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**U.S. WEAPONS TECHNOLOGY AT RISK:
THE STATE DEPARTMENT'S PROPOSAL
TO RELAX ARMS EXPORT CONTROLS TO
OTHER COUNTRIES**

MAY 1, 2004

REPORT

OF THE

COMMITTEE ON INTERNATIONAL
RELATIONS

OF THE

UNITED STATES
HOUSE OF REPRESENTATIVES

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Congress of the United States

Washington, DC 20515

May 1, 2004

LETTER OF TRANSMITTAL

The Honorable J. Dennis Hastert
Speaker of the House of Representatives
H-232, The Capitol
Washington, D.C. 20515

Dear Mr. Speaker:

We transmit, herewith, a report of the Committee on International Relations, which has been endorsed by the Chairman of the Committee on Armed Services, concerning the Department of State's proposal to enact a new law that would suspend the U.S. Government's system of prior scrutiny and control over weapons technology exported through commercial shipping channels from the United States to private companies in the United Kingdom and Australia. We find this proposal, as currently contemplated, to be fundamentally inconsistent with U.S. security interests in the post-September 11th security environment, where the risks and consequences of weapons falling into dangerous hands have increased, not decreased.

Distinguished House colleagues in the 106th and 107th Congresses who examined previous versions of this proposal, prior to the attacks of September 11, 2001, found that it should be approached with an abundance of caution and skepticism due to the inherent risks (and a recent history involving Canada) of unlicensed U.S. weapons technology being diverted to criminal enterprises operating on behalf of state sponsors of international terrorism. The current proposal from the State Department does not mitigate those concerns, but renders them even more acute. The weapons to be deregulated are not, as has been represented, those of "low sensitivity," but involve many lethal items, including terrorist weapons of choice. It would be most unwise, in the name of an initiative launched by the previous administration (before 9/11) to liberalize weapons exports, for the United States to now assume additional and unnecessary risks to our security in the midst of a war on terrorism.

We are persuaded that this is a moment in our Nation's history to strengthen, not relax, export controls over all weapons technology – not only weapons of mass destruction (the ultimate weapons which terrorists seek), but also conventional weapons and munitions, which our enemies are already using against our civilians and U.S. servicemen and women. Indeed, a policy to relax weapons export controls seems unhinged from U.S. counterterrorism and non-proliferation policy. The United States needs to provide international leadership with our friends and allies in the war on terrorism in an effort to strengthen, not weaken, export controls in these areas.

The Honorable J. Dennis Hastert
May 20, 2004
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We continue to hope that the State Department will modify its approach to these matters to meet the national security concerns we have identified. Thank you for your immediate consideration of our report.


Sincerely,



HENRY J. HYDE
Chairman
Committee on International Relations



TOM LANTOS
Ranking Democratic Member
Committee on International Relations



DUNCAN HUNTER
Chairman
Committee on Armed Services

Introduction

This report examines the major issues and implications for U.S. national security and foreign policy in the post 9/11 security environment of the Department of State's proposal to enact a new United States law, which would permit private persons in the United States to export weapons and other defense commodities to companies in the United Kingdom and Australia, without first: (1) receiving a U.S. Government munitions export license, and (2) undergoing the scrutiny and vetting of all involved parties—steps (along with others) that otherwise precede the commercial export of weapons technology from the United States through the export license application process in accordance with the Arms Export Control Act. The State Department proposes that a new law be enacted because arrangements it negotiated with the United Kingdom and Australia pursuant to an export control “reform” initiative of the previous administration do not meet the requirements of existing United States law governing establishment of such an exemption. These requirements are found in sections 38(f)(2) and (j) of the Arms Export Control Act (22 U.S.C. §2778(f)(2) and (j)). They were established by section 102(a) of the Security Assistance Act of 2000 (Public Law 106–280). Under State's proposal, the Executive Branch would be given authority in a new law to waive these requirements and then proceed to establish an exemption in regulation.

The State Department initially proposed new legislation in the first session of the 108th Congress in connection with consideration by the Committee on International Relations of the State Department Authorization Act for Fiscal Years 2004–2005. At that time (April 2003), State explained the problem with Public Law 106–280 was that it required commitments by other countries that were “too strict or specific.”¹ In State's analysis, it would be better for Congress to enact a new law that would permit the Executive Branch to waive any requirements in section 38(j) that would encroach upon giving State “latitude to conclude the best agreements that are achievable and that represent in its judgment sufficient significant improvements in a country's . . . regime so as to justify an exemption.” State's proposal is not limited to the UK and Australia, but is potentially applicable to any country.

However, the Committee deferred action on State's proposal. Chairman Hyde wrote to Secretary Powell on May 5, 2003, explaining why: “any change in law such as that proposed in the Department's draft legislation should only be undertaken, if at all, following careful consideration by the Congress of all relevant facts, including a full understanding of the details of the negotiations to

¹April 1, 2003, Department of State Sectional Analysis, Sec. 603, p. 19.

date, and how the Administration might use any changes in law to establish more exemptions, in addition to what is contemplated for Australia and the United Kingdom.”² Accordingly, the Chairman’s letter requested that the Department furnish the Committee with copies of the arrangements that had been negotiated and other documentation needed to form an opinion about the State proposal.

In making this request, Chairman Hyde also expressed support for deepening defense cooperation with “two of our closest allies” and explained that the Committee would consider other appropriate ways to facilitate bilateral cooperation when taking up the State authorization bill, without prejudice to the possible eventual enactment of changes in law that would permit the exemptions following careful study. Chairman Hyde and Ranking Member Lantos subsequently sponsored legislation (H.R. 1950), since passed by the House, containing a provision (section 1204) that would require “fast track” munitions licensing at the State Department for commercial defense trade with the UK and Australia on the grounds that our closest coalition partners in the war on terror should be accorded the highest priority in our export licensing process. State “strongly” opposed fast track licensing for the UK and Australia as unnecessary, noting that it was already processing license applications for the two countries in under 10 days. But the Committee’s analysis of licensing data subsequently made available by State suggests that hundreds of licenses for the UK and Australia were not processed in under 10 days, and that the provisions of section 1204 are quite necessary.³

By the same measure, Chairman Hyde’s letter also underlined the Committee’s growing concern with the apparent trend towards relaxation of controls over munitions and other arms-related exports, describing this trend as one “that seems unwise and particularly incongruous with the increased threats to U.S. security and foreign policy interests since the attacks of September 11, 2001.”

This report draws on the documentation provided by State in response to the Chairman’s May 5th letter and to a subsequent letter dated June 25th, in which a number of questions were presented concerning various matters affected by the proposed arrangements. The report also draws on the legislative history related to the Security Assistance Act of 2000, relevant communications between Congress and the Executive Branch associated with that Act, and other documents in the public domain.

The State Department has provided considerable—but not all—information requested by the Chairman as of the time of final preparation of this report. Certain information that is essential to a full understanding by Congress of the country exemption issue has not been forthcoming. In particular, State has not provided the description first requested in the Chairman’s May 5th letter of how the

²This concern continued throughout the first session of the 108th Congress as State repeatedly declined to rule-out establishing exemptions for other countries.

³For example, in fiscal year 2002, approximately 850 export license applications for the UK and Australia, which involved weapons categories that have long been eligible for license-free export to Canadian industry, were inexplicably referred by State to DoD for a national security review after evaluation of the application and vetting of the involved parties, but before approving the license. Such referrals typically add a minimum of 4 weeks to the license process. As surprising, more than 60 percent of the nearly 850 cases were only approved with provisos (i.e., specific conditions or limitations to which the license is subject), though the same exports to Canadian industry would contain no such provisos (there being no license in the first place).

requirements of section 38(f)(2)(B) will be met, with respect to a determination required by the Attorney General regarding the ability of the United States to detect, prevent and prosecute criminal violations of the Arms Export Control Act, including efforts linked to international terrorism. The Department responded to some questions raised by the Chairman in his June 25th letter related to law enforcement interests and to the scope of the UK and Australian munitions lists only in the final days and weeks of the first session of the 108th Congress, though it indicated that this information would be forthcoming at an earlier date. The Committee has received excellent cooperation from the British and Australian Embassies in Washington for which it is grateful.

The analysis of issues and implications of State's proposal contained in this report is not an explication of all such matters, but only those that are of a fundamental character with respect to United States interests.

Summary of Findings

- There are inherently greater risks of diversion associated with unlicensed commercial exports of U.S. weapons and other defense commodities, as manifest in the 1999 review of the Canada exemption.⁴ Congress highlighted these risks to the Executive Branch well before the terrorist attacks on New York and Washington of September 11, 2001. Congress also expressly cautioned against using the authority provided in the Security Assistance Act of 2000 to negotiate "Canada-like" exemptions with the United Kingdom and Australia because of the additional risks associated with commercial air and sea cargo transported over much longer routes to those countries. These repeated cautions, however, have gone unheeded.
- The risks of diversion—and their potential consequences—have increased (not decreased) since the attacks of September 11th, as the global war on terrorism continues across a variety of fronts. Criminal investigations by U.S. law enforcement agencies since September 11th provide compelling evidence of these risks, as well as vivid, contemporary reminders that our closest allies are as susceptible as the United States (and probably more so) to illegal arms activities that threaten our mutual security and foreign policy interests.⁵
- By eliminating on the U.S. side nearly all critical elements of prior U.S. Government scrutiny and control that would otherwise

⁴In April 1999, the U.S. Government suspended in part a similar exemption for Canada after front companies in Canada operating in the interests of Iran, Libya, Sudan, the People's Republic of China and other U.S. embargoed countries had extensively exploited the liberal regulatory environment to acquire U.S. weapons technology. The Canada exemption and the weapons diverted are discussed later in this report. For a fuller review of the specific enforcement cases identified publicly in 1999, see also Appendix II to GAO's Report (GAO-02-63), "Summary of Enforcement Cases That Supported Need for Change in the Canadian Exemption."

⁵For example, the December 2003 indictment in U.S. District Court of a UK national arrested in Newark last summer by the FBI Joint Terrorism Task Force on charges related to the sale of shoulder fired missiles to terrorists in order to shoot down commercial airliners, and the July 2003 announcement by the Department of Homeland Security of search warrants executed in ten U.S. states relating to a probe into a front company headquartered in London which procures arms for Iran. In addition, the State Department's own reports to Congress since 9/11 dealing with end use monitoring of U.S. weapons technology exported abroad have also emphasized an increase in suspicious arms activity in Europe.

precede the export of weapons and defense commodities from the United States, the arrangements negotiated by the Department of State will almost surely enlarge these risks. State's approach would suspend the statutory framework that requires the identification of all parties (the applicant, the freight forwarders, the intermediate consignees and the end user) on a license application for the purpose of preventing the involvement of ineligible, unreliable or suspect persons, in favor of a "one-time" vetting of only the end user. U.S. law has long provided for the vetting of *all* parties precisely because illegal traffic in arms is a complex criminal enterprise in which a single diversion may involve an array of brokers, middlemen, banks, transportation companies and transshipment points—as most recently reflected in the shadowy network reportedly utilized for illegal shipments of nuclear materials and equipment by A.Q. Khan, which remained undetected for many years. While State contends the United States would not give up that much in suspending this framework because "not all" unscrupulous middlemen are on its computerized watch list, the Committee does not share this sentiment. On the contrary, this line of argument will likely be of little consolation if U.S. weapons are diverted through the involvement of persons known to be engaged in criminal activities, whose roles were only discovered after the fact because routine computer checks were not conducted.

- The risks of diversion can only partially be mitigated by an effective export control system of a friendly foreign government, even one that is fully "comparable" in effectiveness (as required under current law) to that of the United States (which is not the case here). This is because a foreign government's system generally has operational effect only after U.S. weapons technology shipped commercially has entered its jurisdiction—i.e., near the end of the journey. The risks associated with the particular arrangements State has negotiated may be further accentuated by: (1) the apparent absence of transshipment controls in the UK for most conventional weapons technology;⁶ and (2) State's apparent failure to consider the possible effects of a broad exemption on targeting and screening of weapons exports by Homeland Security personnel at U.S. ports of exit in the post-9/11 environment (where U.S. border personnel are already fully engaged in stepped-up efforts to prevent the *entry* of dangerous goods).⁷ While U.S. border officials have worked effectively since 9/11 to

⁶A license is not required for the majority of transshipments through the UK from one country to another. Most other transshipments can be made under one of the Open General Transshipment Licenses. Open General Licenses allow the export of many controlled goods by any exporter, removing the need for exporters to submit a license application provided various conditions are met (e.g., no WMD, the country is not subject to an EU arms embargo, etc.). See the Guidelines for an Open General Transshipment License at the UK Department of Trade and Industry Internet site: www.dti.gov.uk/export.control/ogelicences.htm

⁷On November 17, 2003, the Department of Homeland Security informed the Committee that, depending on the volume of exempt military cargo, the proposed exemptions could "increase or significantly increase the workloads and require additional inspectors. To automate the processing of electronic export information via the Automated Export System (AES), programming changes and funding . . . will be required." In the same letter, DHS advised that State still has not updated its guidance to Customs concerning inspections of license free weapons exports along the Canadian border as recommended by GAO in its March 29, 2002 report entitled "Lessons to Be Learned from the Country Export Exemption." (GAO-02-63).

close the “front door” to imports of dangerous items, State’s proposal would open the “back door” for export of such items.

- The unlicensed exports that would be susceptible to increased risk of diversion are *not*, as has been repeatedly described by the State Department, merely those of “low sensitivity,” but comprise an impressive array of lethal munitions, including shoulder-fired missiles, bombs, military explosives, operational flight trainers, body armor, and other articles which would figure prominently (and in some cases already have) in the illegal acquisition plans of foreign terrorist organizations, state sponsors of international terrorism, or their brokers. State’s proposal to relax export controls over such terrorist weapons of choice seems incongruous with increased threats to U.S. security in the post-9/11 environment and reinforces the perception that State’s arms export control policy has become unhinged from U.S. counter-terrorism and non-proliferation policy as a consequence of its singular focus on export control “reform”. This policy emphasis is also inconsistent with initiatives undertaken by President Bush to tighten controls, including the Container Security Initiative, the Proliferation Security Initiative and, the “STAR” (“Secure Trade in the APEC Region) initiative, which calls for strict—not relaxed—export controls on items such as shoulder-fired missiles (or “MANPADS”⁸). Other U.S. weapons technology that would be exempt from export licensing include many items having substantial combat utility, and numerous others which, at higher performance levels, are specified on the Militarily Critical Technologies List (“MTCL”) because of their importance to maintaining war fighting superiority for U.S. forces. While State’s proposal would exclude from the exemption some weapons that might present a technological challenge to U.S. armed forces on the battlefield, a conventional battlefield (as noted by the Chairman and the Ranking Member in a recent letter to the Secretary of State) is not where and how our enemies in the war on terror are waging their attacks against the United States and our coalition partners.⁹
- The proposed arrangements fall far short of the laudable goals established by Secretary Cohen in the previous administration of using country exemptions to negotiate “ironclad” arrangements covering key areas of military export controls, such as re-transfers and end use, in order to provide a “dramatic increase in our global technological security.”¹⁰ In fact, the texts State negotiated with the UK and Australia do not contain *any* commitment by either government to seek the prior written consent of the U.S. Government before it re-exports to another country weapons technology it has received from the United States. The decision by the UK not to agree to the U.S. Government’s right to consent to re-transfers and changes in use of U.S. weapons, but only to give “fullest weight” to such interests—and to relegate this fundamental U.S. interest to a civil contractual arrangement between the UK and its firms that is mainly enforce-

⁸ Man Portable Air Defense Systems.

⁹ See Appendix 15.

¹⁰ Letter dated June 18, 2000, from Secretary Cohen to Chairman Gilman, Committee on International Relations (see appendix to this report)

able under English common law—is not only disappointing, but potentially highly prejudicial to United States interests around the world, should this be seen as a precedent for other governments to downplay the U.S. Government’s consent rights. It is difficult to understand the UK position (and the State Department’s acceptance of this proposed outcome) in light of a well-publicized defense cooperation treaty the UK recently ratified, which accords to its European partners essentially the same right of prior written consent for their “commercially” sensitive information that was withheld from the United States (apparently on grounds of “extraterritoriality”) for U.S. Government controlled national security information.¹¹

- Expanded cooperation with both countries in law enforcement matters is desirable and helpful, if fully implemented (particularly inasmuch as there have been few successful prosecutions in the United States of arms export control violations in circumstances where no export license was required). But, in the case of the UK, this cooperation appears to be mainly discretionary, since many areas will not involve dual criminality (a predicate for “required” cooperation under the arrangement), but will come under the aegis of the civil contractual arrangement, noted above. Persons who may willfully violate the civil contract for the most part will not be subject to the sanctions of a UK criminal court, but face only prospects of a civil fine. Even assuming full cooperation by UK authorities, this effort is generally directed to detecting violations *after* they have occurred, rather than preventing them in the first place. U.S. arms export control policy would undergo a fundamental shift away from the “prevention” of unauthorized exports and towards greater dependency on the cooperation of foreign governments to obtain and provide evidence needed to support successful prosecutions. As the Department of Justice predicted in commenting on country exemptions well before 9/11, “our first line of defense against diversions would be moved across the oceans to England and Australia.”¹²
- The UK system, despite a partial closing of gaps in some areas (e.g., brokering and “intangible” transfers, in part), will generally *not* be comparable to the comprehensive system deployed by the United States (other than in the area of weapons of mass destruction and other limited areas), but will remain a “targeted” system. Instead, the UK system for military export controls will more closely resemble the U.S. Department of Commerce’s system for dual use export controls (except that the U.S. dual use system controls intra-U.S. transfers of technology to foreign nationals, while the UK system will not). Even in those areas where the UK is extending coverage of its system (e.g., brokering, “intangible” exports), continued reliance on “open” licenses (self-validating by the exporter) will be the hallmark. The

¹¹ See article 52 of the Framework Agreement Between the UK, France, Germany, Italy, Spain and Sweden concerning Measures to Facilitate the Restructuring and Operation of the European Defence Industry. Done at Farnborough, UK July 27, 2000; entered into force April 18, 2001.

¹² Letter dated April 27, 2000, from Deputy Assistant Attorney General Swartz, Criminal Division, Department of Justice to Senior Adviser Holum, Department of State. The text of this letter was made publicly available by the Center for Strategic and International Studies on its Internet site. www.csis.org/export/ltrholum.htm

UK is implementing certain changes to its system in response to the recommendations of Lord Scott's inquiry into the sale of UK defense technology to Iraq prior to the first Gulf War, and consistent with commitments it made in the G-8 and European Union. But, the UK also appears to have decided that it would not make other changes to its laws or regulations in order to ensure that the U.S.-UK arrangement in this area was compliant with U.S. law. Australia's future export control system is still being debated internally. Little is known about its details. State advises there are certain areas Australia does not plan to control in order to meet requirements of U.S. law, but others where it may be willing to, provided the U.S. Government changes its law so that an exemption could be granted. Moreover, while seeking expansive authority to waive most requirements in existing U.S. law, State appears to misconstrue other requirements in U.S. law in order to assert "comparability" for both the UK and Australian exemptions.¹³

- It is clear that the United States offer of a country exemption has not provided a "powerful incentive" (the stated rationale for the exemption policy) for these countries to strengthen their military export control systems to a level comparable to that of the United States.¹⁴ This development impeaches the original justification for the exemption policy. Yet, neither this development nor others, including the global war on terror, has prompted any serious re-examination to date of State's policy in this area. State's posture of declining to rule-out additional exemptions for other countries suggests that the inter-agency export control bureaucracy remains fundamentally fixated on a policy that began before 9/11 of liberalizing commercial weapons exports in response to globalization. The so-called "bargain" conceived in the previous administration by which the United States would relax its military export controls in most areas as an inducement for other governments to raise their controls has, in fact, not worked out according to plan. In the post 9/11 international security environment, it is reasonable to question why State feels our friends and allies require "incentives" from the United States to close gaps in their controls over weapons technology, and whether it is wise for the United States to continue a policy of weakening and bargaining away its military export controls in exchange for incremental changes in other countries' controls.
- By failing to heed Congress' admonition not to negotiate "Canada-like" agreements, the State Department appears to have fashioned arrangements that are high on risk and low on tan-

¹³For example, there is no obvious reading of the requirement in section 38(j)(2)(A)(iv) requiring "establishment of a list of controlled defense items to ensure coverage of those items to be exported under the exemption" that would permit the conclusion that coverage of a U.S. Munitions List item exported under the exemption could be achieved if the item is *not* on the foreign government's list of controlled *defense* items. Yet, in the proposed exemption arrangements with the UK and Australia, State seems to assume this requirement is met in some cases (specified in the UK agreement, but unspecified in the Australia agreement) if the U.S. Munitions List item is on the foreign government's list of controlled *dual-use* items.

¹⁴June 28, 2000, Letter from Secretary Cohen to Chairman Gilman.

gible benefits, both to the United States and our closest allies.¹⁵ References to improved interoperability and coalition war fighting as a result of the license exemptions seem to be essentially rhetorical, and not demonstrable. In the final analysis, the commodities that would be shipped license-free are as easily—and more securely—acquired by the UK and Australia through issuance of a munitions export license to U.S. suppliers in a time frame that varies (according to relative urgency) from 24–48 hours at one end, to less than 10 calendar days for routine transfers.¹⁶

- While State continues to oppose provisions in H.R. 1950 (passed by the House in the first session of the 108th Congress) that would establish rapid export license processing for the UK and Australia, it inexplicably referred approximately 850 arms export license applications for the UK and Australia to the Department of Defense for national security review during fiscal year 2002 involving weapons categories that would not even require a license if an exemption were established. Such referrals typically involve much longer processing times of 4 to 6 weeks (8 days versus 48 days according to State’s published timelines for fiscal year 2003). It is not easy to understand why 850 weapons technology exports available to Canadian industry for many years without any U.S. Government review, still require lengthy inter-agency review on national security grounds before being made available to our closest allies in the war on terror. Nor is it easy to understand why 60 percent of those exports that were ultimately approved to the UK and Australia contained specific conditions or limitations on the licenses (while exports of the same weapons commodities to Canada involve no such conditions or limitations).¹⁷ Because State’s conflicted position in this matter impedes legitimate exports by U.S. firms, and presents the UK and Australia with a Hobson’s choice between no license and one that takes 48 days to obtain, it is little wonder that both strongly favor the first of these options.
- The Committee is well aware of pressure mounted on State in recent years by our European allies to make the U.S. arms export control system less restrictive in order to help them fulfill the defense and foreign policy commitments of the European Union (EU) and the North Atlantic Treaty Organization (NATO), which they are having difficulty meeting because of flat (or declining) national military budgets.¹⁸ Reflecting its strong bias towards deepening trans-Atlantic defense cooperation by appropriate means, this Committee has repeatedly urged greater prioritization and expedition in licensing exports to NATO allies

¹⁵It is notable that there is essentially no reciprocity in either bilateral agreement: The U.S. exemption would be unilateral in nature. Both Australia and the UK would continue to maintain existing license requirements on their own military exports to the United States.

¹⁶About 70 percent of all U.S. munitions export license applications are currently processed within this 10 calendar day window as a direct result of additional funding and personnel resources Congress provided to State (which did not request these increases) in FY 1999. By comparison, the UK’s target is to process 70 percent of its munitions cases within a 20 working day period.

¹⁷See the discussion of licensing data for FY 2002, annexed to the July 25, 2002, letter from Assistant Secretary Kelly to Chairman Hyde.

¹⁸The same pressure produced the DTSI policy in the previous administration, of which the proposal to exempt countries from U.S. export license requirements is one component.

and our coalition partners, and has provided State all of the resources it needs to do this. The Committee has also been flexible in approving major cooperative projects in recent years in the face of serious questions about the efficacy of our partners' controls. One example is the Joint Strike Fighter program, where the chief medium for export is by computer network, notwithstanding the absence of laws in most partner countries that would provide full protection for such exports. At the same time, it is perfectly reasonable for the United States to want our European allies to: (1) strengthen their arms export controls consistent with the increasingly advanced level of technology being shared with them; and, (2) respect those U.S. requirements (such as prior written consent to third party transfers) that are fundamental under our laws. Unfortunately, below the rhetorical level, the Committee sees little evidence of a serious effort by State to engage our European allies on these important questions. Instead, all indications suggest an unwavering policy to relax U.S. controls in order to establish commonality with European standards—an approach which the Committee finds unwise, as well as inexplicable, in the context of the global war on terrorism.

- The agreements would cover most unclassified exports to the two countries (as described by State), which effectively means the elimination of U.S. Government licensing for up to 20 percent (measured in value) of all U.S. weapons technology currently licensed for export on an annual basis.¹⁹ This would appear to be the single largest deregulatory measure related to armaments involving any country in modern history. It is not obvious to the Committee why it is appropriate for the United States to seek such a distinction at this time in our Nation's history. Given the fiercely competitive nature of the international arms market in which the United States currently holds the largest share, the possibility that other governments might view such a relaxation of controls by the United States as commercially motivated, and as providing a pretext for relaxation of control over their sensitive exports must also be taken into consideration. Similarly, having appropriated substantial funds over the past decade on a bipartisan basis for export control related assistance to other countries so they might strengthen their export control systems, it is reasonable for Congress to consider the apparent contradiction between U.S. exhortations and assistance to other countries to strengthen their weapons export controls and State's proposal to relax U.S. controls.
- Importantly, the United States may be squandering a unique opportunity to establish significant bilateral agreements with our closest military allies, which not only set a high standard for other countries to follow (a goal which seems axiomatic in the context of the war on terror), but which also provide a more appropriate framework for bilateral defense cooperation with these countries. That cooperation is increasingly focused, not on the list of commodities contained in the Canada exempt list, but on

¹⁹If extended to all NATO countries as originally envisaged by State (a position which State explicitly preserves by declining to exclude other country exemptions), unlicensed U.S. weapons exports could approach \$8–10 billion per annum or 60–70 percent (by value) of all commercial weapons exports from the United States.

defense services related to cooperative research projects in high priority areas, such as missile defense.²⁰

- The Congress' options are increasingly constrained by the failure of the Department of State to keep it informed of the actual details of the agreements at an earlier date—including its decision to pursue a substantially different approach than authorized under U.S. law²¹—and by the now well-established perception in London and Canberra that conclusion of the agreements, whatever their shortcomings, has become symbolically important to their relations with the United States. Instead of putting these negotiations on hold in order to consult with Congress when it became clear the UK and Australia could not meet U.S. legal requirements, the Department apparently decided to wrap up the negotiations and present Congress publicly with the requirement for a new law which, if enacted, would jeopardize U.S. interests, but which if not enacted would disappoint our closest allies.
- This report, however, stops short of recommending possible legislative approaches to correct numerous infirmities in State's proposal and merely distills those issues that appear to merit consideration by Congress in deciding whether, and if so how, to fashion a new law that would authorize an exemption. An underlying question prompted at almost every juncture in the State proposal is whether, in the name of an initiative launched in the previous administration to liberalize arms export controls before 9/11, the United States should now, in the midst of the war on terror, assume additional risks, particularly when it is clear that the weapons involved can be as quickly and more securely provided by accelerated licensing procedures that give top priority to our closest allies in the war on terror.

Background

Purpose of U.S. Military Export Controls

The central purpose for U.S. Government control over the export of weapons and defense commodities by private firms is to help ensure that such items, when transferred abroad for use by our friends and allies, do not fall into dangerous hands, either during the course of the original shipment or, thereafter, through subsequent re-transfers or use involving third parties, including third countries (for which third party transfer or use U.S. Government consent is required). The principal means for carrying out this control is the munitions export license system, a relatively stringent (by but no means foolproof) system of prior scrutiny and safeguards

²⁰U.S. defense services exported to the UK in FY 2002 outpaced defense commodities by a factor of nearly 3:1: \$6.6 billion versus \$2.5 billion, reflecting a trend that has dominated U.S. defense trade since the early 1990s.

²¹The State Department acknowledges that it decided to pursue a "different" approach in the case of the UK. That approach for all intents and purposes implied a radical revision of the country exemption policy of offering an exemption only where there was a legally binding international agreement incorporating a foreign government's commitment to change its national laws and regulations where needed to provide controls comparable in scope and effectiveness to the U.S. Government's controls over *all* exports. The "different" approach would be to offer the exemption in exchange for a commitment merely to give "full weight" to U.S. views (but not to obtain U.S. approval)—and this watered commitment could take other forms (e.g. political, civil), and be mainly limited in applicability to "exempt" (not all) items.

whose most significant features are mandated by law in various provisions of the Arms Export Control Act. The system is comprehensive in scope and in application; it includes case-by-case processing of license applications for all items on the U.S. Munitions List that are intended for export to any destination. This permits the U.S. Government to pursue its global interests in ways that protect not only the most advanced military systems critical to assuring U.S. combat superiority, but also to control the supply of spare parts and components in support of U.S. unilateral sanctions and UN Security Council arms embargoes, as well as other U.S. security and foreign policy interests, including nonproliferation and regional security interests, around the world.

Globalization

Globalization of the defense industry provided an overall context for the DTSI initiatives and the country exemption proposal, in particular. Several related factors had combined during the mid to late 1990s to prompt increasing criticism from U.S. and European aerospace companies that the munitions export license process had become an impediment to legitimate transatlantic defense trade. This criticism was levied with increasing frequency after the investigations into illegal technology transfer to China's space launch program, the publication of the House Select Committee's Report ("Cox-Dicks"), and the legislatively mandated return of communications satellite exports from Commerce to State licensing jurisdiction.²²

License processing times were said by industry to be unacceptably high, and the Department of Defense identified a list of cases that it said validated industry concerns.²³ The nature of U.S. defense trade had also begun to change following the end of the Cold War, with a shift away from the supply of finished military products to European allies and towards increasing emphasis on collaborative research and joint ventures, which emphasized technology transfer (including through industrial offset arrangements) and industry work share. This trend was fueled in part by a decline in military budgets across Europe (or in some cases maintenance of military budgets at very low levels in order to fund commercial R&D), and a shake out in European defense and aerospace industry, which became increasingly concentrated in a smaller number of large trans-European companies, formed in part in order to compete with the major U.S. defense firms. Congress responded

²² European aerospace interests were directly affected by these U.S. developments on two levels. First, European companies had also participated in the Chinese launch failure investigations along with U.S. counterparts, though not in apparent violation of their own government's export control laws which, unlike the United States, generally do not control the conduct of their nationals in providing technical assistance to space launch vehicle (SLV) programs. Second, the transfer of satellite jurisdiction to U.S. Munitions List control was viewed as incompatible with the more liberal control philosophy for communications satellites and foreign SLV programs in Europe—and a potentially serious impediment both to continued European interest in space technology cooperation with China (not only in communications satellites, but also in other areas such as global positioning satellites) and to trans-Atlantic cooperation in the satellite industry.

²³ Congress requested the General Accounting Office to establish the true facts about these criticisms and a subsequent audit and report by GAO found that license processing times at State actually were similar to Commerce's dual-use license system, and that DoD had exaggerated problems related to the cases on its list, while that list, itself, was actually provided to DoD by a local trade association of aerospace companies. See GAO 01-528 ("Export Controls: State and Commerce Department Licensing Times are Similar").

to these concerns by effectively doubling the resources available to the State Department office charged with the licensing duties in order to accelerate processing of legitimate arms transfers (though no such funds had ever been requested by State for this purpose).

Early Congressional Opposition to “Country Exemptions”

The proposal to establish “country” exemptions was one in a series of initiatives (referred to as the Defense Trade Security Initiative or “DTSI”) announced by the Clinton Administration in May 2000 by Secretary Albright at a meeting of NATO foreign ministers. The proposal envisaged the elimination of U.S. Government export licenses for most commercial arms transfers to Australia and any member country of NATO (later expanded to include Sweden) provided that the country enhanced its national export control system such that it was comparable in scope and effectiveness to that of the United States. Congress welcomed many of the DTSI initiatives (a number of which reflected ideas it had previously urged in order to expedite licenses for legitimate defense trade with U.S. allies), but expressed serious reservations about country exemptions. Even prior to the May 2000 announcement, the Chairmen and Ranking Members of the Senate Committee on Foreign Relations and the House Committee on International Relations wrote to Secretary Albright on March 16, 2000, to “make clear (their) adamant opposition.”

“We believe that the AECA provides the appropriate structure under which the United States should continue to advance our foreign policy, national security and nonproliferation interests. State Department regulations and practice in implementing U.S. munitions laws, including the AECA, have long provided for individual, case-by-case licenses for defense exports. Yet, we understand that proposed exemptions, if extended as planned for NATO and other non-NATO allies, would exempt about 80 percent of commercial defense trade from licensing. Such exemptions are fundamentally inconsistent with the licensing scheme required by the AECA, and the legislative intent underlying the same.”²⁴

At the heart of Congressional opposition—even prior to 9/11—were concerns that such proposals “not result in additional diversions of technology” and “not weaken, generally, enforcement of export controls and, specifically, the ability of the United States to prosecute and extradite persons that violate U.S. export control laws.”²⁵ Twelve months earlier, in April 1999, State had suspended operation of a similar exemption for Canada in the face of a series of cases demonstrating that the liberalized export control arrangement for that country had been readily—and pervasively—exploited by front companies and illicit arms dealers operating in the interests of state sponsors of international terrorism and other governments prohibited by U.S. law from receiving U.S. weapons and defense commodities (e.g., Iran, Iraq, Libya, Sudan and the Peo-

²⁴ Letter dated March 16, 2000, from Chairmen Helms and Gilman and Ranking Members Biden and Gejdenson.

²⁵ *Ibid.*

ple's Republic of China). Some of these conspiracies were successfully intercepted; others were not.

Department of Justice Concerns

Unknown to Congress at that time, its doubts about the wisdom of the country exemption initiative were being echoed in even stronger terms by the Department of Justice. An April 27, 2000, letter from the Criminal Division to the State Department expressed concern about the proposal and noted that "it will facilitate efforts on the part of counties and factions engaged in international terrorism to illicitly acquire sophisticated U.S. weaponry." The letter warned:

"[W]e are concerned that the exemption will prompt foreign terrorist groups and other potential adversaries to set up storefronts in England and Australia in order to take advantage of the relaxed export control requirements. We have seen this happen in Canada, a country already exempt from most U.S. export license requirements. England and Australia are not contiguous with the United States and likely would be viewed by hostile elements as being even more attractive locations from which to stage an illicit procurement effort."²⁶

The DTISI Proposal

Despite Justice Department concerns (and others reportedly held by the Secretary of State), the previous administration decided to proceed with the country exemption proposal as part of its DTISI Initiative in May 2000. In the run up to the NATO meeting in which the initiative was announced, Secretary Cohen elaborated on the rationale for the proposal:

". . . Negotiation of a 'Canadian-like ITAR exemption' with the UK and Australia . . . will expand the consensus (on technology control and, in particular, on third-party transfers) with these key allies . . . create incentives for other countries to also improve their export controls, and allow us to redirect resources from low-risk to high-risk transfers. . . . In fact, the proposal would require legally binding agreements with the UK and Australia on tight third party retransfer controls and closure of other gaps. This strengthened retransfer control would extend to UK and Australian end-users for all US Munitions List items, not only items entering the UK and Australia under the proposed exemption. Our proposal would dramatically improve our control of third party re-transfers, further enhancing national security."²⁷

The Security Assistance Act of 2000

Congress eventually authorized the negotiation of the proposed agreements when enacting the Security Assistance Act of 2000, while setting forth specific criteria that would have to be met and duly reflected in the international agreements, as well as changes, where needed, in national export control laws and regulations in

²⁶ Letter dated April 27, 2000, from Deputy Assistant Attorney General Swartz to Senior Adviser Holum.

²⁷ Letter dated May 5, 2000, from Secretary Cohen to Secretary Albright.

order to ensure comparability with the U.S. system, and the continued safeguarding of U.S. weapons and defense commodities. These criteria were based on the specific assurances and representations made to Congress by State and other agencies at that time, and were designed specifically to provide a basis in law for the purpose of the exemptions (i.e., “legally binding” agreements on “tight” third party retransfer control for “all” items (not just exempt) in order to “dramatically improve” our control of third party re-transfers, none of which appears to be achieved in State’s negotiated texts). Of particular importance, however, was Congress’ admonition to State and other parts of the administration *not* to pursue negotiations leading to a Canada-like exemption for other countries:

“The Canadian exemption is a unique one. . . . These same considerations do not apply to either the United Kingdom or Australia (to say nothing of other countries). . . . (D)efense commodities being shipped between the United States and Canada are far less susceptible to diversion than items shipped longer distances on cargo vessels which must make multiple port calls before arriving in the final port of destination. Moreover, unlike the case in Canada, many major UK defense companies are now jointly partnered with other European firms.”²⁸

Increased Risks of Weapons Diversion

Exploitation of the Canada Exemption

Gray arms market dealers operating in the interests of rogue governments, criminal organizations and terrorist factions have not disappeared since 9/11, but have become increasingly effective at exploiting weaknesses in export controls by disguising illicit shipments as *bona fide* exports through such techniques as fraudulent documentation, forged end use certificates, establishment of front companies (particularly in the territory of major U.S. partners and along the busiest sea and air routes), and masquerading as legitimate firms using false addresses. The illegal network utilized by A.Q. Khan to conduct clandestine nuclear weapons proliferation typifies a larger problem in international commerce in which weapons technology of all kinds (conventional armaments as well as weapons of mass destruction) may be subjected to various levels of risk.

The 1999 review of the Canadian exemption suggests how pervasive such illegal networks may become in the absence of effective arms export controls. By April of that year, following a mounting number of cases involving violations of the Arms Export Control Act, the Department of State concluded that most state sponsors of international terrorism, illicit arms dealers operating in the interests of such “state sponsors,” and other countries against which the United States maintains arms embargoes had established front companies in Canada for the sole purpose of illegally acquiring U.S. weapons technology. These countries included Iran, Libya, Sudan,

²⁸ See House Report 106–868.

and the People's Republic of China. The U.S. weapons technology involved was extensive, including:

OH-58 Kiowa helicopters; M113 armored personnel carriers; klystron tubes for Hawk missile systems; infrared cameras; infrared detectors; jet engine vanes; fiber optic gyroscopes; gas grenades; projectile guns, military computers, spare parts for armored vehicles; spare parts for F/A-18 and other fighter jets, components for mobile radar systems; and gas turbine engines.

However, not all of the illegal activities were inspired from abroad by illicit front companies. A major U.S. defense firm also had initiated (through a Canadian subsidiary) manufacturing of a military system for Pakistan, a license for which the U.S. Government had denied in view of the sanctions in place on Pakistan at that time. However, the Canadian Government had no similar sanctions. The export from Canada of the system was legal under Canadian law and consistent with Canadian foreign policy at that time—illustrating that even our close allies do not always have the same foreign policy towards different regions and countries, and can sometimes provide a willing venue for military exports of U.S.-origin equipment that the United States does not consider to be in its best interests.

Recent Rise in Illicit Arms Dealers in Europe

What made Canada especially vulnerable to exploitation by illegal arms dealers was not merely its proximity to the United States, but the combination of: (1) the availability in its defense industry of U.S. manufactured components, parts and systems²⁹; and (2) weaknesses in military export control coverage, characterized chiefly by the absence of a U.S. Government export license requirement for most weapons technology exported to Canada.

Furthermore, Canada is by no means the only U.S. ally susceptible to exploitation efforts by illegal arms dealers. Recent reports by the State Department to Congress required under section 655 of the Foreign Assistance Act of 1961 do not indicate abatement, but an upswing, in illegal arms acquisition efforts in the territories of U.S. allies, particularly in Europe. For example, State's report for fiscal year 2001 points out:

“A notable trend revealed by Blue Lantern checks (i.e., State's end use monitoring program for military exports through commercial channels) over the past three years is the incidence of West European based intermediaries involved in suspicious transactions. In FY 2001, 23 percent of unfavorable checks, mostly for export of aircraft spare parts, involved possible transshipments through allied countries. In absolute terms, the number of unfavorable checks involving European based intermediaries increased.”³⁰

²⁹Components, parts and systems manufactured in the U.S. are the first choice for illegal arms dealers, but also present greater difficulties due to the traditional U.S. government emphasis on prevention through case-by-case scrutiny. A close second choice, however, are such items when produced in the territories of U.S. friends and allies under U.S. granted rights (and built to U.S. supplied specifications).

³⁰Recent reports required by section 655 are available from State at www.pmdtc.org.

Post-9/11 Criminal Investigations

Criminal investigations since 9/11 by U.S. law enforcement authorities involving illegal arms activities provide compelling evidence of the risks of diversions of US weapons technology, as well as vivid, contemporary reminders that our closest allies are as susceptible (and probably more so) to illegal arms activities that threaten our mutual foreign policy and security interests. These include:

- The investigation and arrest of a UK national (Mehant *Lakhani*) in August 2003 by the FBI's Joint Terrorism Task Force in Newark (and subsequent indictment in December 2003) on charges that he attempted to broker the sale of shoulder-fired missiles to terrorists who would then use them to shoot down commercial airliners.
- The announcement in 2003 by the Department of Homeland Security of searches conducted in more than ten U.S. states, involving 18 companies, concerning an extensive illegal arms acquisition network reportedly orchestrated from the UK by an Iranian front company (*Multicore, Ltd.*) based in London, which continued to conduct illegal purchases for Iran nearly 3 years after its U.S. subsidiary was shut down by U.S. law enforcement³¹; and
- Numerous other cases highlighted by the Department of Homeland Security's September 2003 report of recent strategic investigations involving conspiracies to divert U.S. weapons technology, including fighter jet components to Iran; components for Hawk missiles, fighter jets and helicopters to the People's Republic of China; aircraft engine components to Libya; howitzer parts, radars, and armored personnel to UAE and Pakistan; unmanned aerial components to Pakistan; MAK-90 assault weapons to Colombian guerillas; radar components to Iran; Hawk missile, TOW missile, AIM-9 Sidewinder missiles, F-4 fighter jet components and F-14 fighter jet components to China; and military encryption devices to China.³²

Weapons and other defense commodities are easier to divert when unlicensed for a variety of reason touched on in this report, but fundamentally because, as summed up earlier this year by the State Department in the sectional analysis it prepared to accompany its proposed amendment to the Security Assistance Act of 2000, such arms exports are "harder to keep track of."³³

³¹In December 2000 U.S. law enforcement filed a criminal complaint against Multicore, Ltd. (the U.S. subsidiary of Multicore, Ltd. UK) in San Diego that led to the conviction of its owner and another individual for illegally transshipping several million dollars worth of components and parts to Iran for F-14, F-4 and F-5 fighter aircraft, as well as for Hawk missile systems.

³²See the Department of Homeland Security, Bureau of Immigration and Customs Enforcement's September 2003 report on recent strategic investigations (appended to this report).

³³Sectional Analysis accompanying Final Administration Approved State Department Authorization Act, Fiscal Years 2004 and 2005. (April 1, 2003).

Nature of the Weapons Technology at Risk

The Department of State has consistently represented that only certain weapons commodities would be permitted for export “license-free” under the exemption, those that are “unclassified” and of “low sensitivity.” The exclusion of classified weapons from the exemption, while appropriate, does not actually serve to limit the application of the exemption to any measurable degree. This is because the number of licenses for classified commodities exported through commercial channels is very small—historically ranging from two to three hundred licenses worldwide on an annual basis (out of approximately 45,000 licenses for all munitions transactions) or .007 percent.

The second criterion used by State—“low sensitivity”—is purely subjective, lacking any definition in the U.S. arms export control system. However, by any reasonable standard, the weapons commodities that would be susceptible to increased risk of diversion are not, as has been described by State, merely those of “low sensitivity”³⁴, but comprise an impressive array of lethal munitions, other items having substantial combat utility, and still other items which, at high performance levels, are specified on the Militarily Critical Technologies List (“MTCL”) because of their importance to maintaining war fighting superiority for U.S. forces.

Many “low sensitivity” items that would be subject to license-free shipments under the State Department’s proposal could be expected to figure prominently (and in some instances are known to have) in the acquisition plans of state sponsors of international terrorism and other countries and groups engaged in illicit arms trafficking, including:

Shoulder fired missiles, patrol vessels, body armor, operational flight trainers, rockets, torpedoes, bombs, mines, military explosives and propellants, amphibious warfare vessels, harbor entrance detection equipment, large caliber ammunition, self-propelled guns, mortars, etc.

The shoulder-fired missiles in the *Lakhani* case and most of the defense commodities in the *Multicore* case would be eligible for license-free export to the UK and Australia under State’s proposal.

Other defense commodities that would be included under the rubric of “low sensitivity” would be about 80 percent of the weapons and other defense commodities that figure in the September 2003 Homeland Security report of recent strategic investigations.³⁵

Still other defense commodities that would be eligible for license-free export under the proposed arrangements are numerous commodities which, at high performance levels, are weapons systems technologies specified on the Militarily Critical Technologies List (“MCTL”)³⁶ because of their importance to maintaining U.S. war

³⁴For example, see the letter dated May 20, 2003, from Deputy Secretary Armitage to Chairman Hyde.

³⁵See Appendix to this report.

³⁶The Militarily Critical Technologies List is required to be maintained and kept up to date by the Department of Defense by the Export Administration Act of 1979, as continued in force by Executive Order. The MCTL is used for evaluating potential technology transfers. It assigns

fighting superiority (e.g., from just two categories of the many USML categories that would be license-free, such MCTL items would appear to include: shaped charges, tandem or multiple warhead munitions, explosively formed projectiles (EFP), gun propellants, certain energetic materials, electronic time fuses, smart mine fuses, guidance integrated fuses, encapsulated multistage munitions, advanced modular artillery charges, surface vessel systems, such as passive mounts for acoustic isolation, active noise reduction or cancellation systems, passive acoustic sensors for locating direct fire weapons on land, phased array radars, and ground radar).

In Chairman Hyde's letter of June 25, 2003, to Secretary Powell, he requested that the State Department consider the removal of items that could not reasonably be characterized as being of "low sensitivity" because of their designation on the U.S. Munitions List as "significant military equipment," a category of weapons commodities that is required by section 47 of the Arms Export Control Act to be so designated because of their substantial combat utility. However, State declined to make this change in its response of July 25, 2003.

Most USG Controls Eliminated

Regardless of the relative effectiveness of either foreign government's arms export control system (discussed later in this report), the proposed arrangements will almost certainly enlarge the risks of diversion by eliminating on the U.S. side nearly all critical elements of prior U.S. Government scrutiny and control that would otherwise precede the export of weapons and defense commodities from the United States—a vulnerability that is not addressed in any substantial way by the proposal.

When juxtaposed against a foreign government's system, the risks of diversion of U.S. weapons technology may be increased or reduced as a result of stringencies (or lack thereof) in the other government's control system. But, even highly effective foreign government controls are mainly applicable only after weapons and defense commodities enter its jurisdiction. In the post 9/11 security environment there are heightened risks associated with all phases of commercial defense trade, including the period during their transport to a port of exit; during their loading and export at U.S. ports of exit; while they are in international transit by air or sea; upon their arrival at a foreign country's port of entry; and following entry into the foreign country's jurisdiction.

Moreover, these risks vary not only according to the geographic distances over which controlled trade must travel, but also increase by any reduction in the U.S. Government's scrutiny and control. These safeguards and control over all exports, which are required by, or derived from, specific provisions of section 38 of the Arms Export Control Act, provide a system (by no means foolproof) that is intended to control these risks at various junctures in the export process. Yet, nearly all levels of U.S. Government scrutiny and con-

values and parameters to weapons systems technologies in order to determine those that are critical to U.S. military forces.

trol would disappear under the proposed exemption arrangements, including:

- U.S. Government evaluation of all contracts and purchase orders to ensure authenticity;
- U.S. Government evaluation of the details of the defense goods proposed for export in the context of their proposed end use, and the requirements and capabilities of the non-governmental end users as well as their recent licensing history;
- Regular, updated computer checks of all U.S. exporters;
- Screening of *all parties* involved in the export transaction, not merely the foreign end user, but also the many freight forwarders and consignees typically involved in both countries for any single arms transfer;
- Pre-license end use checks where indicated to ensure the authenticity and bona fides of proposed transactions; the availability to U.S. Customs from State's licensing database of detailed, near real-time licensing information for all arms exports in order to guide movement of these goods through controlled procedures at U.S. ports of exit; and
- Lodging of licenses with Customs at U.S. ports of exit, which, together with database transfers provided by State, are critical elements of a baseline for targeting and inspection purposes before cargo is loaded.

Few Transshipment Controls in the UK

The risks of diversion associated with the activities of the gray arms market and the elimination of most U.S. Government controls appear to be further accentuated by two additional factors. The first concerns the UK, specifically, and the apparent absence in UK practice of license requirements for most conventional weapons technology when transshipped—or in transit—through the UK to a third country.³⁷ The importance of transshipment controls in protecting against diversion has recently been emphasized by President Bush with respect to weapons of mass destruction in the Proliferation Security Initiative and in recent international conferences spearheaded by the Department of Commerce.³⁸ But, this emphasis appears to be conspicuously absent from the country exemption agreements negotiated by State.

New Burdens on Homeland Security

The second factor concerns the day-to-day functioning of the U.S. arms export control system in the post-9/11 environment. Since the attacks of September 11, 2001, U.S. customs and border protection officials have been required to shift resources and priority away from outbound inspection and targeting of shipments leaving the United States to closely monitoring inbound cargo that could present immediate risks to U.S. internal security. The absence of

³⁷In contrast, the U.S. Government requires a munitions license for all military goods transiting or temporarily imported into the United States through commercial channels. It is not known whether Australia will require such licenses in its future system.

³⁸For a discussion of the latter, see "Department of Commerce Transshipment Export Control Initiative (TECI)" at the Bureau of Industry and Security's website: www.bxa.doc.gov.

detailed license information from State on exempt munitions exports and the absence of licenses to be lodged at U.S. ports of exit—both being inevitable by-products of the proposed arrangements—can only further complicate screening and targeting of commercial arms exports. Early consideration in the country exemption proposal of additional documentation U.S. exporters would be required to file at U.S. ports appears to be no longer the subject of any discussion. In effect, while the Department of Homeland Security is concentrating on closing the “front door” to dangerous imports, the arrangements proposed by State appear to have the consequence of opening the “back door” to dangerous exports.

The Committee understands unofficially that, in response to U.S. law enforcement concerns, the Executive Branch may now be exploring use of the Commerce’s Department’s automated export system (AES) to alleviate part of the additional burden on Homeland Security should exemptions be authorized in law. While this would be a welcome first step in helping to reduce some level of burden shifting (and risk), it remains to be seen what, if anything, will come of this consideration. It is also disappointing that this avenue is only being explored so late in the process when the Congress has repeatedly authorized funding related to AES—and earmarked a portion of that funding for the State Department—for the specific purpose of ensuring strict control over all U.S. weapons-related exports.

However, the Committee notes with concern the Department of Homeland Security’s view that the proposed ITAR exemptions “could . . . require additional inspectors” and that “programming changes used to verify those exports against the proposed ITAR country exemptions, and to target potential shipments in violation of the exemptions” will require additional funding.”³⁹ The fact that additional funding will be required and that additional personnel could be required contradicts the answer provided by the Department of State in its July 25, 2003, letter in response to the Committee’s question concerning projected costs to the U.S. Government, when State advised that “the costs to the USG for regulating these exemptions should arguably decrease as AES goes on line this Fall. . . .”⁴⁰ It would appear that, even at this late date, there has not been any serious consideration of the true costs to the U.S. Government or the implications of additional burdens being imposed on DHS that may go unfunded. Nor has any budget information been provided to Congress concerning the costs associated with implementation.

Impediments to U.S. Law Enforcement

There are corollary impediments to the U.S. Government’s ability to enforce violations arising from the elimination of most U.S. controls, as well as to its ability to prevent and detect of violations. These considerations also need to be weighed against the reality that, historically, there have been few (if any) successful prosecutions in U.S. federal courts of Arms Export Control Act violations

³⁹ Letter dated November 17, 2003, from Under Secretary Hutchinson to Chairman Hyde.

⁴⁰ See July 25, 2003, letter from Assistant Secretary Kelly.

that involve circumstances where no export license is required. This is due to several considerations, including the inclination of most U.S. courts to view the license requirement as highly relevant to the establishment of a person's legal duty under U.S. law, and of most federal prosecutors to regard the absence of a license requirement as signifying an activity of lesser importance to the U.S. Government (for which view they could hardly be faulted in light of State's repeated public description of this proposed exemption as involving only items of "low sensitivity").

These impediments to prosecution, detection and prevention arise, in the first instance, from the elimination of most documentary requirements—sworn applications, signed end user certificates and the like—related to the license application process, and the elimination of the requirement for an exporter to lodge the approved license (there will not be one) with U.S. Customs at the port of embarkation prior to export, as noted above. These impediments remain even if there is the kind of full investigative cooperation on the part of the UK and Australia that is needed to facilitate U.S. law enforcement in an unlicensed environment. But, they may become insurmountable if cooperation from foreign governments is not forthcoming in all instances—and at all levels of the enforcement process, from instances where information or documentation is sought in the early stages of an investigation, to instances where the availability and admissibility of evidence must be ensured in a criminal proceeding. Yet, despite this added premium on foreign law enforcement cooperation, full cooperation is actually not required under the arrangement with the UK. This is apparently because when State decided in the late stages of negotiating the arrangement with the UK to move many important areas to a civil contractual arrangement between the UK and its firms, it appears to have overlooked that the draft memorandum of understanding negotiated 2 years earlier by Department of Justice officials was based (as is customary in such matters) on the principle of dual criminality. Under this principle, the parties agree to cooperate (i.e., commit to cooperation) in areas in which a violation would be an offense under the laws of both countries. However, violations of the civil contract between the UK government and its firms will be legally enforceable in an English court only under English common law, and would not normally involve criminal offenses on the UK side. The net result is that such violations would not require cooperation from UK authorities (though the UK could agree, at its discretion, to provide cooperation on an ad hoc basis).

Even assuming full UK cooperation with U.S. law enforcement authorities in sharing of information and documentation available to it through the civil contracts with its firms, a more fundamental problem is that sharing of information in this fashion is mainly relevant to discovering and prosecuting violations *after* they have occurred, rather than preventing them prior to original export. Independent of the wisdom of such a shift in policy (which has not been established), U.S. law enforcement agencies have long felt that any departure from case-by-case licensing, including in the case of Canada, poses challenges for law enforcement interests and recommended to State in the negotiations with the UK and Australia that both governments amend their laws to ensure a consistent

level of enforcement between exempt and non-exempt items. This has not happened in the UK and it remains to be seen if it will happen in Australia.

The Committee presented several other questions to the State Department related to law enforcement interests that were only answered during the waning days of the first session of the 108th Congress. These answers are appended to this report. One critical question that remains unanswered to this day relates to the requirement in existing law for a determination by the Attorney General with respect to the ability of the United States to detect, prevent and prosecute criminal violations of the Arms Export Control Act, including efforts linked to international terrorism.⁴¹

U.S. Government Consent Rights Adversely Affected

Even under a best-case analysis, the arrangements negotiated by State fall far short of the laudable goals established by Secretary Cohen in the previous administration of using country exemptions as a “powerful incentive” to negotiate “ironclad” agreements with U.S. allies in key areas, such as re-transfer and end use, in order to provide a “dramatic increase in our global technological security.”⁴² In fact, the arrangements appear to reflect a marked deterioration in the status quo for protecting U.S. Government consent rights.

The reason why this area was properly emphasized by Secretary Cohen is because the requirement for prior U.S. Government consent before any transfers to third countries take place or before U.S. defense articles may be used for purposes other than those originally authorized, has long been considered a cornerstone of the U.S. arms export control system. It is indispensable to ensuring: (1) that both secondary uses of U.S. weapons technology involving third countries (e.g., through resale by the original recipient country or commercial vendor to another country) and access by nationals of countries other than those to which the weapons were approved (commonly referred to as “third country” nationals) accord strictly with the same U.S. laws and policies which governed the original export; and (2) that U.S. military systems and components do not fall into dangerous hands. The current, dominant role of the United States and its defense firms in the global arms market and the heightened threat to U.S. interests world wide in the global war on terror suggest this may not be the most appropriate time to attenuate this requirement.

However, a much different outcome has emerged from the negotiations with both countries than described to Congress at the time of enactment of the Security Assistance Act of 2000. Neither the arrangement negotiated with the UK nor the arrangement negotiated with Australia contains a legally binding commitment by either government concerning non-transfer and end use and the requirement for the U.S. Government’s prior written consent over these

⁴¹ See the annex to Chairman Hyde’s May 5, 2003, letter to Secretary Powell.

⁴² Letter dated June 28, 2000, from Secretary Cohen to Chairman Gilman, Committee on International Relations, U.S. House of Representatives.

matters as they pertain to U.S. defense articles and services where the governments, themselves, are the end users.⁴³ State suggests that the arrangements it negotiated could be interpreted in such a way as to imply the necessary commitments. But, the words are simply not there. Nor has State proffered that it will insist on these commitments in an exchange of diplomatic notes (as was done with Canada). Notwithstanding these glaring omissions, the United States would be bound under these arrangements—in language that is very clear—not to seek third party re-export or re-transfer assurances in the future from either the UK or Australia.

In the case of Australia, the Committee had assumed that this omission was an unintentional oversight. But, the State Department has not acknowledged the omission, let alone moved to correct it, raising concern that there may be more involved, such as a substantive objection on Australia's part.

Regarding the UK, instead of providing an increase in U.S. global technological security, the absence of any UK government commitment to seek U.S. Government consent prior to any third country transfer—and the consignment in the UK arrangement of U.S. Government rights over re-transfer and end use of U.S. weapons exports involving UK firms to a civil contract between the UK and those firms (enforceable mainly under English common law)—could be highly prejudicial to U.S. interests, if viewed (as appears certain it would be) as a precedent by other governments for their own defense trade with the United States, a number of which are already hoping the ongoing export control “reform” debate in Washington surrounding NSPD–19 will result in an attenuation of U.S. Government policy in this area.

Further, the State Department did not negotiate a legally binding commitment from the UK government in this area, as required by U.S. law. Rather, it negotiated what it describes as a “politically” binding commitment⁴⁴ from the UK by which the UK government would enter into civil contracts with UK companies qualified to receive license-free U.S. defense articles, which contracts would require, as a condition of their qualification (or eligibility), the UK companies generally to acknowledge and adhere to U.S. non-transfer and end use requirements. However, the UK government, itself, would make no such commitment—even of a political character—under any provision of the draft arrangement. The purpose of requiring a legally binding commitment in the Security Assistance Act of 2000 on this critical matter was not merely to ensure that the commitments were binding under international law, but to ensure that that there was an appropriate domestic legal basis in the “exempt” country to ensure the commitments made were fully enforceable under that country's criminal laws (and not

⁴³The arrangement with Australia contains assurances with respect to issuances of licenses to Australian persons that involve U.S. origin defense articles, and State advised in its July 25 letter that the Government of Australia's own exports are also subject to its licensing process. However, recent discussions between Committee staff and Australian officials have clarified that, in fact, Australia does not issue licenses to itself and that there may be a legal rationale to the omission of third party consent in the bilateral agreement.

⁴⁴Binding commitments between governments are typically reflected in treaties or other international agreements, while “political” commitments, no matter how solemnly made or at what level, do not actually “bind” governments. The term “politically binding” is not in normal diplomatic usage.

through a court of common pleas in which the United States may not even be a party at interest).

The UK commitment is one to give “fullest weight” to U.S. views on retransfers and, in exceptional circumstances, to consult with the United States. The UK government would assure enforcement of such commitments by its qualified companies through its review of individual and general (or open, self-validating) export licenses (though, in fact, governmental reviews of individual exports under general licenses are not typical).⁴⁵ On the other hand, the agreement with Australia expressly precludes the use of general licenses for this purpose, and properly so.

The Committee sought an explanation from State as to the reasons provided by the UK for not accepting the U.S. Government’s rights in this area and was informed by State:

“The UK government would not provide us with a legally binding commitment with regard to U.S. requirements to obtain prior written consent for transfer of U.S. defense articles to third party destinations and changes in end use because it argued to do so would infringe on UK sovereignty including by unacceptably fettering the discretion of the UK Secretary of State for Trade and Industry to make licensing determinations.”⁴⁶

However, the relegation of a fundamental U.S. interest to such a feeble status in the UK arrangement, and the State Department’s explanations for this development, seem inexplicable in view of the UK’s unqualified acceptance of the right of governments to prior consent over the transfer of “commercially” sensitive information in a treaty governing defense industry cooperation that was signed by the British Minister for Defence (and since ratified by the UK) with five other European nations in the midst of the bilateral U.S.–UK negotiations concerning this matter.⁴⁷

Article 52 of that treaty provides:

“The Party receiving information which is of commercial value or market sensitive from another Party shall not use or disclose such information for any purpose other than the purpose for which it was provided, unless it has received the prior written consent of the providing Party.”

It is difficult to understand how such a right could be accorded by the UK to its EU partners for “commercial” and “market sensitive” information, but denied on grounds of UK sovereignty for U.S. Government information that is controlled for export on national security grounds. It is equally difficult to understand why

⁴⁵ However, as most exports under general licenses are self-validating by the exporter and do not involve submission of a license application, there will be few such reviews by the UK government of general licenses.

⁴⁶ July 25, 2003, letter from Assistant Secretary Kelly to Chairman Hyde, p. 14. Similarly, in a related area, State also explained in this same letter that “(i)n part, the point of the agreement is not to give U.S. law extraterritorial effect. . . .”

⁴⁷ See Article 52 of the Framework Agreement Between the French Republic, the Federal Republic of Germany, the Italian Republic, the Kingdom of Spain, the Kingdom of Sweden and the United Kingdom of Great Britain and Northern Ireland Concerning Measures to Facilitate the Restructuring and Operation of the European Defence Industry, done at Farnborough, UK, July 27, 2000; entered into force April 18, 2001. The Framework Agreement is a treaty within the meaning of the Vienna Convention on the Law of Treaties.

the State Department did not pursue this matter with greater vigilance.

Further, while Article 52 specifies the commitments of the Parties with respect to information or data, Article 13 (at paragraph 4) provides a comprehensive procedure for the Parties when authorizing re-exports by private persons, in which, for example, a Party who may not be a participant in a cooperative armament program commits itself to obtain approval from the participating Parties before authorizing any re-export to non-Parties of articles produced under the program. Similarly, Article 13 (at paragraph 5) requires that Parties obtain end user assurances and consult with relevant other Parties if a re-export request is received. In contrast, the commitment negotiated by State in the UK arrangement is for the UK to consult with the U.S. before issuing an export license for U.S. defense articles only in “extraordinary circumstances.”

Taken together, these two principles which found ready agreement in the EU Framework Treaty—prior consent and prior consultation before private exports are authorized—have been cornerstones of the U.S. arms export control system for many years.

With respect to the issue of extraterritoriality more generally, far from being politically or legally opposed to the principle of prior consent requirements of governments, EU members have recognized the validity of such requirements, not only in the case of the Framework Agreement, but also as a principle that may be generally applicable to their arms sales. For example, the Fourth Annual Report on the European Code of Conduct on Conventional Arms states that:

“. . . in accordance with their national legislation, member states can require, inter alia, a clause prohibiting re-export of the goods covered in the end-use certificate. Such a clause could, among other things, . . . provide that re-export will be subject to agreement in writing of the authorities of the original exporting country (and) an undertaking, where appropriate, that the goods being exported will not be used for purposes other than the declared use.”⁴⁸

However woefully short of the statutory standard and prejudicial to broader U.S. interests in third party transfer and use issues, it is also remarkable that the overall arrangement in this area with the UK appears to involve additional specific concessions by the U.S. Government. Under the negotiated arrangement, the U.S. Government would, in exchange for the UK’s “political” commitment, waive (e.g., forsake) its consent requirements in two areas: (1) for all intra-UK transfers of exempt articles involving qualified companies;⁴⁹ and (2) for any use of U.S. defense articles (whether

⁴⁸ DGE VII 13779/02, Brussels, November 11, 2002.

⁴⁹ The re-transferring UK firm would still be required to obtain the assent of the original U.S. exporter in order to avoid infringement of the latter’s commercial rights or interests. There is no firm estimate from State as to how many companies in the UK or Australia could be qualified. State advises it sees no need to place a limit on the number. In the case of Canada, the original estimate of firms that might be eligible under that exemption was around 250, but there are currently more than 600 companies eligible with business premises at 2,000 locations. In Australia’s case, State points out that participation in the exemption is limited to participants in Australia’s Defence Industrial Security Program, which currently has 364 members, though State also points out there could eventually be as many as 600 companies, though it does not

or not exempt) involving UK defense purposes, applicable both to the UK government and third country forces cooperating with it.

Yet, the Security Assistance Act of 2000 did not authorize State to waive or forsake these fundamental U.S. Government requirements; quite the opposite, it provided for such rights to be asserted and protected.

Absence of Comparability

Except in the area of weapons of mass destruction, and discrete other areas where it is closing gaps in implementation of the Export Control Act of 2002, the future UK arms export control system will not be comparable in scope to the comprehensive system deployed by the United States, but will generally remain a “targeted” system, essentially reserving case-by-case licensing to WMD and certain other areas, while relying on a variety of “open” (or general) licenses for the bulk of conventional weapons related exports (an approach that is roughly analogous to the U.S. Department of Commerce’s approach to dual-use trade). The UK did not view the proposed U.S. exemption as an incentive for changes to its laws or regulations. Similarly, the Department of State advises there are certain areas where Australia has decided not to make “comparable” changes, but others where it may view the proposed U.S. exemption as an incentive (though it is not possible to know the precise scope and content of Australia’s future system as it is still being debated internally).

The effectiveness of a government’s arms export control system largely revolves around two main components: The defense control list and the regulations that govern control over, and access to, items and technologies on the defense control list. With respect to the latter, the table at appendix 1 provides a comparison of the U.S., UK, and Australian systems in key regulatory areas. That comparison does not indicate comparability in scope and effectiveness, but significant incomparability.

Regarding the defense control lists, on June 25, 2003, the Committee requested that the Department provide the expert analysis underpinning its conclusions as to comparability of both the UK and Australian military lists with the U.S. Munitions List for purposes of compliance with the statutory criteria. The Committee was advised by the Department in its July 25, 2003, letter that “(t)he expert level analysis . . . is still being worked by the Defense Technology Security Administration.” The Department eventually provided this analysis by letter dated November 6, 2003, which is appended hereto at Appendix 12. This analysis and various provisions of the proposed arrangements indicate that the Department intends to exempt a variety of U.S. Munitions List items, including space systems and space launch vehicles (“SLVs”), from U.S. munitions export licenses even though these items are not included within the coverage of the UK or the Australian “list of controlled *defense* items”, as required by section 38(j), but are in both coun-

explain the discrepancy. There are no estimates available for the UK, but in view of the size of the British defense industry in comparison to Canada’s the number of exempt firms and business locations could be expected to be much greater.

tries treated not as munitions or *defense* items, but as *dual-use* items.

Indeed, the Department appears to have liberally interpreted various provisions of United States law in negotiating these agreements, and to have misconstrued others. The inappropriate inclusion of U.S. defense articles that are handled only as dual-use abroad is but one example. There are others. In the Conference Report accompanying passage of the Security Assistance Act of 2000, the Conferees made clear that—

“*essential* to the initiative to provide license-free trade to various countries is the operation of *domestic export control laws* in such countries. Accordingly, the underlying rationale governing section 102 is that the United States should not provide the benefit of an exemption from licensing of U.S. defense exports unless a foreign country agrees to apply, in a legally binding fashion and in accordance with a bilateral agreement with the United States, *the full range of United States export control and laws, regulations, and policies* appropriate to the sensitivity of defense items exported to a foreign country under the exemption.”⁵⁰ (emphasis added)

Yet, in the proposed arrangements presented by the Department for both the UK and Australia there is little evidence of any attempt to apply (or to achieve) the application of the “the full range” of U.S. controls. Further, the Department appears not to have assigned much importance to the phrase “at a minimum” which appears throughout section 38(j) or to the clear guidance of the Conference Committee—apparently opting, instead, to construe certain provisions in ways that might appear unimaginable to the Conference Committee (e.g., in lieu of changes to UK export control laws, there will be civil contracts between the UK government and its firms covering U.S. exempt weapons technology that would be “legally binding” only under English common law and enforceable by the UK government mainly through the imposition of contractually provided penalties and successful motions filed in UK civil courts for injunctive relief⁵¹).

The UK appears to have made clear that it was not prepared to make changes in its laws or regulations in order to accommodate the requirements of U.S. law. Faced with this position, the Department appears to have set about to construct as elaborate a case as it could for proceeding with the agreement and establishment of an exemption by inserting various palliatives into the proposal to show the negotiations were successful. By itself, such an approach, while not optimal, is at least understandable on one level insofar as it may concern our relations with close allies.

What is less understandable is the Department’s unwillingness to make any commitment with respect to the extension of such exemptions to other countries, in view of the (at best) mixed results of the negotiations with the UK and Australia, particularly if this unwillingness is motivated by a desire to avoid the potential em-

⁵⁰ House Report 106–868, pp. 2–3.

⁵¹ A much different—and untested—form of enforcement from the routine exercise of police powers by UK law enforcement agencies, which would not be available for offenses arising solely from a civil contract (e.g., an export in progress of U.S. weapons technology that had not been authorized by the U.S. Government).

barrassment of retreating from this much-touted DTISI initiative or the defense export control “reform” agenda more generally.

This is a matter of considerable importance to Congress in deciding whether, and if so, how, to authorize exemptions for the UK and Australia because of the possible precedence established by these agreements. For example, there are few elements of the UK system—and none achieved in these negotiations—that would distinguish it sufficiently from the national systems of other EU governments, such that there would be a basis for determining the UK system is “comparable” but others are not. Similarly, while the draft agreement with Australia is a more conventional intergovernmental arrangement and more reflective of the commitments Congress expected to see in these agreements, it is also the case that: (1) there are significant issues related to U.S. Government consent rights and the scope of the exemption insofar as it concerns articles treated as dual-use items in Australia, which State’s presentation merely glosses over; and (2) the text of the arrangement is short on details on the domestic legal framework that will underpin Australia’s commitments—and State has been able to fill-in these details only partially and at a very high level of generality. Unrevealed in the agreements and in the Department’s representations is whether Australia intends to meet all of its commitments through the enactment of new laws and regulations (as clearly intended in section 38(j)) or through more unorthodox means (such as those evident in the UK arrangement).

Concerns that the pursuit of more country exemptions will continue and is motivated primarily by the objective of relaxing arms export controls, are reinforced by the Department’s position that the control systems of both countries are—or will be—“comparable” to the United States notwithstanding the broad noncompliance of the negotiated agreements with the requirements of U.S. law. The Committee is concerned that, if these agreements negotiated by State with our closest allies are inadequate—as it appears they clearly are—additional exemptions for other countries could be dangerous in the extreme.

Most U.S. Statutory Requirements Unmet

The Department’s proposal acknowledges that: (1) the Australian agreement does *not* meet the criterion of section 38(j) regarding retransfers and use (because of the absence of control in the Australian government’s system on in-country transfers or use and its unwillingness to establish such controls); and, (2) the UK agreement does *not* meet several of the mandatory criteria of section 38(j). It, therefore, supported legislation in the Senate (S. 2144) that would authorize the President to waive these requirements (while maintaining the administration position in the House that would permit it to waive any and all requirements for any country). However, it is not easy to support the Department’s reading of the law in order to reach the conclusion that *any* of the mandatory criteria are met in the case of the UK (which raises questions about how it would interpret the Senate bill).

There are two other mandatory criteria, which State appears to believe have been met, but which are open to serious questioning

(and which may help explain why State proposes that the House enact legislation that permits the Executive Branch to waive any provision in section 38(j) for any country (not just the UK or Australia)).

The first is the requirement in section 38(j)(2)(A)(iii) concerning “establishment of a procedure comparable to a ‘watchlist’ (if such a watchlist does not already exist) and full cooperation with United States Government law enforcement agencies to allow for sharing of export and import documentation and background information on foreign businesses and individuals.” The U.S. “watchlist” is a computerized list of more than 50,000 ineligible (for various legal reasons) and suspect or known-diverters, both U.S. or foreign persons (including companies), against which all parties to an export license application are screened. The Department’s June 4, 2003, analysis appears to conflate the “watchlist” requirement with the requirement for sharing of law enforcement information: “The watchlist procedure criterion is addressed under the practice of utilizing intelligence and law enforcement information in the licensing review process and for monitoring trafficking. Such a procedure with the UK would appear, we understand from the regulators, to flow, as a practical matter, from the law enforcement and other commitments provided for in the agreement and the MOU.” However, the fact of *some* use of intelligence and law enforcement information when reviewing license applications is not comparable to a systematic process for collecting and maintaining in a computer database the names of all known ineligible and suspect persons, and does not explain the absence of any commitment in the agreement on the UK side to maintain or establish a “watchlist” of any kind.

Further, with respect to sharing of law enforcement information, since the law enforcement MOU negotiated by the Department of Justice with the UK only requires cooperation in cases where dual criminality is present (and provides that there “may” be additional cooperation in other areas)—and because the general scheme negotiated by State essentially means that enforcement of civil contracts between the UK and “qualified” companies will not generally involve criminality on the UK side—there is also room to question the extent to which (if at all) this arrangement meets a mandatory requirement for information sharing.

The second is the requirement in section 38(j)(2)(A)(iv) concerning “establishment of a list of controlled *defense* items to ensure coverage of those items to be exported under the exemption” (emphasis added), and the problems associated with State’s attempt to interpret this provision as encompassing *dual-use* controls of a foreign government, which were discussed in a preceding section of this report.

Comparison to Canadian Exemption

In response to the illegal exploitation efforts identified in April 1999, the Canadian Government took a number of steps to strengthen its national system of export controls, including enactment of new laws and regulations to harmonize its list of controlled military goods with the U.S. Munitions List; to establish a system

for registering Canadian defense firms; to require U.S. Government re-export authorization in connection with permits to export U.S.-origin military goods from Canada; and, to pledge in an exchange of diplomatic notes that the Canadian Government would not authorize the re-export, resale or other disposition of U.S. Munitions List items outside Canada without first consulting the United States Government to ensure that its re-transfer approval has been obtained. In response to these steps, the United States restored the exemption for Canada on the eve of the announcement of the DTSI initiatives.

While the proposed arrangements with the UK and Australia appear to be modeled after the Canada exemption in some respects, the UK agreement is clearly less satisfactory with respect to third party transfer and use matters and the Australia agreement may be somewhat less satisfactory (in failing to provide such an assurance with respect to the Australian government, itself, as distinct from Australian companies, though State advises this is implied). Both agreements may also be less satisfactory with respect to coverage of military items when incorporated in civil products (which neither agreement appears to control) and also with respect to the actual coverage of the lists. In response to various expert level meetings, the Canadian Government made a number of additions to its control list in order to harmonize it with the U.S. Munitions List. There is no indication of such additions for the UK or Australia.

State has suggested that the agreement with the UK, in particular, represents a significant improvement over the Canada exemption because the U.S. Government has the right of final approval over which UK end users are “qualified” to receive license free US defense commodities, while all companies duly registered in Canada in accordance with new legislation Canada enacted in 1999 are so eligible. However, as noted earlier, the U.S. Government routinely exercises the right to approve foreign end users in the export license process, so such a right does not imply any improvement over traditional licensing procedures (for reasons noted earlier, it actually represents a substantial derogation since licensing procedures approve all parties to the transaction, not merely the end user). With respect to whether it provides an improvement over the Canadian exemption, the State analysis appears to be making a distinction without a difference. By now, State (presumably) would have vetted all Canadian registered companies through the same vetting procedure it intends to apply to proposed UK companies and would have taken appropriate action through diplomatic channels with Canada to disqualify unreliable or suspect end users, if any, following approximately the same consultative process it has sketched out with the UK and Australia.

Of more significance, however, is the impression that, instead of representing a raising of the bar beyond those standards negotiated with Canada by the previous administration in 1999, the proposed arrangements with the UK and Australia are, in the final analysis, less stringent—in some areas, woefully so.

Excessive Delays For UK and Australia Licenses

One troubling piece of information obtained by the Committee in this review was State's acknowledgement that, under current guidelines, there were eight hundred and forty three (843) munitions export license applications for either the United Kingdom or Australia referred for inter-agency review to the Department of Defense before being approved that would be eligible for export without a license under the exemptions, if established. About 50 percent of these applications for the UK and some 64 percent for Australia were approved with limitations or conditions. When a license application is processed by State without referral to Defense or other agencies, it is typically completed within 8 calendar days. Historically, about 70 percent of all munitions license applications are so processed by State. On the other hand, when a license application is referred to Defense or other agencies for review (about 30 percent of all cases), the processing time increases to 4 to 6 weeks.

These figures indicate one of two possibilities: (1) an exceedingly high number of cases for our closest allies are being unnecessarily subjected to lengthy inter-agency review, doubtless contributing to frustration by the interested parties (the relevant governmental agencies and defense firms) in both countries; or (2) Defense's national security review and conditioning of approvals of these cases is necessary and appropriate in order to ensure these exports are consistent with U.S. technology transfer policies administered by DoD. It is unlikely that the second possibility accurately describes the situation because this would imply that various U.S. policies covering technology security and disclosure of military technology to our allies provide for greater access by Canada or Canadian firms (who are currently receiving all of the weapons and other defense commodities in the 843 cases license-free under the Canada exemption without any DoD review or conditions) than for the UK or Australia. To the Committee's knowledge, there are no such U.S. technology security or disclosure policies that discriminate in favor of Canada and against the UK or Australia. State essentially glosses over this matter by observing:

"It should be noted that those cases that were referred to DOD and adopted with provisos were in a context where we did not have the special protections provided under the measures. In the context of those measures, the Departments of State and Defense are fully comfortable with approving the exports of items subject to an exemption to the UK and Australia governments and qualified firms without interagency referral or provisos."

By reference to these "special protections," State presumably means those provisions in the arrangements (or the civil contract in the case of the UK) that concern qualification of the UK and Australian companies and re-transfer and end use. However, these provisions or "special protections" (which, as indicated in this report actually provide less protection and greater risk than traditional licensing) do not in any case relate to any of the factors appropriately related to referral of cases to DoD for a national security review or—if they did—would strongly imply that U.S. policy

governing the conditions for disclosure to Canada, the UK and Australia are seriously conflicted. Based on the explanation provided by State to date, it is difficult to avoid the conclusion that—either intentionally or not—a large number of licenses for the UK and Australia are being unnecessarily delayed and encumbered by excessive inter-agency review. It is a compelling argument not for an exemption, but for enactment of the “fast-track” licensing procedures for the UK and Australia contained in H.R. 1950, which the House passed earlier this year.

Enactment of the fast-track licensing provisions of H.R. 1950 for the UK and Australia would remedy this situation by prompting a review of referral procedures for both countries and by requiring a determination by the Secretary of Defense before any item that is exempt for Canada would be subjected to lengthy inter-agency review for the UK and Australia. This would also surely accomplish more efficiently, and without any of the attendant risks to U.S. national security and law enforcement interests arising from State’s exemption proposal, the objective State and Defense have described of freeing up resources currently devoted to low risk cases (by which they must mean those resources devoted to technology transfer policy, largely resident in Defense, in view of the above data).

Conclusion

The United States may be squandering a unique opportunity to establish very significant bilateral arrangements with our closest allies, which not only set a high standard for other countries to follow (a goal which seems axiomatic in the war on terror), but which also provide an appropriate framework that reflects the nature of current and future cooperative research in areas of high priority to the U.S. Government and our closest allies, such as missile defenses and advanced fighter aircraft.

Such cooperative research areas are primarily carried out through defense services, a form of cooperation that is virtually excluded from the proposed arrangements in favor of the Department’s decision to apply a “Canada-like” list of commodity exports (e.g., trade in components and finished military products) to the UK and Australia. However, commodities are increasingly less prominent in U.S. defense trade with the UK and Australia (and have been for some years) and present higher risks of diversion and greater impediments to law enforcement than defense services related to the personal interactions of leading U.S. and allied defense firms engaged in government-sponsored collaborative research.⁵²

⁵²For example, as a component of U.S. bilateral defense trade with the UK during fiscal year 2002, defense services (e.g., technical assistance) outpaced commodity exports by a factor of nearly 3:1—\$6.6 billion in defense services versus \$2.5 billion in defense commodities. See the report by the Department of State pursuant to Sec. 655 of the Foreign Assistance Act of 1961, covering fiscal year 2002 munitions exports pursuant to Sec. 38 of the Arms Export Control Act.