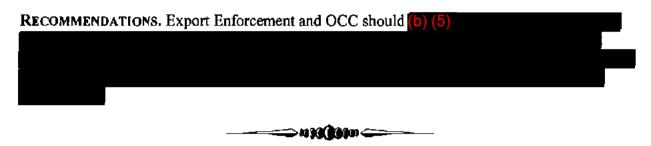
- Neither Export Enforcement nor OCC has established time lines for case processing by OCC: there is no target date (e.g., 30 days from receipt of a case) by which an OCC attorney must present a proposed charging letter to the ACRB. We discussed this issue with the Acting Assistant Secretary for Export Enforcement and the Chief Counsel for Industry and Security; both officials agree that internal processing deadlines are beneficial and intend to move forward on designing new administrative case procedures to include the fast-tracking of certain types of cases.
- OEE's administrative case reports are not always complete or well prepared, and OCC attorneys must contact the agent for clarification or additional information before a case package can be presented to the ACRB. According to the Acting Assistant Secretary for Export Enforcement, the new administrative case procedures will include a new format for OEE to use in presenting its cases. This format should satisfy the requirements of OCC and the ACRB.

Untimely case processing could impede BIS' ability to successfully obtain administrative remedies against violators of the export control laws. A case that is not promptly processed could be terminated should the statute of limitations expire, or weakened as evidence gets old or export control regulations change. In addition, delays in OCC's processing of cases could result

<sup>&</sup>lt;sup>35</sup>A company or individual voluntarily disclosing to OEE that it has or may have committed an export control violation(s).

<sup>&</sup>lt;sup>36</sup>In October 2002, we requested from Export Enforcement the case chronologies of the 34 cases to determine the number of days it took OCC, after accepting the cases, to present the case packages to the Board and issue proposed charging letters. Despite numerous requests to Export Enforcement for the information, we did not receive the case chronologies and, therefore, were unable to evaluate OCC's processing of cases since the ACRB commenced.

in continued shipments of controlled commodities by or to a problem company that has a denial of export privileges sanction pending.



In its written response to our draft report, BIS reported that OEE and OCC (b) (5)

. We believe that BIS' actions will meet the intent of our recommendations once completed. We request that a copy of the new administrative case procedures and the revised OEE case report format be provided to us as part of the action plan.

#### OEE should take stronger action to enforce payment of penalties

Collection of penalties is the final step in Export Enforcement's administrative process. BIS' Office of the Comptroller receives these payments and forwards them to Commerce's National Oceanographic and Atmospheric Administration's (NOAA's) Office of Finance and Administration for processing and deposit in the U.S. Treasury. NOAA sends a reminder letter to late payers every 30 days for up to 6 months, after which the account is considered delinquent and referred to the Treasury for collections. Each month, the comptroller sends copies of account deliverables to both OCC and the Office of the Director of Export Enforcement.

OEE attempts to mitigate the potential for delinquencies in its administrative orders by suspending a denial of export privileges—when applicable—on the condition that defendants comply with the terms of the order, including payment of penalties. Failure to pay penalties could result in the imposition of a full denial of export privileges.

When delinquencies do occur, the EAR gives OEE authority to initiate export denial proceedings. However, we found that OEE is not taking such actions. Specifically, we reviewed five delinquent OEE accounts out of nine being monitored by the comptroller. These accounts had combined outstanding penalties exceeding \$300,000 out of nearly \$730,000 owed BIS. OEE had taken no additional steps to enforce payment from any of the five respondents. This failure to implement measures to secure payment of penalties might encourage noncompliance by EAR violators and thereby diminish the effectiveness of export enforcement. However, as a result of our inquiry, the office of the OEE Director sent emails to the appropriate field offices directing the agents in charge of these cases to contact the companies and/or individuals and investigate these matters further. Since issuance of our draft report, OEE determined that one company had



gone bankrupt, one company went out of business, and three accounts were referred by NOAA to Treasury for collection.

We confirmed that OEE receives monthly account activity reports from BIS' Office of the Comptroller, and is therefore being notified of delinquencies; but we learned that office staff has been simply filing the reports without reviewing them. Instead, a staff person within the OEE Director's office had been relying on direct notification from a staff person in the comptroller's office, via e-mail or phone, regarding specific delinquencies. However, this practice ceased in mid-2000 when the responsibility for monitoring BIS accounts was transferred to another individual within the comptroller's office.

**RECOMMENDATION.** To enforce administrative sanctions, Export Enforcement (b) (5)

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D. Enhanced Special Agent Manual guidance and agent training would improve enforcement capabilities

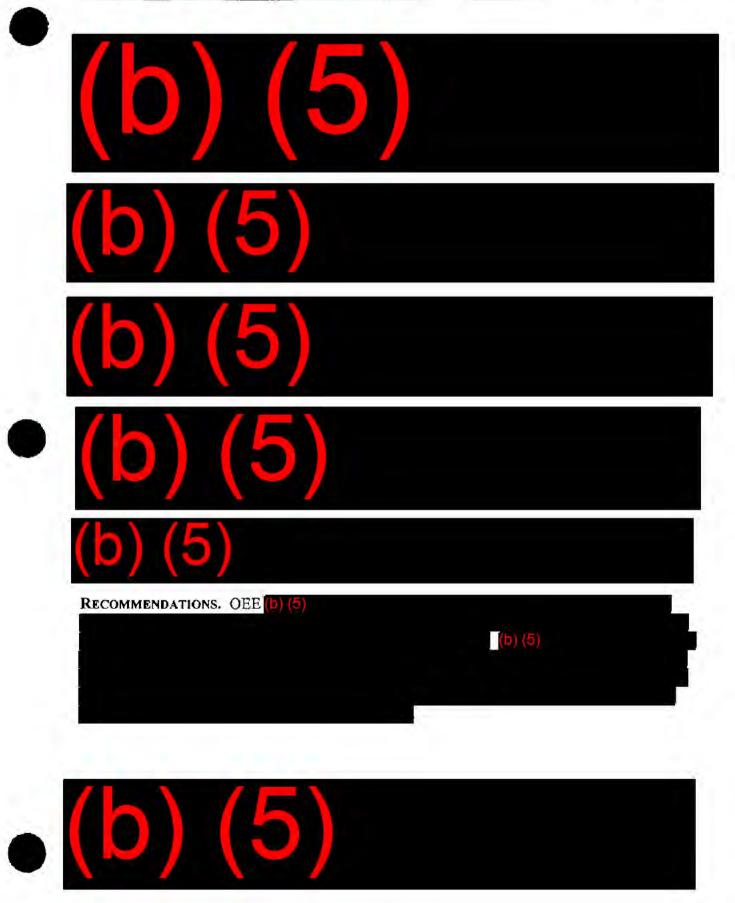
#### BIS (b) (5)

The Special Agent Manual is the OEE agents' guidebook on investigative case management, administrative policies and procedures, personnel issues, and export enforcement operations. Until the manual's revision in November 2002, agents had been working with an outdated 1989 version. We noted that the 2002 SAM is in electronic format, making it easier to update and disseminate to agents nationwide. We also noted significant improvements in the revised manual, such as revised travel and official vehicle use policies, new guidance on outside employment, and agent disciplinary procedures.

While we commend OEE for this revision, we note that the (b) (5)

#### (b) (5)

U.S. Department of Commerce Office of Inspector General





In its written response to our draft report, BIS informed us(b) (5)

We request that a copy of (b) (5)

In addition, BIS (b) (5)

We acknowledge this effort and request that a copy of this statement be provided to us in the action plan.

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completed.

#### Agent training program should be restructured

BIS' 2002 Annual Report to the Congress states, "Training in export control laws and in modern investigatory techniques is crucial to the development of Export Enforcement's special agents." However, we have some concerns about the adequacy of training OEE provides its agents. The agency tries to hold annual training seminars. In FY 2002, it conducted a 3-day basic course for new agents and a weeklong advanced course for all agents. The majority of agents we interviewed spoke highly of these seminars, indicating that the course materials and instructors (e.g., AUSAs, OCC attorneys, and FBI agents) were especially beneficial.

Still, agents we interviewed and surveyed indicated that additional training would improve their performance, especially in areas such as advanced interviewing techniques, presentation skills, intelligence and counterintelligence, money laundering, and export control regulations. We believe improvements in the following areas would also enhance the enforcement capabilities of OEE agents and, by extension, the agency's success at achieving its mission:

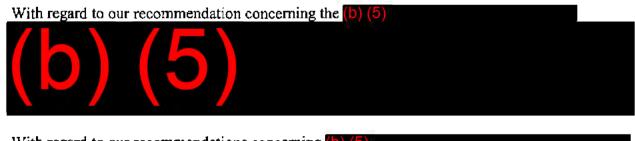
New agent training. This training is not consistently offered. Several agents who participated in the FY 2002 seminar told us that they had been employed by OEE for 3 years and were just now receiving this "basic" training. In addition, while all agents complete formal basic criminal investigative training at a federal law enforcement facility, OEE does not routinely provide orientation that specifically relates this training to the agency's mission, programs, policies, rules, regulations, and investigative procedures, as do some agencies. At Customs, for example, agents who complete basic criminal investigative training receive separate "add-on" instruction in the specialized laws and regulations that the agency enforces. **On-the-job training program.** Both the old and new SAMs provide guidance for an on-the-job training (OJT) program for new agents. OJT allows newly hired agents the invaluable opportunity of working on criminal or administrative export enforcement cases under the guidance of an experienced OEE investigator. (b) (7)(E)

| Career develo | opment. (b) (7)(E) |  |  |
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**RECOMMENDATIONS.** Export Enforcement should do the following:



In its written response to our draft report, BIS stated that it received excellent feedback from the agent training held in April 2002. As such, it is in the process of adapting some of that material together with new case studies and a new regulations course to develop a new agent training module before the end of the year. Furthermore, the response stated that OEE has received good feedback on its revised on-the-job training program that was incorporated into its November 2002 SAM. While we are encouraged by BIS' actions, we want to emphasize the importance of ensuring that the new training materials, including its on-the-job training program, are implemented. BIS' actions meet the intent of our recommendation.



With regard to our recommendations concerning (b) (5) (b) (5)



<sup>*E.*</sup> (b) (5)

Interagency cooperation on export enforcement is essential to better safeguard U.S. national security and foreign policy interests. This collaboration is imperative to using limited investigatory resources efficiently, gaining access to the resources and expertise of others, reducing duplicative efforts, and conducting successful prosecutions. We examined Export Enforcement's relationship with various Assistant U.S. Attorneys located across the country, Customs, FBI, CIA, and the U.S. Postal Service. We found great variation in Export Enforcement's level of coordination and cooperation with these agencies, and noted that the positive interplay of personalities, especially among agents and their counterparts, is key to building long-term, beneficial interagency relationships.



#### U.S. Attorneys

U.S. Attorneys serve as the nation's principal litigators under the direction of the Attorney General and the U.S. Department of Justice.<sup>40</sup> They conduct most of the trial work in which the United States is a party. The U.S. Attorneys have three statutory responsibilities: (1) the prosecution of criminal cases brought by the federal government; (2) the prosecution and defense of civil cases in which the United States is a party; and (3) the collection of debts owed the federal government which are administratively uncollectible.<sup>41</sup>

There are 93 U.S. Attorneys stationed throughout the United States, and on Guam, Puerto Rico, the Northern Mariana Islands, and the Virgin Islands. Each U.S. Attorney is the chief federal law enforcement officer of the United States within his or her particular jurisdiction and has a staff of Assistant U.S. Attorneys (AUSAs), who handle casework and litigation. OEE agents work with AUSAs to make arrests and obtain search warrants, grand jury subpoenas, indictments, and convictions.

We discovered that the OEE field offices have vastly different relationships with the AUSAs located in their respective regions. For instance, according to SACs and agents, some AUSAs are more interested than others in accepting export control cases for criminal prosecution. An OEE agent presents a case to the AUSA for possible criminal prosecution, if the case evidence indicates that an export control violation occurred with criminal intent

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<sup>40</sup> www.usdoj.gov/usao (January 30, 2003).

<sup>&</sup>lt;sup>41</sup>Title 28, Section 507 of the United States Code.

(i.e., it was committed knowingly and willfully). The agent provides the AUSA with a case report that outlines the details of the investigation, including the violations and the specific laws and regulations over which OEE has jurisdiction.

We heard from several AUSAs that OEE's case reports are usually well prepared and contain sufficient evidence and details. As such, the AUSA's decision to accept or decline a case is generally not based on the quality of the work performed by the agent, but rather on other case specific considerations such as the intent of the exporter, number of violations committed, the product type, and the export destination. In particular, the AUSA wants to see evidence of significant violations (i.e., not technical in nature) and an established pattern of misconduct. According to some AUSAs interviewed, although each case is evaluated on its merits, cases that have stronger jury appeal are more likely to be accepted for prosecution (e.g., exports to a designated terrorist entity or embargoed country). Dual-use export control cases, in particular, may lack jury appeal because the products exported may be common items, such as computers, for which the importance of control (versus munitions) is difficult for a jury to understand. In addition, some AUSAs view BIS' internal administrative process as a more appropriate venue for some dual-use cases, especially when the proper punishment is a monetary penalty or when a criminal conviction would yield only probation or a limited prison sentence. Several AUSAs suggested that OEE agents should contact them during the early stages of an investigation for legal assistance to build stronger cases.

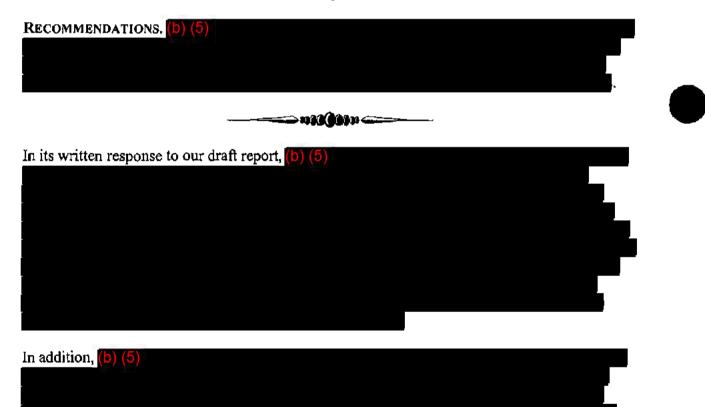
A majority of SACs and agents told us that the expired status of the EAA is the most significant impediment to getting cases accepted by AUSAs—they believe that some AUSAs do not consider export control violations as seriously as other types of cases that have established legal authority for criminal prosecution. Some also believe that the lapse of the EAA undercuts the credibility and importance of the export control laws.

However, while some AUSAs with whom we spoke informed us that the EAA's expired status is not the only indicator as to whether they accept or reject a dual-use export control case, they all acknowledged that the lack of strong export control legislation does play into that decision. Some AUSAs stated that it is difficult for a jury to grasp the importance of export controls when new export control legislation has not been approved by the Congress. Since early 1990, both the Congress and the Administration have tried to rewrite the basic law that authorizes the President to regulate exports from the United States. According to BIS officials and all of the AUSAs whom we spoke with, a new EAA is clearly needed to strengthen BIS' enforcement efforts. The focus of the continuing policy debate about the specifics of different versions of draft EAA legislation pertains to disagreements over what national security and proliferationbased controls are needed to restrict exports of dual-use technologies to high-risk countries and entities of concern. There is a wide range of opinions on how the government's export control policies and practices should balance the need to protect U.S. national security and foreign policy interests<sup>42</sup> with the desire not to unduly hamper U.S. trade opportunities and competitiveness. Striking this balance poses a significant challenge for the parties involved.

<sup>&</sup>lt;sup>42</sup>Foreign policy export controls relate to the broad issues of human rights, anti-terrorism, regional stability, chemical and biological warfare, missile technology, and nuclear nonproliferation.

In addition, some AUSAs indicated that the legal standards for convicting a defendant under IEEPA are higher than those were under the EAA. Under IEEPA, there is a requirement that the crime be willful, i.e., a specific intent offense. As such, the AUSA must demonstrate that the defendant knew of and understood the law, and deliberately violated or attempted to violate the law. Whereas the EAA, which also had criminal provisions that required willfulness, included a provision of mere knowledge of the law. As such, under the EAA, the AUSA had to show only that the defendant acted intentionally, and did not have to prove that the defendant knew what he/she did was a crime.

In previous years, Export Enforcement, OEE, and OCC conducted a few workshops on export control laws and regulations for AUSAs in an effort to promote interest in these cases. Both the Acting Assistant Secretary for Export Enforcement and the Director of OEE emphasized to us the importance of reaching out more to AUSAs on a one-on-one basis to encourage them to accept specific OEE cases for criminal prosecutions. We support these efforts as a means of increasing interagency cooperation but encourage BIS to seek additional ways to work with more AUSAs to increase acceptance of OEE cases for prosecution.



U.S. Department of Commerce Office of Inspector General





U.S. Customs Service

Under the EAA, BIS and Customs share responsibility for enforcing the export control laws on dual-use commodities. (See Figure 5 for more information about Customs.) At one time, BIS' OEE and Customs had persistent disagreements over coordinating investigations, pooling resources, and handling overseas cases, which hampered the investigative efforts of both agencies. As a result, BIS and Customs signed the 1993 Export Enforcement Coordination Procedures between the Office of Export Enforcement and the United

States Customs Service (the 1993 MOU), which outlines the authorities and procedures for coordinating their law enforcement activities.

According to agents and managers at both OEE and Customs, the overall relationship between the two agencies has since improved, with an increase in cooperative efforts and joint investigations. For example, OEE and Customs worked together in investigating TAL Industries, Inc., which was sentenced to pay a criminal fine of \$1 million and to a maximum 5-year period of corporate probation in May 2001, for making false and misleading statements in connection with a application submitted license by the McDonnell Douglas Corporation for the export of machine tools to China. OEE and Customs agents also conducted a joint investigation on Massive International, which received a fine of \$10,000 in April 2002, for the illegal export of hydraulic stud tensioners to a company listed on the Entity List.<sup>43</sup>

However, during our review, we discovered that OEE and Customs are not working together as well as they could. We identified several areas in which the agencies need to evaluate and improve their efforts. Figure 5

#### U.S. Customs

As the principal U.S. border enforcement agency, Customs has inspection and investigative resources for enforcing approximately 400 laws. In addition to maintaining a headquarters office in Washington, D.C., there are 20 Special Agent in Charge field offices serving the 50 states. These field offices administer and manage all enforcement activities. Customs employs approximately 3,000 headquarters and field agents, of which 5 percent, or about 150 agents, are dedicated to the Strategic Investigations Division. Customs' Trade Enforcement Group, part of its Strategic Investigations Division, enforces export control and other laws. There are also 20 Customs Management Centers located across the United States, which have jurisdiction over all U.S. ports of entry and exit. Of Customs' 7,500 inspectors, 400 are dedicated to the Outbound program, which is responsible for preventing the export of illegal dual-use commodities and munitions as well as stolen vehicles and currency.

Source: U.S. Customs Service.



<sup>&</sup>lt;sup>43</sup>The Entity List is a listing of foreign end users involved in proliferation activities. These end users have been determined to present an unacceptable risk of diversion to developing weapons of mass destruction or the missiles used to deliver those weapons. By publishing this list, BIS puts exporters on notice of the export license requirements that apply to exports to these parties.

(b) (7)(E)

First, as stated in the 1993 MOU, OEE and Customs agree to exchange a case report list<sup>44</sup> on a monthly basis; however, (b) (7)(E)

Neither the Director of OEE nor the former assistant director of OEE could recall the date of the last case report list (b) (7)(E). Both officials stated that the relationship between the agencies has improved, and as such, formal meetings to discuss problematic issues are no longer necessary at the headquarters level. Instead, they noted that OEE and Customs communicate as needed to address issues as they arise. They added that case information is being shared between some OEE and Customs field offices, and that Customs field offices are referring cases for administrative action to their respective local OEE field office. Because the procedures for coordinating their law enforcement activities have changed since 1993, and Customs will become part of the Department of Homeland Security, Export Enforcement and Customs should evaluate the MOU to determine if the terms and coordination requirements are still valid and, if not, update it as necessary to reflect current law enforcement practices and procedures.

Second, some OEE agents do not query Customs' Treasury Enforcement Communications System (TECS)<sup>45</sup> to determine if Customs has an investigative interest in the same company or individual before commencing an investigation or scheduling an outreach visit.

Third, many OEE agents are not engaging Customs agents and inspectors for assistance in meeting OEE's mission. OEE and Customs offices that fail to cooperate risk negatively impacting their respective agency's enforcement and prosecutorial efforts, as they may conduct parallel investigations and duplicative outreach visits, and consequently use limited law enforcement resources inefficiently. For example, both OEE and Customs agents conduct outreach visits to U.S. companies to educate them about export controls and elicit their cooperation in identifying illegal export transactions. Hence, they should be coordinating and sharing information from those visits to ensure that they do not duplicate their efforts and place an undue burden on exporters.

We found that the reasons for the mixed relations between OEE and Customs in the field are varied:

Both OEE and Customs agents reported that interpersonal relationships are a significant factor in how well the agencies work together. Some SACs and agents are more congenial and proactive than others in networking with their Customs counterparts. We noted that several OEE agents were once Customs inspectors and are perhaps more able and willing to pursue relationships with former coworkers. For example, one OEE agent who had worked at Customs occasionally examines cargo with inspectors and in one

<sup>44</sup>Per the MOU, the case list is to contain at least (b) (7)(E)

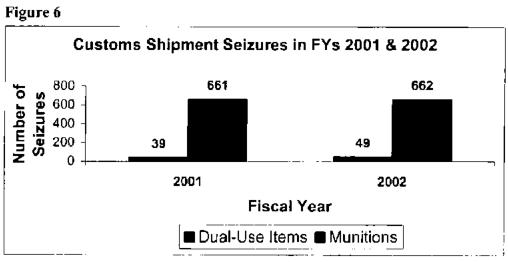
(b) (7)(E)

<sup>45</sup>TECS was created to provide multi-agency access to a common database of enforcement information supplied by Customs, the Drug Enforcement Agency, and the Bureau of Alcohol, Tobacco, and Firearms, instance stopped the export of computer equipment to an Indian company that was on the denied entities list.

- The events of September 11<sup>th</sup> have shifted priorities within Customs' Trade Enforcement Group to a greater focus on the export of munitions and weapons of mass destruction and laundering of terrorist funds.
- Some rivalry between the agencies remains, particularly with regard to which should lead a joint investigation. A number of OEE agents stated that since Customs has more resources for informant payoffs and covert operations, Customs agents sometimes take control of investigations even if the case leads originated with OEE.

Our review identified one area that offers opportunities for greater cooperation between the agencies – Customs' Outbound program which is focused on detecting and stopping the export of illegal items such as unlicensed shipments of dual-use items and munitions, stolen vehicles, and currency. Approximately 400 Customs inspectors are assigned to the Outbound program and are located at most U.S. ports; they are responsible for enforcing the various export regulations. As such, these inspectors conduct outbound examinations (both physical and documentation inspections) of shipments leaving the United States. The inspectors have various computer systems which help them to target certain types of shipments for examinations.

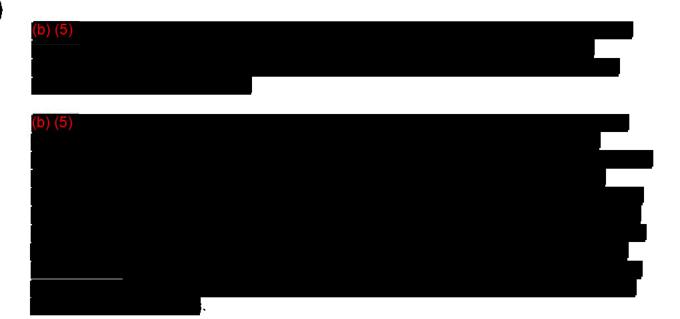
These Outbound inspectors are the last line of defense at U.S. ports and, thus, key in preventing illegal exports of dual-use items. However, in FYs 2001 and 2002, Customs seized far fewer shipments of dual-use commodities than of munitions (see figure 6). According to a Customs official, the majority of dual-use items seized were shotguns. Some Customs inspectors informed us that identifying illegal shipments of dual-use commodities is sometimes difficult because the export regulations are complex and frequently amended. Several inspectors who we spoke with indicated that they would be agreeable to conducting cargo examinations with OEE agents to better identify controlled dual-use items. We believe that, (b) (5)



Source: U.S. Customs Service.

#### **RECOMMENDATIONS.** Export Enforcement should:

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| In its v | vritten response to our draft report, (b) (5) |  |





#### Federal Bureau of Investigation

Overall, our review revealed a somewhat strained relationship between OEE and FBI agents. In particular, we learned that some OEE agents have encountered difficulties working with their FBI counterparts—a situation that sometimes impedes OEE's ability to develop investigations of export control violations. There are, however, a few noted exceptions, especially among those agents assigned to the FBI's Joint Terrorism Task Forces (JTTFs).

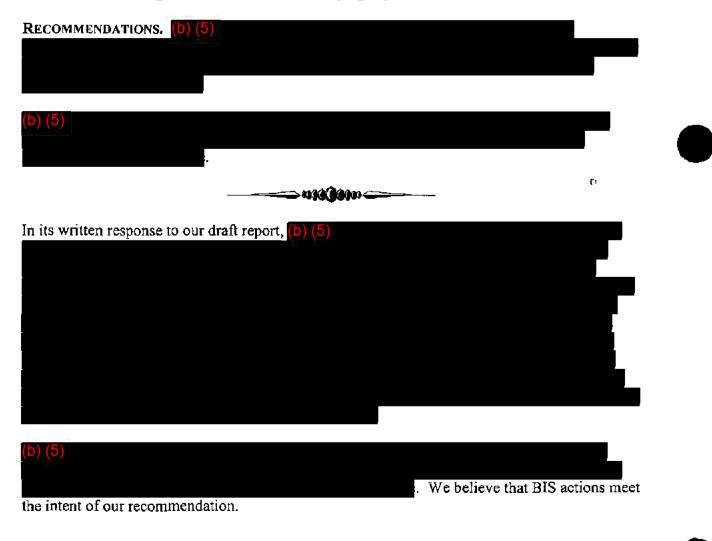
Several factors contribute to the difficult working relationship between OEE and the FBI. Each agency has unique objectives, which, at times, foster divergent goals for an investigation. OEE's primary goal is to develop export control cases for criminal prosecution; the FBI, however, has various missions including conducting counterintelligence activities. Therefore, when the intelligence value of a case exceeds its criminal value, it is not uncommon for the FBI to ask OEE to suspend a criminal investigation so that the Bureau can pursue a suspect for counterintelligence purposes. Two such instances were contained in our sample of 87 closed OEE cases. In addition, OEE agents stated that, because of the "chinese wall" between intelligence and criminal cases, it is often difficult to work a joint investigation with the FBI. Any evidence determined to be of intelligence value becomes "classified," and is thus unavailable for use by OEE.

OEE agents assigned to the JTTFs, however, relate positive experiences working with the FBI. The goal of the JTTFs is to maximize cooperation among federal, state, and local law enforcement and public safety agencies to identify, prevent, and deter terrorist activities.<sup>46</sup>

<sup>&</sup>lt;sup>46</sup>The FBI has established a JTTF in each of its 56 field offices and a national JTTF at its headquarters. The JTTFs are part of the FBI's Counterterrorism Division.

These agents stated that OEE's presence on the JTTFs has improved the FBI's understanding of OEE and its mission and, thus, has enhanced its willingness to share information on potential export control violations. For example, through OEE's participation on the North Texas Joint Terrorism Task Force, OEE's Dallas Field Office became aware of illegal computer shipments to Libya and Syria by Infocom Corporation. On December 18, 2002, a 33-count indictment was returned against Infocom and several individuals. Charges include illegal exporting, making false statements on SEDs, dealing in the property of a designated terrorist, conspiracy, and money laundering.

However, the overall value added to OEE's mission from assigning agents, either full- or parttime, to the JTTFs is uncertain. Several SACs and agents indicated that few export control leads have originated from participation on the JTTFs, and that agents are often tasked with non-export control-related assignments. Agents assigned to a JTTF part-time continue to handle a full OEE caseload, but cannot give total attention to developing export control cases.

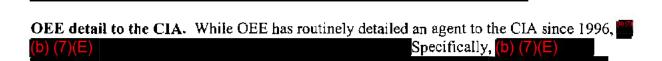




Central Intelligence Agency

The CIA is the U.S. government's lead intelligence agency. Its mission is to provide foreign intelligence related to national security through counterintelligence and other activities, to the President, the National Security Council, and any officials who make and execute U.S. national security policy. The primary objective of intelligence analysis is to minimize the uncertainty with which U.S. officials must grapple in making decisions about American national security and foreign policies.<sup>47</sup> However, during the course of our review, we determined that better coordination is needed between BIS' Export

Enforcement and the CIA to enhance OEE's enforcement capabilities. Specifically, we found that (1)(b)(7)(E)





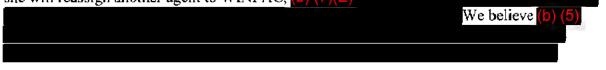
One of WINPAC's<sup>48</sup> key

missions is to study the development of threats, from weapons of mass destruction (nuclear, chemical, and biological weapons) to advanced conventional weapons like lasers, advanced explosives, and armor, as well as all types of missiles. As a part of this mission, (b) (7)(E)

All of OEE's former details to the CIA informed us that they believe there is value added in having an OEE agent detailed to the agency. For example, not only is this agent usually given access to all of WINPAC's databases ((b) (7)(E))

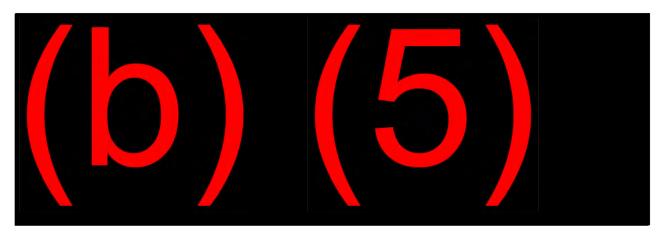
Security Agency and the Defense Intelligence Agency, through their respective representatives at the agency. In addition, one WINPAC official told us that having an OEE agent detailed there helps her analysts better understand OEE's mission. As such, she has formally requested that OEE assign another agent there.

While the Acting Assistant Secretary for Export Enforcement told us that she does not think that she will reassign another agent to WINPAC, (b) (7)(E)



<sup>47</sup>www.cia.gov/cia/di/faq (January 23, 2003).

<sup>49</sup> In 2001, the Director of Central Intelligence merged the CIA's Nonproliferation Center with other CIA units to create WINPAC.



**OEE's participation in the intelligence collection directive process.** During the course of our review, we learned that OEE inconsistently communicates with the CIA regarding the U.S. Government's intelligence collection objectives. Specifically, the intelligence community holds biannual meetings for representatives from various federal agencies to offer feedback on proposed intelligence collection directives. One of the former OEE liaisons informed us that she attended two such meetings—one in early 2001 and one in late 2001. However, OEE has not participated in any such collection meetings since that time. Given that national security issues are incorporated into the CIA's annual collection directives, we believe it is imperative for OEE to actively participate in these meetings. This will help ensure that dual-use export control matters and their connection to weapons of mass destruction, proliferation, and terrorism issues are adequately reflected in the intelligence collection objectives. This is important because it will help determine where the intelligence community's resources will be directed.

CIA's engagement in export control activities. Although one of WINPAC's stated missions involves monitoring activities related to the acquisition of weapons of mass destruction, we are concerned that the CIA may not be (b) (7)(E)

However, given the sensitive nature of this information, we will issue a separate, classified memorandum on this subject. This memorandum will be incorporated in the April 2003 interagency OIG report on export enforcement.

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|----------|---------|
|          |         |
| *        | (b) (5) |
|          |         |
| <b>•</b> | (b) (5) |
|          |         |

**RECOMMENDATIONS.** Export Enforcement should do the following:

In addition, we discuss in a (b) (5) In its written response to our draft report (b) (5) BIS' actions will meet the intent of our

recommendations once completed.

With regard to our recommendation for the Under Secretary of Industry and Security (b) (5)



U.S. Postal Service



During our 1999 export licensing review, we advised BIS that individuals could circumvent dual-use export controls by mailing controlled commodities to countries or entities of concern without seeking an export license. We (b) (5)

The EAR authorizes and directs postal officials to take appropriate action to ensure that individuals and organizations using the U.S. mail service comply with export control laws and

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regulations.<sup>49</sup> Such actions include assuring that exports without a license are either outside the scope of the license requirements of the regulations or authorized by a license exception. In addition, the regulations state that Postal Service officials are authorized to: (1) inspect items or documents to be mailed, (2) question individuals, and (3) prohibit lading. When an item cannot be properly identified, the EAR allows the postal official making the inspection to take a sample for more detailed examination or laboratory analysis.

During our current review, the Director of OEE reminded us that it is important to keep shipments by mail in perspective. Specifically, he stated that there are a large number of these shipments, and the vast majority of them are not subject to the EAR. In addition, many OEE agents informed us that most companies use Federal Express or United Parcel Service for shipping small, high-value exports. While some agents reported coordinating with postal officials to obtain mail covers,<sup>50</sup> no OEE agent, with one exception, reported that they had received leads from or worked an actual export enforcement case with them (see figure 7). Even in this case, the company involved reportedly had never before shipped via the U.S. Postal Service, and it is possible that the company president tried to use the local mail system this time to minimize scrutiny of the packages. Regardless, we believe the case illustrates the potential for using outbound international mail to circumvent dual-use export control laws. Given the fact that the U.S. Postal Service sometimes targets other illegal shipments (e.g., drugs), we believe there may be some mechanism for the U.S. Postal Service to target shipments of dual-use commodities going to countries or entities of concern.

In response to our 1999 recommendation, the U.S. Postal Service stated that, "...a review of the interaction between mail security regulations and export control regulations would be prudent, especially given the sweeping changes in worldwide economic and political conditions...." We believe that this is even more true today, given the continuing war on terrorism. In addition, the Postal Service expressed an interest in learning about what types of exports or geographical areas may be of particular enforcement concern to BIS so that it could create better profiles to improve the U.S. Postal Service's Inspection Service investigations and its coordination with other enforcement agencies.

<sup>&</sup>lt;sup>49</sup>15 CFR, Part 758.7.

<sup>&</sup>lt;sup>50</sup>A mail cover is the process used by the U.S. Postal Service to record information appearing on the outside of any class of mail.

As a part of the current interagency OIG review of export enforcement and the concerns we raised in our 1999 report, the U.S. Postal Service OIG is currently evaluating Postal Service policies and procedures relating to export controls, and we hope that improvements will follow. In our view, the Postal Service's policy for monitoring illegal shipments via the mail appears unchanged since our 1999 review, in that the burden remains only on the customer to fill out the SED.

For example, someone mailing an underwater television camera (assuming that he or she labeled the item correctly on the SED) would not be questioned as to whether the camera was a controlled commodity under the Commerce Control List and required an export license. Under current policy, the Postal Service will assume that if a license was needed, the exporter would be responsible for obtaining it.



#### Figure 7

#### U.S. Postal Service Case Example

In 1995, a San Jose (CA) field office agent received a tip that the president of a small company in Monterey had bypassed the company's export administrator and personally taken four packages to the Monterey post office for shipment to Taiwan. The packages contained pistol laser sights that required an export license, for which the company did not apply. The agent relayed this information to postal inspectors in San Jose, who then contacted the Monterey postmaster, requesting that she detain the packages until the OEE agent could obtain a search warrant. The agent secured the warrant and traveled to the Monterey post office to execute the search, with the postmaster as a witness. When the unlicensed commodities were discovered. the postmaster turned her chain of custody over to the OEE agent, who seized all four packages as evidence. The agent indicated that the postal officials were helpful in offering prompt and immediate assistance.

As a result of the investigation, BIS imposed a \$10,000 civil penalty on the company.

Source: OEE San Jose Field Office, Bureau of Industry and Security.

In its written response to our draft report, BIS stated that it has previously consulted with the U.S. Postal Service on export enforcement matters, and as a result, the Postal Service has revised its mail carrier manual to include red flag warnings for its employees to use when examining mail. BIS has also obtained points of contact in the U.S. Postal Service to notify when it has information concerning suspicious transactions. As such, BIS does not believe that further clarification of roles with the Postal Service is necessary. However, after issuance of our draft report, the U.S. Postal Service OIG informed us that Customs and the U.S. Postal Service conducted a two-week pilot program on reviewing outbound mail at some of the Postal Service's 12 international mail centers. As a result of the pilot program, we understand that Customs and the Postal Service have agreed to expand outbound mail inspections at all 12 centers that process international mail. We believe this is a positive effort and that BIS could be an integral player,

along with Customs and the U.S. Postal Service, in the targeting of potential illegal dual-use exports to be inspected. As such, we (b) (5)

#### II. BIS' Other Enforcement Efforts Need Improvement

To help prevent and detect the illegal export of controlled U.S. technology, BIS monitors export licenses to ensure the holders comply with all license conditions, and conducts outreach to educate industry about dual-use export controls and encourage reporting of potential control violations. In addition to these preventive efforts, BIS announced the Transshipment Country Export Control Initiative in October 2002, which seeks to strengthen the trade compliance and export control practices of both governments and industries at the major international transshipment hubs.

The EAR allows BIS to further limit a transaction authorized under an export license by placing conditions on the license itself. This action is an important part of the interagency export license resolution process and offers BIS an additional means for monitoring certain shipments. Of the 54 possible conditions, only 7 require the licensee to submit export documentation to BIS concerning the shipment (see table 4).<sup>51</sup> For each condition, with the exception of "Write Your Own," a standard message is placed on the license indicating the reporting requirements.

| Condition                                 | Regulrements  |
|---|---|
| 1 – Write Your Own                        | Specific reporting requirements, such as supplying a certified sales contract to the U.S. government, are written on the license by the licensing officer.  |
| 10 – Temporary Demonstration              | Authorization is granted for shipment of the described item(s) to the destination country on a temporary basis for demonstration. At the end of the demonstration, the item(s) must be returned to the U.S. or to another specifically authorized country, no later than 1 year from the date of export. BIS must be promptly notified of an item's return.           |
| 12 – Delivery Verification:<br>Standard   | A delivery verification (DV) document is required for all shipments made under<br>this license. The DV form must be obtained from the government of the<br>destination country and the original copy sent to BIS after the last shipment has<br>been made.  |
| 13 – Delivery Verification:<br>Triangular | A DV document is required for each shipment made under this license. Since<br>the referenced license is supported by information contained in a Triangular<br>Import Certificate issued by the purchasing country, the exporter is reminded<br>that the DV certificate(s) must likewise be obtained from the purchasing country<br>within 90 days of the date signed. |
| 14 Post Shipment Verification             | After the first shipment is made against the license, the applicant must send one copy of its shipper's export declaration and bill of lading or airway bill to the Office of Enforcement Analysis. Upon receipt of the documentation, OEA will initiate a post shipment verification.  |
| 17 – Aircraft on Temporary<br>Sojourn     | Upon return of the aircraft, immediate written notification must be sent to BIS*<br>Office of Exporter Services.  |
| 20 — Eneryption                           | The applicant must report to BIS biannually the item description, quantity, value, and end user name and address of all transactions made under this license. The reports must cover exports made during the 6-month periods of January 1 through June 30 and July 1 through December 31.   |
| *Note: Condition 14 is manifored by       |   |

| Table 4: | License | Conditions | with | Reporting | Rec | uirements* |
|----------|---------|------------|------|-----------|-----|------------|
|          |         |            |      |           |     |            |

\*Note: Condition 14 is monitored by Export Enforcement; all others are monitored by Export Administration Source: Office of Administration, Bureau of Industry and Security.

<sup>&</sup>lt;sup>51</sup>Our review of BIS' license monitoring efforts focused on six of the seven license conditions with reporting requirements (excluding encryption which is monitored by the Office of Strategic Trade's Information Technology Controls Division within Export Administration).

BIS tracks licenses with (b) (7)(E)

- Write Your Own
- Temporary Demonstration
- Delivery Verification: Standard
- Delivery Verification: Triangular
- Aircraft on Temporary Sojourn

Each condition requires the licensee to submit the appropriate export documentation to OExS. BIS policy requires exporters to comply with previous license conditions on expired licenses before they can receive new licenses. Export Enforcement's OEA is responsible for monitoring licenses with post shipment verification conditions (commonly called Condition 14 licenses).

We found that neither Export Administration nor Export Enforcement is adequately monitoring heenses with reporting conditions. We also found that Export Enforcement does not have a national outreach plan to proactively identify which manufacturers and exporters of critical dualuse commodities should be targeted for outreach, or formalized guidance on how agents can strategically identify companies for outreach visits.

### A. Export Administration is not adequately monitoring licenses with reporting conditions

In our 1999 export licensing report, we found that Export Administration was not routinely monitoring licenses, and a backlog of expired licenses requiring agency follow-up had resulted. At that time, OExS informed us that it did not have sufficient resources available to perform this follow-up work. Our current review found that Export Administration's license monitoring remains inadequate.

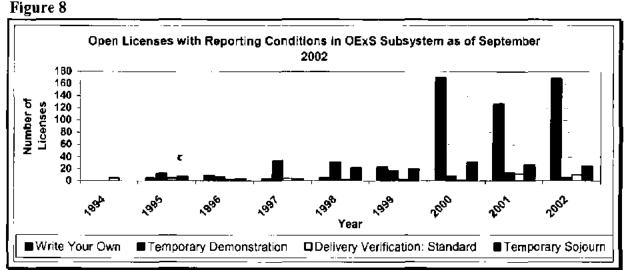
In August 2002, we reviewed 90 open licenses<sup>52</sup> in the Conditions Follow-up Subsystem. Fortyeight had expired, of which OExS had followed up on only 16. On average, 1,037 days—2 years and 10 months—elapsed between a license's expiration and OExS' initial follow-up request for export verification (see appendix C).<sup>53</sup>

<sup>&</sup>lt;sup>52</sup>A license is considered "open" if its conditions have not been met.

<sup>&</sup>lt;sup>53</sup>Generally, an export license is valid for two years. An exporter is required to submit appropriate documentation to OExS about a shipment once it is made against a license. If a license has expired and its conditions remain outstanding, OExS is required to contact the exporter to verify shipment.

# Export Administration's (b) (7)(E)

According to OExS, open license conditions were not properly monitored because the agency lacks staff to handle this responsibility. The Director of OExS stated that, prior to February 2002, the responsible export administration assistant followed up on open licenses only once a month because the assistant was tasked with other job responsibilities that took precedence. A significant backlog of expired licenses resulted, some dating back to 1994 (see figure 8).



Source: Office of Exporter Services, Bureau of Industry and Security.

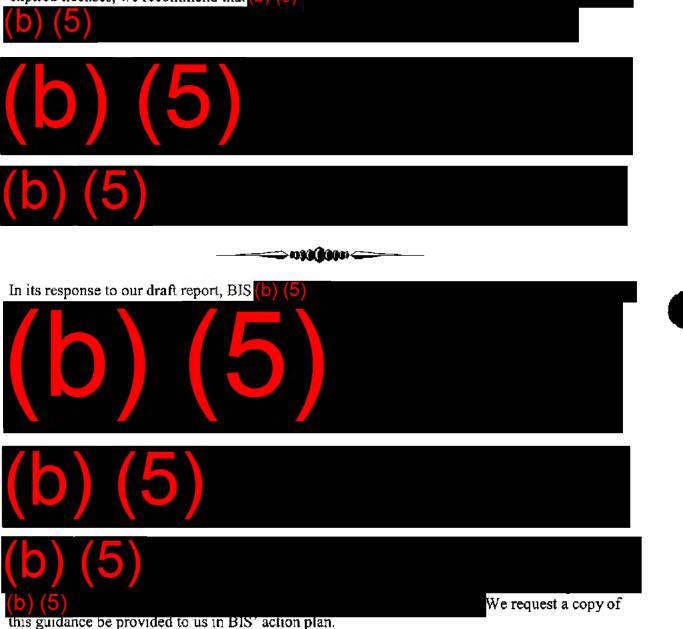
OExS informed us in November 2002 that the export administration assistant now spends approximately 6 hours per day following up on expired licenses. The agency noted that this follow-up can be time-consuming and difficult for a number of reasons. For example, an exporter may have ceased operations, changed its contact information since the license was issued, or may fail to return phone calls or request additional time to search for documentation.

We found that several companies received additional export licenses before OExS had verified their compliance with conditions on previous licenses. Some of the new licenses were issued to manufacturers of controlled commodities such as chemicals, biotechnology products, and night vision and infrared camera technology. This apparent breakdown in the monitoring process might diminish the deterrent effect of the conditional licensing process on potential violators. In addition, failure to monitor license conditions might degrade the integrity of the interagency licensing referral process. For instance, licensing referral agencies (e.g., Defense and State) that depend on BIS to notify them of the outcomes of license conditions might make decisions on



future licenses without having appropriate information on compliance with conditions on previously issued licenses.

**RECOMMENDATIONS.** While we acknowledge OExS' recent efforts to improve follow-up of expired licenses, we recommend that (b) (5)



#### B. Export Enforcement needs to improve its license monitoring efforts

Our 1999 review found that – like Export Administration – Export Enforcement was not routinely monitoring open licenses. This also resulted in a backlog of expired licenses that required follow-up. When an exporter promptly notifies OEA of a shipment, the office can

quickly initiate a PSV to confirm a commodity's stated end-use. PSVs help prevent the diversion of controlled U.S. technology by strengthening assurances that exporters, shippers, consignees, and end users comply with the terms of export licenses. Our current review found that Export Enforcement's efforts at license monitoring and follow-up remain inadequate.

We analyzed 33 open Condition 14 licenses out of 150 expired licenses. Fifteen of these had expired as of September 3, 2002,<sup>54</sup> and while OEA had followed up on 12 of them, the average time from expiration to initiation of follow-up was 553 days or 1.5 years (see appendix C).

Export Enforcement's written procedures state that OEA should monitor open licenses on a monthly basis and follow-up on any that have expired. The Director of OEA's (b) (7)(E) Anti-Terrorism Support Division reviews the subsystem's "tickler," which monitors the status of open licenses, and identifies expired licenses that require follow-up.<sup>55</sup> OEA analysts are then tasked with contacting the licensees to verify whether a commodity was exported and, if so, to request the appropriate documentation.

However, OEA informed us that licenses were not being monitored and followed up properly because analysts are handling additional responsibilities since September 11, 2001, such as expanded reviews of visa requests under the Visa Application Review Program: (b) (7)(E)

### (b) (7)(E)

We found that—because Condition 14 licenses are inadequately monitored (see figure 9 below)<sup>57</sup>—several companies received additional licenses without OEA having verified their compliance with conditions on previous licenses. Some of the new licenses were issued to manufacturers of firearms and ammunition, infrared camera technology, high-performance computers, and other controlled commodities. As with OExS, this breakdown in the monitoring process might diminish the deterrent effect of conditional licensing on potential violators.

<sup>&</sup>lt;sup>54</sup>In September 2002, OIG requested this sample of 33 licenses chosen from a complete list of all licenses that were in OEA's follow-up queue through May 2002.



During FY 2002,

OEA analysts reviewed approximately 53,000 visa request cables compared to 46,900 in FY 1999. <sup>57</sup>It should be noted that some of the open licenses are still valid for which no shipment may have been made; thus, no PSV can be initiated.

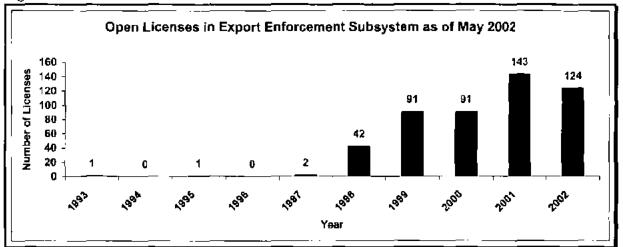
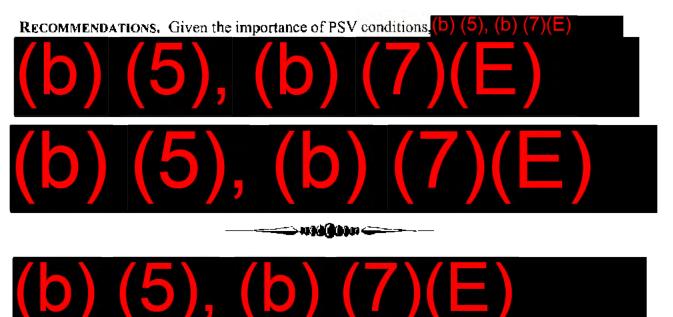
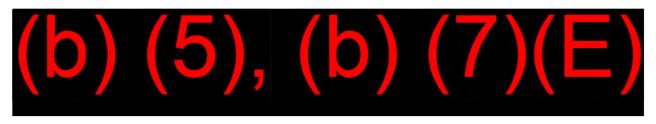


Figure 9

Source: Office of Enforcement Analysis, Bureau of Industry and Security.

In addition, the possibility exists for controlled commodities to be diverted during the license validity period (i.e., 2 years). For example, if the export were shipped one month after the license was issued but not reported to or monitored and followed up by OEA until two years later, the deterrent effect of a PSV would be diminished. Condition 14 is one of the most important conditions placed on a license because, at some point during the licensing process, it was determined by BIS or a licensing referral agency that a PSV was warranted to determine whether goods or technology were being used in accordance with the license provisions. Without proper monitoring, there exists the potential for exports to be diverted unbeknownst to BIS, which bears the responsibility of notifying other referral agencies about the end-use check results. As such, licenses with Condition 14 should be followed up on before they expire in order to minimize the risk of diversion.





Finally, BIS agreed to consider sending automated reminders to exporters with Condition 14 licenses requesting verification and required documentation of pending or completed shipments. We request that BIS keep us informed on its progress in this matter. BIS' action meets the intent of our recommendation.

#### C. Export Enforcement's outreach visits should be more strategically planned

Export Enforcement conducts outreach visits to U.S. companies to educate them about export controls and elicit their cooperation in identifying illegal export transactions. Agents also conduct outreach visits to follow-up on certain types of investigative leads, such as (b) (7)(E) During FY 2001, OEE agents conducted 1,046 outreach visits.<sup>58</sup> However, we found that outreach is not generally used as a proactive, strategic tool for preventing and detecting illegal trade activity. Specifically, there is no system in place for targeting industries for outreach or formalized guidance on how agents can or should strategically identify companies in high-risk categories for visits.

Overall, we found that OEE gives outreach a relatively low priority. Several agents and SACs indicated that outreach visits are considered "fillers"— that is, an activity conducted when agents are not working criminal cases. Outreach also appears to be a reactionary effort, whereby agents meet with company officials after a violation has possibly occurred (e.g., voluntary self-disclosure or (b) (7)(E)). Among the closed cases reviewed, we noted several instances in which, after receipt of a lead, months passed before OEE agents made contact with the company. (b) (7)(E)

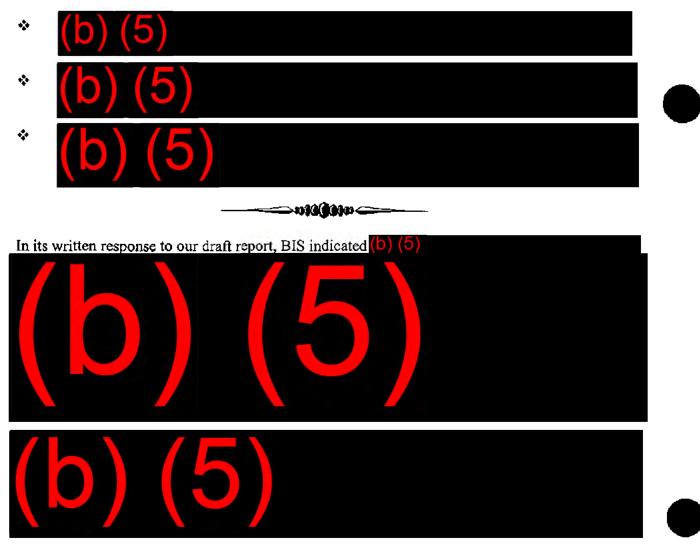
conducted outreach with the U.S. company.

Beginning in FY 2002, there was a policy shift away from conducting outreach to focusing more on the development of criminal cases. As a result, BIS discontinued the "Number of Enforcement Outreach Visits" as a performance measure. BIS however has maintained a certain level of focus on outreach as a means to prevent violations of the export control laws through its performance measure "Number of Cases Opened that Result in the Prevention of a Criminal Violation or the Prosecution of a Criminal or Administrative Case." BIS has set a target of 85 cases to be opened for both FY 2003 and 2004; of the 85 cases, BIS projects that 10 will result from leads obtained through outreach visits.

<sup>&</sup>lt;sup>58</sup>This number includes educational contacts, as well as visits with a person or company in conjunction with an investigation. As stated in the SAM, every one-on-one visit with the representative of a company is considered outreach.

On at least one occasion in the recent past, Export Enforcement has taken a focused, strategic approach to outreach. During the fall of 2001, it implemented a temporary national outreach plan in reaction to the September  $11^{th}$  terrorist attacks. Specifically, OEE agents were instructed to visit all chemical manufacturers within their respective regions. We encourage Export Enforcement to build upon that endeavor and implement a formal proactive annual outreach plan, based on intelligence, proliferation trends, and export data analysis. We further note that Export Enforcement promoted strategic outreach at its 2002 new agent training, which contained a presentation (entitled "Strategic Outreaches") on how agents can identify and target companies of high concern within their respective regions. However, this guidance was not subsequently incorporated into the 2002 SAM. We encourage (b) (5), (b) (7)(E)

**RECOMMENDATIONS.** To make outreach a more proactive and strategic tool, Export Enforcement should do the following:

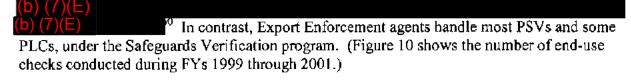


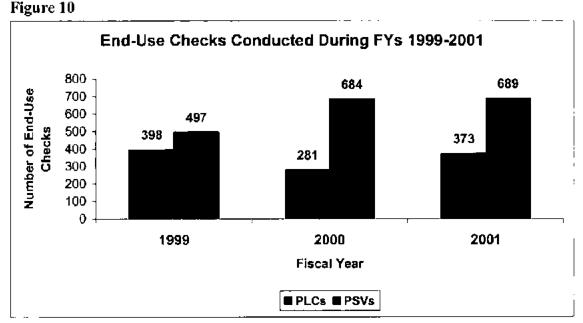


#### III. BIS Should Continue to Improve the End-Use Check Process

BIS conducts two types of end-use checks to verify the legitimacy of the dual-use exports it controls: (1) pre-license checks validate information about end users on export license applications;<sup>59</sup> (2) post shipment verifications determine whether goods or technology exported from the U.S. actually were received and are being used appropriately by the party named on the license or by an authorized end user.

Requests for end-use checks may come from licensing officers, OEE agents, Export Enforcement analysts, and officials from other federal agencies involved in the license review process.





Source: BIS annual reports, FYs 1999-2001.

Safeguards teams also conduct outreach visits to foreign firms to educate them about U.S. export controls, and provide guidance and support on preventive enforcement matters to U.S. embassy personnel and/or to the host government's export control officials. During FY 2001, BIS conducted Safeguards Verification trips to 15 countries: Argentina, Brazil, Hong Kong, India, Israel, Malaysia, Mexico, Pakistan, Panama, the People's Republic of China, the Philippines, Singapore, South Korea, Venezuela, and Vietnam.

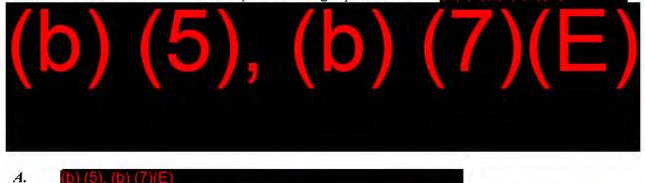


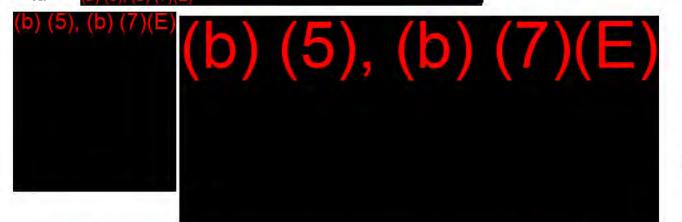
<sup>&</sup>lt;sup>59</sup>A PLC determines if an overseas person or firm is a suitable party to a transaction involving controlled. U.S.-origin goods or technical data.

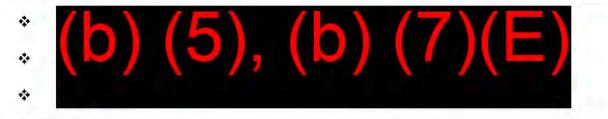
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Our current review found that while some improvements have been made (e.g., officers conducting on-site PLCs as well as better record-keeping), many of the problems with end-use checks we identified in our 1999 export licensing report still exist. (b) (5), (b) (7)(E)







(b) (5), (b) (7)(E)



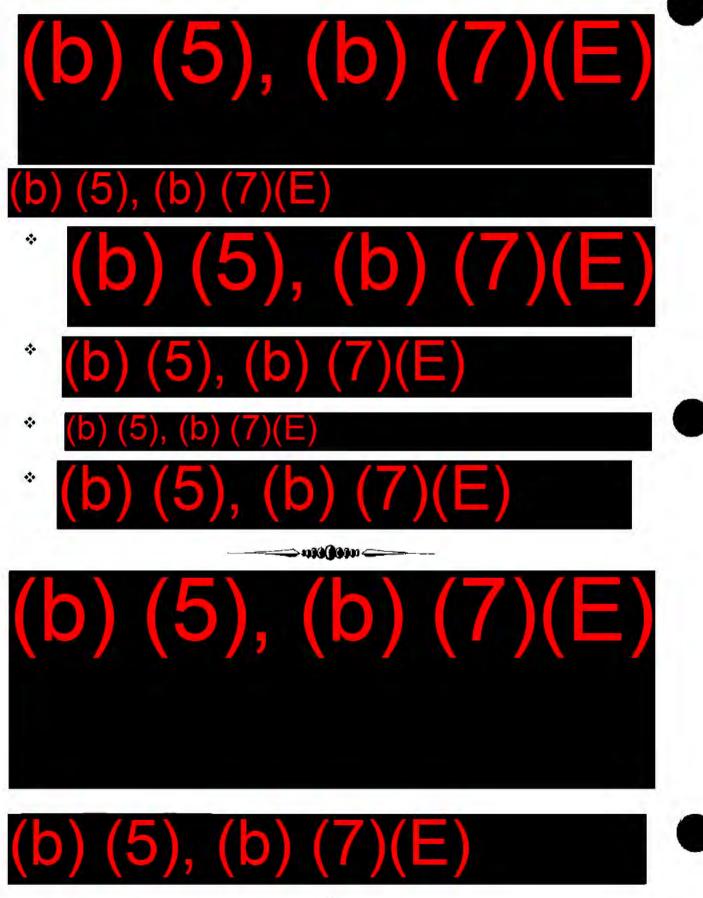




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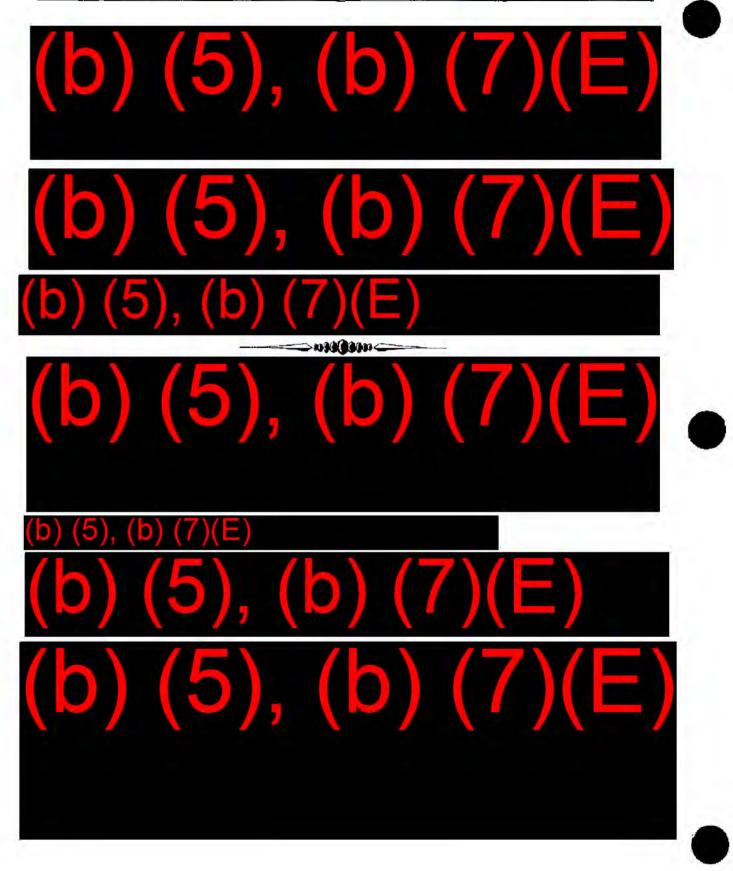
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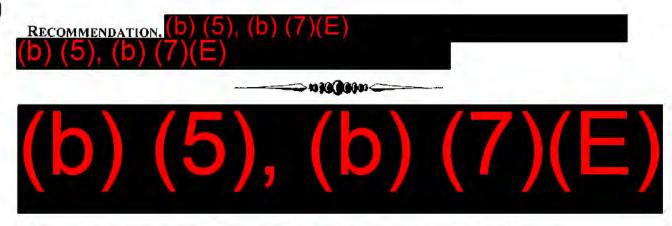


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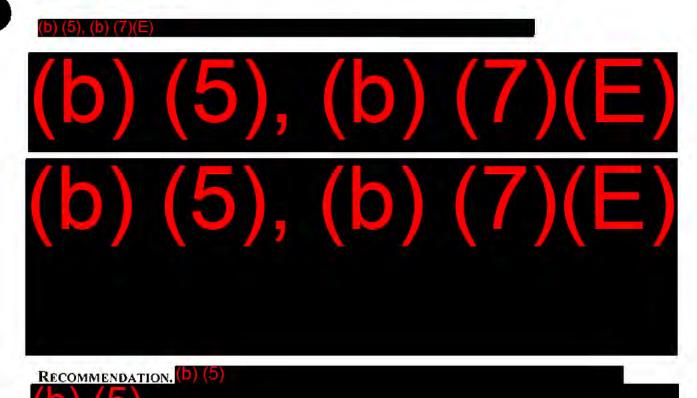
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B. Weaknesses in the Safeguards Verification Program need to be addressed

Overall, we believe the Safeguards Verification Program is working reasonably well. The work of OEE Safeguards teams helps ensure the legitimate use of sensitive U.S. controlled dual-use commodities. Our 1999 review identified weaknesses in OEE agents' performance of Safeguards verifications, such as failure to consult with other U.S. agencies at the post; submission of late, inconsistent, and poorly disseminated trip reports; and lack of criteria for selecting PSVs. Unfortunately, our current review revealed that all but the selection problem persists. We have identified several areas where we believe improvements would make this program more effective.



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# (b) (5)

In its response to our draft report (b) (5)

. We should note that our review of

FY 2001 Safeguards trip reports revealed that teams met with other U.S. Government agencies in only 5 out of the 15 countries visited. However, we acknowledge BIS' renewed commitment to these briefings. In addition, we will follow-up on this issue as a part of our annual NDAA FY 2000 follow-up review.

#### b) (5)

Office Director's Memorandum 99-02 requires Safeguards teams to submit their reports to the OEE Director within 30 days of a trip's conclusion. This protocol was revised in June 2002 (and incorporated into the new SAM) to require agents to adhere to this requirement or risk losing their privileges to participate in future Safeguards assignments.

We reviewed the 10 Safeguards trip reports issued for FY 2001, and found that 6 were submitted to headquarters more than 30 days after the trips' conclusion—and in most cases, well beyond the required time frame (see table 5).

|            | Countries Visited   | Number of Days to            |
|------------|---|------------------------------|
|            | Countines risined   | Submit Report:               |
| 1          | People's Republic of China  | 272                          |
| 2          | South Korea and Vietnam   | 261                          |
| 3          | Argentina, Brazil, and Venezuela  | 111*                         |
| 4          | Pakistan and India  | 89                           |
| 5          | Hong Kong and Malaysia  | 45                           |
| 6          | Panama and Mexico   | 38                           |
| not<br>che | ote: Export Enforcement's Intelligence and Fix<br>verify this report's submission date. However<br>sks were entered into Enforce on October 20, 2<br>r the trip's conclusion. | , the results of the end-use |

#### Table 5: Late FY 2001 Safeguards Trip Reports

Source: Office of Export Enforcement, Bureau of Industry and Security.

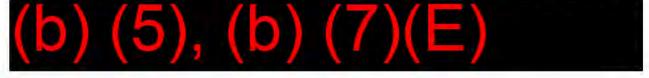
We found that confusion among team members over report writing responsibilities delayed the submission of one report, but we could not readily determine why the remaining five reports were submitted late.

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RECOMMENDATION. While we acknowledge OEE's new Safeguards protocol as a positive step,



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# (b) (5) BIS' action will meet the intent of our recommendation once completed.

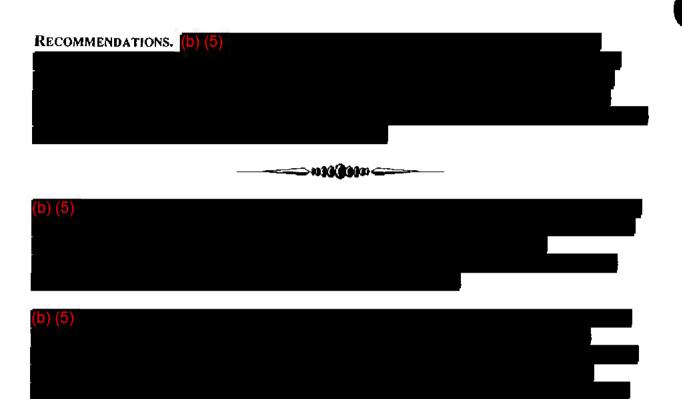




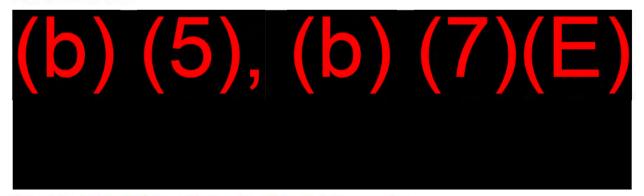


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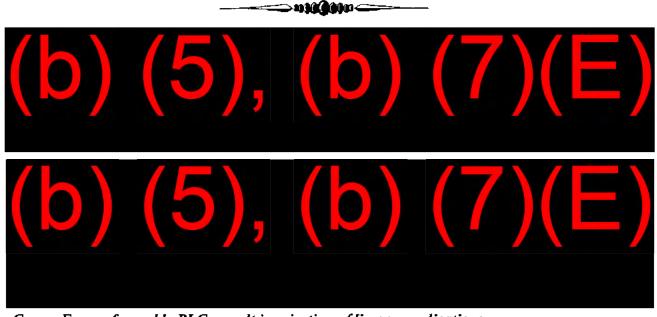
(b) (5), (b) (7)(E)





 $\begin{array}{c} \text{Recommendation.} \\ \text{(b) (5), (b) (7)(E)} \\ \text{(b) (5), (b) (7)(E)} \end{array}$ 

# (b) (5), (b) (7)(E)



C. Few unfavorable PLCs result in rejection of license applications

Both BIS and licensing referral agencies rely on the results of PLCs to determine the ultimate disposition of a license application. Of the 373 PLCs conducted in FY 2001, 27 received an unfavorable determination. License applications for 15 of these were returned without action,<sup>67</sup> 9 were rejected, and 3 were approved with conditions after BIS took action to ensure that the concerns raised during the check were corrected or addressed. However, we identified a number of cases in which BIS' decision to return the application without action,<sup>68</sup> rather than reject it, is questionable.

#### (b) (5)

(b) (5)
 (b) (5)
 (b) (5)
 (c) 1996 MOU between Export Administration and Export Enforcement.<sup>69</sup> The MOU indicates that if Export Administration disagrees with a licensing recommendation made by Export Enforcement.<sup>(b)</sup> (5)

<sup>69</sup>Export Administration and Export Enforcement entered into an MOU in 1996 regarding Export Enforcement's recommendations on export license applications. The MOU includes a dispute resolution process to be used by both organizations.



<sup>&</sup>lt;sup>67</sup>One license application involved two PLCs for two separate entities.

<sup>&</sup>lt;sup>68</sup>A decision to return a license application means that the application has been neither approved nor denied, thereby blocking the export.

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## Figure 11 **Dispute Resolution Process** If staff personnel (licensing officers, agents, and analysts) are not able to reach agreement on the outcome of a license application, the applicable Export Administration director shall consult with the Director of OEE or OEA. This must be done within five days of the Export Enforcement recommendation. If the directors disagree, they shall refer the issue to the Deputy Assistant Secretaries for Export Administration and Enforcement. All applications must be resolved or escalated to the Deputy Assistant Secretaries within 20 days of the initial recommendation made by Export Enforcement. Source: 1996 MOU between Export Administration and Export Enforcement. **RECOMMENDATIONS.** b) (5) >030000m~





We found four instances in which Export Enforcement recommended that an application be returned without action, considered on merits with conditions,<sup>71</sup> and/or rejected—then later changed its position to return without action. Two of the four cases involved commodities that fell under the Australia Group<sup>72</sup> and thus, had the applications been rejected, could have qualified for the "no undercut rule."<sup>73</sup> In the remaining two cases, an Intent to Deny Letter had been mailed to the exporter before the case was returned without action. While there is no indication in the official licensing history as to why BIS changed its position from denial to return without action for those two cases, the explanation for the return without action is as follows:

> "[BIS has been] unable to confirm the existence of the named consignee and is therefore returning the case without action. An actual pre-license check was made in country and the named consignee could not be found and was not known to any government official. For that reason, any resubmission of this request should be supported by comprehensive consignee information."

The specific criteria in the EAR<sup>74</sup> for returning a license application without action is as follows:

- \*\* The applicant has requested its return.
- A license exception applies. ÷
- ÷ The items are not under Department of Commerce jurisdiction.

<sup>&</sup>lt;sup>71</sup>Certain conditions are imposed on a transaction to minimize risk in cases where the transaction raises questions or presents a risk of diversion.

<sup>&</sup>lt;sup>72</sup>The Australia Group consists of 34 countries that cooperate in curbing the proliferation of chemical and biological weapons through the coordination of export controls, the exchange of information, and other diplomatic actions.

<sup>&</sup>lt;sup>23</sup>So as not to "undercut" the denial, member countries agree not to approve an identical sale without first consulting with the member issuing the denial notification. <sup>74</sup>15 CFR 772.

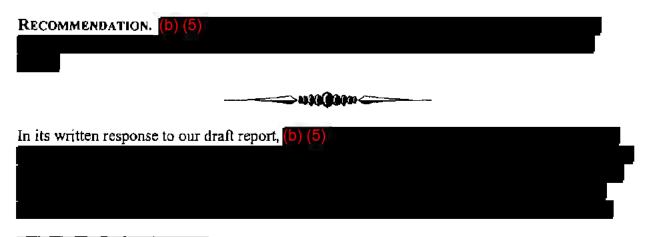
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- Required documentation was not submitted with the application.
- Attempts to contact the applicant for additional information needed to process the application have failed.

In addition, the 1996 MOU provides guidance on when to approve, reject, or return a license application without action, but we believe its direction for the latter action may be inadequate:<sup>75</sup>

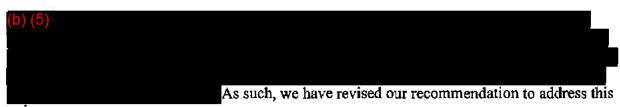
"A recommendation that an application be returned without action must be based on one or more of the following reasons: (1) the application omits essential information; (2) the application contains a misleading statement about a material fact; (3) determination has been made that the item or technical data in question does not require a license or reexport authorization for export to the destination and/or end-use identified in the application; or, (4) other reasons as agreed to by OEE, OEA, and CBTC, NMT, and STFP<sup>76</sup> in writing."

While we understand a decision to return a license application without action for omitting essential information (e.g., insufficient end user information or technical documentation), it is not clear why BIS would return a license application without action versus rejecting it if it contained a misleading statement about a material fact. This is especially true if the information only came to light after a PLC was conducted. A denial sends a clear message that some part of a transaction involving controlled U.S.-origin goods or technical data is not suitable. In addition, when such licenses are not denied, the U.S. government is unable to use the "no undercut rule" established by the multilateral control regimes, which ensures that a member country does not approve an identical sale without first consulting with the member country issuing the denial notification.



<sup>&</sup>lt;sup>75</sup>Guidelines for Making Recommendations on Export Licenses and Licenses Exceptions (Suspension or Revocation of Existing Licenses; or Rejection, Return Without Action, or Consider on Merits [With or Without Conditions] of License Application), Section 5.3.2 of the guidelines, March 1, 1996.

<sup>&</sup>lt;sup>76</sup>Chemical and Biological Controls Division, Nuclear and Missile Technology Controls Division, and Strategic Trade and Foreign Policy Controls Division.



point.

#### (b) (5)

In response to our 1999 export licensing report, BIS agreed to inform the licensing referral agencies (e.g., Defense and State) when it receives a negative result on a PLC involving a case that had been referred to them, understanding that this additional information may affect the agencies' original position on the application. BIS restated this policy during our current review. However, we identified four instances in which the official case history did not indicate that the referral agencies were notified of an unfavorable PLC or agreed with the decision to return without action.

| RECOMMENDATION, (b) (5        |   |
|-------------------------------|---|
|                               |   |
|                               |   |
|                               |   |
| In its written response to ou | ur draft report, (b) (5)                              |
|                               | As such, we will follow-up on this matter as a part o |

our annual follow-up review per the FY 2000 NDAA requirement.



#### IV. Export Administration's Processing of License Determinations for Customs is Untimely

As previously mentioned in this report, BIS and Customs share responsibility for enforcing the export control laws on dual-use commodities. Customs' responsibility includes the detention and seizure of goods departing from U.S. ports whenever its agents or inspectors know, or have probable cause to believe, that a shipment is in violation of the export control laws. The EAA allows Customs to detain a shipment for up to 20 days, after which it must either formally seize or release the goods.<sup>77</sup> Within this 20-day window, Customs must ascertain whether the detained commodity is controlled under the EAR and thus may require a valid license for export. Customs therefore requests a license determination (LD) from Export Administration if the exporter cannot produce evidence of a valid license.

Agents and inspectors request LDs via Customs' Exodus Command Center<sup>78</sup> by submitting an LD referral that contains, among other information, the name and address of the exporter and foreign consignee, destination, monetary value of the shipment, and description of the product (including technical specifications) to be exported. (b) (7)(E)



We examined Export Administration's processing of LDs requested by Customs in our 1999 export licensing report. We found that the LDs were not processed in a timely manner. In particular, our review demonstrated that the average response took 36 days. We therefore recommended that BIS work with Customs to (1) automate the referral of Customs' LD requests and (2) formulate a written agreement outlining the responsibilities of each party involved in the process. Although BIS agreed with our recommendations, it has not initiated efforts in either area.

In the current review, we examined several hard copy LDs which Customs requested in FY 2001, and a report which contained the status and processing time of the 588 LD referrals which Export Administration received from Customs during FY 2002. We discovered that Export Administration's processing of Customs LDs remains untimely. Of the 588 LD referrals, Export Administration processed 284 (48 percent) of them in 20 days or less, and 220 (37 percent) in more than 20 days. The remaining 84 LD requests (14 percent) were pending as of December 20, 2002. While Export Administration did process many requests expeditiously, we noted several that were egregiously untimely. For instance, an LD received on November 27, 2001,

<sup>77</sup>Section 12(2)(a) of the EAA.

<sup>78</sup>The Exodus Command Center, established in 1982, 15 part of Customs' Strategic Investigations Division. In addition to requesting LDs from various regulatory agencies, the center conducts license history checks and license verifications.



was not completed until October 16, 2002 – a processing time of 319 days. An LD referral requested on May 7, 2001, remained pending as of January 6, 2003.

When Customs agents and inspectors do not receive determinations within 20 days, they have three options: they can (1) continue to detain the shipment in violation of the EAA, (2) formally seize the shipment, or (3) release the shipment. Each option is potentially problematic. If Customs chooses option 1 or 2, it may unnecessarily delay legitimate trade if the licensing officer determines, in time, that the item does not require a license. If Customs chooses option 3, it could allow sensitive dual-use commodities to leave the United States that should not be shipped without a valid, proper license or, possibly, should not be exported at all.

Several factors contribute to Export Administration's untimely handling of Customs LD requests: First, and most important, the two agencies have no written guidelines that establish a time frame and procedure for the LD process or outline the responsibilities of each party involved in the process. Customs does not always provide the necessary product specifications required for a determination. In these cases, the licensing officer must contact either the Exodus Command Center or the Customs agent or inspector, who requested the LD, to obtain information needed to classify the commodity—which could lengthen the turnaround time. Most of the Customs agents and inspectors with whom we met stated that they would benefit from better guidance from Export Administration on the LD process (e.g., what information they need to provide to Export Administration to get a more timely LD). Therefore, Export Administration should (b) (5)





**RECOMMENDATIONS.** We recommend that Export Administration work with Customs in undertaking the following actions:

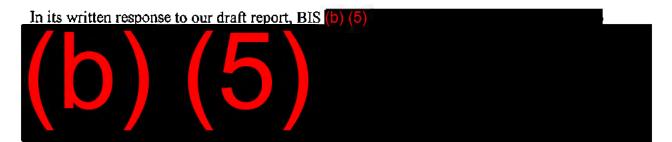


U.S. Department of Commerce Office of Inspector General

/

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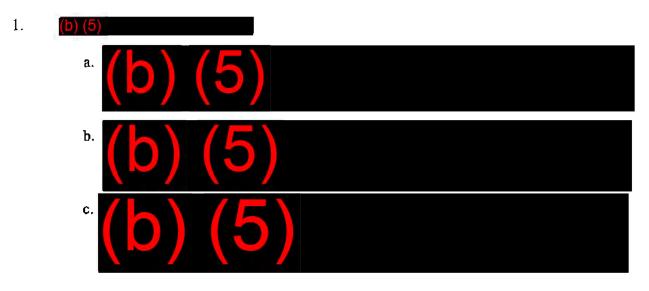




## **RECOMMENDATIONS<sup>80</sup>**

We recommend that the Under Secretary for Industry and Security ensure that the following actions are taken:

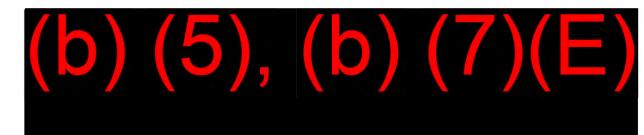
### Case Development



d. Requiring SACs to provide quarterly reports to OEE headquarters on the status of their quarterly case reviews. Such reports should include the total number of cases open in their field office, the number of cases opened and closed during a particular quarter, as well as warning letters, indictments, convictions, and the number of administrative cases pending at headquarters (see page 15).

### Case Leads

2.



<sup>&</sup>lt;sup>80</sup> We have designated which recommendations below we consider closed. We will follow up on the remaining recommendations as a part of our annual follow-up work required by the National Defense Authorization Act for FY 2000.

## License Determinations

- 3. Ensure that Export Administration and Export Enforcement implement the License Determination Work Plan and that the plan's objectives are achieved (see page 24). We consider this recommendation to be closed.
- 4. Improve Export Administration's processing of license determinations by:
  - a. Ensuring that division directors and licensing officers complete "accurate and timely" license determinations, as required in their respective performance plans (see pages 23 and 24). We consider this recommendation to be closed.
  - b. Providing more instruction and guidance to OEE agents on the information needed to complete a determination accurately and in a timely manner (see pages 23 and 24).
  - <sup>c.</sup> (b) (5)

### Administrative Case Processing

6.

- 5. Improve administrative case processing by:
  - a. (b)(5)b. (b)(5)(b)(5)

Collection of Administrative Penalty Payments

<sup>7.</sup> (b) (5)

## Special Agent Manual & Agent Training

| 8, | (b) (5 |         |
|----|--------|---------|
|    | а.     | (b) (5) |
|    | b.     | (b) (5) |
|    | c.     | (b) (5) |
|    | d.     | (b) (5) |

9. Improve agent training by directing OEE to:

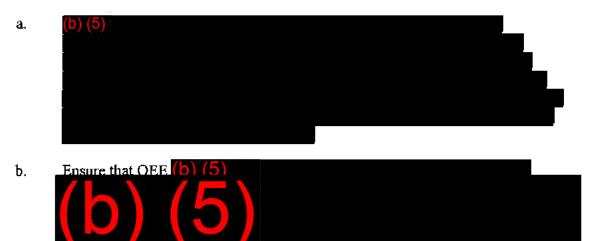
| а. | (b) (5) | We consider this recommendation to be closed. |
|----|---------|---|
| b. | (b) (5) | we consider this recommendation to be closed. |
|    |         |   |
| C. | (8) (8) |   |
|    |         | We consider this recommendation to be closed. |

## Interagency Relationships

10. Strengthen Export Enforcement's relationship with U.S. Attorneys and Assistant U.S. Attorneys by:



11. Enhance its enforcement relationship with the U.S. Customs Service by having Export Enforcement:



- ç. (b) (5)
- 12. Improve Export Enforcement's relationship with the FBI by directing it to:
  - a. (b) (5)
    b. (b) (5)
    b. (b) (5)
    We consider this recommendation to be closed.
- 13. Improve Export Enforcement's relationship with the CIA by:





## **Monitoring of License Conditions**

16. Improve BIS' monitoring of license conditions by taking the following actions:



## Outreach

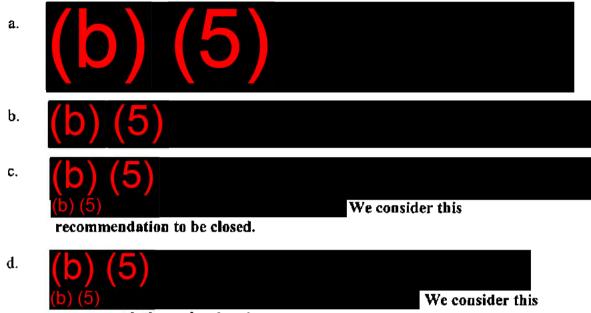
17. Make outreach to industry a more proactive and strategic tool by:



## **End-Use Checks**



19. Revise the guidance for the Safeguards Verification program and enhance the quality and timeliness of Safeguards checks conducted by agents by:



- recommendation to be closed.
- <sup>e.</sup> (b) (5), (b) (7)(E)

# Status of Unfavorable Pre-license Checks

| 20.         | (b) (5) |
|-------------|---------|
| <b>2</b> 1. | (b) (5) |
| 22.         | (b) (5) |
| 23.         | (b) (5) |

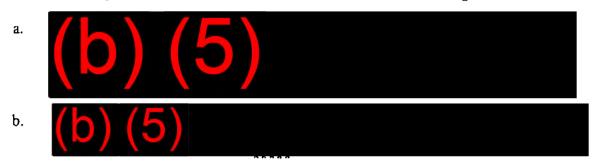
•

Final Report IPE-15155 <u>March 2003</u>

to:

## License Determinations for Customs

24. Ensure that Export Administration works with Customs in the following areas:



We recommend that the Under Secretary for International Trade direct the (0)(5), (0)(7)(E)

(b) (5), (b) (7)(E)
 (b) (5), (b) (7)(E)
 (b) (5), (b) (7)(E)
 (b) (5), (b) (7)(E)

# APPENDICES

# APPENDIX A

# List of Acronyms

| ALJAdministrative Law JudgeAUSAAssistant United States AttorneyBISBureau of Industry and SecurityCFRCode of Federal RegulationsCIACentral Intelligence AgencyEAAExport Administration ActEARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOCCOffice of Chief CounselODMOffice of Enforcement AnalysisOEEOffice of Export EnforcementOEAOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipor's Export DeclarationTECSTreasury Enforcement Communications SystemUS&FCSUnited States and Foreign Commercial Service | ACRB   | Administrative Case Review Board                      |
|---|--------|---|
| AUSAAssistant United States AttorneyBISBureau of Industry and SecurityCFRCode of Federal RegulationsCIACentral Intelligence AgencyEAAExport Administration ActEARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Enforcement AnalysisOBEOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agent AnnualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | ALJ    | Administrative Law Judge                              |
| CFRCode of Federal RegulationsCIACentral Intelligence AgencyEAAExport Administration ActEARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Enforcement AnalysisOEEOffice of Export EnforcementOEXSOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | AUSA   | •   |
| CFRCode of Federal RegulationsCIACentral Intelligence AgencyEAAExport Administration ActEARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Enforcement AnalysisOEEOffice of Export EnforcementOEXSOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | BIS    | Bureau of Industry and Security                       |
| EAAExport Administration ActEARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of the Director MemorandumOEAOffice of Export EnforcementOESSOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | CFR    | • •   |
| EAAExport Administration ActEARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of the Director MemorandumOEAOffice of Export EnforcementOESSOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | CIA    | Central Intelligence Agency                           |
| EARExport Administration RegulationsECASSExport Control Automated Support SystemFBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOEXSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agent SanualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | EAA    |   |
| FBIFederal Bureau of InvestigationFYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Export EnforcementOEXSOffice of Export EnforcementOEXSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | EAR    |   |
| FYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | ECASS  | Export Control Automated Support System               |
| FYFiscal YearIEEPAInternational Emergency Economic Powers ActIFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | FBI    |   |
| IFSDIntelligence and Field Support DivisionJTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Export Enforcement AnalysisOEEOffice of Export ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | FY     |   |
| JTTFJoint Terrorism Task ForceLDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | IEEPA  | International Emergency Economic Powers Act           |
| LDLicense DeterminationMOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | IFSD   | Intelligence and Field Support Division               |
| MOUMemorandum of UnderstandingNOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | JTTF   | Joint Terrorism Task Force                            |
| NOAANational Oceanographic and Atmospheric AdministrationOACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOEXSOffice of Exporter ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | LD     | License Determination                                 |
| OACOffice of Antiboycott ComplianceOCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Export EnforcementOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | MOU    |   |
| OCCOffice of Chief CounselODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Exporter ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | NOAA   | National Oceanographic and Atmospheric Administration |
| ODMOffice of the Director MemorandumOEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Exporter ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | OAC    | Office of Antiboycott Compliance                      |
| OEAOffice of Enforcement AnalysisOEEOffice of Export EnforcementOExSOffice of Exporter ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | OCC    | Office of Chief Counsel                               |
| OEEOffice of Export EnforcementOExSOffice of Exporter ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | ODM    | Office of the Director Memorandum                     |
| OExSOffice of Exporter ServicesOIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | OEA    | Office of Enforcement Analysis                        |
| OIGOffice of Inspector GeneralPLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | OEE    | Office of Export Enforcement                          |
| PLCPre-License CheckPSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | OExS   | •   |
| PSVPost Shipment VerificationSACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   | OIG    | -   |
| SACsSpecial Agents-in-ChargeSAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | PLC    | Pre-License Check                                     |
| SAMSpecial Agent ManualSEDShipper's Export DeclarationTECSTreasury Enforcement Communications System  | PSV    | Post Shipment Verification                            |
| SEDShipper's Export DeclarationTECSTreasury Enforcement Communications System   |        |   |
| TECS Treasury Enforcement Communications System   |        | . –   |
|   | -      | •• •  |
| US&FCS United States and Foreign Commercial Service   |        | •   |
|   | US&FCS | United States and Foreign Commercial Service          |

85

## APPENDIX B

# Improvements Needed in the Special Agent Manual

| SPE  | CIAL AGENT MANUAL<br>SECTION                                    | WEAKNESS |
|------|---|----------|
| Over |   |          |
| 2.   | Firearms  |          |
| 6.   | Travel  |          |
| 8.   | Project Outreach  |          |
| 9.   | Case Control  |          |
| 10.  | Sources of Information  | •        |
|      | License Determinations  |          |
| 20.  | Administrative/Civil<br>Procedures                              |          |
| 21.  | Reporting   |          |
| 24.  | Cooperation with Export<br>Administration and<br>Other Agencies |          |

Source: 2002 Special Agent Manual, Office of Export Enforcement, Bureau of Industry and Security.



# APPENDIX C

## Export Enforcement and Export Administration License Monitoring Efforts

#### OExS Response Time on Expired Licenses with Conditions

|          | License | Date Expired    | Initial OBx8 Follow-up  | Response Time (days) |
|----------|---------|-----------------|-------------------------|----------------------|
|          | D214678 | 10/31/96        | 8/23/02                 | 2,122                |
| 2        | D216310 | 12/31/96        | 8/23/02                 | 2,061                |
| }        | D217546 | 2/28/97         | 8/23/02                 | 2,002                |
| (        | D222931 | 9/30/97         | 8/23/02                 | 1,788                |
| 5        | D227981 | 3/31/98         | 7/21/00                 | 843                  |
| 5        | D229809 | 4/30/98         | 8/8/02                  | 1,561                |
|          | D237825 | 4/30/99         | 8/23/02                 | 1,211                |
| <b>i</b> | D242425 | 8/31/99         | 8/22/02                 | 1,087                |
|          | D245059 | 10/31/99        | 8/23/02                 | 1,027                |
| 0        | D242518 | 10/31/99        | 8/23/02                 | 1,027                |
| 1        | D247849 | 12/31/00        | 8/23/02                 | 600                  |
| 2        | D264806 | 7/31/01         | 8/23/02                 | 388                  |
| 3        | D266091 | 9/30/01         | 8/23/02                 | 327                  |
| 4        | D268703 | 11/30/01        | 8/23/02                 | 266                  |
| 5        | D268367 | 1/31/02         | 8/6/02                  | 187                  |
| 16       | D274142 | 4/30/02         | 8/14/02                 | 106                  |
|          |         | Average Follow- | up Response Time (days) | 1,037                |

Source: Office of Exporter Services, Bureau of Industry and Security,

### **OEA Response Time on Expired Licenses with Conditions**

| 1  | license | Date Expired   | Initial OEA Follow-up    | Response Time (days) |
|----|---------|----------------|--------------------------|----------------------|
|    | D194898 | 7/31/95        | 3/8/99                   | 1316                 |
| 2  | D225086 | 10/31/97       | 3/5/99                   | 490                  |
| )  | D241265 | 8/31/99        | 5/28/02                  | 1001                 |
| •  | D251254 | 6/30/00        | 5/15/02                  | 684                  |
| 5  | D251855 | 9/30/00        | 5/8/02                   | 585                  |
| 6  | D256663 | 11/30/00       | 5/21/02                  | 537                  |
| 7  | D255344 | 12/31/00       | 5/23/02                  | 508                  |
| 8  | D260887 | 3/31/01        | 5/21/02                  | 416                  |
| 9  | D261643 | 5/31/01        | 5/21/02                  | 355                  |
| 10 | D262835 | 6/30/01        | 6/18/02                  | 353                  |
| 1  | D266157 | 8/31/01        | 5/21/02                  | 263                  |
| 2  | D268107 | 12/31/01       | 5/15/02                  | 135                  |
|    |         | Average Follow | -up Response Time (days) | 553                  |

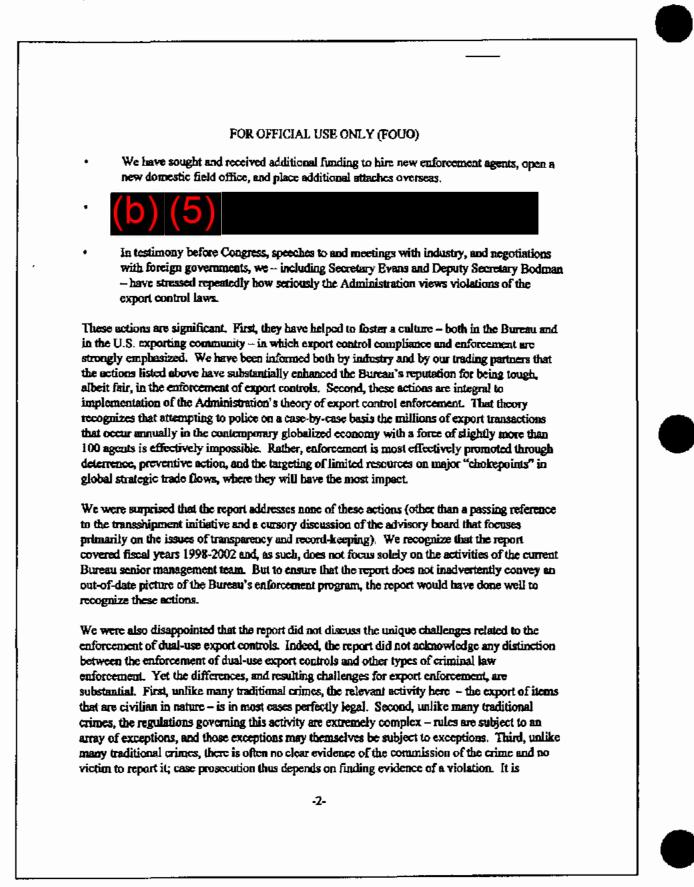
Source: Office of Enforcement Analysis, Bureau of Industry and Security.



## APPENDIX D

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|             |  | UNITED STATES DEPARTMENT OF COMMERC<br>Under Sacretary for industry and Security<br>Washington, D.C. 20230<br>March 25, 2003   |
|-------------|--|--|
| -           |  | FOR OFFICIAL USE ONLY (FOUO)   |
| ME          | MORANDUM FC  | DR JOHNNIE FRAZIER<br>INSPECTOR GENERAL  |
| FR          | DM:  | Kenneth I. Juster  |
| <b>S</b> UI | BJECT:   | Draft Inspection Report No. IPE-15155, "Improvements are<br>Needed to Better Enforce Dual-Use Export Control Laws"   |
| the pres    |  | tial time and resources that you and your staff have devoted to preparing<br>our acknowledgment of the Bureau's assistance to you during your<br>rt.   |
| seni<br>exp | or leadership are fi   | hat this Bureau's senior management team and this Department's most<br>ally committed to taking vigorous action to promote compliance with our<br>to that end, since assuming office in 2001, we have taken a number of  |
| seni<br>exp | or leadership are fi<br>ort control laws. T<br>recodented steps:<br>We have issued<br>unequivocally i  | ally committed to taking vigorous action to promote compliance with our  |
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| seni<br>exp | or leadership are fi<br>ort control laws. T<br>recodented steps:<br>We have issued<br>unequivocally i<br>security and the<br>laws.<br>We have launce<br>conster violation<br>through major is<br>We have succes<br>attention in the  | ally committed to taking vigorous action to promote compliance with our<br>to that end, since assuming office in 2001, we have taken a number of<br>d, for the first time, a set of Guiding Principles for the Bureau that state<br>that the Bureau's paramount concern is the protection of U.S. national<br>at express our commitment to vigorous enforcement of the export control<br>and a significant international public-private sector initiative designed to<br>one of U.S. export controls arising from the diversion of controlled goods  |
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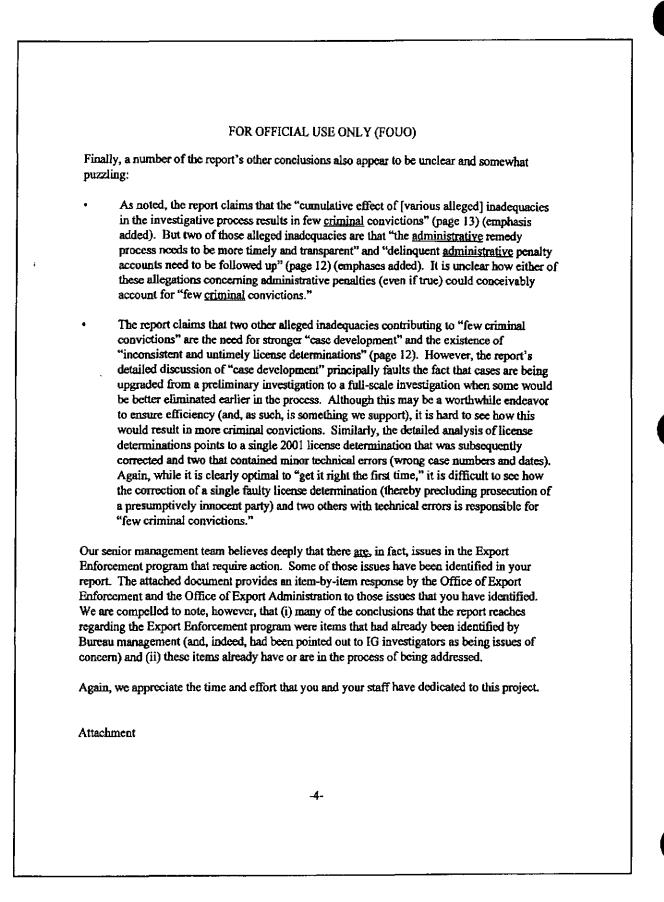
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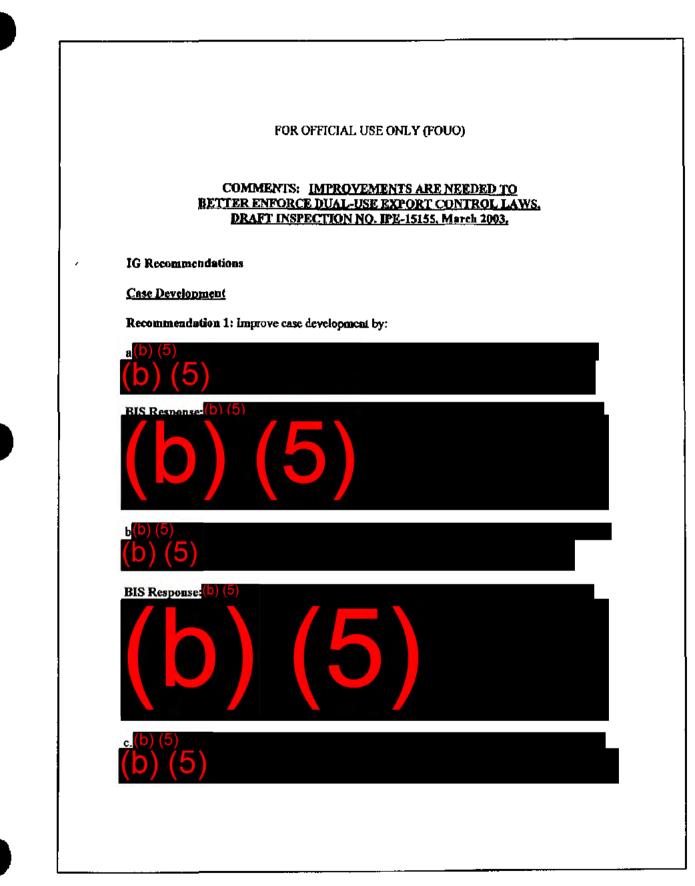
important to recognize these challenges not to excuse any failure to enforce the export control laws, but rather to appreciate the importance of a comprehensive approach to export enforcement – one that emphasizes preventive enforcement and deterrence as well as case prosecution. To this end, Export Enforcement has adopted as a performance measure the number of cases opened in which export control violations are <u>prevented</u> through, for example, temporary denial orders, detentions, proactive outreach to targeted industries, and the issuance of "Is Informed" letters under the Enhanced Proliferation Control Initiative. The report risks missing the critical importance of such preventive enforcement measures by focusing on the narrow category of prosecution of alleged violations.

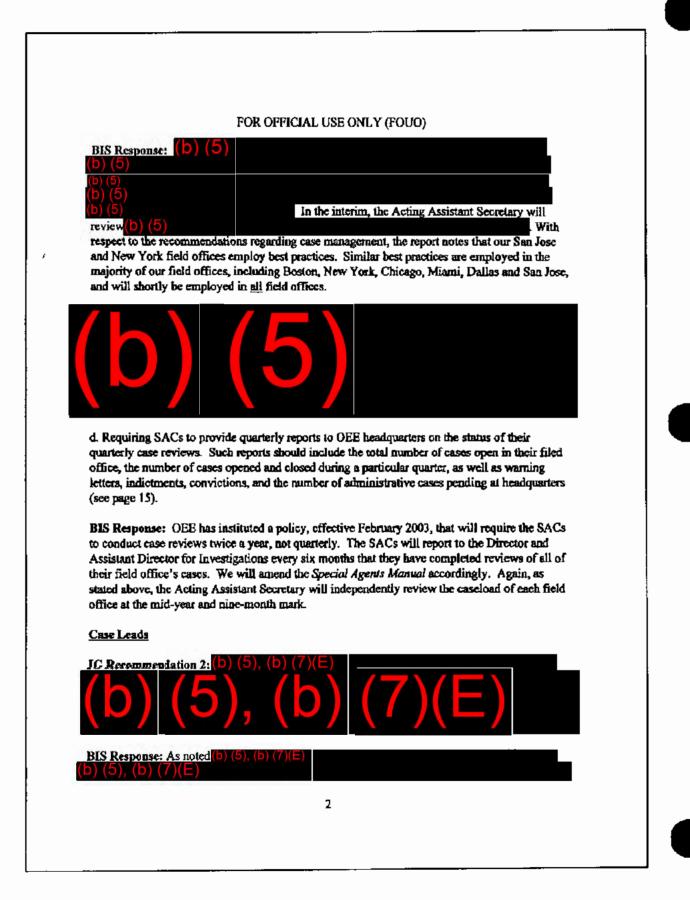
We must also express concern over the report's analysis on a number of other key points. For example, the report's finding that "Export Enforcement's Investigative Process Produces Few Criminal Prosecutions' and Administrative Sanctions" (pp. ii and 12) is misleading and potentially subject to misinterpretation. As a preliminary matter, it should be noted that obtaining criminal convictions and administrative sanctions is a reflection of the success of the respective U.S. attorneys offices and the Commerce Department's Office of General Counsel (OGC) in prosecuting cases that BIS has built. The report acknowledges the key role played by U.S. attorneys in prosecuting the cases, but then proceeds effectively to disregard that point. Moreover, the report never acknowledges the role of the OGC in prosecuting administrative cases. Most troubling, the report fails to explain why it believes that the number of convictions and sanctions attributable to Bureau investigative efforts can appropriately be labeled "few." The report cites raw data showing that 36 criminal convictions were obtained and 149 administrative sanctions imposed during a five-year period between Fiscal Years 1998-2002. However, the report supplies no basis on which to judge these numbers. How many criminal convictions in total (or on a per employee basis) did other enforcement agencies with concurrent jurisdiction (e.g., Customs) bring during this time period for export control violations? How many did other enforcement agencies (e.g., the FBI) bring for comparable white collar crimes? A recent National Journal article indicates that the U.S. Customs Service - with an enforcement force far larger than the Bureau - only launched 80 export investigations in total last year, far fewer than the 1015 cases opened by the Bureau. In short, the report's conclusion is not adequately supported.

<sup>1</sup>Although the report uses the term "prosecutions" in its header, the text of the report address only criminal "convictions." See page 13 ("the cumulative effect of these inadequacies in the investigative process results in few criminal <u>convictions</u> from the many cases opened by Export Enforcement") (emphasis added).

-3-







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# (b) (5), (b) (7)(E)

The Office of Enforcement Analysis (OEA) conducted a comprehensive assessment of its Visa Application Review Program and will conduct a similar assessment of its Shipper's Export Declaration Review Program, in addition to any other applicable programs at the end of FY 2003. Resource adjustments will be made based on these assessments. The comprehensive assessment of the Visa Application Review Program completed in January 2003 was forwarded to the OIG in connection with this review. That assessment showed the success of the visa program in generating case leads for OEE that resulted in successful criminal and administrative cases and other outcomes.

In addition, OEA has been tracking the total number of <sup>OI(0)(0)(0)(0)</sup> and unfavorable pre-license checks and post shipment verification referrals. OEA also reviews OEE and OCC weekly reports to determine which of the significant enforcement actions resulted from leads initiated by OEA.

Contrary to the report's assertion that many agents and SACS dislike headquarters leads because they take up a lot of their time, but do not result in criminal or administrative cases, OEA's statistical research suggests just the opposite. For example, in a survey of case actions between fiscal years 1999 and 2002, between 25 and 50 percent, on average, and, in some cases, a significantly higher percentage (60-80 percent) of headquarters leads resulted in cases accepted by Assistant U.S. Attorneys.

Consistent with our Congressional mandate, we consider the acquisition of controlled technology by foreign nationals to pose a significant threat to our national security (b) (5), (b) (7)(E) (b) (5), (b) (7)(E)

#### License Determinations

IG Recommendation 3: Ensure that Export Administration and Export Enforcement implement the License Determination Work Plan and that the plan's objectives are achieved (see page 20).

BIS Response: EE agrees. Again, we note that the problem regarding the processing of licensing determinations (LDs) was identified months ago and has been proactively addressed by EE and EA management. We have established a LD Tiger Team comprised of personnel from EE and EA, which meets weekly to review new and pending LD requests. This is working effectively to address the problem and ensure timely responses.

**IG Recommendation 4: Improve Export Administration's processing of license determinations** by:

a. Ensuring that division directors and licensing officers complete "accurate and timely" license determinations, as required in their respective performance plans (see page 20).

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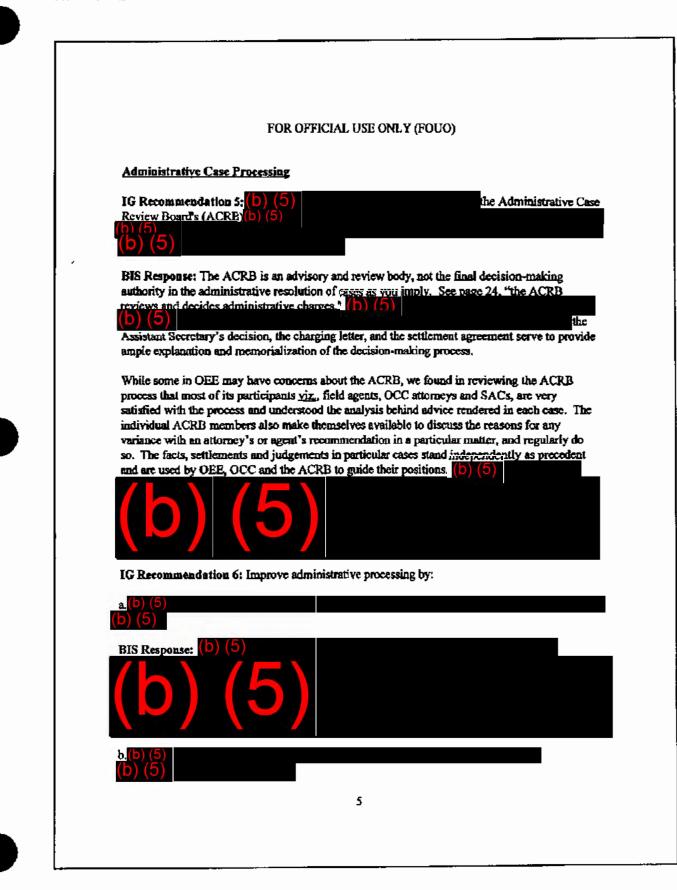
BIS Response: BIS has already taken steps to enhance the timeliness and accuracy of LDs. The average processing time for LDs closed in February 2003 was 27 days compared to an average processing time of 64 days for LDs closed in October 2002. This improvement in timeliness is a result of the EA/EB weekly LD meetings, BA staff increases, and LD training conducted by EA personnel at the EE field offices.

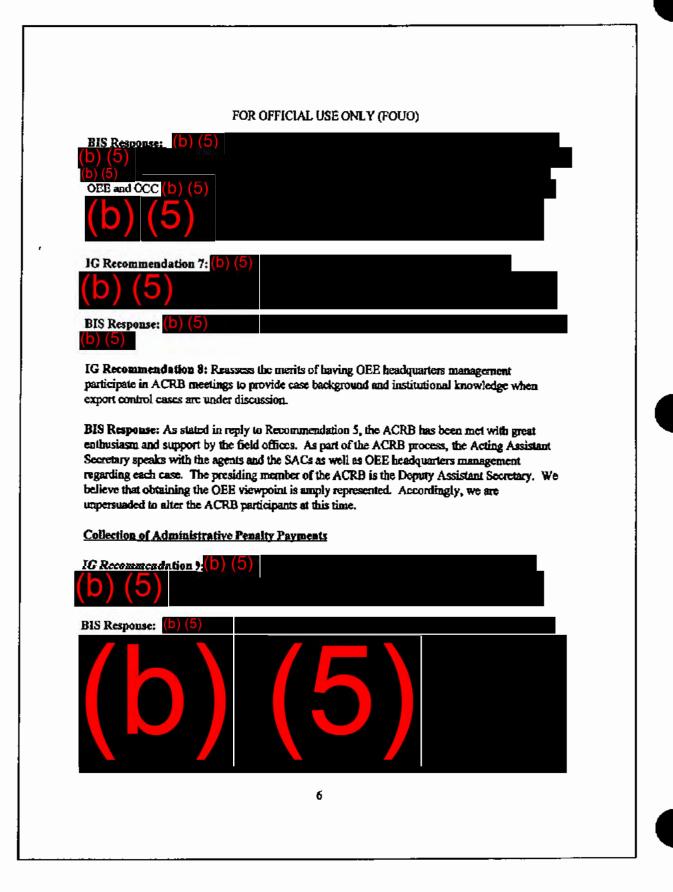
It should also be noted that the OIG has identified problems with only a handful of LDs out of the 334 completed in fiscal year (FY) 2002. Nonethess, EA has taken steps to further ensure the accuracy of LDs. To address the first example cited by the IG, EA clarified its internal policy to require the division with the strictest controls (such as the Nuclear and Missile Technology (NMT) Division for items controlled for nuclear or missile proliferation reasons) to have the final sign-off on an LD. To address the second issue - LDs with clerical errors - EA has instituted an additional review process to ensure such errors do not occur. The electronic request in ECASS is printed out and reviewed against the certified response, and any other information related to the request, to ensure that data elements, such as commodity description, country of destination, and time period under review, are correct. This second level review is done by an NMT employee not involved in the case under review as a licensing officer or a signing official. This procedure was adopted to ensure that unintentional errors related to document preparation are caught and corrected.

b. Providing more instructions and guidance to OEE agents on the information needed to complete a determination accurately and in a timely manner.

BIS Response: Written LD guidelines for EA licensing officers and EE agents have been in place since 1998. Additional guidelines are being prepared. BIS has also initiated training on LDs at EE Field Offices throughout the United States. These sessions, conducted by EA engineers, provide EB agents with specific guidance on the information needed to accurately determine the license requirements of an item, identify applicable exceptions, and jurisdictional issues. To date five of the eight field offices have received the training in FY 2003 and all offices will have received it by May 2003. In addition, EA provided LD training at EE's FY 2002 special agent training.







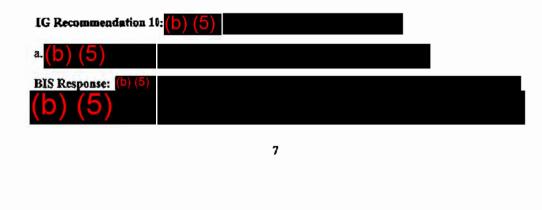
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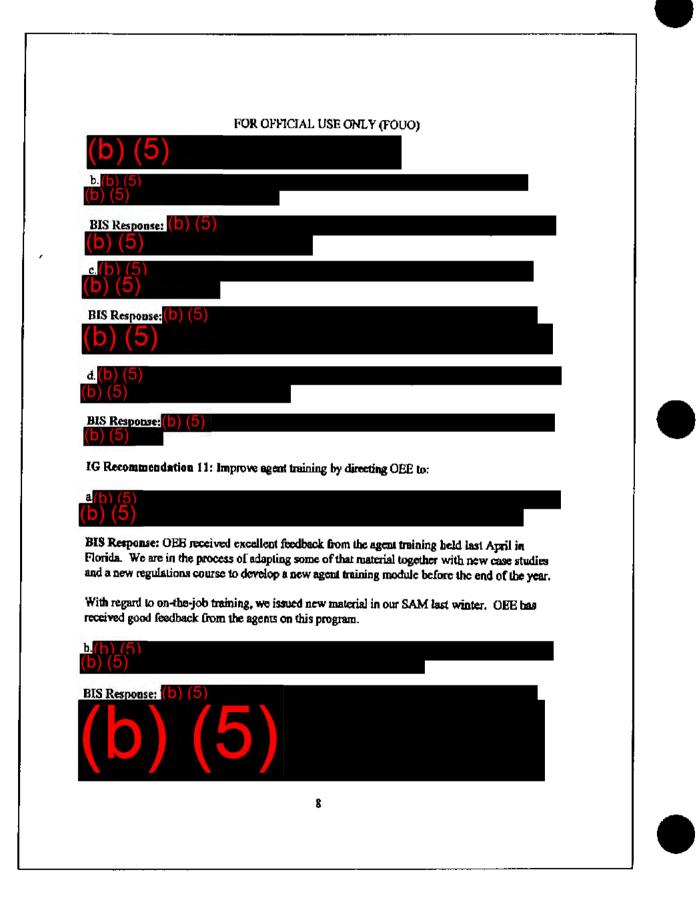
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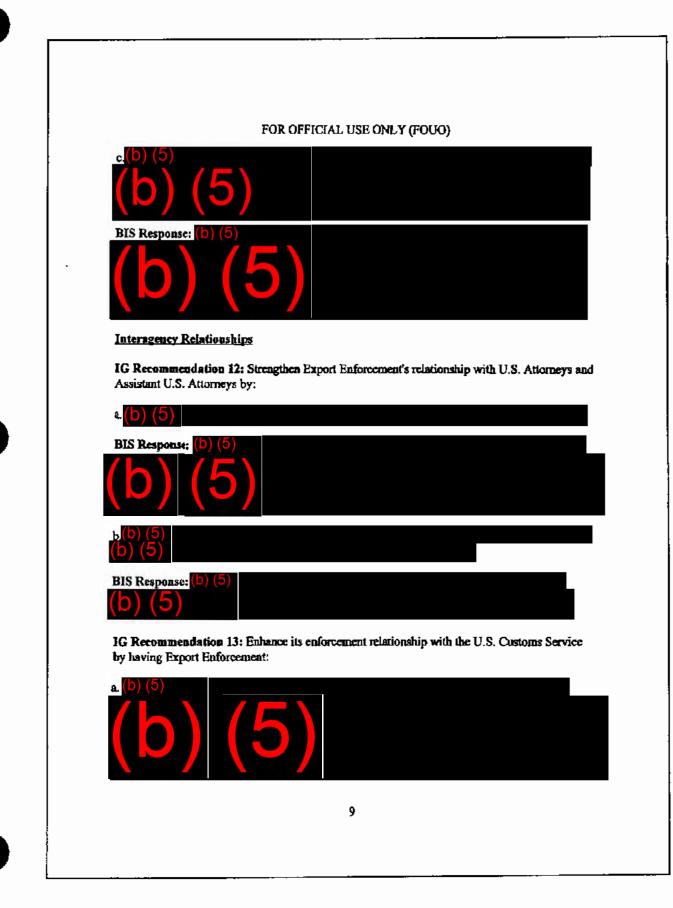
We have reviewed the five accounts noted by the IG during its review that were delinquont. We determined that one company had gone bankrupt, one company went out of business, and three accounts were referred by NOAA independent of the IG review to Treasury for collection. Pursuant to your recommendation, we have investigated the following delinquent accounts, and their status is reflect below:

| Company             | Status  |
|---------------------|---|
| Everex System       | Company paid \$3,634 of \$75,000 penalty. It<br>has filed for bankruptcy. Once we receive the<br>bankruptcy documents, we will determine a<br>course of action in consultation with coursel.  |
| IGG Corporation     | Company paid \$250,000 of \$400,000 penalty.<br>OEE's investigation revealed that the<br>company went out of business in March 2002.<br>We will recommend that the penalty be<br>written off as uncollectible.  |
| Refinery Industries | Company claims to have gone out of<br>business. The matter has been referred to the<br>Treasury Department for collection.  |
| Federal Parts       | Company claims to have gone out of<br>business. The matter has been referred to the<br>Treasury Department for collection. Section<br>11(h) denial order has already been imposed.<br>Therefore, no additional denial for failure to<br>pay may be imposed. |
| (b) (6)             | This matter has been referred to the Treasury<br>Department for collection.   |

#### Special Agent Manual & Agent Training

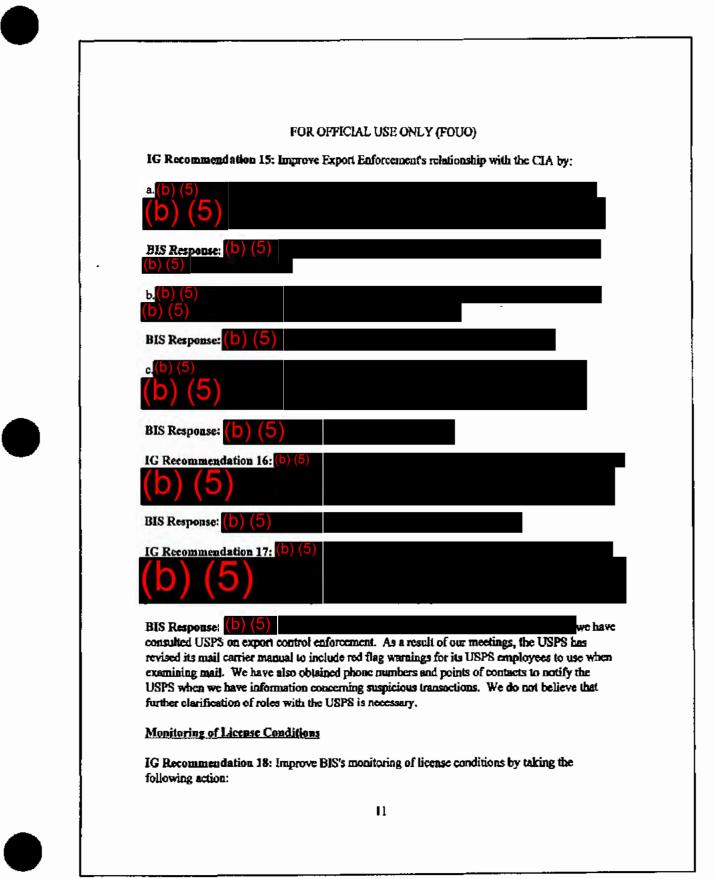


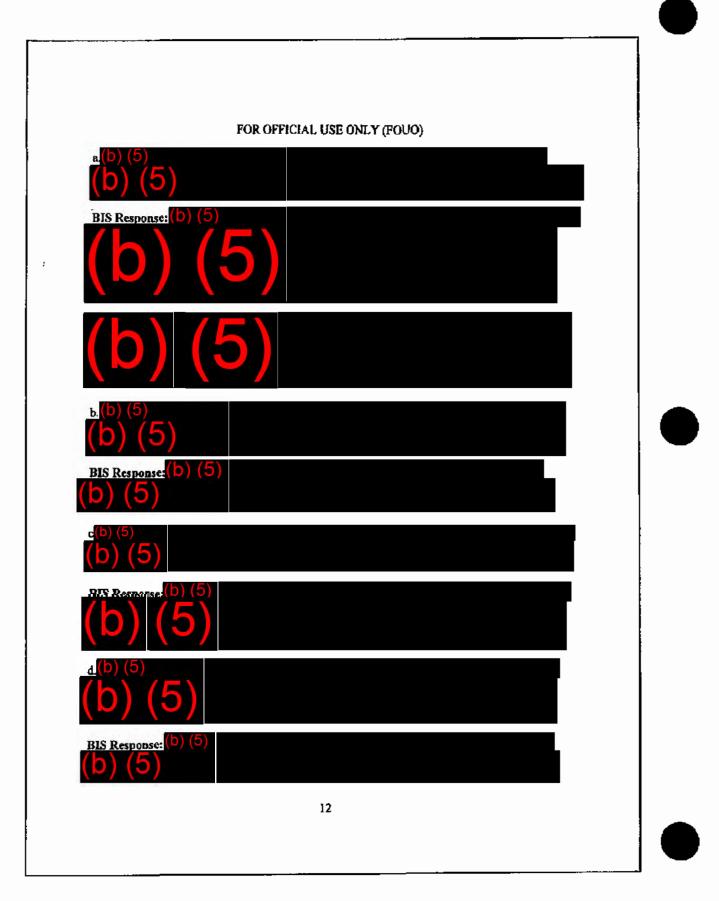




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|--------|---|--|
|        | $\begin{array}{c} \text{BIS Response:} (b) (5) \\ \hline (b) (5) \\ \hline (5) \\ \hline \end{array}$ |  |
|        | b. Ensure that $OEE(b)$ (5) (5) (5) (5)   |  |
|        | BIS Response: $(b)$ (5) (b) (5) (b) (5)   |  |
| ĺ      | (b) (5)<br>(b) (5)  |  |
| 6      | BIS Response: (b) (5)<br>(b) (5)<br>IG Recommendation14:(b) (5)<br>b) (5)                             |  |
| a<br>( | a. (b) (5)<br>(b) (5)   |  |
| I      | $\begin{array}{c} \text{BIS Response:} (b) (5) \\ (b) (5) \end{array}$                                |  |
|        | (b) (5)<br>(b) (5)  |  |
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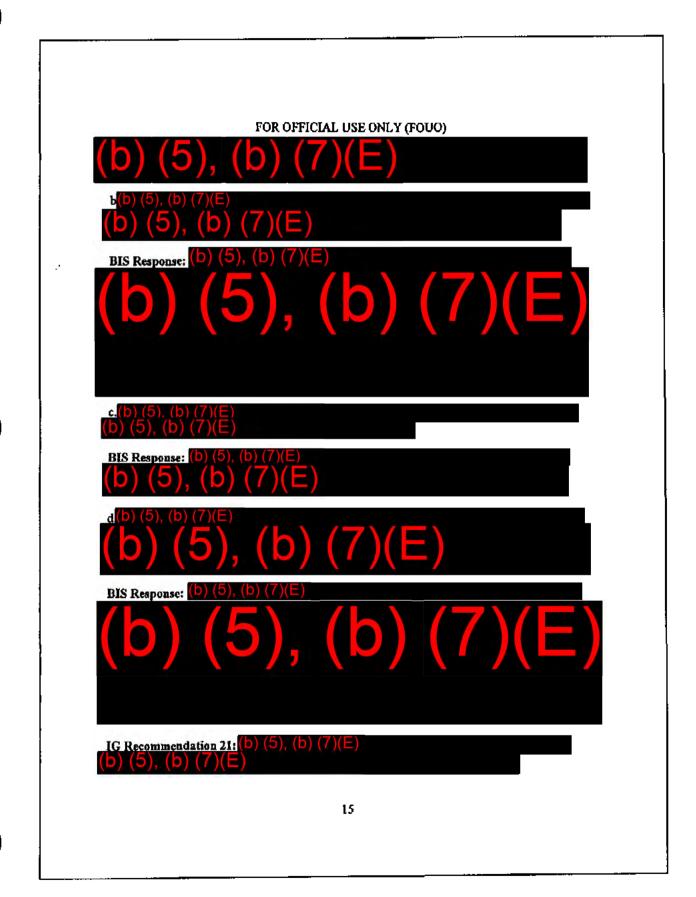
EE wishes to make a few observations about the IG's report on this issue. First, Figure 9 on p. 47, entitled, "Open Licenses in Export Enforcement Subsystem as of May 2002" is misleading because it suggests OEA has failed to verify the conditions on a significant number of licenses. It should be noted that a number of the open licenses in this table are still valid for which no shipment has yet been made; thus no PSV can be initiated.

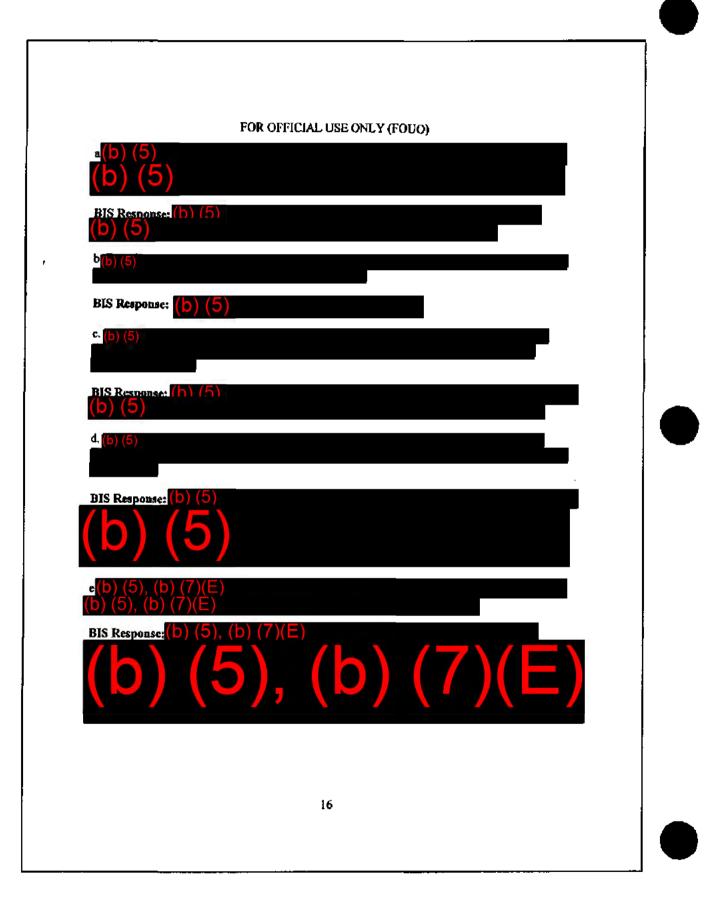
Second, the IG's point about untimely follow-up on license conditions misses the importance of varying the timing on initiated PSVs, from a few months to several months after shipment has occurred, when misuse or illegal diversions are more likely to be uncovered. For example, PSVs initiated 30 days after export will most likely find the export still with the consignee; whereas, PSVs completed several months to a year after shipment are more likely to uncover misuse or illegal diversions.

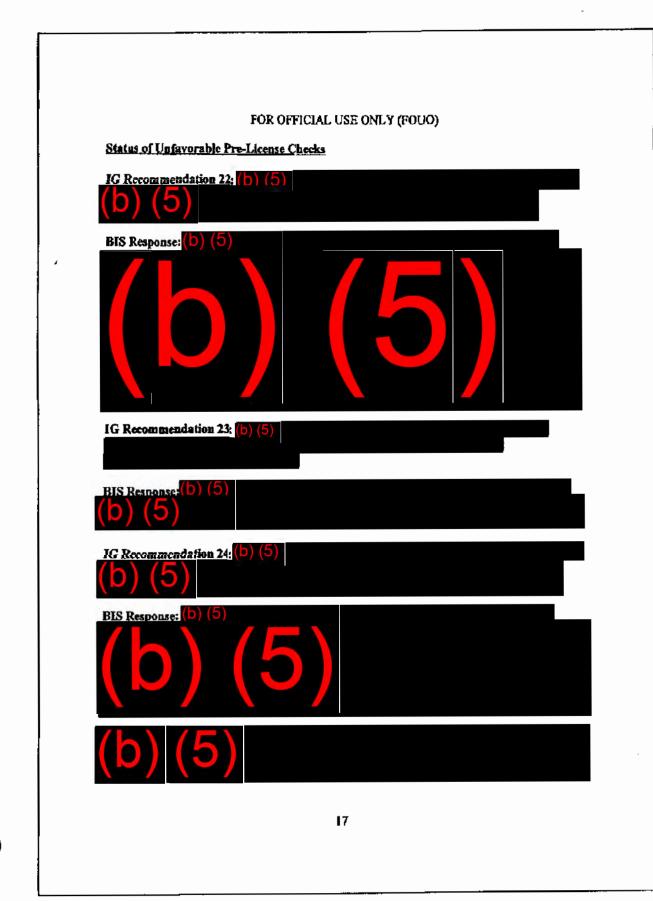
Finally, the IG's example used to illustrate average OBA follow-up response times on license conditions (p. 46) is not representative and does not reflect the true average follow-up response times. We provided several years of this data to the IG.



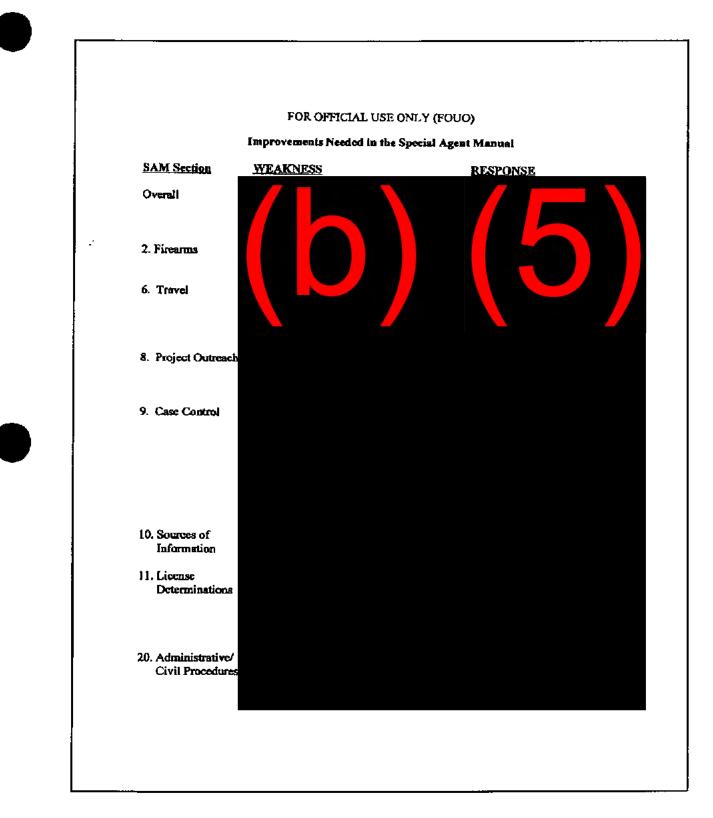
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|---|------------------------------|---------------------------|--------------|---|
| BIS Response:   | 5)                           |                           |              |   |
| Outreach  |                              |                           |              |   |
| a. (b) (5)<br>(b) (5)   | Make outreach to industry a  | more proactive and strate | gic tool by: |   |
|   |                              |                           |              |   |
| b.(b) (5)<br>(b) (5)  |                              |                           |              |   |
| BIS Response: (b) (5)   |                              |                           |              |   |
| (b) (5)   |                              |                           |              |   |
| $\begin{array}{c} \text{BIS Response:} \\ \text{(b) (5)} \\ \text{(b)} \\ \text{(5)} \\ $ |                              |                           |              |   |
| End-Use Checks  |                              |                           |              |   |
| $\begin{array}{c} \text{IG Recommendation 20:} \\ \text{(b) (5), (b) (7)} \end{array}$  | o)(5)(b)(7)(E)<br>E <b>)</b> |                           |              |   |
| a. (b) (5), (b) (7)(E)<br>b) (5), (b) (7)(E)  |                              |                           |              |   |
| $ \begin{array}{c} \text{BIS Response:} \\ \text{(b)} \\ \text{(b)} \\ \text{(b)} \\ \text{(b)} \\ \text{(b)} \\ \text{(b)} \end{array} $   | (b) (7)(E)<br>(7)(E)         |                           |              |   |
| (b) (5), (l   | o) (7)(E)                    |                           |              |   |
| (b) (5), (b)  | (7)(E)                       |                           |              |   |





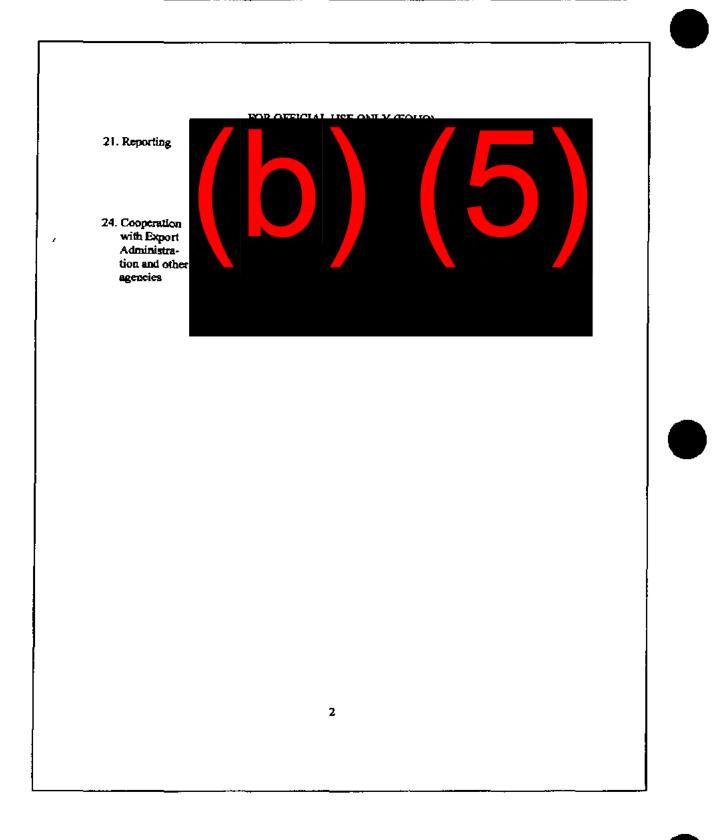


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|--|---|--|
| IG Recommendation                                    | n 25: <mark>(b) (5)</mark>  |  |
|  |   |  |
| BIS Response:  | (5)   |  |
| License Determinati                                  |   |  |
| IG Recommendation<br>following areas:                | a 26: Ensure that Export Administration works with Customs in the |  |
| (b) (5), (b) (<br>(b) (5)                            | 7)(E)   |  |
| BIS Response (b) | 5)  |  |
| ь(b) (5), (b) (7)(<br>(b) (5), (b) (7)(E)            | Ε)  |  |
| BIS Response: (b)                                    | (5)   |  |
| (6) (6)  |   |  |
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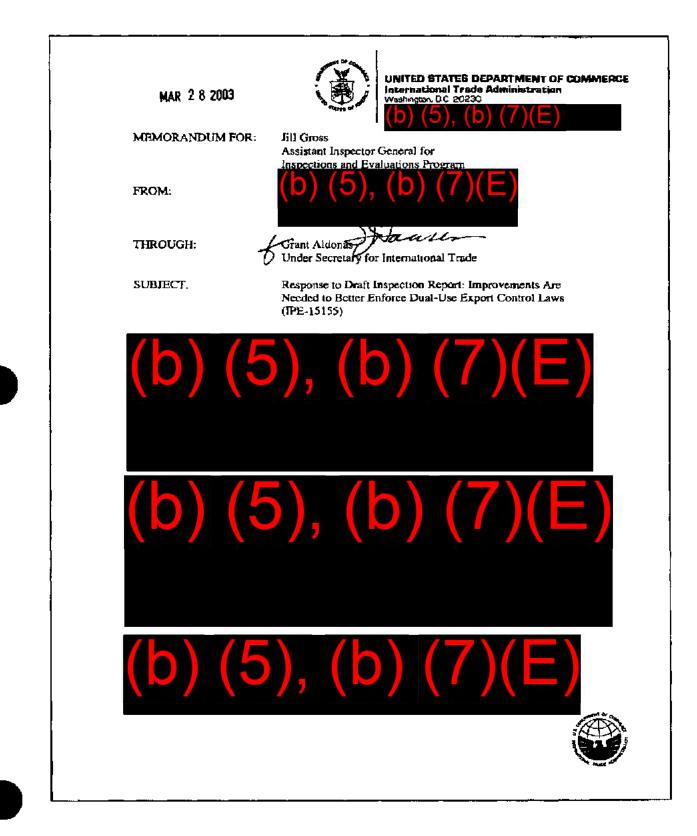


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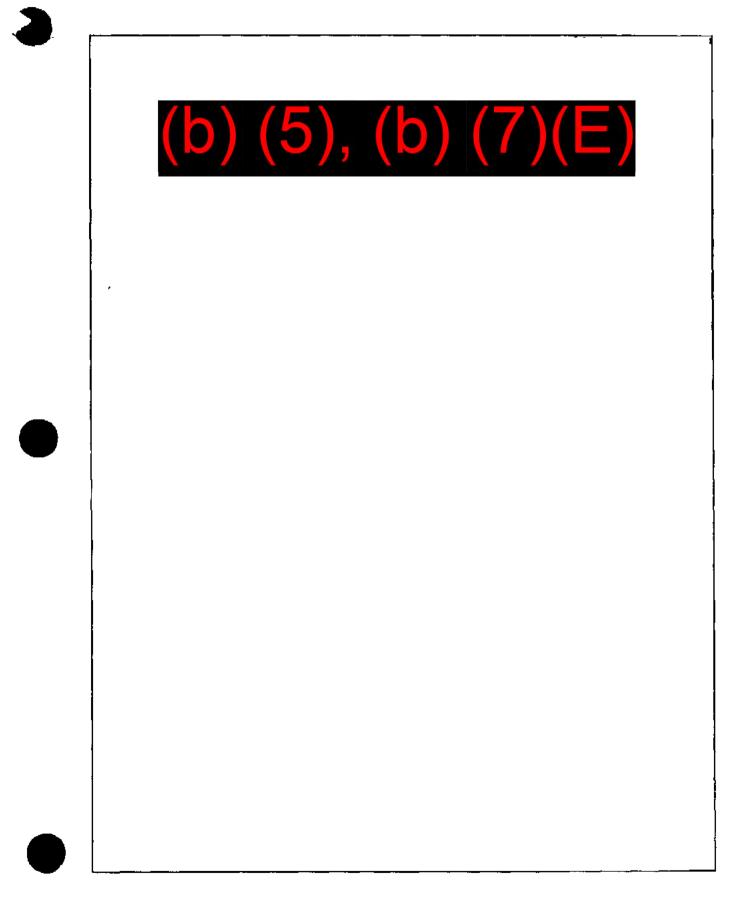
# APPENDIX E



Final Report IPE-15155 March 2003









UNITED STATES DEPARTMENT OF COMMERCE The Inspector General Washington, D.C. 20230

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# **MEMORANDUM FOR:**

Kenneth I. Juster Under Secretary for Industry and Security

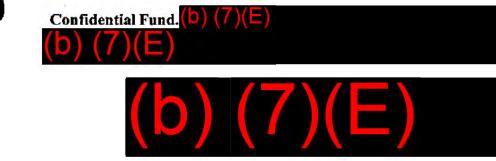
FROM:

SUBJECT:

Johnnie E. Frazier

Administrative Matters Concerning BIS' Export Enforcement (IPE-15155-2)

During our recent review of the Bureau of Industry and Security's (BIS) efforts to enforce dualuse export controls, issues arose concerning several administrative matters, including the usage of confidential funds by the Office of Export Enforcement (OEE), vehicle usage, and physical security and location of OEE field offices. Because these issues were beyond the scope of our export enforcement review, we did not attempt to thoroughly examine all of their causes and effects. Nonetheless, we think these issues are important enough to bring to your attention for appropriate management consideration and action. We have recently discussed these issues with BIS Deputy Under Secretary Karan Bhatia, Acting Assistant Secretary for Export Enforcement Lisa Prager, and other BIS officials.







While these activities are essential to carrying out

OEE's export enforcement activities, Section 14 (Undercover Operations) lacks clarity on the use of confidential funds for these purposes. Specifically, Section 14 states that a special agent's request for an undercover operation must include, among other informatiou, "a thorough cost projection, including travel, per diem, and confidential expenses, and other related expenses." However, there is no subsection dealing with confidential fund management as it relates to undercover operations.

We also noted that BIS field offices maintain their confidential fund accounts in very different ways. The following table (Table 1) details the varied use of confidential funds by OEE field offices and leads us to believe that Export Enforcement should issue clearer guidance on the appropriate use and handling of confidential funds.

| Field Officet:                                      | Boston              | New York-           | Dallas                  | San Jose   | Los Angeles         |
|---|---------------------|---------------------|-------------------------|--|---------------------|
| Amount  | \$1,250             | \$5,000             | 0                       | \$5,000  | \$5,000             |
| Account Type  | Checking<br>account | Checking<br>account | Convenience<br>checks** | Cash   | Checking<br>account |
| Account Fees  | No                  | Yes                 | N/A                     | N/A  | No                  |
| Types of<br>charges                                 | (b) (7)(E)          | (b) (7)(E)          | (b) (7)(E)              | (b) (7)(E)   | (b) (7)(E           |
| Date/Amount/<br>Type of most<br>recent<br>charge*** | 9/5/02              | 6/3/02              | 10/31/02                | 2/2/02   | 3/01                |
|   | \$64.18             | \$21.00             | \$130.53                | \$67.00  | \$500.00            |
|   | (b) (7)(E)          | (b) (7)(E)          | (b) ( <i>1</i> )(E)     | (b) (7)(E)   | (b) (7)(E           |
| ** Convenience                                      | checks are checks   | issued against a ca |                         | lential funds.<br>card account and may<br>advance fee for each t |                     |
| apply.  |                     |                     |                         | on for BOFO and DA   |                     |

# Table 1: OEE Confidential Fund Activity, 2000-2002

**Vehicle Usage.** Over the past three years, OEE has spent approximately a half million dollars annually to lease 94 to 96 vehicles from a major car rental agency headquartered in New Hampshire.<sup>2</sup> Each OEE field agent is assigned a car that is to be used for official purposes only, including the special allowance for transportation between their home and work.

 $<sup>^{2}</sup>$  OEE leasing costs for the past three years are as follows: (a) FY 2000 for \$435,751; (b) FY 2001 for \$547,488; and (c) FY 2002 for \$527,208.

Our review of OEE's vehicle usage disclosed that OEE has too many vehicles. In fact, the number of vehicles leased by OEE at the time of our inspection exceeded the number of agents in OEE field offices. However, according to BIS' vehicle leasing guidance:<sup>3</sup>

- Requests for all leased vehicles must be approved, as appropriate, by the Deputy Assistant Secretary of Export Enforcement and the Director of Export Enforcement.
- There must be at least one agent on board for each car leased.
- Leasing will not be approved for prospective employees.
- Any full-time position left unfilled for two months shall lose the assigned leased vehicle.

Despite the requirement that there must be at least one designated driver for each vehicle (or not more than a two-month vacancy), our review revealed instances where the number of leased vehicles assigned to the OEE field offices exceeded the number of agents assigned to those offices. For example, the (b) (7)(E)

We also noticed similar trends at other field offices visited during our review. When asked about the vehicle surplus, OEE Special Agents-In-Charge and headquarters managers informed us that they were holding onto some of the excess vehicles "in anticipation of new hires."

Using the lowest cost for vehicles leased over the past three years as a baseline, we calculated the cost savings possible if OEE had adhered to the BIS vehicle leasing policy. In FY 2000, the least expensive leased vehicle was \$303 per month (1997 Chevy Lumina). In FYs 2001 and 2002, the least expensive leased vehicle was \$361 per month (2000 Dodge Intrepid). Table 2 documents the minimum potential cost savings for excess OEE-leased vehicles assigned to the 8 field offices over the past three years. Moreover, these estimated cost savings do not include the additional savings possible that would be associated with any parking or maintenance fees paid in connection with the leased vehicles.

| Fiscal<br>Year   | # of Field<br>Agents | # of Vehicles<br>in the Field* | Difference | Potential Cost Savings<br>Over 12 Months |  |  |  |
|--|----------------------|--------------------------------|------------|--|--|--|--|
| 2000   | 89                   | 91                             | 2          | \$ 7,272                                 |  |  |  |
| 2001   | 84                   | 92                             | 8          | \$34,656                                 |  |  |  |
| 2002   | 77                   | 92                             | 15         | \$64,980                                 |  |  |  |
|  |                      | Total                          | 25         | \$106,908                                |  |  |  |
| *This table does not include any excess vehicles that may be assigned to headquarters' units |                      |                                |            |  |  |  |  |

# Table 2: Minimum Potential Cost Savings for Excess Leased Vehicles

**\*** This table does not include any excess vehicles that may be assigned to headquarters' units. Source: Export Enforcement, Bureau of Industry and Security.

Although OEE plans to hire several new agents in the upcoming months, significant savings could have been achieved if unused vehicles were returned to the rental company. While the lease agreement states that the Government has the right to terminate the contract in whole or in part, for its sole convenience, the rental company would be entitled to receive some unspecified

<sup>&</sup>lt;sup>3</sup> Bureau of Export Administration Vehicle Policy, September 25, 1991.

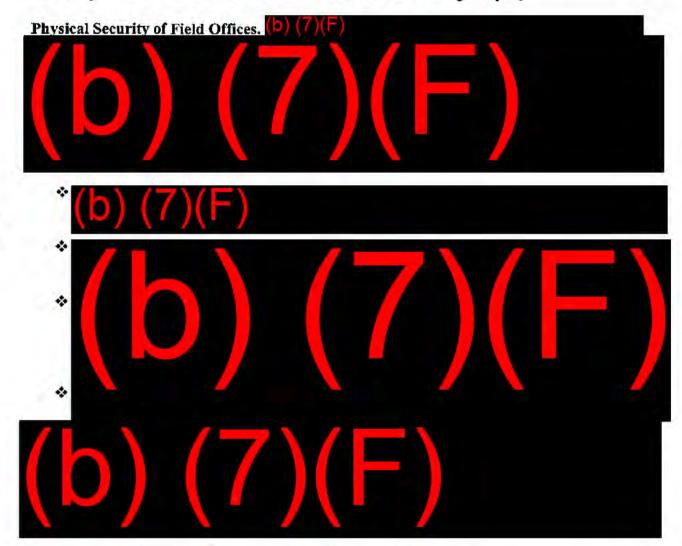
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compensation if BIS had returned the excess vehicles (the lease agreement does not specify what this penalty would have been). Specifically, the contract states that, "Subject to the terms of the contract, the Contractor shall be paid a percentage of the contract price reflecting the percentage of the work performed prior to the notice of termination, plus reasonable charges the Contractor can demonstrate to the satisfaction of the Government using its standard record keeping system, have resulted from the termination."

Therefore, we encourage OEE to follow BIS' vehicle leasing policy and, at a minimum, ensure that there is at least one designated agent on board for each car leased. In addition, BIS should return any excess and/or underutilized leased vehicles to the leasing company.



Location of Field Offices. It is our understanding that BIS requested funding to open two additional offices during FY 2003—a field office in Seattle, Washington, and a satellite office in Houston, Texas. These sites were chosen as proposed OEE office sites because (1) Houston is deemed to be a high risk area for export violations and currently accounts for 40 percent of





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IPE-15155-2 June 2003

DAFO's caseload; and (2) a high dollar volume of exports passes through the state of Washington, which ranks fifth in exports from the United States. According to the Acting Assistant Secretary for Export Enforcement, BIS did not receive the requested funding in its FY 2003 budget to open both offices. As such, BIS informed us that it will only open the Houston office this year. While OEE was able to provide a clear, mission-related rationale for the site selection of the proposed new offices, it did not have a similar rationale for the locations of its current eight field offices.

As BIS assesses future locations of OEE field offices, we believe that Export Enforcement should reassess whether the current field office sites remain the most appropriate locations. In doing so, we believe it would be prudent for OEE to apply the criteria it recently established and used for its proposed new offices, including the number and dollar value of exports in the region; export destinations; commercial companies involved in dual-use controlled commodities; licensing requests; historical trends and the potential for export violations; the amount of casework in the region; and the physical proximity to airports, seaports, and other law enforcement agencies. Obviously, decisions affecting BIS' field office locations must also take into account the full range of related issues, anticipated benefits, and intangible costs.

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We would appreciate hearing back from you within 60 days as to how BIS intends to address these issues. If you have any questions or would like to discuss these issues further, please contact me on (202) 482-2754.

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U.S. DEPARTMENT OF COMMERCE Office of Inspector General



# PUBLIC RELEASE

# NATIONAL OCEANIC AND ATMOSPHERIC ADMINISTRATION

Weather Service Modernization Contract To Be Reduced

Audit Report No. ENT-8749-7-0001 / March 1997

Office of Audits Environment and Technology Division



MAR 4 1997

MEMORANDUM FOR:

Dr. Elbert W. Friday, Jr. Assistant Administrator for Weather Services National Oceanic and Atmospheric Administration

William O. Mehuron Director, Systems Acquisition Office National Oceanic and Atmospheric Administration

FROM:

George E. Ross Assistant Inspector General for Auditing

SUBJECT:

Weather Service Modernization Contract to Be Reduced Final Audit Report No. ENT-8749-7-0001

The Office of Inspector General has completed a limited review of the National Oceanic and Atmospheric Administration's use of support contractors to assist with the National Weather Service's modernization and restructuring effort. NOAA has used support contractors in this capacity since 1983. To date, NOAA has spent over \$34 million on these services, with another \$28 million projected as the ceiling cost of the recently recompeted contract.

Our review focused on the accelerated level of expenditures on the recently completed contract and the planned expenditures for the follow-on contract. Specifically, we sought to determine whether administrative controls are in place to ensure that contract expenditures are proper. We found that although the contract, originally scheduled to expire in May 1997, appeared to be well managed, it nevertheless ran out of funds early in fiscal year 1997. According to NWS officials, unforeseen complications with deploying new systems and congressionally mandated certification procedures resulted in the need for increased contractor support.

We also found that the level of effort projected for the new contract, awarded in September 1996 and scheduled to run through 2001, appeared too high for the phasing-down period of the modernization effort. We discussed our observations with NOAA officials, who stated that the projected level of effort could be reduced without seriously affecting the modernization. Consequently, NOAA agreed to reduce its projected costs by \$6.3 million. Because of our agreement on reducing the projected level of effort, this report is issued in final with the consent of NWS and NOAA's System Acquisition Office.

We appreciate the cooperation and courtesies extended to us by program and procurement officials during the review.

#### Introduction

NWS is undergoing a transition that involves consolidating approximately 300 field offices into 119 weather forecast offices and deploying state-of-the-art technology. To assist in this effort, NOAA has been acquiring system engineering and technical support services through level-of-effort contracts. Under these contracts, costs are incurred as services are acquired. The contracting officer initially negotiates the estimated total contract cost, including option years, based upon minimum and maximum levels of effort and predetermined labor rates for the various types of skills expected to be needed. As program needs arise, task orders are issued, and specific resource estimates are negotiated for each task. The contract remains in effect until the maximum level of effort is reached or the contract expires, whichever comes first.

A previous review of an earlier contract disclosed that NWS had allowed the contractor to use higher skilled employees than agreed to, increasing the cost of the services acquired. When we learned that NOAA had reached the 1992 contract's dollar limit earlier than planned, we became concerned that a similar situation had occurred. As a result, we began this review of the 1992 support contract and its replacement contract.

## Purpose and Scope of Review

The purpose of our review was to determine the reasons for the early completion of the 1992 contract and to assess the validity of the level of effort and costs proposed in the follow-on contract. We limited our scope to reviewing contract-related documents, analyzing labor hours and costs charged to the completed contract, and evaluating the acquisition plan, cost estimates, and other documentation for the follow-on contract. We also interviewed NWS managers, Systems Acquistion Office managers, NOAA contracting officials, and contract employees. We conducted our audit from December 1995 through November 1996 at NOAA offices in Silver Spring, Maryland, and Sterling, Virginia.

Because of the limited scope of our work, we confined our review of internal controls to those associated specifically with the 1992 contract. We found them adequate to ensure that costs and task orders were proper. We did not evaluate the reliability of computer systems because we did not rely on computer-generated information. We did not perform any compliance testing because there were no specific laws or regulations associated with the review. Our work was conducted in accordance with generally accepted government auditing standards. This audit was performed under the authority of the Inspector General Act of 1978, as amended, and Department Organization Order 10-13, dated May 22, 1980, as amended.

# Concerns About the 1992 Contract Proved Unfounded

We determined that NOAA had properly managed the 1992 contract and that it reached its dollar limit earlier than expected as a result of additional work assigned to the contractor. In 1992, when the contract was awarded, NOAA anticipated that approximately \$19 million would cover the cost of the five-year contract, which was to expire in May 1997. However, NOAA officials later realized that funds would be expended earlier than the anticipated expiration, and in July 1995 approved a plan to acquire a new contractor by the beginning of fiscal year 1997. Based on our audit of the prior contract (see audit report no. NOA-4646-2-0001, September 1992), we were concerned that the funds had been expended due to an unsupported increase in skill level. However, our review disclosed that this was not the case. In fact, NOAA had used the services faster than planned primarily because of problems with the deployment of the new systems and congressionally mandated certification procedures for closing old weather offices. As a result, we plan no further review in this area.

## Agreement Reached on Reducing Level of Effort for Follow-on Contract

We reviewed the follow-on contract's level of effort and found that it appeared too high for the phasing-down period of the modernization effort. We discussed our concerns with Automated Surface Observing Systems (ASOS) and Transition Program Support managers, who, upon reevaluating the proposed level of effort, agreed that it could be reduced without seriously affecting the modernization.

#### Automated Surface Observing Systems

The ASOS program office is responsible for deploying the ASOS systems that should be in place in 1997. However, we found that the office did not reduce its projected use of the contractor as the systems were deployed. According to one program official who has since retired, the level of effort remained unchanged to cover potential delays in the deployment schedule. When this situation was brought to their attention, program officials immediately reduced the estimate to coincide with the current deployment schedule. This reduced the follow-on contract's level of effort for ASOS acquisition support from 45 staff years to about 12 over the five-year life of the contract. The chart below shows the estimated difference in staffing between the NOAA's original and revised projections for ASOS acquisition.

| Number of Projected Staff Years for ASOS Acquisition  |   |   |   |   |   |    |  |  |
|---|---|---|---|---|---|----|--|--|
| ProposalContract<br>Year #1Contract<br>Year #2Contract<br>Year #3Contract<br>Year #4Contract<br>Year #5 |   |   |   |   |   |    |  |  |
| Original  | 9 | 9 | 9 | 9 | 9 | 45 |  |  |
| Revised   | 9 | 3 | 0 | 0 | 0 | 12 |  |  |

Source: OIG analysis of NOAA data.

# **Transition Program Support**

Various program offices are responsible for managing the transition of the field offices. Transition activities include preparing and monitoring modernization budgets and schedules, monitoring weather office construction plans and schedules, communicating the progress of the transition and answering questions from interested parties, and maintaining transitionrelated data bases. The level of effort requested by the program offices to accomplish these tasks increased over the contract performance period. However, we expected to see a decrease as the transition comes to a close.

In reviewing the tasks proposed in the follow-on contract, we noted that by performing some tasks in-house and eliminating others, this level of effort could be reduced. For instance, one task included developing a national maintenance plan for newly constructed offices. We believe that this task could be performed by NWS facilities staff in the Office of Systems Operations, with the assistance of field employees who have been maintaining the old weather offices. Another task included construction site survey work that we believe could be eliminated from the follow-on contract because the work is already being managed by the Special Engineering Projects Office. We discussed these and other observations with NWS program officials. Accordingly, program officials reevaluated and subsequently reduced their projection for the follow-on contract's level of effort from 260 staff years to about 203 over the five-year life of the contract. The chart below shows the estimated difference in staffing between the original and revised projections for the Transition Program Support area.

| Number of Projected Staff Years for Transition Program Support  |    |    |    |    |    |     |  |  |
|---|----|----|----|----|----|-----|--|--|
| ProposalContract<br>Year #1Contract<br>Year #2Contract<br>Year #3Contract<br>Year #4Contract<br>Year #5TO |    |    |    |    |    |     |  |  |
| Original  | 48 | 54 | 54 | 52 | 52 | 260 |  |  |
| Revised   | 42 | 48 | 46 | 35 | 32 | 203 |  |  |

Source: OIG analysis of NOAA data.

## **Recommendation**

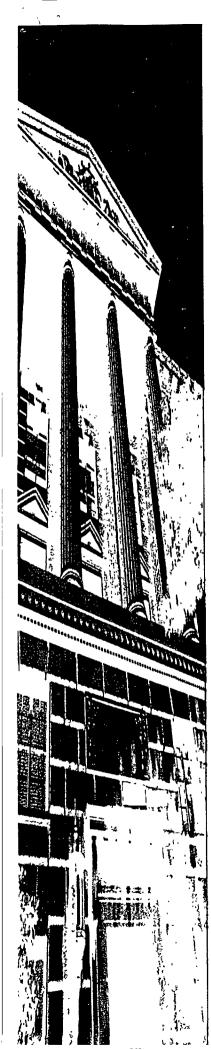
During this review, we recommended, and NOAA program managers agreed, that NOAA should reevaluate the level of effort projected for the ASOS and Transition Program Support areas.

# Funds to Be Put to Better Use

As a result of our recommendation, projections for ASOS Acquisition and Transition Program staffing requirements during the follow-on contract were reduced from 305 to 215 staff years over the five-year contract (see previous charts). Reducing the projected level of effort will reduce the NOAA cost projections by \$6.3 million. NOAA officials pointed out that the recent budget reductions made it uncertain whether funding would be available to support even these reduced projections. Memorandums from the ASOS program office and the Transition Program Support area outline the revised level of effort. The following chart shows the projected cost reductions by contract year.

| Cost Reductions Resulting from Revised NOAA Projections<br>(\$ x 1000) |                     |     |                     |                     |                     |                     |          |  |
|--|---------------------|-----|---------------------|---------------------|---------------------|---------------------|----------|--|
| Estimated Reductions for:  | Contract<br>Year #1 |     | Contract<br>Year #2 | Contract<br>Year #3 | Contract<br>Year #4 | Contract<br>Year #5 | TOTAL    |  |
| ASOS Acquisition   | \$                  | 0   | \$ 380              | \$ 603              | \$ 627              | \$ 652              | \$ 2,262 |  |
| Transition Program Support   |                     | 316 | 410                 | 608                 | 1,217               | 1,523               | 4,074    |  |
| Total  |                     |     |                     | <u></u>             |                     |                     | \$ 6,336 |  |

Source: OIG analysis of NOAA data.



U.S. DEPARTMENT OF COMMERCE Office of Inspector General



# NATIONAL INSTITUTE OF STANDARDS AND TECHNOLOGY

NIST FY 1996 Charges to the Environmental Protection Agency

EDAD-10062-7-0001/August 1997

Office of Audits Economic Development Audits Division



UNITED STATES DEPARTMENT OF COMMERCE Office of Inspector General Washington DC 20230

AUG | 8 1997

**MEMORANDUM FOR:** 

John C. McGuffin Controller National Institute of Standards and Technology

FROM:

Andrew R. Cochran Andrew R. Cochran Director For Director. Economic Development Audits Division Office of Audits

SUBJECT:

NIST FY 1996 Superfund Charges to the Environmental Protection Agency Final Report No. EDAD-10062-7-0001

The Office of Inspector General has completed its audit of NIST's use of EPA Superfund appropriations and prepared the final audit report. The audit was completed to fulfill the requirement under the Superfund Amendments and Reauthorization Act of 1986 for an annual audit of all Superfund payments and obligations.

We found that NIST had accurately accumulated, documented and charged the Superfund reimbursable costs for the funds received. The funds were received in advance for all the work performed by NIST. Our evaluation of the agency's compliance with laws and regulations indicated that NIST was in compliance with the relevant financial provisions of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended.

NIST also was in compliance with the terms and conditions of the interagency agreement, and controls over Superfund activities were adequate. During fiscal year 1996 NIST properly tracked EPA Superfund monies by providing segregated cost centers for the Superfund expenditures. As a result, we are issuing this report in final form with no recommendations for future action by NIST.

We appreciate the cooperation and courtesies extended to us by NIST officials during the audit.

#### Introduction

Among its many efforts to contribute to public health and safety, NIST provides technical research to counteract the effects of toxic waste spills. This work is performed on a reimbursable basis through interagency agreements with the EPA. Funds for the agreements are appropriated through the Hazardous Substance Response Trust Fund, more commonly referred to as the "Superfund." The Superfund is used to identify the nation's uncontrolled hazardous waste sites, assign priorities to the risks they create and work to eliminate those risks.

The Superfund program, created under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, established the Superfund to provide funds for identifying, prioritizing, and remedying the nation's uncontrolled hazardous waste sites. The 1980 Act, as amended by the Superfund Amendments and Reauthorization Act of 1986, provides for full recovery from responsible parties of all response costs incurred by the Federal Government. Response costs generally include expenses for investigations, cleanup, enforcement, and administrative activities.

The 1986 Act also provides that the Inspector General will conduct an annual audit of all payments, obligations, reimbursements, or other uses of the Superfund to assure that the fund is being properly administered.

#### **Purpose and Scope of Audit**

The purpose of our audit was to determine whether NIST had properly managed the financial aspects of its Superfund interagency agreements. We evaluated whether NIST had (1) accurately accumulated, documented and charged EPA for the Superfund reimbursable costs; (2) established adequate internal controls over reimbursable work related to the interagency agreement; and (3) complied with the terms and conditions of its Superfund interagency agreement with EPA. Our review covered interagency agreements entered into or continuing between EPA and NIST during the period October 1, 1995 through September 30, 1996.

We reviewed NIST's policies and procedures for accepting reimbursable work, identifying and assigning actual costs to the project, and recovering all eligible costs. We also interviewed NIST's scientific and administrative personnel. Our review was conducted at NIST offices in Gaithersburg, Maryland from June through July 1997.

To confirm direct costs, we reviewed the agency's financial and program records as well as EPA documents and records. In reviewing indirect costs, we limited the scope of our review to performing an analytical review of indirect costs and rates charged, investigating any differences from the previous fiscal year. We found no significant unexplained differences in the indirect cost rates we compared.

Our audit included an evaluation of internal controls to the extent that they related to the administration of the Superfund interagency agreements with EPA We relied upon our own review, as well as the internal control reviews performed by the independent accountants for NIST for fiscal

year 1996. We found reasonable assurance that there was no material weakness in the recording of the Superfund appropriations.

In our review, we relied on computer-based data obtained from NIST's Office of the Controller. We assessed the reliability of the data by tracing it to source documents and comparing it to other summary data prepared by the laboratories. We found the data sufficiently reliable to be used in meeting the audit objectives. In addition we evaluated the agency's compliance with laws and regulations applicable to the Superfund monies. We identified the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended, as the authorizing and governing legislation. The terms and conditions of the interagency agreement were identified. The review was conducted in accordance with generally accepted government auditing standards, and was performed under the authority of the Inspector General Act of 1978, as amended, and Department Organization Order 10-13, dated May 22, 1980, as amended.

#### Superfund Charges Accurately Accumulated, Documented and Billed

One NIST operating unit administered a single Superfund interagency agreement with EPA during fiscal year 1996. The Technology Laboratory received funding of \$300,000 during FY 1995, of which \$170,320 was unobligated at the beginning of FY 1996. The laboratory expended \$142,650 during FY 1996 under this continuing agreement.

We tested the accuracy of the accounting data by tracing it to original source documents and to the NIST/EPA entry recorded in the Working Capital Accounts. We compared the data to summary information contained in the costs center statements and other documents. All costs were confirmed to their limitation ledgers and related to the NIST Working Capital Account.

In the Technology Laboratory the data was accurately recorded from time sheets to the labor cost summaries. The NIST administration overhead charges were properly documented in the cost center. We traced the indirect costs assigned to the laboratory to the cost center report. The data recorded in the accounting records was accurate and reliable in all material respects, and reflected reasonable costs incurred for the services provided by NIST.

We determined that the costs for the interagency agreement projects were appropriately charged. Costs incurred did not exceed the specified interagency agreement obligation limits. We found that NIST properly reported the use of their Superfund funds, that all billings appeared reasonable for the work performed or the objectives anticipated, and that NIST performed in compliance with the applicable legislation. Moreover, as previously recommended by this office, all costs were accumulated in a segregated cost center for the work performed under the Superfund interagency agreement.

The following is the Superfund agreement under which funds were obligated and expenses incurred during fiscal year 1996:

# Summary of FY 1996 Obligations and Disbursements Under Interagency Agreement DW 1393-5578-05

| Object Class                              | Unobligated<br>Beginning<br>Balance | Expended<br>Appropriations<br>(Cost Center 879-3401) | Net<br>Unobligated<br>Balance |
|---|-------------------------------------|--|-------------------------------|
| Personnel                                 |                                     |  |                               |
| Sponsoring Division                       |                                     | \$63,252   |                               |
| Other Division                            |                                     | 10,959   |                               |
| Fringe Benefits                           |                                     |  |                               |
| Matching Costs                            |                                     | 14,792   |                               |
| Overhead                                  |                                     |  | · ·                           |
| Applied DE                                |                                     | 4,223  |                               |
| Applied OU                                |                                     | 9,507  |                               |
| Applied NIST                              |                                     | 39,917   |                               |
|   |                                     |  |                               |
| Totals                                    | \$170,320                           | \$142,650  | \$27,670                      |
| DE = Applied for D<br>OU = Applied for th | epreciation<br>e Operating Unit     |  |                               |

OU =Applied for the Operating UnitNIST =Applied for NIST Administration

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In summary, we found that NIST properly accumulated, documented, and billed all of the Superfund work performed during fiscal year 1996 under the NIST/EPA Superfund agreement. Our findings, therefore, result in no recommendations for action by NIST.

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