

## **End-Use Monitoring of Defense Articles and Defense Services Commercial Exports FY 2014**

This report summarizes the Department of State's administration of the Blue Lantern end-use monitoring program for fiscal year (FY) 2014. The Blue Lantern program fulfills requirements found in section 40A of the Arms Export Control Act (AECA) (22 U.S.C. 2785, as amended). The program 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 CFR Parts 120-130), which implement the AECA. Following the reorganization of the Directorate of Defense Trade Controls (DDTC) in July 2014, the Blue Lantern program is now managed by the Regional Affairs and Analysis Division (RAA), Office of Defense Trade Controls Policy (DTCP), Bureau of Political-Military Affairs (PM).<sup>1</sup>

Blue Lantern's mission is to help ensure the security and integrity of U.S. defense trade. Through Blue Lantern inquiries, it prevents unauthorized acquisitions and uses of U.S. defense articles, combats gray arms trafficking, uncovers violations of the AECA, and builds cooperation among defense trade partners.

Blue Lantern end-use monitoring includes pre-license, post-license, and post-shipment inquiries or checks 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."<sup>2</sup>

In FY 2014 DDTC had a full-time complement of approximately 70 State Department personnel, which is supplemented by eight active-duty military officers, approximately 65 contract personnel, a Department of Homeland Security Investigations Special Agent, and a Federal Bureau of Investigation Special Agent. In FY 2014, DDTC had a diplomatic and consular programs budget of

---

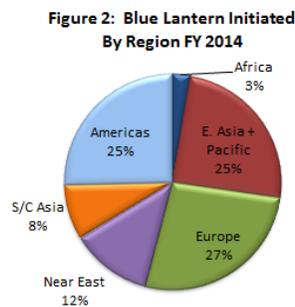
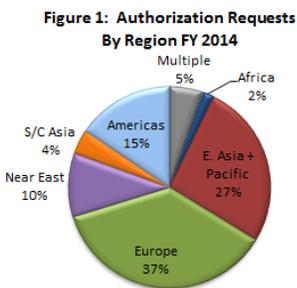
<sup>1</sup> Section 40A(c) of the AECA, as amended, requires the submission to the Congress of a report describing actions taken to implement the end-use monitoring of defense articles and defense services exported abroad, including an account of the costs and number of personnel associated with the monitoring program, known as "Blue Lantern."

<sup>2</sup> See section 40A(a)(2) of the AECA, 22 U.S.C. 2785(a)(2).

approximately \$1.5 million and received approximately \$41 million in registration fees. Six State Department employees and two contractors in RAA managed the Blue Lantern program, among other duties. End-use checks were conducted by U.S. embassy personnel. RAA staff also traveled to meet with embassy personnel, host government officials, and local businesses engaged in defense trade of U.S. ITAR-controlled items. These visits were designed to educate parties about the Blue Lantern program and U.S. defense trade controls and policy, and to elicit cooperation with U.S. end-use monitoring.

### Blue Lantern End-Use Inquiries Initiated in FY 2014

In FY 2014, the Department adjudicated approximately 63,000 license applications. RAA initiated 564 Blue Lantern checks in 79 countries. Figures 1 and 2 illustrate the regional distribution of license application requests and Blue Lantern inquiries, respectively.<sup>3</sup>



Figures 1 and 2 illustrate that the ratio of Blue Lantern checks to license application requests was relatively low in European countries with long-established U.S. defense trade relationships. The highest ratio of Blue Lantern inquiries to license application

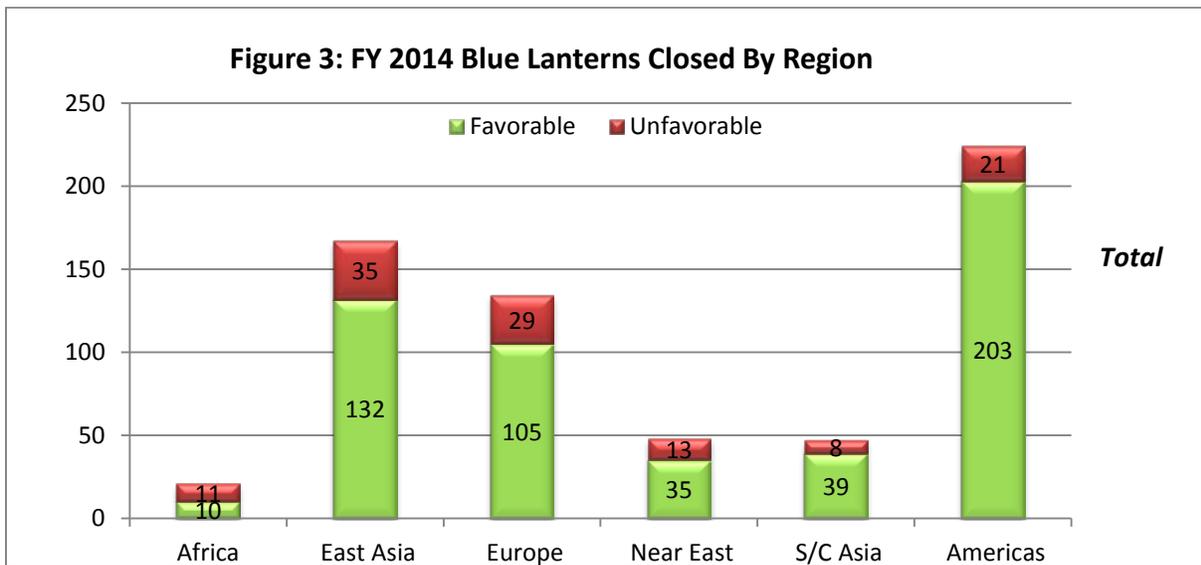
requests was in the Americas and South Central Asia due principally to concerns about unfamiliar foreign parties and the effect on regional security and stability of firearms and ammunition exports. For most of the rest of the world, checks were proportionate with license application requests.

### Blue Lantern End-Use Inquiries Closed in FY 2014

In FY 2014, RAA closed 641 Blue Lantern cases. Figure 3 illustrates the number of Blue Lantern cases closed, broken down by region. Of the cases closed, 524 (82 percent) reported “favorable” results. These favorable checks verified that defense articles were received and secured by authorized end-users, verified the bona fides of parties, especially intermediaries, and enhanced understanding of U.S. export laws and regulations.

---

<sup>3</sup> For statistical purposes, RAA attributes a Blue Lantern check to the country of the end-user listed on the license application request. Blue Lantern inquiries, however, may be initiated due to concerns over foreign intermediaries in third countries.



In FY 2014, RAA had 117 “unfavorable” Blue Lantern cases (18 percent), meaning the findings of fact were not consistent with information in the license application request. The average global unfavorable rate for the past four years is 21 percent.<sup>4</sup> In FY 2014, Africa’s unfavorable jumped substantially to 52 percent (compared to 16 percent in FY 2013), although the absolute number of checks (21) was significantly less than other regions. RAA attributes this spike not to a specific case or trend, but rather due to the targeting decisions of analysts and the limited defense trade and small number of Blue Lanterns conducted in the region. Also noteworthy, the unfavorable rate in the Western Hemisphere dropped by over half from last fiscal year, from 20 to 9 percent. There is no discernable reason for this decrease, but it may reflect a combination of the targeting decisions by analysts and improved understanding of end-use requirements by foreign parties. The unfavorable rate in the Near East region also increased, from 21 to 27 percent, creating a two-year trend. Other regions hovered around previous year averages.

In addition to verifying the security of exports and improving defense trade cooperation, the Blue Lantern program prevented and uncovered illicit export transactions and nefarious procurement agents. This included screening export license applications for “red flags,” such as unfamiliar or Watch-Listed parties, sensitive/in-demand commodities, or unusual routing. DDTC’s Watch List is an internal screening tool containing over 100,000 entities, ranging from the suspect to the sanctioned. RAA uses this database to flag export license applications for

---

<sup>4</sup> Blue Lantern checks are selected based on several risk factors, including unfamiliar foreign parties, sensitive technology, or unusual shipping routes. Because of this risk-based selection process, transactions targeted for Blue Lantern checks are more likely to result in unfavorable findings than a random sampling of license applications.

possible Blue Lantern checks. In FY 2014, RAA reviewed 16,727 Watch List name matches, or “hits” (including false hits), and made 14,270 additions, 62 deletions, and 8,496 modifications to the Watch List.

#### Reasons for Unfavorable Checks in FY 2014

Of the 117 Blue Lantern cases which ultimately were closed “unfavorable,” 65% were initiated due to the involvement of a Watch Listed party or other diversion concern, while 35% were conducted for more routine post-shipment verifications or bona fides checks. Figure 4 illustrates the reasons why Blue Lantern checks were found to be unfavorable as well as the rationale for their initiation.<sup>5</sup>

The leading cause of an unfavorable finding in FY 2014 was ***derogatory information / foreign party deemed unreliable*** (29 cases). This broad category includes criminal records, derogatory information from various sources, and concerns regarding a company’s *bona fides*. For example, a post-shipment check on multiple licenses to a firearms reseller in South America uncovered that the Director of the company had been arrested and charged with weapons smuggling and possession of unregistered weapons. In another example, a pre-license check on a Manufacturing License Agreement (MLA) to provide technical data and defense services involving satellites revealed that one of the European signatories in the MLA was dormant and had no customers nor knowledge of the transaction.

The second most common reason for an unfavorable check in FY 2014 was ***violation of license terms*** (23 cases). This total was unusually large due to an unfavorable post-shipment check on 15 licenses related to a single program involving the same parties. In this particularly egregious case, Blue Lantern inquiries revealed parties who provided misleading information regarding the actual end-use of hardware. Other cases uncovered intermediaries who ordered quantities in excess of their customer’s order or without an actual order from an end-user.

RAA had 13 instances of ***indications of diversion or unauthorized retransfer or re-export***. RAA initiated 11 of 13 checks due to a Watch List hit or other diversion concerns, suggesting effective targeting. Six of the 13 cases were pre-licenses checks, which resulted in the denial or return of those applications to prevent diversion. For example, a pre-license check for satellite components destined for a Watch Listed end-user located in East Asia revealed that the multiple intermediaries

---

<sup>5</sup> A change in the counting methodology was used in FY2014 for Reasons for Unfavorable Results to provide clarity. Each case was assigned a single, primary reason. In the past, several reasons were assigned to a single case.

Reasons for Unfavorable Results	Reasons for Checks		Total
	Routine - Bona Fides	Watch Listed Party - Diversion Concerns	
Derogatory information/ foreign party deemed unreliable recipient of USML	8	21	29
Violation of license terms	4	19	23
Unable to confirm order or receipt of goods by end-user	13	4	17
Indications of diversion or unauthorized retransfer or re-export	2	11	13
Foreign party involved in transaction but not listed on license/ application	5	7	12
Refusal to cooperate / failure to respond	5	5	10
Inability to confirm existence of a foreign party	1	6	7
Lack of secure storage facilities	2	3	5
Regional concerns	1	0	1
Figure 4: Reasons for Checks and Unfavorable Results (FY 2014)	41	76	117
Total			

involved in the transaction provided false statements regarding the actual end-user. In another case, an intermediary requested helicopter parts purportedly for end-use by a police agency. The Blue Lantern check revealed that the police never placed the order and that an unlicensed, third-party agent was involved in the transaction.

The other leading categories for unfavorable determinations in FY 2014 were generally similar to those seen in previous years. Checks continued to reveal the involvement of unauthorized foreign parties (12 cases). In some export transactions, unauthorized parties appeared to have been an administrative oversight. However, identifying all involved parties is a critical element in maintaining a secure chain of custody from U.S. exporters to foreign end-users. Lack of transparency on involved parties increases the risk of diversion to unauthorized end-users and end-uses.

Blue Lantern checks revealed 17 instances where the end-user was ***unable to confirm order or receipt of goods***. RAA closed 10 Blue Lanterns unfavorable due to ***refusal to cooperate*** and seven because of the ***inability to confirm the existence of a foreign party***.

Unfavorable Blue Lantern cases resulted in several types of actions, including returning or denying license applications, removing parties from licenses, revoking licenses, updating the Watch List, or referring the case to the Office of Defense Trade Controls Compliance (DTCC) and/or U.S. law enforcement agencies for appropriate civil and/or criminal enforcement investigation and action. In FY 2014, pre-license checks led RAA to recommend denial of 14 license application requests, return of 23, and revocation of one. In FY 2014, RAA referred 11 unfavorable Blue Lanterns to DTCC, which in turn directed companies to disclose information related to suspected ITAR violations. RAA referred one unfavorable Blue Lantern case to U.S. law enforcement for criminal investigation.