

105th Congress, 1st Session - - - - - House Document 105-125

END-USE OF DEFENSE ARTICLES AND SERVICES

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COMMUNICATION

FROM

**THE PRESIDENT OF THE UNITED STATES**

TRANSMITTING

THE FIRST ANNUAL REPORT ON THE IMPLEMENTATION OF A  
COMPREHENSIVE PROGRAM TO MONITOR THE END-USE OF DE-  
FENSE ARTICLES AND SERVICES, PURSUANT TO 22 U.S.C. 2785



SEPTEMBER 4, 1997.—Referred to the Committee on International  
Relations and ordered to be printed

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U.S. GOVERNMENT PRINTING OFFICE

39-011

WASHINGTON : 1997

THE WHITE HOUSE,  
*Washington, August 18, 1997.*

Hon. NEWT GINGRICH,  
*Speaker of the House of Representatives,*  
*Washington, DC.*

DEAR MR. SPEAKER: As required by section 40A of the Arms Export Control Act (22 U.S.C. 2785), I transmit herewith the first annual report on the implementation of a comprehensive program to monitor the end-use of defense articles and services, and to prevent the diversion of technology incorporated in defense articles, sold, leased, or exported under the Arms Export Control Act and the Foreign Assistance Act of 1961 (22 U.S.C. 2151 et seq.).

Sincerely,

WILLIAM J. CLINTON.



END-USE MONITORING OF DEFENSE ARTICLES  
DEFENSE SERVICES, AND RELATED TECHNOLOGY

This Report responds to the requirements of Section 40A of the Arms Export Control Act (AECA), "End-Use Monitoring of Defense Articles and Defense Services" (as added by P.L. 104-164, Sec. 150). The legislation requires the establishment of a comprehensive program for the monitoring of such articles and services sold, leased or exported under the AECA and the Foreign Assistance Act of 1961 (FAA) in order, inter alia, to provide "reasonable assurance" of recipient compliance with USG export control requirements with regard to use, transfers and security of such articles and services.

The Departments of State and Defense share policy goals in this area that include consideration of:

- the impact of the proposed transfer on United States capabilities and technological advantage, particularly in protecting sensitive software and hardware design, development, manufacturing and integration knowledge;
- the degree of protection afforded sensitive technology and potential for unauthorized third-party transfer, as well as in-country diversion to unauthorized uses;
- the risk of revealing system vulnerabilities and adversely impacting U.S. operational capabilities in the event of compromise;
- the ability of the recipient effectively to field, support, and appropriately employ the requested system in accordance with its intended end-use.

Each Department is actively engaged in substantive efforts to control the end-use of government-to-government transfer programs and of direct commercial arms exports. They routinely exchange relevant information about transfers, and consult regularly in interagency fora on developments affecting their programs.

Specific legal authorities to control end-use of arms sales, leases and exports are as follows:

- Section 515 of the FAA assigns responsibilities for carrying out duties of Security Assistance Offices (SAOs), including program monitoring. These functions provide in-country management oversight of all security assistance activities to ensure they are conducted in a proper and legal manner and to provide for the exchange of information and advice between the host nation's military establishment, the U.S. Chief of Mission, and Department of Defense (DoD) components responsible for security assistance programs. As part of normal duties, SAOs are responsible for observing and reporting on utilization by the host country of defense articles and defense services, including training.
- Section 623 of the FAA requires the Department of Defense to supervise "end-item use" of defense articles and services provided under FAA grant programs. These responsibilities are largely exercised through the FAA Section 515 activities discussed above.
- Pursuant to Section 38 of the AECA, end-use monitoring of direct commercial exports are administered by U.S. diplomatic posts abroad under the direction of the Department of State's Office of Defense Trade Controls. This is known as the Blue Lantern program, which is discussed below.
- State's Office of Defense Trade Controls also analyzes reporting from a variety of intelligence and diplomatic sources, wherever information surfaces that previously authorized transfers of U.S.-origin defense articles or services (including Foreign Military Sales transactions) may have been retransferred to a third party abroad without prior USG approval.

#### MONITORING OF GOVERNMENT-TO-GOVERNMENT PROGRAMS

Section 40A of the AECA, as added by P.L. 104-164, requires that controls used for identifying high risk exports developed under Section 38(g)(7) of the AECA and subsequently used in the Blue Lantern program for commercial arms exports also be applied for government-to-government sales and lease programs. The Department of Defense (DoD) reviewed its procedures for government-to-government shipments and determined that existing

pre-shipment controls are comparable to the Blue Lantern program.

Before government-to-government shipments are made, the DoD coordinates the transfer closely with the country team, appropriate regional commander-in-chief, and other interagency offices. Whether a minor item, which is readily available commercially or a high technology weapon system, each defense item transfer must be preceded by formal agreement with appropriate end-use and retransfer restrictions.

In addition to the general steps discussed above, DoD applies tighter controls for more sensitive items. For example, DoD's physical security requirements for transfers to foreign governments of arms, ammunition and explosives are similar to those required by U.S. military forces. The most stringent controls are reserved for classified items. The additional controls for classified items include security surveys, special bilateral agreements prior to release and follow-on security surveys to ensure that recipients retain the will and capability to protect the items.

The above-mentioned review of government-to-government controls revealed that there had not been any pre-shipment end-use problems or diversions. There were a relatively small number of problems after delivery was completed. Overall, it was concluded that the period after an item is delivered to the recipient provides the "least reasonable assurance" of appropriate accountability controls. Therefore, changes based on the new legislation were directed toward the period between physical turnover to the recipient and ultimate disposal. These changes are addressed in the Additional Measures section of this report.

#### OVERSEAS MONITORING: THE BLUE LANTERN PROGRAM

End-use monitoring of commercial arms sales occurs in several channels. The best known is the Blue Lantern program through which U.S. embassy personnel abroad are engaged to verify directly with local authorities and foreign firms or persons the bona fides of proposed transactions or shipments in certain circumstances -- or randomly as warranted by acquisition patterns or other trends. The program is managed by the State Department's Office of Defense Trade Controls, located within the Bureau of Political-Military Affairs. Individual instructions containing the relevant background on particular cases are issued through State Department telegraphic channels

in close consultation with the relevant country desks and intelligence agencies, where appropriate. Nearly 3,000 Blue Lantern cases have been initiated since the program's inception in 1990. Key indicators of inquiry provide "flags" for transactions deemed to be "high risk," such as:

- Requested equipment does not match known requirements or inventory of foreign end user.
- Insufficient information about parties to the transaction.
- Requests for spare parts are in excess of projected needs.
- Involvement of foreign consignee or foreign intermediate consignee located in a third country.

These and other "flags," together with reporting by U.S. embassies and intelligence and law enforcement agencies, open source literature on foreign government arms policies, holdings and acquisition plans, as well as the analysis of individual officers in the Office of Defense Trade Controls, provide the basic terms of reference for the program. In most cases, end use monitoring abroad has confirmed the thoroughness of State's munitions controls system for commercial arms exports. The program has had an important deterrent effect. Foreign governments and firms understand increasingly that the USG attaches great importance to ensuring defense articles exported from the United States are used for their intended purposes by the authorized end-user. The program has also been effective in recent years in disrupting grey arms market transactions:

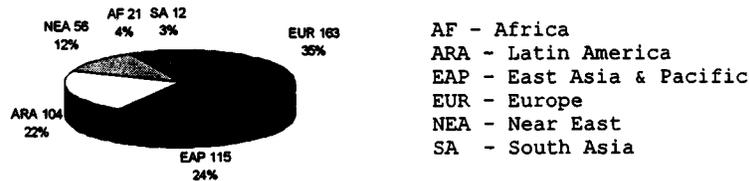
- The central European network of a major arms broker for Iran has been disrupted and investigations launched by two European governments into the broker's activities following effective action by U.S. Embassy personnel in Vienna.
- An attempted diversion to Iran of U.S. aircraft parts was foiled in London and the responsible parties tried and convicted by the UK Government thanks to the efforts of personnel in the U.S. Embassy in London.
- A moratorium has been established on U.S. firearms sales to Paraguay in the wake of careful work by the U.S. Embassy, while tough new laws are being instituted in Montevideo to prevent unauthorized acquisitions by criminal elements in neighboring countries.

Annual State Department guidance to posts has been aimed at clarifying and enhancing U.S. embassy programmatic responsibility to make clear that Blue Lantern is a global end-use monitoring program, developing end use check implementation plans so that operations conform with program parameters, and focusing on policies and procedures to encourage improved foreign government cooperation in the conduct of end-use checks so that they are completed in a timely, effective manner.

As a result of the Blue Lantern program, many foreign government recipients of U.S. defense exports recognize that offenses against arms export control laws and regulations are prejudicial to security and foreign policy interests they share with the U.S., and accept the need for international cooperation in the administration and enforcement of arms export control laws. In the vast majority of cases, U.S. inquiries of host governments are responded to fully and promptly. An audit of the program by the State Department's Office of the Inspector General completed in September 1996 found that the Blue Lantern program "is working as intended" in terms of successfully averting the diversion of munitions exports and heightening the awareness of defense export control issues among foreign officials.

#### BLUE LANTERN ACTIVITIES IN 1996

471 cases were subject to Blue Lantern end-use verification in CY-96, compared to the CY-95 total of 462 cases. The regional breakdown of the 471 cases is as follows:



Thirty-one cases subject to Blue Lantern end-use verification in CY-96 received unfavorable responses, representing about six percent of cases subject to verification, a figure within the

norm, which runs typically 5-10 percent. In these cases, concerns about possible diversions are reinforced, and action is taken to deny or revoke authorizations. The regional breakdown of the 31 licenses where concerns were corroborated is as follows:

Africa	2	Europe	12
Latin America	12	Near East	4
East Asia	0	South Asia	1

#### DOMESTIC MONITORING: STATE - USCS COOPERATION

In addition, State's Office of Defense Trade Controls and the U.S. Customs Service (which does enforcement work relating to criminal violations of the FAA and AECA on behalf of the State Department) have a cooperative program in which all licensing data for commercial arms sales are communicated electronically on a daily basis to Customs officials at airports and seaports throughout the United States, permitting accurate, real-time monitoring by U.S. Customs officials of commercial arms moving in and out of the United States. Through the U.S. Customs Service's Operation Exodus the Office of Defense Trade Controls also provides authoritative opinions on a daily basis to U.S. Customs officials throughout the United States concerning the licensing and other regulatory requirements of defense articles detained or seized by the U.S. Customs Service at ports of exit owing to suspicious factors or other irregularities.

In fiscal year 1996, these cooperative programs between State and U.S. Customs facilitated more than 300 commercial arms seizures at U.S. ports of exit totaling more than \$40 million, 97 percent of all commodity seizures. Further, 93 criminal arrests for AECA violations by U.S. Customs in fiscal year 1996 led to 86 indictments, of which there were 42 convictions, 2 pleas of nolo contendere, 2 dismissals, and zero acquittals; the remaining cases continue to be prosecuted.

#### MONITORING OF PAST TRANSFERS

A 1991 revision of the defense trade control compliance function included the establishment of a small staff within the Office of Defense Trade Controls primarily devoted to identifying and handling alleged unauthorized retransfers and diversions. This staff, with interagency participation, evaluates information for reliability, prepares reports to the Congress as appropriate, initiates consultations with other countries involved,

recommends other steps necessary to stop the violation or prevent a recurrence, and backstops bilateral discussions on these matters involving higher level State officials and foreign governments. With rare exceptions (e.g., cases such as those where intelligence sources may be implicated), U.S. diplomatic posts are directed to deliver formal demarches and conduct checks to the appropriate foreign government concerning a finding that a violation pursuant to the AECA has or may have taken place.

#### ADDITIONAL MEASURES

The Department of Defense's review of the government-to-government programs indicated that controls are already in place that are equivalent to the end-use monitoring standards published in accordance with Section 38(g)(7). A number of adjustments are, however, being undertaken to strengthen the end-use control process:

- Additional guidance to personnel in the field has been published. This guidance focuses on the post-delivery phase of item life, when accountability controls are less structured and less visible from the U.S. perspective.

This included:

- A message and other guidance changes for the security assistance community worldwide, summarizing the background, purpose and new requirements.
- Supplementing existing Blue Lantern standards, which relate primarily to pre-delivery warning flags, with post-delivery standards for all items. These five additional standards are found at Attachment I.
- Clarification of guidance pertaining to mandatory end-use checks, including post check actions and reporting of any indications of misuse for further action.
- Further training is being planned. Controls in government-to-government programs are dependent upon several organizations carrying out responsibilities in a way which leaves no accountability gaps. In order to more systematically keep the parts working properly, a booklet has been published in order to provide the security assistance community with the conceptual framework of end-use monitoring. The booklet also

shows how Blue Lantern and government-to-government monitoring programs interface. In addition to providing an end-use primer for experienced security assistance personnel, the booklet is expected to become the basis for a block of instruction within appropriate courses at the Defense Institute of Security Assistance Management (DISAM). The booklet and other information will also be used to develop articles to be published in the DISAM Journal, the security assistance quarterly magazine.

Moreover, State and Defense plan to continue technical expert-level discussions to determine what end-use monitoring information each agency holds that is mutually relevant and how it can be exchanged in an effective and efficient manner. For example, State has briefed DoD on Blue Lantern procedures and regularly receives from DoD export related information. State and DoD also exchange quarterly reports of Congressional notifications that involve FMS-origin equipment or technical data. Further, DoD closely maintains continuing coordination with State, even after initial State Department approval of an FMS case (as required by law) regarding FMS programs with all offices concerned with arms transfers and export control policy. This activity ensures that basic information used in end-use monitoring of defense exports and transfers is constantly updated. It complements information compiled from law enforcement agencies, the Intelligence Community, open source materials and other data developed or collected by Department of State and Defense offices.

#### END USE MONITORING RESOURCES

To date, provisions of Section 40A of the AECA have been implemented within existing personnel and resources ceilings. End-use monitoring is fully integrated into normal security assistance procedures and licensing of commercial arms sales. As such, end-use monitoring is an inherent part of the duties of State's DTC complement and most DoD personnel associated with security assistance programs.

Attachment  
Additional Department of Defense End-Use Monitoring Standards

ADDITIONAL DEPARTMENT OF DEFENSE END-USE MONITORING STANDARDS

The need for Post Delivery checks is indicated when:

1. There is any indication an Arms Export Control Act (AECA) violation has occurred. These checks are normally confined to the indicated problem, but expand if a larger problem or weakness is found.
2. Substantial defense interaction or other ties are developing with countries whose interests are not compatible with those of the United States. For example, the end-user holds relatively high technology U.S. items and also holds items from, or has defense relationships with, countries (1) not eligible for Foreign Military Sales and other AECA or FAA programs, (2) for which AECA and FAA programs have been suspended for other than financial reasons, or (3) to which exports are proscribed.
3. Significant and unusual political or military upheaval is impending or has occurred. This includes unusual troop and equipment movements which could weaken normal accountability controls.
4. Countries unfriendly to the U.S. in the region are illicitly seeking U.S. equipment or support items of the types held by the end user.
5. Substantial problems or weaknesses are found during a General Security of Military Information Agreement (GSOMIA) security survey.