

End-Use Monitoring of Defense Articles and Defense Services Commercial Exports FY 2011

This report summarizes the Department of State's administration of its "Blue Lantern" end-use monitoring program in FY 2011. The program is operated in accordance with section 40A of the Arms Export Control Act (AECA) (22 U.S.C. 2785), as amended. It monitors the end-use of defense articles, defense services, and brokering activities exported through commercial channels and subject to Department of State licenses or other approvals under section 38 of the AECA and the International Traffic in Arms Regulations (ITAR) (22 C.F.R. Parts 120-130), which implement the AECA. The Blue Lantern program is managed by the Research & Analysis Division (RAD), Office of Defense Trade Controls Compliance (DTCC), Bureau of Political-Military Affairs (PM). The program has been in existence since 1990.

Blue Lantern end-use monitoring entails pre-license, post-license, or post-shipment inquiries or "checks" undertaken to verify the bona fides of proposed foreign consignees and end-users, to confirm the legitimacy of proposed transactions, and to provide "reasonable assurance that –

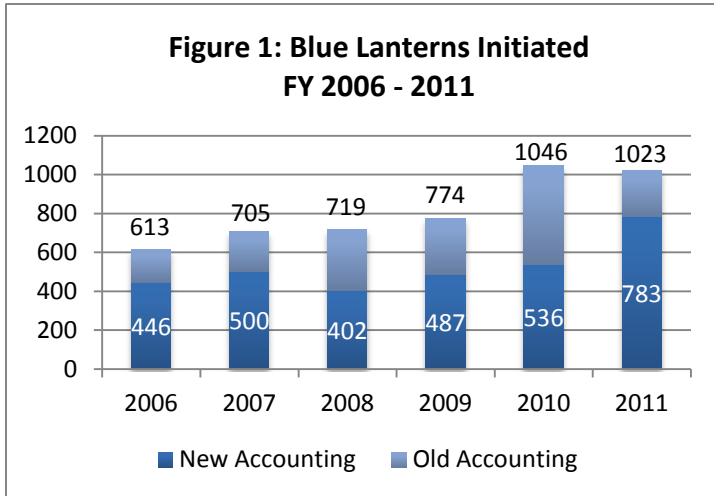
- i) the recipient is complying with the requirements imposed by the U.S. Government with respect to use, transfers, and security of defense articles and defense services; and
- ii) such articles and services are being used for the purposes for which they are provided.”¹

PM/DTCC/RAD's operational budget for FY 2011, in addition to salaries, was approximately \$2.17 million. Four State Department personnel and three contract personnel currently manage the Blue Lantern program in RAD, among other duties. End-use checks are conducted by U.S. embassy personnel in country.

Blue Lantern End-Use Inquiries Initiated in FY 2011

In this FY 2011 report, the office has adopted a new accounting method for the number of Blue Lantern inquiries initiated. In the past, the number represented several types of actions, including inquiries subject of a diplomatic cable to an embassy, inquiries resolved via e-mail exchanges with an embassy, inquiries subject of independent research by RAD staff, and cases targeted for inquiry to an embassy but awaiting hardware export. However, we reassessed the previous

¹ See section 40A(a)(2) of the AECA, 22 U.S.C. 2785(a)(2).



accounting method and determined that only counting inquiries subject of an official diplomatic cable and contact by U.S. embassy staff with a foreign government or company regarding an export transaction or ITAR compliance matter provides a more precise metric of total Blue Lantern inquiries initiated in a given year. We believe this accounting method

reflects a more traditional understanding of end-use monitoring. While the total number is lower than the previous accounting method, the number still demonstrates an increase in Blue Lantern inquiries over the past three years. Figure 1 provides the total number of cases for both the previous and new accounting methods.

In FY 2011, the Department adjudicated over 83,000 license applications and other approval requests. Figures 2 and 3 illustrate the regional distribution of authorization requests and Blue Lantern inquiries, respectively. For statistical purposes, DTCC/RAD attributes a Blue Lantern check to the region of the end-user listed on the authorization request. Blue Lantern inquiries, however, may be initiated or determined to be “unfavorable” due to foreign intermediaries in third countries.

Figure 2: Authorization Requests By Region FY 2011

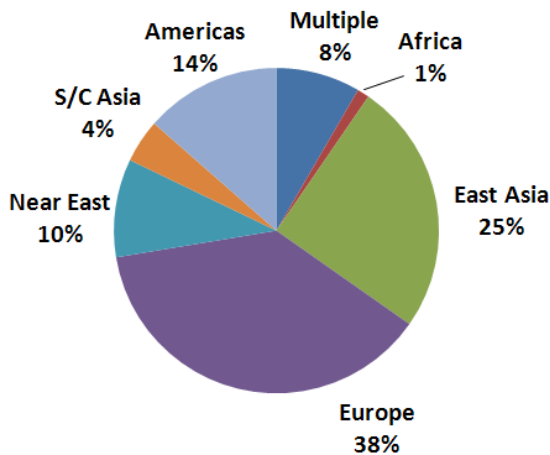
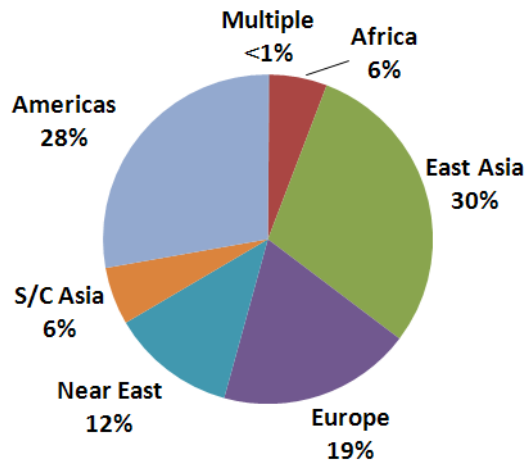


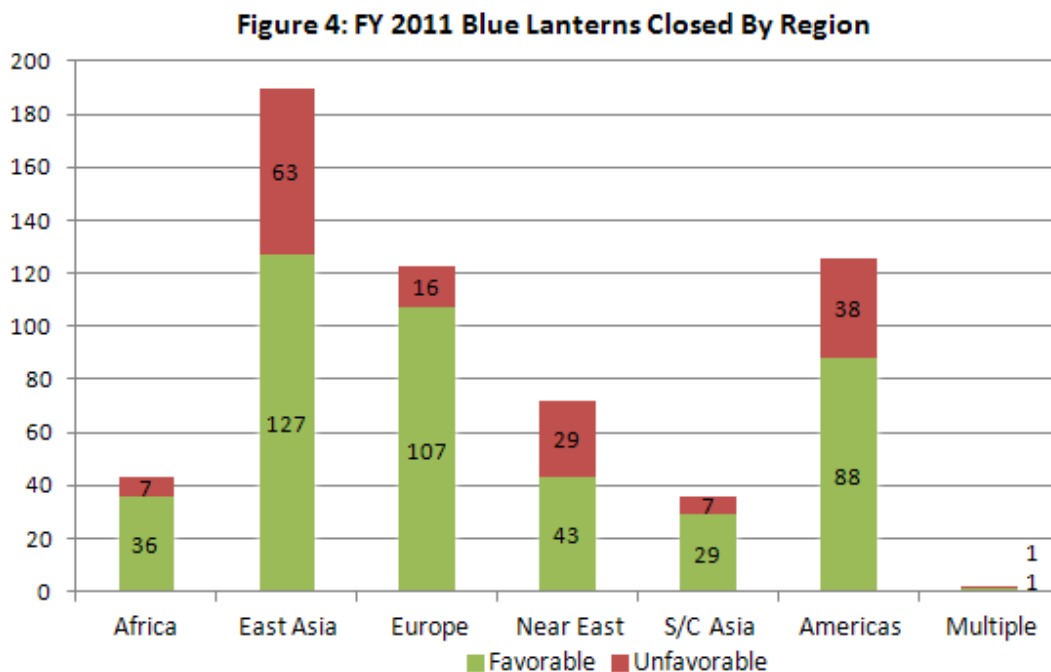
Figure 3: Blue Lanterns Initiated By Region FY 2011



In FY 2011, Blue Lantern checks were conducted in 88 countries. Figures 2 and 3 illustrate that fewer checks are done among North Atlantic Treaty Organization member countries with long-established trade patterns, whereas there are proportionally more checks in the rest of the world. In FY 2011, the proportion of checks conducted in the Americas was double that region's share of license applications (28% vice 14%). This was due to a significant number of inquiries on firearms authorizations, where security and diversion of such weapons is an ongoing concern.

Blue Lantern End-Use Inquiries Closed in FY 2011

Figure 4, a new graph to the Annual Report, illustrates the total number of Blue Lantern cases closed, broken down by region. In FY 2011, DTCC closed 592 Blue Lantern cases, of which 161 (27%) were determined to be "unfavorable." This means the findings of fact were not consistent with the authorization request or approval. Blue Lantern checks are selected based on potential risk of diversion or misuse and are not a random sampling across all State Department licenses. Because of this selection process, the transactions targeted for Blue Lantern checks are more likely to result in unfavorable findings. An unfavorable Blue Lantern does not necessarily mean diversion or illicit activity was involved. While some cases are closed for such reasons, other cases may be closed unfavorable for less egregious reasons. For example, a case where the authorized end-user received U.S. defense articles, but an unlicensed intermediate foreign consignee was involved in the transaction.



Unfavorable Blue Lantern cases may result in the rejection, denial, or revocation of a license application, removal of a party, update of the DTCC Watch List, or referral to the office's Enforcement Division (END) for appropriate action. In FY 2011, DTCC denied 13 authorization requests and returned without action 33 as a result of Blue Lantern pre-license checks. DTCC revoked 12 authorizations and suspended one as a result of Blue Lantern checks conducted after export authorizations were approved. In FY 2011, unfavorable Blue Lanterns referred to END resulted in 19 directed disclosure cases involving potential civil violations of the ITAR. Unfavorable Blue Lantern referrals to federal law enforcement resulted in the opening of six criminal investigations.

In FY 2011, the Near East region had the highest unfavorable rate, where 29 out of 72 cases were unfavorable. This is due in part to multiple checks on the same entities that resulted in either the inability to confirm the bona fides/existence of the company or unauthorized brokering. The lowest unfavorable rate was in Europe (16 out of 123 cases).

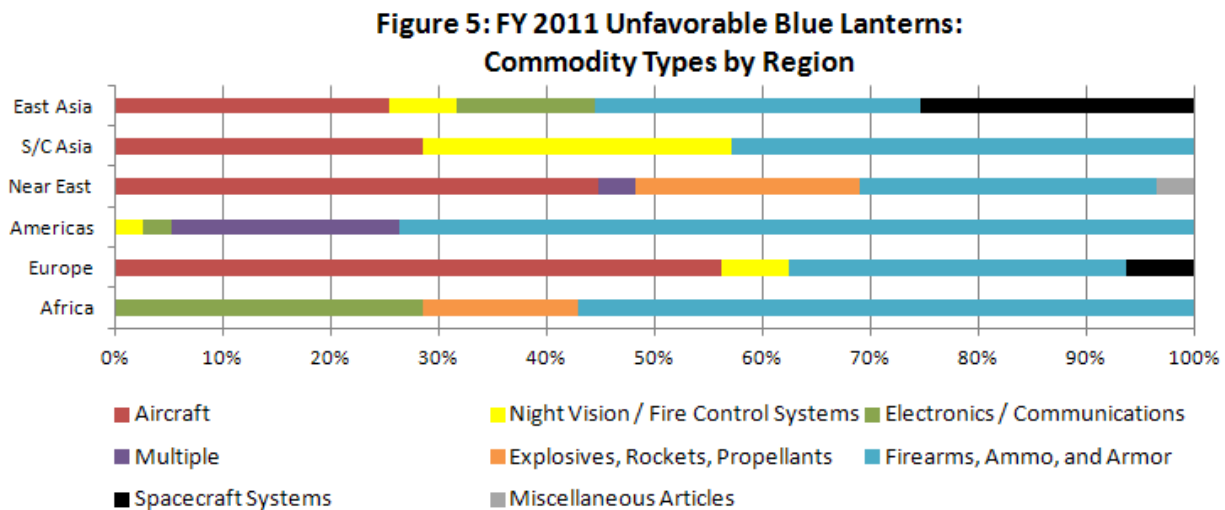


Figure 5 provides a breakdown of unfavorable Blue Lantern checks by region and commodity. In East Asia, most unfavorable Blue Lanterns involved aircraft parts, firearms/ammo/armor, or spacecraft systems. In South Central Asia, aircraft parts, night vision/fire control, and firearms/ammo/armor were the primary commodities involved in the unfavorable checks. In the Near East, nearly half of unfavorable checks involved aircraft parts while in the Americas, nearly three-quarters of unfavorable checks involved firearms/ammo/armor.

Analysis of Unfavorable Checks in FY 2011

The reasons for unfavorable Blue Lantern results and the number of instances in which they occurred in FY 2011 are illustrated in Figure 6. Blue Lantern cases can be closed unfavorable for one or more of the reasons.

Derogatory information/ foreign party deemed unreliable recipient of USML	76
Unable to confirm order or receipt of goods by end-user	43
Foreign party involved in transaction but not listed on license/ application	30
Indications of diversion or unauthorized retransfer or re-export	34
Inability to confirm existence of foreign party	12
Unauthorized brokering	12
Refusal to cooperate	7
Lack of secure storage facilities	6
Unauthorized stockpiling	5

Figure 6: Reasons for Unfavorable Results and Number of Instances (FY 2011)

The leading cause of an unfavorable result in FY 2011 was ***Derogatory information / foreign party deemed unreliable*** (76 cases), a dominant factor in previous years. This broad category includes criminal records, negative intelligence information, and varying concerns regarding a company's *bona fides*. For example, a check on a reseller of firearms located in Southeast Asia revealed that the proprietor was the daughter of individuals previously arrested in the U.S. for attempted firearms smuggling. A second example involved a European aircraft parts reseller who ran his business out of a home office and had no firm contract with the end-user.

The other leading categories for unfavorable determinations in FY 2011 are generally similar to those seen in the previous fiscal years. However, there has been an increase in the prevalence of unfavorable determinations involving unauthorized foreign parties (30). In many cases, this was not due to an intentional attempt to hide the involvement of an intermediary. Rather, company-level administrative oversights and insufficient knowledge of ITAR requirements on the part of U.S. and foreign parties led to incomplete information on authorization requests. End-use checks also uncovered 34 instances of ***Indications of diversion or unauthorized retransfer or re-export***. Finally, there

was an increase in the number of cases involving an ***Inability to confirm existence of foreign party***. This category describes cases where an embassy official was unable to contact or locate a foreign party listed on an export authorization. This was a rare occurrence in FYs 2010 and 2009. However, in FY 2011, twelve checks involved this factor.