

**INTERNATIONAL AFFAIRS FUNCTIONS OF
THE TREASURY AND THE EXPORT
ADMINISTRATION ACT**

HEARINGS

BEFORE THE

**SUBCOMMITTEE ON INTERNATIONAL FINANCE
AND MONETARY POLICY**

OF THE

COMMITTEE ON

BANKING, HOUSING, AND URBAN AFFAIRS

UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

FIRST SESSION

ON

**THE INTERNATIONAL AFFAIRS FUNCTIONS OF THE DEPART-
MENT OF THE TREASURY; AND THE EXPORT CONTROL SYS-
TEM FOR COMMERCIALLY AVAILABLE COMMODITIES AS
ADMINISTERED BY THE DEPARTMENT OF COMMERCE AND A
GROUP OF CONSULTING AGENCIES**

APRIL 30, 1981

Printed for the use of the
Committee on Banking, Housing, and Urban Affairs

[97-16]



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON: 1981

79-280 O

5241-33

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INTERNATIONAL AFFAIRS FUNCTIONS OF THE TREASURY AND THE EXPORT ADMINISTRA- TION ACT

THURSDAY, APRIL 30, 1981

U.S. SENATE, COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON INTERNATIONAL FINANCE
AND MONETARY POLICY,
Washington, D.C.

The subcommittee met at 9:40 a.m. in room 5302 of the Dirksen Senate Office Building, Senator John Heinz (chairman of the subcommittee) presiding.

Present: Senators Heinz and Garn.

OPENING STATEMENT OF SENATOR HEINZ

Senator HEINZ. The purpose of today's hearing is to review the international affairs function of the Treasury and the Export Administration Act in order to garner the information necessary to reauthorize these two important functions.

The subcommittee will hear witnesses from the administration and the General Accounting Office, and further hearings on the subjects may be held later in the year, after the nomination process has been completed. We hope it will be completed, but for now it is necessary to press ahead with the reauthorizations to meet our May 15 deadline.

I might say that of late the news on the dollar has been good. It has been stronger than it has been in many years. It has regained most of the value it had lost against other major currencies over the last year or two. But that is, of course, not an unmixed blessing. A strong dollar means, theoretically, less competitiveness for U.S. products on the world markets.

And the days are long gone when we could ignore the international marketplace or insulate our economy from its effects. Happily, however, many of the things that we market internationally are less price-sensitive than one might otherwise expect.

We will hear from a representative of the Treasury, the Department charged with defending the dollar as well as representing our Nation in negotiations for international trade. The administration has enunciated a new policy of nonintervention in currency markets to let the market work its will. It will be interesting to get some of the details and parameters of that new strategy.

As my colleagues on the committee and I think the Treasury representatives here today know, I have been vitally involved in urging an aggressive negotiating policy, both to this and the last

administration, with regard to officially subsidized export credits. The French at the last OECD meeting in December refused to really negotiate this issue in good faith, and their refusal to do so is, in my judgment, unconscionable. And, as I said in my letter to the President on March 19, I would no more counsel unilateral disarmament for dealing with our allies on trade matters than counsel such a strategy for dealing with the Russians on matters of national security.

To that end, I have introduced the Competitive Export Financing Act of 1981, to provide our trade representatives with the negotiating chips necessary in order to be taken seriously at the next round of credit negotiations in Paris on May 12, and thereafter, if necessary (see p. 111). I would be interested in the comments of Treasury on that bill, and on the aggressive strategy that I have put forward on the export credit issue.

Turning to the Export Administration Act, you cannot escape a sense of *deja vu*. Two years ago, when this same subject was chaired by Senator Stevenson, we heard a report from the GAO on the inadequacy and inefficiencies of the export control process. We heard complaints that the process was inconsistent, plagued by uncertainty and vagueness, threatening to undermine our representation as a reliable supplier in the world marketplace. Others warned that significant technology would still slip through the export control net, which would strengthen the warmaking capacity of our adversaries.

Unfortunately—although I believe the 1979 Act was a significant improvement over its predecessor—the complaints about the process have not yet gone away. The administration of this act has not been all that it could have been, or all that the authors, such as myself, envisaged.

We need not be faced with the unpleasant choice of inefficiency and delay or the leakage of sensitive national security-related technology. Export sales and security can be reconciled. That is what my colleagues and I intended in writing the 1979 act, and that is what good administration of the act ought to achieve.

In the area of foreign policy control, my predecessor, Senator Stevenson, was fond of noting that we were prone to shoot ourselves in the foot. What I find remarkable is not the original event so much as our capacity to quickly reload and repeat the process. [Laughter.]

As President Reagan, has noted, we are ill-served by controls which hurt us more than they do the intended target. Wisely applied—particularly if they are multilateral—export controls can be a vital and effective tool of foreign policy, but done on an *ad hoc* basis, or in a fit of pique, or extremist, export controls can be terribly counterproductive. Indeed, they can signal the opposite of the strength they are intended to project. Let's hope that our new, brightly scrubbed administration has learned from the errors of its predecessors, and is not doomed to repeat them.

Our first witness will be Tom Leddy, Assistant Secretary of the Treasury for International Affairs.

And if you want to summarize your statement, it is always appreciated by everybody. I have had some summaries that go

much longer than if they had been delivered, so please feel free to summarize.

Mr. LEDDY. I will be brief. Let me introduce Cora Beebe, Assistant Secretary for Administration of the Treasury; John Lange, Acting Deputy Assistant Secretary for Trade and Investment Policy, who has been intimately involved in the export credit negotiations; and John Ostrowski, Budget Officer for International Affairs.

STATEMENT OF THOMAS LEDDY, ACTING ASSISTANT SECRETARY FOR INTERNATIONAL AFFAIRS, TREASURY DEPARTMENT, ACCOMPANIED BY CORA BEEBE, ASSISTANT SECRETARY FOR ADMINISTRATION; JOHN LANGE, JR., DIRECTOR, TRADE FINANCE OFFICE; AND JOHN OSTROWSKI, BUDGET OFFICER, INTERNATIONAL AFFAIRS

Mr. LEDDY. The committee has asked that I speak on the authorization for the international affairs function of the Treasury, the international position of the dollar, and the status of the export credit arrangements.

On the authorization, we are requesting \$23.9 million for fiscal year 1982. This includes \$22.9 million for the basic program, and an additional \$1 million to permit us to return, if necessary, to the appropriations committees during 1982 for supplemental funding to cover the cost of any civilian pay raises or overseas cost-of-living allowance increases that take place during the year.

What we are requesting this year represents continuation of a very considerable reduction in staffing in the international affairs area of the Treasury, from a level of about 555 positions 5 years ago to the 428 positions we are requesting for fiscal 1982.

We have made a consistent effort to reduce the cost of the international affairs function as much as we can, while trying to keep the staffing up to where we can properly serve the Secretary's role in this area.

You commented on the recent strength of the dollar. This is due to a number of factors—a relatively strong U.S. current account, relatively high U.S. interest rates and the attractiveness of investments in dollars. There have also been political developments in eastern Europe that have tended to stimulate flows into the dollar.

I think, basically, there has also been a change in psychology toward the dollar from the situation of, say, 2 years ago. There is a growing perception abroad that this Administration is absolutely determined to solve the problems of inflation, low productivity and slow growth of this economy.

If we can do that, if the administration's program can succeed in those objectives, I think basically the dollar will be strong. The dollar will be stable. And that essentially underpins the approach of this administration. It will be a policy of returning to the fundamentals. Minimal intervention in the exchange markets in support of the dollar complements this approach. If we are successful, I am encouraged about our economy's ability to compete.

On the export credit negotiations, you have outlined where we stand.

Senator HEINZ. Unilateral disarmament?

Mr. LEDDY. I don't think it is unilateral disarmament. I would ask Mr. Lange to comment in more detail on that. But the situation is totally unsatisfactory.

This administration will continue to assign very high priority to negotiating this issue. We are negotiating seriously. Secretary Regan has made this clear. We are looking for ways to put more teeth into our position. We intend to negotiate seriously, and let our trading partners know that we mean it.

I cannot be terribly optimistic about the short-term prospects. But we do attach high priority to this and I hope that we will have some significant negotiating progress later this year.

That summarizes the three main points covered in my statement.

Senator HEINZ. Very well. Let me ask you, first, about some of the international monetary functions that you are involved with. Beryl Sprinkle stated recently the Treasury would only intervene in foreign exchange markets in emergency situations. Would this preclude participation in swap agreements with our allies, in cases where continued deterioration caused concern?

Mr. LEDDY. Not necessarily. He was commenting on our own intervention policy in the dollar market. I think we very much want to maintain strong cooperative relationships with the other major countries with which we maintain the swap network. I would not rule that out; if another country is in serious difficulty, I think we would be receptive to helping them out.

Senator HEINZ. I gather you see no need to establish a floor at which the dollar would have to be supported?

Mr. LEDDY. No, sir. I think it would be a great mistake to try to pick a level. I think we are incapable of that. The market has demonstrated repeatedly that attempts to do that really don't succeed for very long, if you are wrong—and people have very seldom been right.

Senator HEINZ. Britain's great statesman said he would rather be asked why he did not make a statement than why he did make a statement.

Why did the administration feel constrained to state the new nonintervention policy, particularly because such an authoritative statement is likely to lead to speculators' betting against the dollar when it begins to drop relative to other currencies.

Mr. LEDDY. There would undoubtedly be questions about what policy would be followed. I think it is preferable to articulate it fairly carefully.

Senator HEINZ. Why?

Mr. LEDDY. So it can be explained, carefully —

Senator HEINZ. That is not a reason.

Mr. LEDDY. If a policy —

Senator HEINZ. Who are we trying to help in articulating this policy?

Mr. LEDDY. I think we are trying to be clear on what the policy is.

Senator HEINZ. Clarity is not a virtue in and of itself. It is only a virtue with respect to a particular end you hope to achieve. I don't hear what particular end you hope to achieve.

Let me put it another way. Let's go to national defense. People want to know what our policy is on the use of nuclear weapons.

They want to know whether we will entertain the possibility of the first strike, or whether we won't. Should we tell them? And the answer, as you know, is no, we shouldn't. Why should we tell everybody what our policy is? What is the point of telling people, clearly or unclearly? That is a stylistic concern.

Mr. LEDDY. This administration, in contrast with the policies of the last few years of the last administration, wants to place greater reliance on market forces, generally, and specifically in the exchange area. The levels of intervention in the past few years did get very heavy. I'm not trying to convey criticism. There was a completely separate set of circumstances from today. This administration wanted to explain that its approach would be different. It would become clear that the approach was different, but less clear what the approach was, unless it was articulated.

Under Secretary Sprinkle will be testifying next week, and will lay this out in greater detail, presenting it as a component of the administration's overall economic policy. I think that is desirable. Actions inevitably raise questions, and the answers, unless they are stated clearly, inevitably raise uncertainty about what is being done. I think it is desirable to explain the approach.

Senator HEINZ. You may be right. I think as a personal matter it is possible to get the point across that we do not agree with the massive interventionist policies of the Carter administration and our general philosophy is we believe the market forces should be the principal determinant of the rise and fall of currency.

Do you think it is wise to go beyond that, and say, in effect, that, "Here are the very limited set of conditions under which we would consider intervention?"

Mr. LEDDY. We have not specified the conditions under which we would. This is not a statement of absolute, never-under-any-circumstances intervention.

Senator HEINZ. Let me ask you a different question. It has been said by a number of people that the new strengthened dollar will have an adverse effect on U.S. trade competitiveness in the latter half of 1981. Do you agree with that?

Mr. LEDDY. Yes. I think it will have an impact. Two points: One, measuring from what reference point? You have to look at the base you are measuring from. Certainly, measuring against the low point of the dollar, there will be an impact. I think, in fact, in retrospect, it has been shown that the low point for the dollar—exports did benefit from very low dollar exchange rates in terms of our competitive position.

Two, the U.S. export performance in the last 2 years has been remarkable. U.S. exports rose at a rate more than twice the rate of growth of world trade between 1978 and 1980. Our overall trade position has improved, despite still massive increases in oil import costs.

Senator HEINZ. Has our market share of manufacturers grown?

Mr. LEDDY. Yes, it has. I don't have the figures here. I could supply them.

Senator HEINZ. Have we improved our market share to the more developed countries? The OECD countries?

Mr. LEDDY. I don't have the details. I believe so. Yes.

Senator HEINZ. You believe our export performance on balance has been healthy?

Mr. LEDDY. Yes, it has been extremely healthy in the last 2 or 3 years. Remarkable, in terms of the several years before.

Senator HEINZ. What product categories in that export performance do you believe have benefited particularly by the then weakness of the dollar?

Mr. LEDDY. I can supply details. Manufactured goods, capital goods exports, have done very well in the last couple of years.

[The following article and table from the April 6, 1981, issue of "Business America," published by the Commerce Department's International Trade Administration, show quarterly figures for the U.S. share of world exports of manufactures, from 1976 through third quarter 1980 for total manufactures and beginning in 1978 for major subcategories as well:]

U.S. Manufactures Share Levels In Third Quarter Of 1980

*Prepared by the Office of Planning and Research,
International Trade Administration*

The U.S. share of world exports of manufactures remained almost unchanged in the third quarter of 1980 following a strong gain in April-June. At 18.5 percent, the U.S. position was less than one-tenth of a percentage point higher in July-September than in the second quarter. Although these U.S. exports increased in value at a slightly faster rate than in the preceding three months, our competitors' sales to foreign countries advanced about as rapidly so that our relative position did not change. The U.S. share position in the two middle quarters of 1980 was at its highest level since late 1976, but nevertheless remained far below the 21.3 percent share achieved in 1970.

U.S. exports of manufactured goods advanced by 4.6 percent in the third quarter of 1980. Overseas shipments by the other 14 leading manufactures exporters as a group, on the other hand, rose by 4.3 percent in that period. Several of our competitors—principally Sweden, Japan, and the United Kingdom—reported faster growing exports than did the United States.

Our position continued to be maintained in the third quarter primarily because of a considerable increase in the U.S. share of the chemical market. There was also a slight gain in our position in nonelectric machinery exports. These were more or less balanced by sizable deteriorations in our relative position in transport equipment, electric machinery, and miscellaneous manufactures, which are largely consumer-type products.

The leveling in the overall U.S. share of manufactures exports occurred despite a decline in the value of the dollar relative to the currencies of our competitors. The drop in the dollar's value averaged 2-3 percent in the third quarter of 1980. Such a decline tends to increase the value of other countries' trade when their national currencies are converted to dollars.

Competitor Nations. The competitive position of the majority of the other major exporters of manufactures was relatively unchanged in the third quarter of 1980. Japan's share, however, increased strongly, and the Swedish and the British positions also improved. Germany and Belgium, on the other hand, sustained share losses.

The Federal Republic of Germany, the world's leading exporter of manufactures, recorded its second consecutive quarterly share loss. Its third quarter share of 19.7 percent dipped below the 20 percent level for the first time since late 1975. German exports of manufactures rose by only 2.7 percent in value in the third quarter. This recovery, which followed a decline in the previous quarter,

was not sufficient to raise exports to the level achieved in January-March. Belgium's position also weakened to 5.6 percent, a half percentage point decline from the preceding quarter.

The Japanese share, in contrast, continued to move strongly upward in the third quarter. The value of Japanese exports of manufactures jumped by 8.6 percent from the April-June level and its share, at 12.3 percent, moved to the highest level since mid-1978. Sweden posted the largest gain in the value of exports, with a 23 percent climb in overseas deliveries. As a result, that country's share rose to 3.1 percent. Britain's share also increased during July-September, to 10.0 percent.

Commodity Groups. It should be noted that the commodity share data shown in the adjoining table are based on data which have not been adjusted for seasonal variation, while data from which the total manufactures shares were calculated have been so adjusted. Since there is a considerable seasonal shift in trade between the second and third quarters, the share calculations for commodity groups and that for the total cannot be directly compared.

The largest U.S. share loss occurred in transport equipment, where our share fell by nearly a full percentage point to 21.6 percent. U.S. exports of this equipment, which are typically erratic, soared in value in the second quarter, then abruptly declined in the third by 11.4 percent. Among our largest competitors, the French and German positions also weakened, but that of the U.K. moved upward. Japan's share jumped by nearly four percentage points to 19.0 percent as auto exports soared.

The U.S. position also weakened significantly in electric machinery and in the miscellaneous manufactures group. In electric machinery our share declined to 19.2 percent, as U.S. exports dropped slightly after a substantial increase in the second quarter. Germany's share of electric machinery also fell, while Japan's rose by three full percentage points to 22.4 percent. U.S. exports in the miscellaneous manufactures group declined for the second consecutive quarter, following the exceptional position in January-March when exports in this group soared as a result of unusual shipments of coins. Our three largest competitors in this commodity are—Germany, Italy, and Japan—all recorded strong share increases.

The only sizable U.S. share rise was in chemicals. At 20 percent, our share was two and a half percentage points above that in the first quarter. It was the second consecutive quarter that there was a large improvement in our position. Among our principal competitors in these products, Germany, France, and the United Kingdom recorded share losses, only the Dutch share expanded

U.S. SHARE OF WORLD EXPORTS OF MANUFACTURES

Commodity	U.S. exports (million dollars)	U.S. share * percent of world ex-manufactures	Commodity	U.S. exports (million dollars)	U.S. share * percent of world ex-manufactures
Manufactures, total (SITC 5-8)			Electric machinery (SITC 76 & 77)		
1976	77,241	18.8	1978	9,655	17.8
1977	80,157	17.3	1978 1st qtr	2,153	18.2
1978	94,546	17.0	2nd	2,444	18.3
1979	116,678	17.4	3rd	2,426	18.1
	(Seasonally Adjusted)		4th	2,632	16.4
1976 1st qtr	18,213	19.0	1979	11,591	18.5
2nd	19,245	19.3	1979 1st	2,682	18.3
3rd	19,622	18.7	2nd	2,935	19.5
4th	20,069	18.4	3rd	2,832	18.6
1977 1st	19,797	17.7	4th	3,142	17.8
2nd	19,928	17.6	1980 1st	3,266	19.1
3rd	20,319	17.4	2nd	3,540	19.7
4th	20,133	16.6	3rd	3,466	19.2
1978 1st	20,667	16.2	Transport equipment (SITC 78 & 79)		
2nd	23,000	17.0	1978	22,248	22.4
3rd	24,409	17.3	1978 1st qtr	4,637	20.2
4th	26,458	17.2	2nd	5,850	22.6
1979 1st r	27,052	17.4	3rd	5,172	23.1
2nd r	27,786	17.3	4th	6,589	23.2
3rd r	30,454	17.5	1979	25,751	22.7
4th r	31,569	17.3	1979 1st	6,306	23.6
1980 1st r	34,175	17.4	2nd	6,634	23.3
2nd r	35,525	18.4	3rd	6,030	22.8
3rd	37,156	18.5	4th	6,781	21.3
	(Not Seasonally Adjusted)		1980 1st	6,842	22.1
Chemicals (SITC 5)			2nd	7,312	22.5
1978	12,618	17.3	3rd	6,480	21.6
1978 1st qtr	2,744	16.4	Basic manufactures (SITC 6)		
2nd	3,053	16.7	1978	12,467	8.7
3rd	3,424	19.0	1978 1st qtr	2,746	8.5
4th	3,397	16.9	2nd	3,182	9.0
1979	17,306	17.9	3rd	3,097	9.1
1979 1st	3,913	18.1	4th	3,442	8.3
2nd	4,124	17.2	1979	16,236	9.2
3rd	4,570	18.4	1979 1st	3,641	9.1
4th	4,699	17.8	2nd	4,052	9.3
1980 1st	5,035	17.4	3rd	3,933	9.3
2nd	5,464	19.3	4th	4,610	9.1
3rd	5,218	20.0	1980 1st	5,265	9.9
Nonelectric machinery (SITC 71-75)			2nd	6,022	11.2
1978	27,367	23.0	3rd	5,508	11.1
1978 1st qtr	6,148	22.9	Misc. manufactured articles (SITC 8)		
2nd	7,011	23.5	1978	10,191	15.0
3rd	6,631	23.4	1978 1st qtr	2,254	14.8
4th	7,577	22.0	2nd	2,627	16.3
1979	33,150	23.9	3rd	2,525	14.7
1979 1st	7,775	24.7	4th	2,811	14.3
2nd	8,327	24.4	1979	12,644	15.1
3rd	8,067	24.1	1979 1st	2,924	15.4
4th	8,981	22.6	2nd	3,113	15.9
1980 1st	9,507	24.7	3rd	3,118	14.5
2nd	10,821	25.9	4th	3,489	14.5
3rd	10,546	26.1	1980 1st	4,528	18.2
			2nd	3,935	16.5
			3rd	3,846	15.1

NOTE: Beginning in 1978, data for all countries except Canada and Japan are reported according to Revision 2 instead of Revision 1 of the United Nations Standard International Trade Classification (SITC). Canadian data are reported according to Revision 2 beginning in 1979. Since some types of manufactures were shifted from one classification to another in 1978, data for earlier periods are not

shown for the separate product categories. The figures for total manufactures, however, are reasonably comparable and therefore are shown.

* U.S. exports of its major industrial countries to the world, excluding re-exports to the United States.

r—Revised

Senator HEINZ. You believe they have done so across the board?

Mr. LEDDY. Generally, yes.

Senator HEINZ. If, as you suggest, a stronger dollar is going to impact adversely our export performance toward the end of this year, is there anything that we should do to ameliorate that performance?

Mr. LEDDY. It will have some impact. I would not overstate it. I think, basically, the main thing that we have to do is get inflation in this economy under control. That is the fundamental determinant of our export performance. That is what we have to focus on. Obviously, we have to follow up on efforts to reduce export credit subsidies. But the fundamental point is to get this economy in shape, and we will be successful if we can do that.

Senator HEINZ. Let's turn to the OECD negotiations. Secretary Baldrige was quoted in the Washington Post, promising to restore Eximbank funding next year, if the United States is unsuccessful in its attempt to induce our OECD counterparts to reduce their export subsidies. Would you be willing to, later on this year, join in such a campaign?

Mr. LEDDY. Can I ask Mr. Lange to respond to that?

Mr. LANGE. Thank you, Mr. Chairman.

The Treasury would certainly join in recommending ways to strengthen the U.S. marketing position by international export credits, if the negotiations are not successful. Among the options to be considered would be an increase in Eximbank's financial guarantee program, which is a rough substitute for a direct lending program. And also, we would similarly give thorough, and thoughtful consideration to the chairman's bill, which is also a very effective device in this regard.

Senator HEINZ. Would you be prepared to advocate credits?

Mr. LANGE. Not only are we prepared, we are advocating it now. If the Chairman would permit me, I can indicate a change, shift in strategy that has occurred. We would recommend to the Chairman to allow us the opportunity to give it a try.

In the past, the administration decided to fight fire with fire. As the Chairman knows, the previous administration asked for, and Treasury supported strongly, increases in the Eximbank's direct loan budget to as high as \$5.5 billion in fiscal year 1981. At the close of the last administration we realized, quite frankly, that this strategy was not working. We were still negotiating from weakness, even though we were matching foreign export credits often. We thought that if we matched, there would be no gain in it for countries that wanted to continue to subsidize their exports, particularly France. That strategy was not successful. Such countries, in effect, said the United States is joining us in our policies, and so be it.

Where it does hurt those countries who are recalcitrant is when the United States draws from its strength, which is going out in tenor in excess of 10 years on credits for projects which are suitable and have a useful life in excess of 10 years. Accordingly, that is our current strategy.

We should not worry so much about the size of the Eximbank's direct loan budget. Even if it were doubled or tripled, we are not confident that that would necessarily bring about an international

agreement to reduce export credit subsidies. And certainly, with respect to the budget, in times when we are trying to cut back on public spending, and to increase the productivity of our industries by cutting back on taxes, and to increase defense expenditures, it would be imprudent in our judgment to not cut back somewhat on the Eximbank budget.

We would hope Eximbank would use its budget judiciously, use it carefully, and not match in every case, as essentially it did in the last administration. Indeed, as the Chairman knows as a result of the hearings you held, from Treasury's point of view the matching was overdone in some instances. Those very large projects such as the Ansett aircraft loan were very expensive, in terms of the budget.

What Eximbank is doing now and has done in four cases so far, is to go out in term and up in interest rate. This will make the Bank more self-sustaining. When the Bank offers very long terms the French, for example, have difficulty matching.

The way the French budget system works, the longer the term, the less they can discount their export credit paper through the Bank of France. France essentially discounts through its Central Bank credits which are shorter in term than 7 years. The very long-term credits, in excess of 7 years, have to be funded just the way Eximbank does on its direct credits. The French have to go to market. When they go to market, with the French market rates as high as they are, it hurts the French Treasury to subsidize their export credits just as it hurts us to do that. In other words, the subsidies are apparent and not masked by a central bank discount procedure.

The more Eximbank derogates in term, the more the French, and other recalcitrant countries are forced to derogate in term. With this policy we will be negotiating from strength.

If we derogate generally, however—across the board on everything and in every industry—we do not think it would be productive. The French or others might accept that longer terms for a particular industry are required from now on.

Senator HEINZ. Have you considered in particular, going into those markets that have been, traditionally the reserve of the French, or anybody else, who has really ignored the arrangement, or who has simply gone in for obstructionism in the OECD. The French certainly have done that.

Mr. LANGE. In the case of the French, we already have gone into their traditional market. For example, in the Ivory Coast, in two cases, Eximbank derogated in respect of term. And in one case, a communications project, the United States manufacturer won the bid over a French manufacturer.

Senator HEINZ. That took place last year.

Mr. LANGE. In December, sir.

Senator HEINZ. The new administration cannot claim that one. Mr. Ulmer was hired by the Commerce Department as Under Secretary. He happened to be a part of that, as I understand it.

Mr. LANGE. I am not aware of that, sir. Of course, during this time—it was a time of transition. We would not have moved forward in this respect if we were to have to reversed ourselves in a

month. In all fairness, this was an unstated policy of the new administration.

Senator HEINZ. The point is, that it is now a stated policy. It sounds like you and I pretty much agree. I assume you have read my letter of the 19th.

Mr. LANGE. Yes.

Senator HEINZ. Do you have any disagreements?

Mr. LANGE. No, sir. I thought it was a very well-written letter.

Senator HEINZ. Flattery will get you someplace. [Laughter.]

Mr. LANGE. The points are well-taken. It is not that it was well-written; that's form. The substance was good, as well, sir.

Senator HEINZ. You have no policy disagreements, other than that you do not want to—I could be contentious and say that that means that you endorse my bill, but I know you don't mean that at this time.

Mr. LANGE. I was hoping you wouldn't ask that.

Senator HEINZ. Do you believe that with the funding of the Eximbank at current levels that you can be credible in these negotiations regardless of how hard you work to make due with the resources available? My concern is that Exim is already overcommitted. How do you convince the French that although in December of last year we snuck into the Ivory Coast, that we have the ability to do that, post-May, which is what they have to worry about. If they can sneak past May, from their point of view, they have a free, wide field.

Mr. LANGE. There are two elements to that. One is that in the past we have considered the Export-Import Bank's budget to be not only the star in the crown, but even more colorfully characterized, the major weapon to use to try to bring some discipline in the arrangement on Export Credits. That is important but we have not used other systems. We are now convinced that we need much more than simply an Eximbank budget. The other element, therefore, is the need for a strong political will, one which is demonstrated by senior officials of the administration. And as Mr. Leddy pointed out, we have that. This issue is a very high priority in the mind of the Secretary of the Treasury.

Deputy Secretary McNamar, after the IDB meeting, made a round of trips to London, Paris, and Bonn, with the express purpose of letting our trading partners know that this administration considers the reduction of export credit subsidies of the highest priority. It is absolutely antithetical to the Reagan administration's efforts to increase productivity, to stand by while foreign countries subsidize the export of perhaps less productive firms.

I think with that political will, and it will take political will more than just technical work to succeed. The technicians have really done all the technical work. In fact, Peter Gerring, the German delegate, said there are no more questions to ask; all of the questions are answered in terms of the techniques to reduce export credit subsidies. The techniques have been in place a year. What it will take now is a strong political will. That means other measures than simply derogating or increasing Eximbank's budget.

Senator HEINZ. Mr. Leddy. Thank you. I note the chairman of our committee, Senator Garn is here. He is here for two reasons. He is here because he has a great deal of interest in this subject,

and the next subject, the Export Administration Act, which he has been quite a leader in and has gone over with a fine-tooth comb, and he is also here, I hope, because he knows that I have a markup in the Finance Committee, disposing of roughly \$9 or \$10 million of cuts in entitlement programs we are going to be deciding on.

So Mr. Chairman, I appreciate your being here for that reason as well. I have completed my questioning of the Treasury witnesses. Let me, if I may, turn the hearing over to the chairman.

Senator GARN [presiding]. We are playing musical Senators. I am chairman of the HUD, Independent Agencies Subcommittee which is holding hearings on the National Science Foundation appropriations. But I have a good substitute. I have Senator Schmitt. He knows far more about science than I do. And he just replaced me, so I could come up and replace John. So wherever you are going—[Laughter.]

I have no questions of this panel, unless you have any concluding statements or anything you would like to add.

Mr. LEDDY. I have nothing further.

Senator GARN. Thank you very much.

[Complete statement follows:]

Statement of Thomas Leddy
Acting Assistant Secretary of the Treasury for International
Affairs
before the
Subcommittee on International Finance and Monetary Policy
of the
Senate Committee on Banking, Housing and Urban Affairs
April 30, 1981

Mr. Chairman, I am pleased to appear before your Subcommittee in support of the authorization of appropriations for the Treasury's international affairs functions. I understand that the Subcommittee is also interested in the Treasury Department's views on the international position of the dollar, and the status of export credit arrangements in the OECD, and I will comment on those points as well.

Authorization for International Affairs

We have requested an authorization of \$23.9 million for fiscal year 1982. This includes \$22.9 million for the basic programs planned for fiscal year 1982 and an additional \$1.0 million that will permit us to return, if necessary, to the appropriations committees during 1982 for supplemental funding to cover the cost of any civilian pay raises or overseas cost-of-living allowance increases that take place during that year.

The basic authorization of \$22.9 million that we have requested for 1982 reflects the President's budget request for Treasury's international affairs programs. In keeping with the President's program of reducing the size of the Federal Government, our 1982 budget request reflects a net reduction of \$767 thousand from the current year funding levels. Similar reductions are included in our proposed authorizing legislation. For 1981, this committee approved funding authorizations of \$24.8 million for

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Treasury's international programs. The bill before you today reflects a decrease of approximately \$900 thousand from last year's level.

The Secretary of the Treasury has a variety of responsibilities in the area of international economic and financial policy that are based on statutes, Executive Orders and his traditional role as chief financial officer of the Government. The Secretary serves as Governor for the United States in the International Monetary Fund, the World Bank Group and the regional development banks, and directs the Treasury's activities in the Organization for Economic Cooperation and Development. In addition, the Secretary is co-chairman of the U.S.-Saudi Arabia Joint Economic Commission and serves as chairman or member of a number of other bilateral groups that deal with issues of particular concern to the U.S. economy. The Secretary oversees U.S. international monetary policy and operations; represents the United States in bilateral and multilateral negotiations of international financial and economic issues with other nations; and is a key advisor to the President at Economic Summit meetings. As the chief financial officer of the Government, as economic spokesman for the President, and as chairman of the Cabinet Council for Economic Affairs, the Secretary must assure that the entire range of U.S. international economic, financial and monetary policies is consistent with and supportive of both our domestic economic requirements and our interests in the global economy.

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Assurance of proper support for the Secretary and other senior Treasury officials in fulfilling these responsibilities requires competent and highly professional staff, able to respond creatively and promptly to often rapidly changing international circumstances. The staff must maintain a high degree of current knowledge of economic conditions and policies abroad, while maintaining the ability to develop, represent, and negotiate U.S. policy positions and interests with their counterparts abroad. Much of this substantive staff work is performed within the Office of the Assistant Secretary for International Affairs in areas dealing with trade and investment policy, commodities and natural resources policy, policy dealing with financing international development, international monetary affairs and our economic and financial interests in the Middle East. The international affairs programs also are involved in a wide range of issues dealing with international taxation, including the development and negotiation of tax treaties with a number of foreign governments. Additional staff support is provided on legal matters, legislative liaison and general administrative operations.

The request we have made for fiscal year 1982 represents, in our judgement, the minimum amount necessary to enable us to carry out the Treasury's international responsibilities while being consistent with and contributing to the President's efforts to control the rising cost of government.

We have included in our request a provision for authorizing such sums as may be necessary for fiscal year 1983.

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This concludes this portion of my statement, Mr. Chairman. I urge the subcommittee to act favorably on this request. I would now like to turn to the international position of the dollar and the export credit arrangements.

The Position of the Dollar

The position of the dollar in international markets reflects the relative performance of the United States economy compared with that of other major countries, and expectations regarding future trends. During the last decade countries experienced sharp increases in energy prices; slow, uneven and in some cases negative growth rates; and serious inflationary pressures. The performance of the U.S. economy, however, declined relative to the performance of other major currency countries, including Japan and Germany. This was particularly true with respect to inflation and productivity. As a consequence, the dollar fell against the yen and mark during much of the last decade.

The dollar has been on a firming trend in the foreign exchange market since last summer. Since the first of the year, the dollar has appreciated against all major foreign currencies, rising on a trade-weighted basis against other OECD currencies by about 5 percent. The dollar has been particularly strong against the currencies within the European Monetary System. The exchange market's behavior has suggested growing confidence in the dollar, and a conviction that the Reagan Administration is determined to succeed in its effort to correct the fundamental problems of inflation and low productivity in the U.S. economy.

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The recent strength of the dollar also reflects the relatively favorable U.S. current account position -- the balance on goods and services and unilateral transfers. The U.S. current account has been in approximate equilibrium over the past two years and is expected to remain roughly in that position again this year. In contrast, the current account positions of most major foreign countries have been in substantial deficit.

The foreign exchange markets, certainly so far as the dollar is concerned, have functioned relatively well in recent months, although some pressures have developed from time to time on other currencies. Exchange rates have tended to fluctuate rather widely from day to day, but the markets have shown a good ability to regain balance quickly and without undue strain. In large part, the short-run exchange rate movements we have witnessed have been influenced by domestic economic and financial instability, in particular wide fluctuations in short-term interest rates and changing expectations. The only sure way to reduce exchange rate volatility is for the leading countries to improve the performance of their economies.

A major objective of this Administration's domestic program is to restore the U.S. economy as a source of stability and growth for the larger world economy. Monetary and price stability on the domestic front will go a long way towards permanently restoring confidence in the dollar and will contribute to stability in the international as well as the domestic financial markets. Cuts in marginal tax rates, control over the growth of government expenditures and regulatory reform will increase

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saving and investment and lead to a more dynamic and innovative U.S. economy. As a consequence, the international competitive position of the U.S. economy will be strengthened.

Negotiations on the International Arrangement on Export Credits

The negotiations to reduce export credit subsidies will have a continuing high priority for the United States under the Reagan Administration. The present international export credit Arrangement in the OECD is not adequate. It condones subsidies estimated by the OECD staff to have been as much as \$5.5 billion in CY 1980.

Its minimum interest rates apply to all currencies, irrespective of financial market conditions that differ widely from currency to currency. The following table contrasts the secondary market yields of several of the major trading currencies with the export credit interest rate most frequently charged:

<u>Currency</u>	<u>Export Credit Rate Most Frequently Charged</u>	<u>Long-Term Government Bond Yield (February 1981)</u>	<u>Subsidy Difference</u>
French franc	8.35%	15.05%	6.70%
British pound	8.10%	13.84%	5.74%
Deutsche mark	8.90%	9.8%	0.90%
Japanese yen	7.85%	8.79%	0.94%
U.S. dollar	8.60%	12.23%	3.63%

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For the past three years, the United States has sought to improve the export credit Arrangement by bringing its minimum interest rate requirements closer to financial market conditions. In 1980, a report prepared by the Chairman of the OECD Export Credits Group, (Mr. Wallen of Sweden), proposed two simple alternatives to the static and rigid interest rate matrix of the present Arrangement.

The first alternative was to weight the yields of government bonds in the five major trading currencies by the weights they have in the basket comprising the IMF's Special Drawing Right (SDR). The basket interest rate that emerged from the sum of the five weighted interest rates would, under this proposal, become the benchmark for the new minimum export credit rates, applicable to all currencies. This alternative was titled the Uniform Moving Matrix or UMM.

The second alternative, the Differentiated Rate System or DRS, would use the secondary market yields on long-term government bonds in each currency to determine the minimum export credit rate. In both systems, the benchmark interest rates would be adjusted periodically to take account of financial market movements.

At a meeting in May 1980, the United States indicated its preference for the DRS system, inasmuch as it most effectively reduced export credit subsidies. Most other countries, however, indicated they preferred the UMM system as a less drastic change from their traditional export credit practices. And one or two countries indicated they preferred no change at all toward either the DRS or the UMM.

A compromise was fashioned in which it was agreed that slight increases in the rates of the static matrix would take place on July 1, 1980, while more far reaching reforms would be negotiated in the fall.

At both the 1980 OECD Ministerial meeting and the Venice Summit of last year, communiques were issued declaring the agreement of all participating countries that an acceptable solution to bring the Arrangement's terms and conditions "closer" to financial market conditions should be reached by December 1, 1980.

With this seemingly broad consensus, the U.S. government approached the round of meetings in fall 1980 with a certain amount of optimism. That optimism was misplaced.

The European Community, as the result of a French veto, was unable to offer more than a trivial rise in the minimum export credit rate of 0.8 percent for poor country borrowers and 1.0 percent for intermediate and rich country borrowers. The United States labeled this offer "grossly inadequate," but indicated that it would accept the proposed increases while continuing to push for an Arrangement more like that envisioned in Mr. Wallen's Report.

For countries whose market rates of interest are low, however, the proposed increases ran counter to the Venice Summit commitment to bring export credit terms closer to financial market conditions. Japan, for example, noted that the EC proposal would force the Japanese Eximbank to charge rates above Japanese long-term prime lending rates. Justifiably, Japan refused to accept an interest

rate matrix that allowed some governments to subsidize with impunity while governments with low market rates were forced to charge a premium above their cost of money. As a result of this impasse, the EC offer was not accepted, and no changes were made in the interest rate matrix of the Arrangement.

In the interim between the December 1980 OECD export credit meeting and the OECD meeting scheduled for next month, the Reagan Administration has warned foreign governments that it is strongly opposed to export credit subsidies. Secretary Regan has made it clear to foreign economic leaders that we consider an improved Arrangement a high priority goal. We have also made it clear that we will not accept in May 1981 what we rejected as a solution in December 1980. A trivial one or two percent rise in the matrix is not a solution to the problem of export credit subsidies.

We are considering ways to lend teeth to our negotiating efforts, and remain hopeful that significant progress can be achieved this year.

Senator GARN. We will invite GAO to come up.

STATEMENT OF FRANK CONAHAN, DIRECTOR, INTERNATIONAL DIVISION, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY STEWART TOMLINSON AND ALLAN MENDELOWITZ

Senator GARN. I appreciate your being here. During the past years Congress has heard repeated testimony from leading experts regarding Soviet diversion of United States and other Western goods and technology for military purposes. The Soviet invasion of Afghanistan was supported in part by U.S. technology. This proved that such a military diversion was taking place and was a common occurrence. It became clear to me that much of the problem is the result of inadequacies in our current national security export control system and its administration, primarily the Department of Commerce.

Therefore, in February of 1980, I requested that GAO carry out a complete investigation of the deficiencies of this system. I understand that a draft of the report will be ready shortly, followed by the issuance of an unclassified report later in the year.

I certainly wish to thank GAO for participating in this hearing today and the assistance that they have provided my staff over the last year, and the staff of this subcommittee.

I am aware of some of the initial difficulties. In my conversations with Elmer Staats, I had trouble in gaining information a year or so ago. So I very much appreciate your efforts. If you would like to proceed, I would be happy to hear your testimony.

Mr. CONAHAN. Senator Heinz asked that we summarize in the interest of time.

Senator GARN. I assume that the Senator had asked that. That is standard operating procedure. We will place your statement in the record.

Mr. CONAHAN. As you mentioned, this study is being done primarily at your February 1980 request. On that same day in February we received a request from Senator Harry Byrd to do a collateral study. I should like to reflect back also on comments made by Senator Heinz at the outset, and that is that U.S. industry complains about the cumbersome, inconsistent, and unnecessarily rigid procedures, and uncertainties in the system impact on their reliability. Thus they maintain that sales are lost or potential markets cannot be expanded. Other critics believe the system is too loose and inadequate safeguards are permitting Communist countries to enhance their military capabilities through U.S. technology.

Our overall observation is that the administration of export control draws criticism from all sides. To evaluate the system, we selected a random sample of 94 license applications approved for shipping technology to the Eastern bloc. The period of these licenses was the last quarter of 1979 and the first quarter of 1980. We found that criteria for inclusion of technology subject to control are too broad. Few items are actually being controlled.

A large part of the system is a process that overly burdens U.S. exporters and reduces the time available to review important applications. Review of critical cases may be improved, and there are serious constraints to deterring unauthorized exports. With more narrowly focused procedures, the current system can better protect national security while lessening the burden on U.S. exporters.

I would like to discuss some of the important influences that have a bearing on how the export control system operates.

The system consists of three principal activities; one, identifying technologies and products that need to be controlled; two, deciding individual export license applications; and three, providing an effective deterrent to unauthorized exports.

Recognizing that effective export control requires international cooperation, the United States carries out these activities in conjunction with its NATO partners and with Japan. This informal organization referred to as the Coordinating Committee, or COCOM, establishes a common list of items which participating governments will control for reasons of mutual security.

In addition to that, the U.S. unilaterally controls a number of items for national security purposes.

Within the COCOM community, or for that matter within the U.S. licensing system, there are different levels of control. Militarily significant items, or items which we will refer to as high technology items today, require unanimous approval from all COCOM members prior to export and are referred to as exception requests. On the other hand, lesser technology requires only that a member

notify the other members that such items have been exported. In effect, such items are freely exportable.

Another important influence on the control system is that it is a reflection of changing national priorities—both legislative and foreign policy.

Since 1969, export control legislation, has been shifting toward liberalizing controls on trade with Communist nations. This can be seen by looking at the U.S. unilaterally controlled list of items which has declined from 494 items in 1971 to just 33 this year. The licensing process is a vehicle for foreign policy implementation. That is seen in the controversy that has surrounded the approval of certain cases of technology transfer, such as ball bearing machines, high powered computers and heavy truck manufacturing facilities.

To understand what is eventually controlled by the U.S. Government for national security reasons, one needs to go beyond the commodity control list to identify what applications were reviewed by the Department of Defense. We've found that there is a genuine concern of the Department of Defense with only a small percent of the total number of export applications received.

In 1980 the licensing system handled between 75,000 and 80,000 applications for export for commodity control list items to various destinations around the globe. Of this total, only 3,000 were reviewed by the Department of Defense. Even for the Warsaw Pact countries, our random sample showed that the Department of Defense reviewed only 30 percent of these applications.

Defense asked to examine only those applications involving high technology. It has concluded that lower technology exports do not constitute a significant military risk and Commerce should assess the risk without Defense review.

Accordingly, and in the very formal sense, Defense has delegated authority to Commerce to decide on all such cases because the vast majority of applications involve low technology and are routinely processed with little, if any, review currently.

The licensing system has become a meaningless paper exercise. Such a situation detracts from the importance of control and raises serious questions as to whether low technology items should require export licenses.

One would think that, over time, such low technology items would have been eliminated from licensing requirements. This has not happened apparently because of the desire on the part of the executive agencies not to weaken the mechanism available for changing controls in response to foreign policy, the need for export information, and the unwillingness to reduce the margin of safety in the system.

We have reason to think that there are other mechanisms in place to address all three.

We selected 94 approved cases processed just before and after Russia's invasion of Afghanistan. The Department of Defense is making a good review of these cases but we think some improvements can be made. We found some problems in the way in which the Commerce Department is carrying out its responsibility to identify the significant cases for Defense review. We identified ways that the national security review process can be improved.

We do think, however, that the process does deny more applications than is commonly perceived.

Insofar as the Defense involvement in the process is concerned, we looked at 14 of the 28 cases in our sample that Commerce sent to Defense to review. We found that 12 of the 14 cases received technical command input; 8 cases were recommended for approval but, in 4 of these cases, at least 1 of the technical commands recommended denial. In three cases the denial was overruled by approving the items with limits on the technical specifications or reducing the equipment's performance characteristics. The remaining case was approved without conditions following detailed discussions with the technical command.

Defense officials have generally acknowledged that the technical commands have differing opinions on recommendations. Defense R. & E. sometimes overrules technical command positions because they are not adequately supported in their view. On the other, there have been cases where the technical commands recommended approval, but because of other considerations, Defense recommended denial.

Insofar as Commerce is concerned, the trigger mechanism for getting the cases to Defense is an identification of the technical specifications of each proposed export. Commerce refers to the formal delegations of authority from Defense in making decisions on whether Defense should review the case. We found some problems in the Commerce administration of that which we can talk about if you would like, sir.

The third important aspect of the control systems is enforcement. The export control process for the most part, as you know, is an honor system which relies on the basic integrity of the export community and its willingness to abide by the law.

Major difficulties accompany the enforcement effort. There are 300 air, sea, and highway exit points in the United States, and there are also frustrating difficulties involved in dealing with enforcement abroad. Therefore, any effort that would be comprehensive enough to insure compliance with controls would probably be cost prohibitive. However, we believe that better use can be made of the resources that are now available.

We noted that the FBI reports that Russia has indeed stepped up its efforts to obtain Western technology. The FBI has increased its foreign counterintelligence effort—an area that includes export control. However, the FBI has not been asked by Commerce, as far as we can determine, to investigate any specific cases, nor does it feel it has statutory authority for enforcing the Export Administration Act. Its work involves export control only as a part of its foreign counterintelligence effort.

Another major problem has to do with diversions once the commodities have left our shores. We know that about 36 potential violations involved exports of computers, semiconductor technology, and other sophisticated equipment were discussed with foreign governments during 1980.

As we mentioned above, full compliance is not perhaps feasible considering the enormity of the potential problem but better use could be made of available resources. As an example, Commerce has made very little effort toward adopting recommendations we

made in the 1979 report, discussed before this committee about 2 years ago. Random cargo inspections are not yet being made at a representative sample of ports nor are they being scheduled around the clock or on weekends. Furthermore, Commerce has not yet tightened its management of the program to monitor the end use of critical items.

Mr. Chairman, we will take any questions you may have at this time.

[The complete statement follows:]

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

FOR RELEASE ON DELIVERY
EXPECTED AT 10:00 a.m.
THURSDAY APRIL 30, 1981

STATEMENT OF

FRANK C. CONAHAN

DIRECTOR, INTERNATIONAL DIVISION

BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL FINANCE AND MONETARY POLICY

SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

ON THE ADMINISTRATION OF

EXPORT CONTROLS UNDER THE EXPORT ADMINISTRATION ACT

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to share with you our views on the export control system for commercially available commodities as administered by the Department of Commerce and a group of consulting agencies. As you know, under the Export Administration Act, the United States controls the export of "dual use" commercial products and processes for national security, foreign policy and short supply purposes. Our current review addresses congressional concerns about how well the system is carrying out the Act's national security goal of controlling exports of militarily significant technology and products to Russia and other Eastern bloc nations. This particular aspect of the control system requires that the Department of Defense must be consulted by Commerce and that Defense may recommend that the President deny any application on national security grounds.

The administration of export control is an onerous paperwork system that draws criticism from all sides. U.S. industry complains about cumbersome, inconsistent and unnecessarily rigid procedures and that uncertainties in the system impact on their reliability. Thus, they maintain, sales are lost or potential markets cannot be expanded. Other critics believe that the system is too loose and that inadequate safeguards are permitting the Communist countries to enhance their military capabilities through U.S. technology.

To evaluate the system, we selected a random sample of 94 license applications approved for shipping technology to the Eastern bloc. We also reviewed actions taken to amend the control lists and to enforce compliance with control legislation.

We found that

- criteria for inclusion of technology subject to control is too broad--far fewer items are actually being controlled;
- a large part of the system is simply a paper process which overly burdens U.S. exporters and reduces the time available to review important applications;
- the review of critical cases should be improved; and
- there are serious constraints to deterring unauthorized exports.

We believe that with more narrowly focused control criteria and procedures, the current system can better protect national security while lessening the burden on U.S. exporters. Before elaborating on these points, we would like to discuss some of the

important influences that have a bearing on how the export control system operates.

INFLUENCES ON THE
EXPORT CONTROL SYSTEM

The export control system consists of three principal activities: (1) identifying technologies and products that need to be controlled, (2) deciding on individual export license applications, and (3) providing an effective deterrent to unauthorized exports.

Recognizing that effective export control for Communist country destinations requires international cooperation, the United States carries out these activities in conjunction with its NATO partners and with Japan. This informal organization, referred to as the Coordinating Committee, or simply COCOM, establishes a common list of items which participating governments will control for reasons of mutual security.

Under the COCOM mechanism, members must all agree on items added or deleted from control. Since compromise is a critical element of the process, members obviously do not get all that they want--be it for more control or less. In the last COCOM list review, for example, we were told that the United States has achieved most of what it wanted. This apparent success, however, must be tempered by the fact that Defense technicians wanted more items controlled than the U.S. position called for and no agreement has yet been reached on some of the more critical items, most notably, computers, lasers, and numerically controlled machines.

Currently, COCOM member governments control 125 categories of industrial items. In addition, the United States unilaterally controls 33 items for national security reasons, including

technologies and products unique to the United States and items for which more control than agreed to in COCCOM has been deemed appropriate.

Within the COCCOM community, or for that matter within the U.S. licensing system, there are different levels of control. Militarily significant items, or items which we will refer to as high technology items, require unanimous approval from all COCCOM members prior to export and are referred to as exception requests. On the other hand, lesser technology requires only that a member notify the other members that such items have been exported. In effect, such items are freely exportable. The United States, for example, approves almost all such items for export with little or no review.

Not only is the distinction between high and low technology defined in the COCCOM list, but the U.S. Government also uses such criteria to determine what cases receive critical review by Defense. Commerce is delegated the authority by Defense to decide on low technology applications without referral to Defense. We might note, in this connection, that such distinctions are not part of the Commodity Control List provided to U.S. industry.

Changing national priorities

Another important influence on the control system is that it is a reflection of changing national priorities -- both legislative and foreign policy. Since 1969, export control legislation, has been shifting toward liberalizing controls on trade with Communist nations. This can be seen by looking at the U.S. unilaterally controlled list of items which has declined from 494

in 1971 to just 33 in 1981. This does not mean, however, that there have not been continuing concerns about the strategic implications of U.S. East-West trade.

In the foreign policy area, there have been alternating political highs and lows in U.S. relationships with Communist countries. This includes shifts from a virtual trade embargo just after World War II to liberalized trade during the detente period and then recently back to a partial embargo on Soviet trade as a result of the Afghanistan invasion. These policy shifts affected the export control system by making decision-making more restricted during confrontation periods and more permissive during cooperative periods. Thus, the licensing process becomes a vehicle for foreign policy implementation. This is seen in the subsequent controversy that has surrounded the approval of certain "celebrated" cases of technology transfer, during the period of detente, such as ball bearing machines, high powered computers and heavy truck manufacturing facilities.

Another illustration is the recent liberalizing of trade with the Peoples Republic of China. The resulting rapid increase in exports of products with dual use potential to that nation could be subject to strong criticism and concern sometime in the future if relations with the PRC were to deteriorate. We are not making a judgment on these shifts in foreign policy, but are merely pointing out their importance in operating the export control licensing system.

CONTROL CRITERIA SHOULD
BE MORE NARROWLY FOCUSED

To understand what industrial exports are eventually controlled by the U.S. Government for national security reasons, one must go beyond the Commodity Control List (CCL) to identify which applications were reviewed by the Defense Department. In doing this, we found that there is genuine concern with only a small percent of the total number of export applications received. In 1980, for example, the U.S. licensing system handled 80,000 industry applications for export of CCL items to various destinations. Of this total, only 3,000 were reviewed by the Defense Department. Even for Warsaw Pact countries, our random sample showed that Defense reviewed only 30 percent of the applications approved for those countries.

Why does Defense review so few applications? The answer stems from the fact that Defense asks to examine only those cases involving high technology. Defense has concluded that lower technology exports do not constitute a significant military risk and that Commerce should assess the risk without Defense review. Accordingly, Defense has delegated authority to Commerce to decide all such cases. These delegations of authority cover most items on the CCL and contain specific performance characteristics above which Commerce must send the application to Defense for review. Delegations of authority also apply to destinations. Consequently, what is considered high technology for one country may not be for another. The most restrictive standards are for the Communist bloc countries.

Because the vast majority of applications involve low technology and are routinely processed with little if any review, the licensing system has largely become a meaningless paper exercise. Such a situation clearly detracts from the importance of control and raises serious questions as to whether low technology items should require export licenses.

On this point, the Congress has supported eliminating controls for items that no longer represent a military risk. For example, section 5(g) of the Export Administration Act states that:

"INDEXING--In order to ensure that requirements for validated licenses and qualified general licenses are periodically removed as goods or technology subject to such requirements become obsolete with respect to the national security of the United States, regulations issued by the Secretary [of Commerce] may, where appropriate, provide for annual increases in the performance levels of goods or technology subject to any such licensing requirement. Any such goods or technology which no longer meet the performance levels established by the latest such increase shall be removed from the list * * *."

Industry has also argued for stronger decontrol of exports, particularly to the non-Communist world. The executive branch, however, has done little with regard to formal decontrol. During the most recent COCOM review, the United States introduced only two proposals for indexing and both were later withdrawn. Further, since passage of the 1979 Act, the United States has eliminated no unilateral controls.

One would think that, over time, low technology items would have been eliminated from licensing requirements. This has not happened, apparently because of a desire not to weaken the mechanism now available for changing controls in response to foreign policy shifts, the need for export information, and an unwillingness to reduce the margin of safety in the system.

As to weakening our response to foreign policy shifts, we believe that eliminating low technology items from control does not preclude the Government from subsequently embargoing commodities. With regard to information needs, the Government would continue to receive sufficient information on decontrolled exports through shippers' export declarations, which are required on all U.S. exports, licensed or not. Finally, the definition of high technology includes a safety margin. Defense approves many exceptions in the high technology classification, suggesting that lower technology can be decontrolled without losing the necessary safety margin.

In summary, since the Government does not now critically review low technology exports, such items, as defined for Warsaw Pact countries, could be removed from licensing requirements without jeopardizing U.S. national security. Such action would remove an unnecessary and costly burden from both industry and Government and free more resources to review high technology applications.

CRITICAL CASE REVIEW
SHOULD BE IMPROVED

To analyze how national security cases were being reviewed, we randomly selected 94 approved cases processed just before and after the Russian invasion of Afghanistan. The Department of Defense has the key role in reviewing cases involving militarily significant technology; and it is generally making a good review of these cases; but that review could be improved. We also found problems in the way in which the Commerce Department is carrying out its important responsibility to identify the significant

cases for Defense review. We identified ways that the national security review process can be improved.

The system, however, does deny more national security sensitive applications than is commonly perceived. Although less than one percent of the total applications processed by Commerce are denied, this figure increases significantly when one examines the situation regarding Warsaw Pact destinations. For example, in the last quarter of 1979, and prior to the invasion of Afghanistan, 7.7 percent of requests for export to the Warsaw Pact countries were denied. Furthermore, if only the high technology exports to the Pact are considered, approximately one out of every four cases was denied. In addition, our sample cases indicated that about 7 percent of the approved Warsaw Pact cases were modified to reduce the technical capabilities of the items before they could be exported.

Defense's key role
in analyzing cases

Defense's evaluation of high technology cases for potential military significance is carried out by the Defense Research and Engineering staff with the assistance of the military technical commands, certain technical experts, and Defense intelligence. We looked at 14 of the 28 cases in our sample that Commerce sent to Defense for review. We found that 12 of the 14 cases received technical command input; 8 cases were recommended for approval but, in four of these cases, at least one of the technical commands recommended denial.

--In three cases the denial was overruled by approving the items with limits on the technical specifications or reducing the equipment's performance characteristics.

--The remaining case was approved without conditions following detailed discussion with the command.

Defense officials acknowledged that the technical commands frequently have differing opinions on recommendations. Defense Research and Engineering sometimes overrules technical command positions because they are not adequately supported. On the other hand, there have been cases where the technical commands recommended approval, but because of other considerations, Defense recommended denial.

In 1979, we reported that the technical commands were not specifically funded for export licensing reviews and this still hampers Defense Research and Engineering officials. As a result, technical command reviews receive a low priority and according to Defense officials, the cases are not always assigned to the best qualified people. Defense officials indicated that the technical commands' reviews are critical and they could be made much better if they were part of their specifically assigned duties with appropriate funding instead of having the costs covered by the budget for overhead.

Defense intelligence makes checks on the designated end users plus some technical analyses for all Soviet Union cases and some other Communist country cases. Greater emphasis was placed on these reviews starting in 1979. Before then, only about 25 cases were reviewed a year but this has increased now to more than 100 per month. According to Defense officials, about 2 to 3 percent of the cases have been found to involve unacceptable end users and another 5 to 6 percent have been found to involve questionable end users. Defense intelligence is scheduled to

receive an increase in funding for this activity in its fiscal year 1982 budget. Defense noted that this inhouse intelligence effort is necessary because it cannot rely on Commerce's identification of end user activities.

Some problems with Commerce's
initial reviews

The trigger mechanism for getting the proper cases to Defense is Commerce's identification of the technical specifications of each proposed export. Commerce refers to the delegations of authority from Defense in making the decisions on whether Defense should review a case. We found that there is a problem with the way Commerce is carrying out this responsibility. For example, Commerce failed to send Defense 3 of 31 cases, or about 10 percent of such cases in our sample, that should have been sent for review according to the delegation of authority criteria. In two of the cases, Commerce officials said precedent was involved and that such precedents were interpreted under the delegations to allow them to approve the cases without referral to Defense. However, the third case did not involve such interpretation and, therefore, was in clear violation of the delegation, and Defense had no opportunity to deny the sale as allowed under the law.

Another problem is that Commerce is not getting the cases to Defense in a timely manner. Under the Export Administration Act, within 10 days from receipt of an application Commerce must make an initial decision whether or not the application requires Defense and other agency review. This action is not being completed within the required timeframe and often takes about

30 days. Therefore, the reviewing agency has that much less time to analyze the case. Defense complains about this and adds that over the last 1-1/2 years, Commerce did not provide enough information to analyze many of the cases.

We also identified various management weaknesses within Commerce's daily processing of export license applications, including (1) the need to streamline the flow of applications within the system and eliminate duplicative review efforts, (2) institute an adequate system for monitoring safeguard provisions which are added to certain licenses before they are approved, (3) require greater accountability through better recordkeeping, and (4) update the Office of Export Administration procedures manual. Commerce is currently addressing some of these problems and expects to improve its operation.

INEFFECTIVE DETERRENT TO
UNAUTHORIZED EXPORTS

The third important aspect of the control system is enforcement of the export control law. As you know, the export control process for the most part is an honor system which relies on the basic integrity of the export community and its willingness to abide by the law.

Major difficulties accompany the enforcement effort. There are some 300 air, sea, and highway exit points from the United States and there are also frustrating difficulties involved in dealing with enforcement abroad. Therefore, any effort that would be comprehensive enough to insure compliance with controls would probably be cost prohibitive. However, better use could be made of available resources.

Detecting unauthorized shipments

During 1980, Commerce's compliance activity opened 354 investigations of alleged violations of the Export Administration Act. It also imposed administrative penalties in 12 instances. Further, the Justice Department imposed criminal penalties against four individuals. This compares to 224 investigations, 11 administrative penalties and two criminal penalties in 1978.

At the same time, the backlog of uncompleted investigations at Commerce has grown from 189 in fiscal year 1976 to 426 in fiscal year 1980. Many of these cases also involve alleged unlicensed technology exports, which may result in criminal or administrative penalties.

Rapid changes in technology have increased the desirability of U.S. products, and miniaturization of computer programs and other products have made clandestine shipment easier. Also, it is reported that policy restrictions on exports to the Soviet Union following the invasion of Afghanistan have made violations even more profitable.

The FBI reports that Russia has stepped up its attempts to obtain Western technology, especially computers, microelectronics, fiber optics, and lasers. The FBI has increased its foreign counterintelligence effort--an area that includes export control. However, the FBI has not been asked by Commerce to investigate any specific cases, nor does it feel it has statutory authority for enforcing the Export Administration Act. Its work involves export control only as a part of its counterintelligence work.

Another major problem is that such items can also be easily diverted after leaving U.S. shores. Of course, the magnitude of such diversions can only be estimated, but Government agencies have reported on the problem. The State Department noted that in 1980 about 45 diversion cases were discussed within an inter-agency committee. Also about 36 potential violations involving alleged illegal exports of computers, semi conductor technology, and other sophisticated electronic equipment were discussed with foreign governments during 1980.

Such problems can and have occurred not only in other countries but within the COCOM countries themselves. Obtaining an adequate degree of cooperation among COCOM members in investigating and prosecuting diversion cases is difficult. Each violation is handled on a case-by-case basis and no formal mechanism exists to coordinate and assist each countries' efforts.

How effective is the Government's enforcement effort?

A recent National Security Council export control study identified two major areas of concern--insufficient resources devoted to enforcement, and lack of adequate coordination among Government agencies concerned with export control enforcement.

As we acknowledged above, insuring full compliance is not really feasible considering the enormity of the potential problem; but better use could be made of available resources. As an example, Commerce has made very little effort toward adopting recommendations we made in a 1979 report. Random cargo inspections are not yet being made at a representative sample of ports of exit nor are they scheduled around the clock or on weekends.

Furthermore, Commerce still has not yet tightened its management of the program to monitor the end use of critical items, although efforts continue to include onsite visitation clauses in approved license applications.

We are prepared to repeat our prior recommendations regarding compliance efforts and suggest that greater cooperation be pursued not only among our own agencies but with the COCOM countries as well. In this regard, we believe that our proposal for adjusting the criteria for control will also assist in alleviating the inspection workload and encourage other countries to better control that which is really important.

Mr. Chairman, we believe that potential adjustments to lighten the export control workload exist, and that these might well be considered before more resources are applied to the system.

This concludes our prepared statement and we will be happy to answer any questions that you may have on the points we have covered today.

Senator GARN. Thank you very much. First of all, do you feel that you have sufficient capability under section 12(c) of the Export Administration Act to gain access to necessary information from various agencies? I'm referring back to our problems initially, your inability to get information, specifically if requested by a member of the Senate or of this committee.

Mr. CONAHAN. After a protracted period and with a great deal of assistance from yourself, Mr. Chairman, we were, in midsummer of last year, given what we consider to be sufficient information in order to carry out the objectives of this review. That information is proprietary in nature. It needs to be protected. We appreciate the sensitivities in handling it. We feel that they could have been more forthcoming and they could have acted in a more timely fashion in cooperating with us in that regard. We did eventually get it.

Senator GARN. Do you recommend any changes in the act to solve that problem?

Mr. CONAHAN. I think if a support agency such as our own were included under the provisions of 12(c), we could directly deal with the Department of Commerce in that regard, and it would be helpful and it would cut down on the problems of getting that.

Senator GARN. Since 1972 how many items that are transferred to the Soviet Union have been subject to export control safeguards such as visitation inspection rights and who within the executive branch reviews the safeguards?

Mr. CONAHAN. I'm not in a position to quantify that. I can say that the system as we found it does not permit one to get a very good feel for how well the safeguards program is indeed working. For the most part, safeguards are associated with exports of computers. For example, there are limitations put on the provision of spare parts. Spare parts are limited to a 6-month period.

The inspector is an employee of the supplier, and indeed might be not a U.S. citizen, but a foreign national. We found there is not a system in place to track safeguards within the Department of Commerce that in the first place have been put on these licenses, nor is there any sort of file to determine that reports are being made on the part of these folks.

And third, there really has not been, as far as we can see, any sort of a negative report. We are left with the uneasy feeling that the system is simply inadequate to answer the question.

Senator GARN. What you are discarding is a system, no matter how much in the last couple of years I have heard Congress defend it, where all of the information shows you have a system that is a bureaucratic nightmare, causing all sorts of paperwork burdens. There is practically no way to determine whether it is functional, and we are imposing all of the rules and regulations in filling out the forms, but there is no way to find out whether it is being observed.

It seems incredibly loose. It flies in the face of Congress testimony over the last couple of years.

Mr. CONAHAN. That is particularly true with respect to the point of your question. Indeed, our position is that a study be made in an effort to cut down on the items that are ultimately subject to licensing, a move toward reducing the burden on the executive

agencies in this area, with the view that perhaps they could redirect their efforts and concentrate on the more important things.

Senator GARN. Beyond the honor system without having people—somebody who wants to subvert the export controls, it appears there is no problem at all. Somebody who wants to be dishonest, it sounds like there is not even a small sieve. There are huge holes.

Mr. CONAHAN. The Department will testify that they are attempting to make some improvements in that area. I think there is some recognition of the problem and a move to correct it, but as of today there quite frankly has not been any movement in this regard over the last 2 years.

Senator GARN. Our testimony in a previous session was they were not even attempting to hire. They had vacancies making no attempts to hire. That is standard testimony before this or any other committee that when something is not being done, they are attempting to solve the problem, attempting to improve. Years pass; months pass. They are still attempting.

That is standard bureaucratese that comes on the record all the time from agencies that are not performing the way they should.

How many reports of diversion on Soviet bloc companies have been received since 1972?

Mr. CONAHAN. I think the Department of State records show there were 45 alleged diversions during 1980.

Mr. TOMLINSON. The Department of Commerce cannot tell us just how many cases there are without a manual search of their files, but the Export Administration's compliance division shows 350 cases a year, and estimates about 5 to 10 percent of these cases will show diversion to Communist countries.

Senator GARN. Are you aware of how many investigations have been conducted regarding these diversions?

Mr. TOMLINSON. These would be the investigated cases. As they said, going back this far, there is some difficulty in pulling it out of the files. It is not readily available.

Senator GARN. Do you know whether any sanctions have been applied?

Mr. TOMLINSON. Of course there are different sanctions that have been applied, both by the Office of Export Administration, administrative sanctions, and also criminal sanctions applied by the Justice Department. We have some figures in our statement for the record in that regard. If I remember correctly, last year there were 4 criminal penalties by the Justice Department and 12 administrative penalties, I believe, by the Office of Export Administration.

Senator GARN. In light of the fact that the backlog has gone from 189 in 1976 to 426 in 1980, why has not the FBI asked to assist in investigating specific cases?

Mr. CONAHAN. I believe the FBI, Mr. Chairman, takes the position that it does not have authority to investigate compliance within the Export Administration Act. Thus, it does not entertain the notion of doing investigations concerning compliance with the act, unless it is in connection with its other counterintelligence activities.

Senator GARN. I do intend to introduce an amendment to the act that will prevent all departments and agencies from withholding

information needed for enforcement of the act. After our experience last year, I would expect the Commerce Department, Customs and the FBI would then begin to share information that will enhance enforcement, which obviously they are not capable of due to numbers or desire or whatever.

Can you tell me why it is, that the distinction between high and low technology goods are not part of the commodity control list provided to the industry, as you testified a few minutes ago?

Mr. CONAHAN. There are several lists, I suppose, that we have to think about. We have a COCOM list which requires prior consent from COCOM countries to export what is considered a high-technology item. But items considered low technology may be exported, and COCOM need only be notified after the fact.

There is a general consistency, between that distinction and the distinction within the U.S. Government between what we called earlier high-technology and low-technology items—the latter is what the Department of Commerce rules on under the DOD delegation of authority.

Senator GARN. How do the other COCOM countries handle this distinction? You are also saying, possibly saying that by making the distinctions public we could cut the number of companies needing to file applications.

If that is so, how do other COCOM countries handle these distinctions?

Mr. TOMLINSON. Of course, if we were to make a change in our criteria, we would have to get the concurrence of the other COCOM nations. In regard to the lower technology or the less militarily critical items, these are called, under COCOM, administrative exception notes to the list which makes these allowances. Member countries are to report to COCOM in regard to the value of items which are shipped under these administrative exception notes.

As a matter of fact, there is much delinquency involved in these countries, even reporting on these.

In regard to whether exceptions are run through the COCOM system on the higher technology items and how well that is being handled, I know it does concern us. There are discussions among the countries within the COCOM area to ask that we get better cooperation. As we said, there is a problem in getting cooperation. There are many different levels of adherence in these countries.

Senator GARN. On the low technology items, ones that can be shipped by non-COCOM members unilaterally?

Mr. TOMLINSON. Yes.

Mr. CONAHAN. Let me add one note to that. In the COCOM list itself are a number of explanatory notes. These notes are considered sensitive and within the U.S. system are not available to U.S. suppliers. The COCOM list, essentially, absent the explanatory notes, is put in the Federal Register, and that is what our suppliers see, thus giving them some difficulty as to what the item really is.

Our understanding is that in the United Kingdom, the entire list is published, and it is available to United Kingdom suppliers.

Senator GARN. In what agency or agencies of the Government is there major resistance to reducing the technical requirements of licensing, which you have spoken about?

Mr. CONAHAN. I think the Department of Defense.

Senator GARN. What is your assessment of the Commerce Department's effectiveness in providing a complete and accurate trail of goods and commodities of technical data exported to the Soviet bloc? In other words, what was exported in what quantities? When was it exported? And so on.

Mr. CONAHAN. Generally it is not very good, and it has not improved over time. For example, we are able to determine the value of export licenses approved in any given fiscal period, but there is no system which matches licenses with actual shipments as contained in an exporter's declaration. With a license one never knows at any one time how much of the goods licensed have indeed been shipped. Half of those items covered by a license may have gone, or even less than half. Indeed, more than what was licensed could have gone. The system does not show us that.

Senator GARN. Are current control procedures carried out by the Commerce Department adequate to protect against military-critical technology on security-sensitive goods and technology being sent to the Soviet Union? Specifically as the commodity control list has been issued by Commerce, is it adequate to prevent these occurrences?

Mr. CONAHAN. We think that the system is working reasonably well. There are a lot of pressures, not only in the Department of Commerce, but also in other agencies, particularly in the Department of Defense on that system. These pressures that I speak of, which you were not terribly impressed with earlier, Mr. Chairman, have to do with the ability of the people to get the job done. The job, as it presently stands, seems to be bigger than the resources available with which to do it, both in Commerce and in the Department of Defense.

That is one thing. There are honest differences at the technical level as to what constitutes a militarily critical item. We have not yet spoken of the foreign policy considerations involved in these approvals.

In connection with some of the earlier cases that we looked at outside of our random sample, clearly those cases received attention far beyond what is the usual case.

Senator GARN. You said the items controlled unilaterally by the U.S. declined from 494 in 1978 to 33 in 1981. Do you have some samples of those items that were dropped, and why?

Mr. CONAHAN. The why, I think, is the general liberalization of trade during that period. We have categories of examples. Mr. Tomlinson?

Mr. TOMLINSON. In these items there are various chemical type things, silicone fluids, resins. You can have marine items, turbines, aircraft landing mats, various things of this nature, which, as we said, are not controlled by COCOM. Many are chemicals.

Senator GARN. You also mentioned in your testimony the recent liberalization of trade with the People's Republic of China, and say that many exported goods have dual potential and we may regret at some point, that we are doing that with China. Are these goods subject to the same analysis as other exports to the Communist bloc, or is China being treated differently?

Mr. TOMLINSON. Of course they are treated the same with regard to the review in the system, yes. They are reviewed as to end use,

the same as the others, the point being more of these have been approved in recent times because of the policy than they might have been a few years ago. There is the general trend of this.

Mr. CONAHAN. The reason that is in our statement is precisely what Mr. Tomlinson said. The system does react to the current policies. Right now the policy is a liberalization toward the People's Republic of China. The point is if that policy changes, and we see a restriction or a constraint of that liberalization, some of these could, using the criteria of the day, be looked on differently from the way they were looked on at the time they were licensed.

Senator GARN. You cite the fact that they are screening only 3,000 of the 80,000 license applications. The majority were Warsaw Pact countries. Also, only 1 percent of the total applications were denied, while 25 percent of the high technology export were refused licenses. I assume this is the reason that you were talking about recommending we reduce the need for licensing on the low-technology items.

Have you considered the effects of eliminating licenses based on destinations, such as COCOM countries?

Mr. CONAHAN. I think that, perhaps, would be a second step. We have considered it. I am not sure that we have come to a conclusion on it. It certainly is in the same direction.

Senator GARN. If these were done, do you think COCOM controls would be strengthened enough to prevent illegal diversions?

Mr. CONAHAN. I do not know that I can comment on that. That would be a long, involved negotiating process.

Senator GARN. Do we really have any enforcement powers at all, if goods are reexported from a foreign country.

Mr. CONAHAN. Only in terms of what we can negotiate.

Senator GARN. In your investigation, were you able to determine what steps were taken when we discover that an export has been diverted or reexported to a country that is not cleared to receive it?

Mr. TOMLINSON. What steps are taken? What steps are taken is that these are taken up diplomatically, or through the COCOM mechanism when we meet in Paris. There have also been some special reviews of this, in which staffs have met just for the purpose of reviewing the diversion area. I think much of this has been at the behest of the United States.

Senator GARN. You state that there are 36 potential violations that were discussed with foreign governments in 1980. What were the results of these discussions and are there any other steps we can take to enforce compliance?

Mr. TOMLINSON. We are not in a position to inform you as to the results of those. There are classifications involved. In fact, I might say with respect to some of the publication of these cases in the past there has been a question about classification. It does deal with national sovereignty, et cetera. It is difficult to talk about these in an open forum, to obtain the information.

Senator GARN. I understand. I'll read about it in the Washington Post. [Laughter.] Or in the Aviation Week and Space Technology. Do you have any feelings about how the issue of foreign availability has influenced you as export controls?

Mr. CONAHAN. I think it is one of a number of factors, and frequently not a very important factor, in the consideration to

issue a license. Based on our interviews, it is considered, but it does not loom all that terribly important.

Senator GARN. Is the indexing concept—does that provide adequate control in the high technology areas of computers, microelectronics, semiconductors, and so on?

Mr. CONAHAN. Except in the sense that indexing is a concept that comes into play in terms of revisions, periodic revisions to the COCOM list. Indexing, per se, really has not been given a chance. It has not operated. I believe the U.S. provided two cases to COCOM but withdrew both. I think we have to wait and see on that.

Senator GARN. Do you have an assessment as to whether the intelligence agencies are doing an adequate job regarding the export of goods?

Mr. CONAHAN. We have difficulty getting a good handle on that, perhaps for the same reason that people in the Department of Commerce have, for example, difficulty in getting good intelligence information. The sharing of intelligence information is something that is very difficult to bring about. There are real considerations as to exposing sources and methods. Clearly there needs to be a better cooperation between the intelligence agencies, between themselves and with the other executive agencies.

There have been assertions that some improvements have been made in that area over the last year or two. Quite frankly, we have not seen any real improvement.

I guess I'm not giving you a very good answer, but I'm not really in a position to give you a very good answer.

Mr. TOMLINSON. DIA has stepped up their assistance to the Department of Defense quite a bit with regard to work in this particular system, checking end users, et cetera.

Senator GARN. Gentlemen, there are additional questions I would like to ask you, but they get into more technicalities and probably some classifications, so what I would like to do—what I was going to say is that I would submit some questions to you for later response.

However, I have been asked to ask you a question for Senator Proxmire. You have stated that the administration of the export laws is an onerous paperwork system. The question is, what percentage approximately of the activities of the export administration in Commerce would you say is onerous and unnecessary?

He must be looking for a candidate for the Golden Fleece Award. [Laughter.]

Mr. CONAHAN. I think a fairly substantial percentage of the applications that are now being made and reviewed by the system could be done away with without impairing the control of technology to the Eastern Bloc.

Senator GARN. Thank you very much, gentlemen. We will have some additional questions, possibly from other members of the committee. I apologize that there are so few of us here, but there are so many hearings and markups going on to meet the May 15th deadline that we can hardly get one Senator to one hearing. As a matter of fact, I have three different places I am supposed to be right now.

Thank you very much for your testimony.

Mr. CONAHAN. Thank you, Mr. Chairman.
[Recess.]

STATEMENTS OF PAUL T. O'DAY, ACTING UNDER SECRETARY FOR INTERNATIONAL TRADE, COMMERCE DEPARTMENT, ACCOMPANIED BY SHARON CONNELLY AND WILLIAM SKIDMORE; OLES LOMACKY, DIRECTOR FOR TECHNOLOGY TRADE, OFFICE OF THE SECRETARY OF DEFENSE, ACCOMPANIED BY COL. JOHN HAGGER; AND HARRY KOPP, DEPUTY ASSISTANT SECRETARY, DEPARTMENT OF STATE

Senator GARN. We're back on the record.

Mr. O'DAY. I am Acting Under Secretary for International Trade in the Commerce Department. I am pleased to be here today to support the administration's request for authorization of the fiscal year 1982 and fiscal year 1983 appropriations for the Export Administration Act of 1979.

I have with me on my far right William Skidmore, who is the Director of the Office of Export Administration, and on my immediate right, Sharon Connelly, who runs the Compliance Division in the Office.

Mr. Chairman, under the standard procedure, if you so approve, I will briefly summarize our statement and leave time for questions.

Senator GARN. Your entire statement will be placed in the record.

Mr. O'DAY. Over the past year the export administration program has been affected by developments that are well-known. From the program management standpoint, the most important development was the set of new requirements and standards enacted when the act was renewed in 1979, as a result of which we had to issue a whole set of new regulations and guidelines the filing of licensing applications.

During the past year, we completely reorganized the International Trade Administration and there have been a number of key personnel appointments throughout the export administration function. In addition, the Soviet invasion of Afghanistan led to a set of new restrictions on exports to the Soviet Union. This included a suspension and review of outstanding licenses as well as the development of a new set of policies for application to export or re-export to the U.S.S.R.

In a number of these cases, we had to act, Mr. Chairman, without precedent which increased the amount of time that our licensing officers had to spend in this area.

Finally, as was noted in the previous testimony, continued opening of the relationship with the People's Republic of China led to a new set of guidelines announced last fall, allowing licensing for a range of previously restricted products. This increased the time that we had to spend in this area, and in 1980 our caseload grew to record levels. The applications grew 7 percent over 1979, and so far this year they have dropped about the same rate, so we are back to the 1979 level at present.

With regard to the new statutory guidelines that were passed when the act was renewed, we feel we have been able to meet these requirements in most of the cases. The developments over the past

2 years and the vacancies have taken their toll. Since we last testified before this committee, we have reduced the vacancy level to zero. That has brought our strength up from about 135 to nearly 170 people.

In addition, our request for fiscal year 1982 includes a fiscal year 1981 reprogramming of 33 positions from other parts of ITA to bring the total onboard strength in the office to nearly 200 people. That is a significant increase in the resources of the office from about 135 to about 200 over a period of 1½ years, assuming that Congress approves the fiscal year 1981 programming. We think that as these people come onboard and are trained, we will be able to make some more significant progress on the very tight statutory guidelines that we are now operating under.

In the compliance area, although we still have a number of problems in this, the most complex part of our program, we have made substantial progress in the past year. The number of investigations nearly doubled over 1979. Our enforcement capability will increase further as we add new people. Of the 33 reprogrammed individuals, 15 of these will go directly into compliance, and 14 of the 15 will be used to establish a new office on the west coast which will give us added capacity to deal with increasing problems we have had recently with semiconductor shipments from the west coast that are a problem in the program.

With regard to the specific issue before this committee, Mr. Chairman, the authorization for appropriations for the remaining 2 years, the administration supports levels of \$9,659,000 and \$8,454,000 for fiscal years 1982 and 1983, respectively. The higher number for fiscal year 1982 is associated with a one-time request that we have for \$1,205,000 to carry out three specific projects. First, a complete rewrite of the export administration regulations, which as anyone knows who has to deal with this program, consist of a collection of incremental changes over the past decade that are very difficult to use with all of the cross-references, in these 500 pages of regulations.

Second, we will carry out specific studies on foreign availability, and third, we expect to improve our computer system to allow us to better track our cases and take care of some of the problems that were raised in the GAO report that you have just heard.

Mr. Chairman, that concludes my summary. We look forward to your questions.

[Complete statement follows:]

STATEMENT OF
PAUL T. O'DAY
ACTING UNDER SECRETARY FOR INTERNATIONAL TRADE
U.S. DEPARTMENT OF COMMERCE

before the
SUBCOMMITTEE ON INTERNATIONAL FINANCE
of the
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
WASHINGTON, D. C.
APRIL 30, 1981

Mr. Chairman, I am Paul O'Day, Acting Under Secretary for International Trade in the Department of Commerce. I am pleased to be here today to support the Administration's request for authorization of FY 1982 and 1983 appropriations for the Export Administration Act of 1979.

The basic purpose of ITA's Export Administration program is to regulate exports to protect the national security, promote U.S. foreign policy, and prevent short supply conditions in a manner that minimizes any adverse impact on the U.S. business community. Our antiboycott compliance program is designed to protect the trading interests of the United States and American

companies from interference by foreign nations as they attempt to enforce their trade boycotts. The Office of Antiboycott Compliance enforces the antiboycott provisions of the Export Administration Act and provides companies with guidance and advice on how to comply with its terms.

EXPORT CONTROLS

The export control functions we carry out under the Export Administration Act of 1979 include the following activities in policy planning, licensing, and compliance:

In policy planning, we develop and coordinate recommendations for the overall export control program, and review export license applications that present particular foreign policy or national security problems. This unit coordinates its work with other agencies on license applications and on policies requiring interagency review.

Our workload in this area has been continually increasing due to the growing technical complexity of the applications filed. Requirements imposed by the 1979 Act for continuous review and justification of U.S. export control policy toward individual countries, and for review and

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simplification of our export regulations and control lists, have also placed heavy new demands on this unit.

Our Licensing Division reviews the technical aspects of goods and technology for which export licenses are sought. It carries out a number of complex tasks related to the interpretation and application of current policies on export license applications. This unit documents significant policy problems on specific transactions for interagency consideration and also conducts technical and foreign availability analyses on individual products. Six formal government/industry technical advisory committees, chartered by the Export Administration Act, are consulted for technical support.

The main responsibility of our Compliance Division is the detection, investigation, and prevention of unauthorized exports. This Division develops information on possible violations, conducts investigations, and prepares cases for administrative and criminal actions when warranted. Criminal cases are referred to the Justice Department for prosecution.

Over the past year, these programs have been affected by a number of new developments. From a program management viewpoint, the most important development was the set of significant new requirements and standards enacted in the Export Administration Act of 1979, as a result of which we had to issue major new regulations and revise our licensing procedures. In addition, the International Trade Administration reorganization was completed during the past year, resulting in an overall realignment of functions and a number of key personnel changes.

The Soviet invasion of Afghanistan led to a new set of restrictions on exports to the Soviet Union. These included a suspension and review of outstanding licenses as well as the development of a new set of policies for applications for export or re-export to the U.S.S.R. The new set of guidelines on exports to the Soviet Union required our licensing officers to handle a considerable number of cases for which there were no precedents. This situation greatly increased the amount of

time that we and our advisory agencies spent on each of these cases.

Finally, continued opening of the relationship with the People's Republic of China led to a new set of guidelines announced last fall allowing licensing for a range of previously restricted products to the People's Republic of China. Here, too, the lack of precedents has had a substantial effect on the time required to process each case.

Other significant developments have occurred since we last testified before your Committee. Our vacancy level, which stood at more than 27 vacancies last May, has been eliminated. In addition, we have given priority to the Exporters Service section of the Office of Export Administration, which handles inquiries and complaints from the general public. We have enhanced the capability of that office and have eliminated virtually all complaints about its operation. In response to the high complaint level experienced last year, our capacity to handle telephone inquiries has been increased from under one thousand per week in August of last year to well over two thousand in January of this year.

During FY 1980, our caseload grew to a record level, totaling 75,929 applications, up 7 percent from FY 1979. During the first half of FY 1981, applications have fallen back to the FY 1979 rate. A summary of our processing data for FY 1980 is presented in Attachment 1. Attachment 2 contains a report of cases in process as of April 3, 1981.

With regard to the new statutory time guidelines for case processing, we have been able to meet these requirements in most, but not all, of our cases. At the beginning of this month, the Office of Export Administration had 4,567 cases in process. Of this total, 1,610 had been in process over 30 days, 1,313 over 90 days, and 668 over 180 days. The factors that I have outlined above have been responsible for many of the delayed cases. However, as the new personnel we have hired to fill vacancies become experienced, and as the procedural changes we have made begin to take effect, we are confident we will make significant progress on the delays and backlog inherent in the licensing process, without jeopardizing national security.

Our budget request for fiscal year 1982 increases the personnel available to the Office of Export Administration by 33, through

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reprogramming of resources from other programs in ITA. This would bring the total export control operating strength to approximately 200. We plan to add 15 of these positions to the Compliance Division, primarily for a West Coast staff. The other 18 would be assigned to the Licensing Divisions and to operations support. This increased staff will serve a dual purpose -- expedited processing of license applications in conjunction with strengthened compliance and enforcement.

On foreign availability monitoring, the 1979 Act authorized appropriations of \$1.25 million for 1980 and 1981 but no funds were appropriated. As a result, our expenditures this year for this task have been limited to \$60,000. Our preliminary work on the process has been useful in planning our FY 1982 budget request for \$280,000 to design an effective system to review foreign availability.

In addition to the \$280,000 for work on foreign availability, the proposed budget would make \$915,000 available to be used for a complete redrafting of our Export Administration Regulations and procedural manuals, and for expansion of our computer capacity for processing and tracking export license applications within statutory deadlines. Both of these

activities would, in our view, substantially improve the quality and speed of the license processing system.

On compliance, we believe we have made substantial progress during the past year in increased enforcement activities.

The number of investigations completed this past year has nearly doubled over 1979, resulting in the referral of more violations to our General Counsel's office for administrative actions and to the Department of Justice. Our enforcement capability will increase further as we establish a compliance office on the West Coast and institute a new procedure using personnel in Commerce's district offices around the country to aid in our compliance activities.

Also, the substantial increase in staff resources proposed for this division will continue our progress in assuring compliance with the Act. Obviously, with thousands of ship and plane departures for foreign destinations each week, there is no limit to the amount of resources that could be applied to the compliance function. We believe, however, that the Administration's budget proposal represents a reasonable balance between the resources devoted to compliance and to license processing.

ANTIBOYCOTT COMPLIANCE

Under the International Trade Administration reorganization, the Antiboycott Compliance Staff and the OEA unit responsible for processing boycott reports were combined into the Office of Antiboycott Compliance (OAC). OAC presently has 30 permanent employees in the combined unit, the number authorized in the Administration's budget. With this record number of employees, OAC expects to be able to sustain if not enhance its enforcement activities and carry out its report processing responsibilities.

During fiscal 1980, the Office entered into consent agreements with 10 companies and issued charging letters against two others. To date this year, the Office has charged another two companies and reached consent agreements with 15 others. A total of \$128,500 in fines was imposed in 1980 and \$340,000 so far this year.

As part of its commitment to vigorous enforcement of the antiboycott law, the Department intends to proceed as soon as possible with the selection of a permanent director and to establish a formal structure for the new office. We are also

planning to clarify a number of complex elements of our antiboycott regulations with formal, published interpretations.

Appropriation Authorization for the Export
Administration Act of 1979

With regard to the need for authorization of appropriations for the remaining two years of the Export Administration Act of 1979, the Administration supports authorization levels of \$9,659,000 and \$8,454,000 for fiscal years 1982 and 1983, respectively. The higher number for FY 1982 is required to support our current budget requests for one-time funding of \$1,205,000 for the following projects:

- A complete rewrite of the Export Administration regulations,
- Studies on foreign availability, and
- Improvement of our computer system for case processing management.

Authorization at these levels for FY 1982 and FY 1983 will allow us to support the increased staff made available to the

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Office of Export Administration via reprogramming in the current fiscal year. We believe that earmarking portions of these authorizations for specific purposes is not desirable, from a management standpoint, since this would deprive OEA of the flexibility needed to respond to the wide variety of complex demands placed on the Agency.

Mr. Chairman, this concludes my statement. I will be pleased to respond to the Committee's questions.

ANALYSIS OF LICENSE PROCESSING FOR FY 1980

	<u>Received</u>	<u>Approvals</u>	<u>RWA's 1/</u>	<u>Denials</u>	<u>Total Processed</u>	<u>Backlog for FY 1980</u>	<u>Carry Over Backlog FY 1979</u>	<u>Total Backlog 9/30/80</u>
Non-Communist Country Applications <u>2/</u>	68,244	59,826	6,660	80	66,566	1,678	536	2,214
Communist Country Applications <u>3/</u>	7,716	5,111	1,318	323 <u>4/</u>	6,752	964	1,057	2,021
TOTAL	75,960	64,937	7,978	403	73,318	2,642	1,593	4,235

- 1/ Returned without action.
2/ Includes Country Groups S, T, and V.
3/ Includes Country Groups P, Q, W, Y, and Z.
4/ Includes Partial Denials.

OFFICE OF EXPORT ADMINISTRATION
CASES IN PROCESS

ATTACHMENT 2

APR 03 1981

<u>OPERATIONS DIVISION</u>	<u>TOTAL CASES IN PROCESS</u>	<u>OVER 30 DAYS IN PROCESS</u>	<u>OVER 90 DAYS IN PROCESS</u>	<u>OVER 180 DAY IN PROC</u>
Registration	640	--	--	--
Front Door	500	--	--	--
Multiple Licenses	46	26	6	--
Review	178	1	--	--
Issuance	991	28	7	4
	<u>2355</u>	<u>55</u>	<u>13</u>	<u>4</u>
<u>COMPLIANCE DIVISION</u>	51	7	--	--
<u>LICENSING DIVISIONS</u>				
Computer	293	82	23	41
Electronics	252	38	38	12
Capital Goods	217	98	4	19
Short Supply	25	2	2	2
<u>TOTAL LICENSING DIVISIONS</u>	<u>787</u>	<u>220</u>	<u>67</u>	<u>74</u>
<u>POLICY PLANNING DIVISIONS</u>				
East-West Branch				
PPN Analysis	101	92	70	49
Referred to DOD	208	199	139	91
Referred to State	9	9	9	5
Referred to DOE	10	9	8	8
Referred to CIA	39	37	19	3
Multi Agency	305	302	255	133
Operating Committee	84	84	83	72
COCOM	139	137	115	68
Negative Letters	138	135	116	74
NSC	20	20	20	17
<u>BRANCH TOTAL</u>	<u>1053</u>	<u>1024</u>	<u>834</u>	<u>520</u>
Special Programs Branch				
PPN Analysis	92	92	19	11
Referred to DOD	2	2	2	2
Referred to DOE	86	86	11	9
Referred to State	93	93	35	33
Referred to CIA	4	4	2	1
Referred to SNEC	8	8	4	4
Negative Letters	36	33	26	10
<u>BRANCH TOTAL</u>	<u>321</u>	<u>318</u>	<u>99</u>	<u>70</u>
<u>POLICY PLANNING TOTAL</u>	<u>1374</u>	<u>1328</u>	<u>933</u>	<u>590</u>
<u>GRAND TOTAL</u>	<u>4567</u>	<u>1610</u>	<u>1013</u>	<u>668</u>

Senator GARN. Thank you very much.

Dr. Lomacky?

Dr. LOMACKY. The Department of Defense welcomes this opportunity to contribute to the hearing. With your permission, I would like to summarize my statement rather than read it. You have already inserted my statement in the record.

I have with me Col. John Hagger in case questions come up for him later. I would like to say that the Export Administration Act has helped to clarify and more clearly define the DOD policy on technology transfer. The act, as you know, requires restriction of goods and technologies that would make a significant contribution to the military potential of nations that are a potential threat to U.S. security.

In this spirit, we in the Department of Defense bear the responsibility for the control of those goods and technologies. Part of our responsibility is the identification of militarily critical technologies and preparation of the technical drafts of the proposals for both unilateral and multilateral controls.

We recognize that these responsibilities must be pursued without restricting U.S. trade and exports any more than necessary. We also recognize that we must encourage transfer of technology to our allies to optimize our joint military capabilities. It is the Department of Defense's concern to control exports to principal adversaries and the application of technology to military capabilities.

In the aftermath of the Soviet Union's invasion of Afghanistan, the U.S. export control policy to the Soviet Union has been tightened. In our view, this tightening of export controls on strategic technologies is a long-term measure independent of any peace offensive, a withdrawal from Afghanistan, or whatever happens in Poland. DOD in cooperation with the Departments of State and Commerce has worked to implement three initiatives to reduce the flow of technologies to the Soviet Union. These are the "no exceptions" policy toward the U.S.S.R., more stringent review of licensing applications of the Warsaw Pact, and preparation of new proposals to COCOM.

I would like to comment on the status of the military critical technologies list. The initial version was prepared as mandated by the Export Administration Act, and its table of contents was published in the Federal Register in October 1980. This was truly a national effort, Mr. Chairman. It resulted from efforts by hundreds of technologists using a variety of approaches. These were a review of the commodity control list by industry/government working groups, second, a review of basic areas of technology, and the breakdown of these areas into specific critical elements—this effort was primarily by the U.S. Navy—and third, an independent review in the compilation of a critical technologies list by the Air Force. Each of these reviews used resource material for Department of Defense technology compilations, industry reports, Industry Advisory Committee reports, and prior COCOM distributed data.

The initial version of the list was an integration of these three reviews. The resulting list was prepared in a format required by the Export Administration Act. Each subcomponent of the list includes Keystone equipment, Keystone materials, and goods accompanied by sophisticated know-how and arrays of know-how. The

list was not published in the Federal Register due to concern that such a publication would provide focus for enemy intelligence, but the Department realizes that as we proceed from the identification of the list to the establishment of appropriate controls more and more of some of the information must be provided to the exporters.

Although considerable effort was expended on the initial version of the list, we recognize that considerable work is still ahead. These efforts include identification of nuclear-specific items—and here we are working with the Department of Energy. Second, we need additional industry review, additional supporting data, increased specificity, additional items that have to be added to the list, transfer mechanisms, and also items that could possibly be taken off the commodity control list.

Although additional effort is underway, DOD believes that the initial version is very responsive to the Export Administration Act. Above all, this list identifies the essential technological elements that must be required to achieve military capability with superior operational characteristics. We believe the list provides guidance within the Department of Defense for the review of those export device applications that particularly involve the transfer of know-how to Warsaw Pact countries. The application of this initial list by the Department of Defense export of equipment will be in a manner commensurate with the CCL monitor control list. The export administration regulations will not supersede the technical definitions of the control until further refinements dictate suitable specification changes. The timetable for this project is included in my prepared statement.

The Department of Defense recognizes the export control process to be effective. The technologies on the critical technologies list should be controlled unilaterally, and we will work with other agencies regarding COCOM. Some of the proposals we now have in COCOM, we have used the information that was developed in preparation of the critical technologies list.

The question that was asked by Senator Heinz in his letter to us was: Is the distinction between products and technologies valid?

We believe we have established that such a distinction can be made. Areas do exist where products are linked with the advance of technology. The critical technologies list provides examples whereby products are identified which are key to the advancement of technology—for example, keystone or production equipment.

For those products that cannot be used without providing information which provides for critical technologies, the products are transfers of technology and should be treated as such.

There is another class of products which should be considered, and these are the products which have intrinsic military utility. Those products do not transfer critical technologies; their production by an adversary may be of insufficient quantity or quality for full realization of their military utility, and they must be controlled.

Products that do not fall in these categories are candidates for removal.

Can national security controls be used to create bottlenecks in Soviet energy production?

This was asked by Senator Heinz. Our expert control process in ongoing critical technology analysis are considered as approaches for controls on individual transactions based on established high-technology thresholds. These controls, however, may be insufficient to prevent the U.S.S.R. from modernizing or increasing its efficiency over an entire industrial sector which is relevant to military production.

The Soviets have imported know-how equipment which were inadequately controlled because of transactions involved which fell below the so-called high-technology thresholds.

We believe it is possible, although fairly difficult, to inhibit the growth in Soviet military industrial sectors, including oil and gas production, by controls on know-how, keystone equipment and critical raw materials.

We have identified industrial sectors which we intend to analyze for these bottlenecks in conjunction with our allies. However, additional controls on exports of this type have to await the result of an interagency study. And that is when the decision will be made as to what extent we will be requiring additional controls in this area.

Finally, I would like to comment on the Department of Defense workload with regard to license applications.

The workload of the Department with respect to license applications has been a subject of considerable interest because of the time limits imposed by the Export Administration Act. But also from changes which resulted regarding export policy with the People's Republic of China, which has resulted in a reassessment with the risk of exports to the Communist countries, and we have perceived an increased risk that security-sensitive goods to the Soviet bloc will be first diverted for military use or diverted through more indirect channels to the Soviet Union.

Exports to the P.R.C. is not perceived to be in the national interest, and this has had an impact on the workload of the Department beyond that which is demonstrated by statistics, although there has been a reduction in applications for exports to the Soviet Union, the reduction has been offset by the increase in applications for the P.R.C.

Moreover, Warsaw Pact exports have had to be reviewed with even greater scrutiny to examine carefully the potential for diversions to military use.

P.R.C. has also taken longer to process as analysts have been given every consideration. During the period October 1979 to March 1981 my office reviewed over 4,200 applications for exports. Of these, 3,000 were roughly U.S. origin export applications, 1,100 were non-U.S. applications for COCOM countries.

The time required to process these applications is indicated in the table in my prepared statement. Our overall record is that we have arrived at a Department of Defense position on 90 percent of the cases received within 30 days, and 95 percent of all cases within 60 days.

In addition to the 4,200 applications which I discussed above there were another 1,000 applications for the Soviet Union which were reviewed as a result of Afghanistan. They included those licenses which had previously been approved but which had been

suspended January 1980, and those which the Department of Defense does not normally review. These were subjected to a review in accordance with the newly established, more stringent guidelines.

Thank you, Mr. Chairman.

[Complete statement follows:]

PREPARED STATEMENT OF DR. OLES LOMACKY
DIRECTOR FOR TECHNOLOGY TRADE
OFFICE OF THE UNDER SECRETARY OF DEFENSE
FOR RESEARCH AND ENGINEERING

before the

SUBCOMMITTEE ON INTERNATIONAL FINANCE AND MONETARY POLICY
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
WASHINGTON, D. C.

APRIL 30, 1981

Mr. Chairman and distinguished members of the Senate Subcommittee on International Finance and Monetary Policy. It is a pleasure to be able to participate in your hearing on authorization of funds for the Export Administration Act of 1979. This Act has helped to more clearly define the Department of Defense policy on technology transfer. A provision of the Act is, "To restrict the export of goods and technology which would make a significant contribution to the military potential of any other country or combination of countries which would prove detrimental to the national security of the U.S."

In this spirit, we in the Department of Defense recognize our responsibilities for the control of technologies and and strategic commodities, the acquisition of which, by our adversaries, would be detrimental to the security of the United States. These technologies must be identified, and incorporated into the appropriate control lists. We must discharge this concern, however, without

restricting U.S. trade and exports any more than necessary. We in the Department of Defense also recognize that we must encourage the transfer of technology to our Allies in those areas where we are trying to optimize our own deployed military capability.

This morning, I would like to report on the Department of Defense initiatives which respond to the Export Administration Act of 1979. Specifically to:

1. Offer Department of Defense views on the role of national security control in our overall National Security Policy and the effect of the tightening of controls to the Soviet Union since the invasion of Afghanistan.
2. Review the development and status of the Militarily Critical Technologies List program.
3. Discuss the distinction between "product" and "technology" in the context of export control.
4. Comment on the usage of national security controls to create bottlenecks in the Soviet industrial structure and energy production.
5. Outline DoD workload with respect to license applications, and the time required to process the applications.

DOD View of National Security Controls in the Overall National Security Policy.

The Department of Defense views are consistent with the Export Administration Act of 1979. We feel that controls should be used "only after a full consideration of the impact on the economy of the United States and only to the extent necessary . . . to the National Security of the United States." In determining the extent necessary, it is the Department of Defense's foremost concern to control exports only as needed to protect the United States lead time relative to its principal adversaries in the application of technology to military capabilities. It remains important to protect lead time as long as possible to insure time for the continued growth of technology through new research and development. In addition, it is not in the national interest to assist any country in advancing its technology in ways that would be detrimental to the security of the United States.

Tightening of Controls to the Soviet Union, Post-Afghanistan

In the aftermath of the Soviet Union's invasion of Afghanistan, United States Export Control Policy to the Soviet Union has been tightened. In our view, this tightening of export controls on strategic technologies is a long-term measure, independent of any peace offensives or Afghanistan withdrawals which the USSR may undertake. DoD, in cooperation with the Departments of State and Commerce have worked to implement three initiatives to reduce the flow of technology to the Soviet Union:

1. The "no exceptions" policy toward the USSR.
2. More stringent review of licensing applications to the USSR.
3. Submission of new proposals to COCOM.

To offer a tangible example of the effect of the tightening of controls on the Soviet Union, a large number of previously approved licenses were suspended on 8 January 1980. These licenses were subjected to a second review in accordance with the more stringent post-Afghanistan guidelines. As a result approximately 15% were denied.

In addition, all delegations of authority to the Department of Commerce for licenses to the Soviet Union were cancelled. The Department of Commerce normally reviews these low technology exports for the Department of Defense. The 400 cases involved were reviewed by the Department of Defense with respect to end-users. The purpose was to ensure that Soviet consignees were not engaged in military-related programs. An estimated 2-3 percent of the applications reviewed were denied on the basis of end-user information, and 5-6% were identified as questionable or marginal. The marginal rating indicates to Commerce that subsequent sales to this end-user would require greater scrutiny.

Development and Status of the Militarily Critical Technology List

The initial version of the Militarily Critical Technologies List (MCTL) was prepared as mandated by the Export Administration Act and its table of contents published in the Federal Register on 1 October 1980. This List resulted from efforts by hundreds of technologists using a variety of approaches including:

- A review of the Commodity Control List (CCL) by industry-government working groups - The significant technologies used in the design, development, and production of products on the CCL were identified and those deemed critical, based on their military utility, were recommended as MCTL list entries. This review included extensive participation of representatives from the Army, Navy, Air Force, National Security Agency, NASA, Commerce, State, Defense Intelligence Agency, Central Intelligence Agency and industry.
- A review of basic areas of technology and breakdown of these areas into specific critical elements by the Navy
 - Areas of technology used in military systems were categorized in 18 areas and these areas subsequently broken down into their critical elements.

- An independent review and a compilation of a critical technology list by the Air Force - the process followed was similar to that of the industry-government technical working groups with emphasis placed on technologies unique to key Air Force programs.

Each of these reviews used resource material from prior Department of Defense technology compilations, industry association reports, industry advisory committee reports, and prior COCOM List Review data.

The initial version of the MCTL was an integration of these three reviews. The selection of items for the MCTL, however, did not take into consideration the availability of the selected technology elements to potential adversaries from foreign/non U.S. sources. The resulting List was prepared in a format which included critical elements specified by the Export Administration Act (Section 5.d(2)). This List addresses marketable commodities and industrial design and manufacturing processes but excludes university-based research and publications. These critical elements were identified for sub-components for sixteen (16) general areas of technology (see Figure 1). Each sub-component of the MCTL includes:

- A. Arrays of know-how - (Processes, procedures, information, services and techniques required to

achieve a significant development, production or utilization purpose.

- B. Keystone Equipment - That equipment specifically necessary for the effective application of significant arrays of know-how.
- C. Keystone Materials - Materials specifically necessary for the effective application of significant arrays of know-how.
- D. Goods Accompanied by Sophisticated Know-How
- Goods which can only be used with the provision or disclosure of significant arrays of know-how.

The MCTL as described above was not published in the Federal Register due to concern that such a publication would provide focus for enemy intelligence. The Department realizes, however, that as we proceed from identification of the List items to the establishment of appropriate controls more and more information must be provided to the public. The form and mechanism for making this information available, however, remain under debate.

Voluminous reports (totaling over 5,000 pages) on military utility, foreign and adversary capability and the significant aspects of each technology have been prepared to support the selection of items for the MCTL.

Although considerable effort was expended on the initial version of the MCTL, we recognize that considerable work on the MCTL has yet to be completed. Specific effort required includes:

- ← Identification of nuclear specific items ← the Department of Energy (DOE) has identified a list of critical technologies which are being incorporated in the MCTL. The items on the DOE list of primary concern relate to nuclear specific technologies.
- ← Additional industry review ← the initial version of the MCTL has been submitted to industrial associations and industry technical advisory committees for review. Due to time constraints, such a review could not be thoroughly conducted prior to 1 October 1980.
- ← Additional support data ← supporting data pertaining to the military utility, foreign capability, and adversary capability, are required for many MCTL data items. This supporting data has been developed and reported for approximately 80% of the MCTL items.
- ← Increased specificity ← in the MCTL development, items were often broadly defined to avoid the risk of missing something important by use of a narrow definition. Consequently, many items must be defined in more specific terms to be fully useful.

- Additional items - the development of the MCTL concentrated primarily on the technologies associated with the dual-use (military and civilian) products. Additional effort is required if the List is to include technologies underlying items on the Munitions List (the Munitions List predominantly includes items with military applications although there are some notable exceptions; inertial navigation systems, for example).
- Transfer mechanisms - the mechanism by which a technology can be transferred is key to the control of exports. These mechanisms must be identified to determine what products can be released from control. This project is underway.

Although additional effort is underway to refine and elaborate the MCTL, DoD believes the initial version to be very responsive to the Export Administration Act. Above all, this List identified the essential technological elements that must be acquired to achieve a military capability with superior operational characteristics. We believe the List, with its supporting reports, provides guidance within the Department of Defense for the review of those export license applications that particularly involve the transfer of know-how to Warsaw Pact countries. The application of this Initial List by the Department of Defense to the export of equipment will be in a

manner commensurate with the CCL and Export Administration Regulations, and will not supercede the technical definitions of the CCL until further refinement dictates suitable specification revision.

The Department recognizes that the initial version of the Militarily Critical Technologies List is only a first step. This process must proceed from internal agreements among technologists to interagency agreements among those with non-technical perceptions to international agreements among those who must consider different laws as well as views. The technical-to-interagency-to-international procedure is required in proceeding from the identification of militarily critical technologies to a Commodity Control List (CCL) which includes these technologies (as called for by the Export Administration Act). In this year's program, the Department will identify the necessary revisions to the CCL after consultation with our allies to fulfill the requirements of the Export Administration Act. Specifically, the CCL is being reviewed to determine:

- Revisions to the CCL required to assure control of critical technology transfer. What technologies are there on the MCTE which are not now under adequate CCL control?

- ← Revision to remove products from control which do not transfer critical technology when exported and which do not have intrinsic military utility. What products do have intrinsic military utility?

As shown in Figure 3, the CCL review as described above should be completed by this August. Proposals to revise the CCL to incorporate MCTL items will first be available for interagency review in July of this year. Spearheading these proposals will be one specific technological area, semi-conductor/electronic component technologies. After interagency review of proposals in the semi-conductor area, proposals will be developed to revise the COCOM List and the CCL to incorporate MCTL items in the remaining technological areas. Proposals will also be submitted to the other agencies for modifications, addition or deletion of the CCL product control. These draft proposals should also be available in August of this year.

The Department recognizes that if the export control process is to be effective, the technologies on the MCTL should be controlled multi-laterally. Toward this end, we will be working with the other agencies to prepare proposals to COCOM.

Is the Distinction Between Products and Technology Valid?

The distinction between products and technology is valid. Areas do exist, however, where products are inextricably linked with the advance of technology. The MCTL provides examples whereby products are identified which are key to the advancement of a technology (e.g., keystone equipment) or which cannot be used without providing information which embodies a critical technology. These products are transfer mechanisms of technology and must be treated as such for export control purposes.

There is another class of products which must also be considered for control. These products are those which have intrinsic military utility. Although such products may not transfer a militarily critical technology, their production by an adversary may be of insufficient quantity or quality for full realization of their military utility. Exports which provide such realization must be controlled.

Products that do not fall under the above categories will be reviewed for removal from the control lists.

Can National Security Controls be used to Create Bottlenecks in the Soviet Industrial Structure and in Soviet Energy Production?

Our export control process and on-going critical technology analysis are considered as micro-approaches, instituting

controls on individual transactions based on established high technology thresholds. These controls, however, may not be sufficient to prevent the USSR from modernizing or increasing the efficiency of entire industrial sectors which are relevant to military production or operations. The Soviets have imported know-how, equipment and entire turn key operations which were inadequately controlled because the transactions involved fell below the "high technology" thresholds.

We believe it is possible to inhibit growth in Soviet militarily-relevant industrial sectors (including Soviet oil and gas production) by controls on know-how, keystone equipment and critical raw materials.

We have identified industrial sectors which we intend to analyze for the bottlenecks in conjunction with our allies. Additional restriction on exports could be imposed, however, the policy decision as to the extent to which our export policy in this area should be revised has not been made pending the completion of an interagency study.

ADDITIONAL INFORMATION

Mr. Chairman, there are two other areas that should be of interest to the subcommittee. The workload of the Department with respect to license applications, and the time required to process applications.

DoD Work Load with Respect to License Applications

The workload has been a subject of increasing interest in the Department, not only as a result of the time limits imposed by the Export Administration Act of 1979, but also from changes resulting from post-Afghanistan policy and an increase in trade with the Peoples' Republic of China. These changes have resulted in a reassessment of the risk associated with export to proscribed countries. In this reassessment, we have perceived an increased risk that security sensitive goods exported to the Soviet Bloc will be (1) diverted to military use; or (2) diverted to the Soviet Union. Concurrently, a selective increase in exports to the PRC is now perceived to be in the national interest. This reassessment has had impact on the workload of the Department beyond that demonstrated by statistics. Although there has been a reduction in applications for exports to the Soviet Union, this reduction has been offset by the increase in applications for PRC exports. Moreover, Warsaw Pact exports have had to be reviewed with even greater scrutiny to examine carefully the potential for diversion to military use.

PRC export applications have also taken longer to process as analysts have been giving every consideration to parameter changes that can make the application acceptable.

During the period October 1979 to March 1981, my office reviewed over 4,200 license applications for exports. Of these,

3,031 were U.S. origin export applications, 1,100 were non-U.S. applications from COCOM countries.

Of the 3,031 applications for exports from U.S. companies, Defense has submitted its position on 2,652. The remainder (379) are currently still being processed. Of those licenses which were completed, 1,389 or 52% of the cases were validated license requests for the sale of high performance computer equipment to non-Communist countries. Two hundred fourteen (214) or 8% of the cases involved sales to the USSR; (645) or 24% of the cases involved sales to Eastern Europe and (404) or 16% of the cases involved sales to the Peoples' Republic of China (See Figure 2).

As shown by the attached graph, (Figure 3) we have arrived at a Department of Defense position of 90% of cases received within 30 days and 95% of all cases within 60 days.

The referenced figures and graph do not include the 1,100 non-U.S. COCOM cases. In addition, to the 4200 applications above, another 1,000 license applications for the Soviet Union were reviewed as a result of Afghanistan. They included those licenses which had previously been approved, but had been suspended on 8 January 1980, and those which DoD does not normally review. These licenses were subjected to a review in accordance with the newly established (more stringent) guidelines.

FIGURE 1

CRITICAL TECHNOLOGY PROJECT — 1981/1982

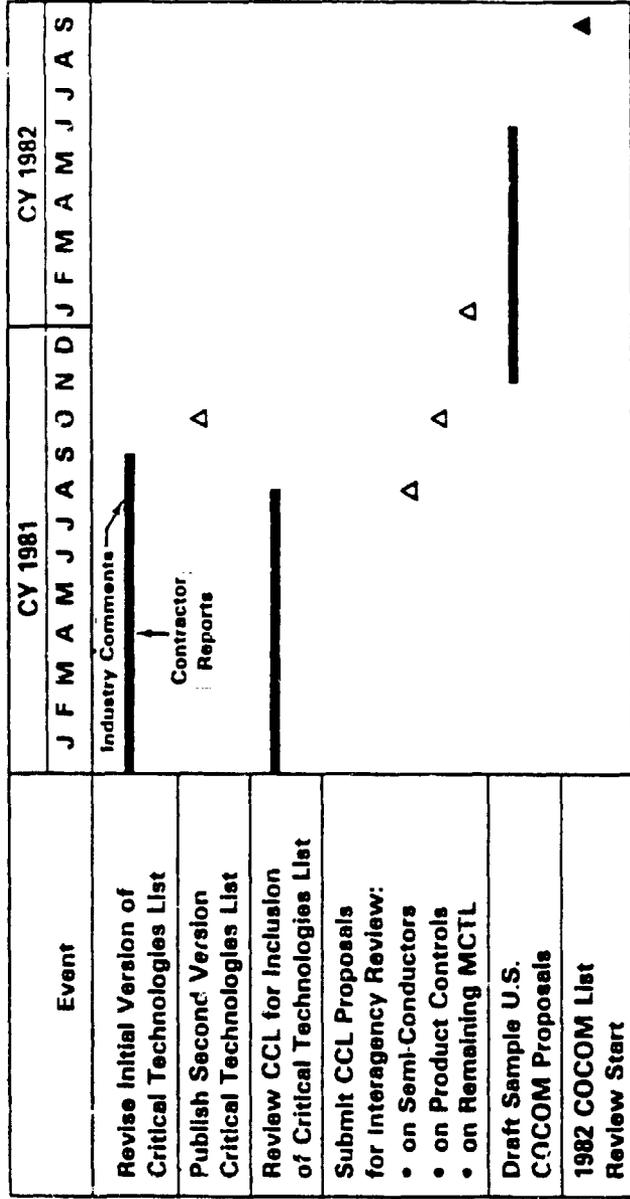


FIGURE 2

U.S. APPLICATIONS FOR TECHNOLOGY EXPORTS
TO COMM PROSCRIBED DESTINATION
1980 FROM OCTOBER 1, 1979 TO MARCH 31, 1981

Country	Processing Time (Days)						TOTAL APPROVE DENY
	0 - 30		31 - 60		61 or more		
DISPOSITION	APPROVE	DENY	APPROVE	DENY	APPROVE	DENY	APPROVE
SOVIET UNION							
No. of Applications	116	21	29	10	55	5	211
Percentages	54%	10%	14%	5%	16%	1%	
	64%			19%		17%	
EASTERN EUROPE							
No. of Applications	420	50	79	40	54	22	635
Percentages	65%	8%	12%	6%	5%	4%	
	75%			18%		9%	
FRG							
No. of Applications	217	32	58	31	27	39	101
Percentages	54%	8%	14%	7%	7%	10%	
	62%		21%			17%	
TOTALS							
No. of Applications	753	103	166	81	96	64	1,363
Percentages	60%	8%	13%	6%	8%	5%	
	68%		19%			13%	

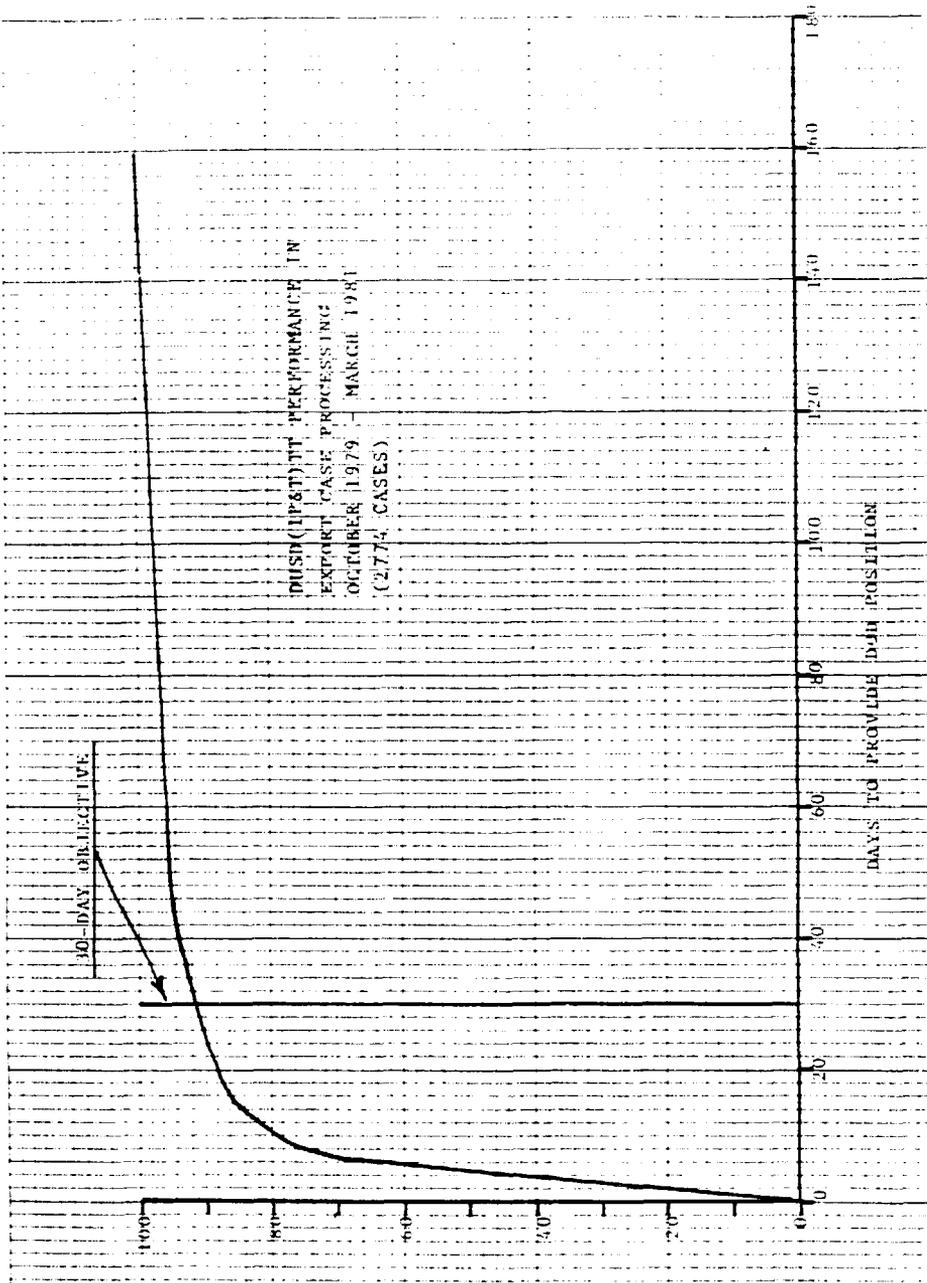


Figure 4

United States SenateCOMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS

WASHINGTON, D.C. 20510

April 20, 1981

The Honorable Richard DeLauer
Under Secretary of Defense for
Research and Engineering, Designate
Department of Defense
The Pentagon
Washington, D.C. 20301

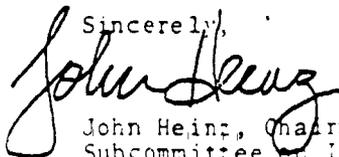
Dear Dr. DeLauer:

You are invited to testify before the Subcommittee on International Finance and Monetary Policy on Thursday, April 30, 1981, at 9:30 a.m., in Room 5502 Dirksen Senate Office Building. The principal purpose of the hearing is to provide the Subcommittee with information necessary for a decision on the authorization of appropriations for fiscal years 1982 and 1983 of the Export Administration Act.

Since your department plays the principal role in formulating national security controls, you would be a valuable witness. In particular, we would be interested in your views with regard to the role of national security controls in our overall national security policy. Such controls have been tightened in response to the Soviet invasion of Afghanistan, and it would be useful to hear a report on the effect of that tightening. It would also be useful to get a progress report on the "critical technologies" effort which your department has undertaken. Is the distinction between "product" and "technology" a valid one? Finally, it has been argued that national security controls can be used to create bottlenecks in the Soviet industrial structure and in Soviet energy production. The Subcommittee would be interested in your comments on that usage of national security controls.

In accordance with Committee rules, 100 copies of your testimony should be delivered to the Committee 24 hours in advance of the hearing.

Sincerely,



John Heinz, Chairman
Subcommittee on International
Finance and Monetary Policy

Senator GARN. Mr. Kopp?

Mr. KOPP. Thank you, Mr. Chairman. I will try to be quite brief in summarizing my statement, which I presume will be placed in the record.

Senator GARN. Yes, it will be placed in the record.

Mr. KOPP. We are involved with foreign policy controls and national security controls. With respect to the former, foreign policy controls, the comprehensive account of controls in place at the end of 1980 has been published and is available to the committee.

There have been some developments since the beginning of the year in the new administration which I would like to call particularly to your attention.

First of all, in the area of licensing policy, we have notified the Congress, we and the Commerce Department notified the Congress on March 31 regarding the sale of five Boeing aircraft to Iraq. That license should be issued within the next day or so.

In the area of control policy, the committee is aware of the lifting of the controls on agricultural products to the Soviet Union.

The other foreign policy controls that we have in place are to be reviewed by the new administration and further adjustments or changes may be forthcoming.

In the area of security controls, the Department of State participates under Commerce Department leadership with the Defense Department in making decisions on individual cases that come up for licensing. Our primary role is representation of the United States in COCOM and in other discussions and negotiations with our allies on multilateral export controls for security purposes.

COCOM, as you are aware, is an informal organization of the NATO countries plus Japan. It is based on no treaty. There are no sanctions for violations of COCOM rules and procedures. Nevertheless, the recognition of the need for multilateral controls is so strong that the organization has stayed intact for more than 30 years. The instances of violation of rules and procedures have been extremely rare.

We now have pending before COCOM several proposals aimed at tightening controls on certain items. These are the proposals that, as Mr. Lomack described before, we put forward following the Soviet invasion of Afghanistan.

As a result of the critical technologies exercise now underway in the Department of Defense we have raised these issues with our allies at high levels as well as at the technical level in COCOM. We will continue to press these issues with our allies.

Thank you, Mr. Chairman.

[Complete statement of Mr. Kopp follows:]

STATEMENT OF HARRY KOPP, DEPUTY ASSISTANT SECRETARY OF STATE

Mr. Chairman, I welcome this opportunity to review for the committee the State Department's role in implementing the Export Administration Act of 1979 (Hereafter, "The Act"). The State Department is actively involved in carrying out many functions authorized by or referred to in the Act. The most important are foreign policy and security export controls.

FOREIGN POLICY

Controls on exports, for the purpose of promoting the foreign policy goals expressed in the Act, come under continual review. A comprehensive review soon after

passage of the Act led to publication in the Federal Register on January 8, 1980, of controls for the areas of human rights, terrorism and regional stability, South Africa, the four embargoed communist countries. Oil and gas equipment to the USSR, and nuclear non-proliferation. Subsequently, controls were placed on other items to the USSR. Controls to combat international terrorism were expanded on May 21, 1980. In the renewal of these controls which became effective December 31, 1980, a revision was made in controls on computers to South African government agencies.

We should note the distinction between the control of an item, which gives the State Department the opportunity to review applications of a given category, and the Licensing policy, which states which items should be denied and which should be approved. Of the 247 cases received by the Department of State for foreign policy review in the past three months, 82 percent have already been recommended for approval, 3 percent for denial, and 15 percent are still under consideration. Below, I describe some recent examples of revisions in the controls themselves, and of licensing decisions taken under those controls.

Our embargo on sales to the South African police and military and restrictions on exports of computers to South African Government agencies serve to underscore U.S. opposition to the policy of apartheid. On December 31, 1980, State recommended, and Commerce concurred in a revision of controls on computer sales to South African Government agencies to cover low capacity computers.

Controls on the sales of items which could significantly contribute to the military potential of the four countries which have repeatedly provided support for acts of international terrorism, (Libya, Syria, Iraq and the People's Democratic Republic of Yemen) indicate our strong opposition to such acts and our determination to use export controls judiciously in efforts to discourage support for such acts.

Aircraft valued at more than \$3 million are subject to review for foreign policy reasons if they are destined to these countries. The Departments of State and Commerce notified Congress on March 31, of their intention to issue licenses for five aircraft for civil use in Iraq. In this particular case, we took into account the economic importance of the transaction for the U.S., its commercial importance for the U.S. manufacturer, the civil end use of the aircraft on scheduled domestic and international routes, Iraq's adherence to the three major conventions dealing with the safety of international civil aviation, and the assurances which have been received that the aircraft will not be used by military or police services.

In a separate case, an application to renew the export license for engine cores to be used in Italian built naval frigates ordered by the Iraqi Navy was referred to the Department of State under controls issued in accordance with Section 6(i) of the Act. This application is directly affected by our policy of not approving significant military sales clearly destined for use by one of the combatants while the conflict between Iran and Iraq is continuing.

Several years ago, regional stability controls were imposed on exports to Libya of large vehicles capable of transporting tanks. This was in response to Libyan destabilizing actions against neighboring countries. We are now recommending to the Department of Commerce that small aircraft be added to this control category, because Libya has previously used such aircraft for military purposes.

While the circumstances that prompted the original imposition of our almost total embargoes on trade with Vietnam, North Korea, Kampuchea, and Cuba have changed, it would not be in the U.S. foreign policy interest to ease these restrictions except as part of a general improvement in relations with these countries.

Restrictions on sales of crime control equipment are designed to help deter human rights violations. State has recommended to Commerce that four items not originally envisaged for this category but put there in 1979 for administrative convenience be removed from the crime control list. They would continue, however, to be controlled to countries supporting terrorism and to South Africa. These items are military specification vehicles, specialized machinery for arms and ammunition manufacture, equipment for production of military explosives, and components and parts for ammunition.

The foreign policy controls which have been most in the public eye are those imposed on the Soviet Union. Restrictions on the sale of grain and other agricultural commodities, phosphates, items connected with the Moscow Olympics, and the diesel engine assembly line for the Kama River truck plant were all imposed to demonstrate that the USSR could not with impunity invade Afghanistan. The controls on grain, other agricultural commodities, and phosphates were lifted on April 24 in order to follow through on a commitment that the President undertook before taking office to relieve the unfair burden imposed on the American farmer, and because the President found the policy ineffective.

Controls on the export of oil and gas exploration and production equipment and technology were imposed in 1978 to provide a flexible foreign policy tool which might be used in efforts to influence Soviet behavior. In 1980 it was decided that applications to export industrial technology for manufacturing such equipment should be subject to a presumption for denial. The presumption for approval of oil and gas end-use equipment not otherwise subject to national security controls was continued. These controls allowed, as an example, the issuance of a license in November 1980 for sale of pipelayers for use on the gas pipeline from Siberia to Western Europe, although the license was not followed by a Soviet order for that purpose. We are now in the process of reviewing these foreign policy controls as well as our overall policy towards Soviet oil and gas production. Questions regarding Western dependence on the USSR for natural gas are related to this issue and are being discussed with our Allies.

Section 17(D) of the Export Administration Act of 1979 and section 309(C) of the Nuclear Non-Proliferation Act of 1978 are relevant to controls on commodities and related technical data that could be of significance for nuclear explosive purposes. The objective is to deter proliferation of nuclear weapons. The Department of Energy reviews license applications for export of these items and refers those requiring additional review to the interagency NSC subcommittee on Nuclear Export Coordination (SNEC), which is chaired by the Department of State. This review process includes consideration of the stated end-use of the commodity, its sensitivity and foreign availability, the assurances and guarantees provided by the importer, and the non-proliferation credentials of the recipient country. During the past year, the SNEC has reviewed approximately 200 cases.

A detailed list and justification of all outstanding foreign policy controls being renewed was submitted to the Congress on December 31 and the year-end report pursuant to section 14 of the EAA describes activity during 1980.

SHORT SUPPLY CONTROLS

The Department of State provides foreign policy guidance in the administration of export controls on commodities considered to be short supply. Our most significant recent involvement in this area has concerned review of proposed exports of refined petroleum products which require a license pursuant to Section 7(e) of the Act.

SECURITY CONTROLS

The Department of State is an active participant in the administration of security export controls in accordance with Section 5 of the Act. Working through the Commerce chaired Advisory Committee on Export Policy (ACEP) and its working level "operating committee", State assists in assessing the national security implications of specific U.S. transactions and licensing policy decisions. State also insures that decisions on policy and on particular cases are consistent with relevant U.S. foreign policy objectives and with efforts to maintain effective multilateral controls through COCOM. As directed by Section 10 of the Act, State has established internal procedures designed to expedite responses to Commerce requests for recommendations on U.S. cases.

Pursuant to section 5(k) of the Act, State conducts negotiations with other countries regarding cooperation in controlling exports for security purposes. This is done primarily in the Coordinating Committee known as COCOM. State responsibility includes conducting "negotiations with respect to which goods and technology should be subject to multilaterally agreed restrictions and what conditions should apply for exceptions from those restrictions." COCOM is a voluntary organization established in 1950 to coordinate Allied national strategic export controls. It has 15 members—the NATO countries minus Iceland, plus Japan. Actions in COCOM are in effect recommendations to member governments, and they become effective only as they are carried out by member governments through their individual export control programs under their own national laws and regulations.

A basic rule for COCOM from the outset has been that all COCOM decisions require unanimous agreement. COCOM members have agreed to control the technically detailed list of items negotiated in the Committee.

The COCOM list has evolved over the last thirty years. It now consists of three parts: A munitions list, an atomic energy list, and an industrial list. These lists are comprehensively reviewed approximately every three years, in lengthy and detailed list review negotiations. The last such list review was completed on December 14, 1979, and the results became effective April 1, 1980. The next list review has tentatively been scheduled to begin in the fall of 1982. Between list reviews, definitional discussions are held on specific embargo items, so that updating does not have to wait for the next list review.

Exceptions from the multilaterally agreed control list can be approved at national discretion for the low performance portions of some items. Otherwise, exceptions can be granted only with the unanimous consent of the Committee. A member state may choose to disregard the COCOM decision on an exception case, but this has not occurred often.

The Department of State chairs the inter-agency Economic Defense Advisory Committee (EDAC) structure for formulating U.S. proposals and positions on COCOM issues. This structure channels to State technical guidance and policy advice from interested U.S. agencies, particularly the Departments of Defense, Commerce, and Energy.

Section 5(f)(4) of the Act provides for the initiation of negotiations with other countries to prevent U.S. national security export controls from being undercut by the availability from third countries of similar commodities or technologies. Foreign availability is taken into account during COCOM list reviews. It is therefore seldom a determining factor in the review of individual cases. State initiates appropriate discussions with relevant foreign governments in efforts to eliminate or reduce foreign availability. These discussions may be held bilaterally or in COCOM. They usually entail a request that a foreign government forgo the transaction or condition its approval along lines which would minimize security concerns. Following the last list review, State discussed the resulting controls with several non-COCOM countries in efforts to obtain their informal cooperation.

Section 5(I) of the Act calls for negotiations with the governments participating in COCOM with a view toward (1) obtaining agreement to publish the COCOM embargo lists, (2) Holding periodic meetings with high level representatives to discuss export control policy issues and provide guidance, (3) reducing the scope of export controls to a level acceptable to and enforceable by all COCOM members, and (4) improving enforcement procedures regarding such export controls. The Congress was notified in the 1980 year end report pursuant to Section 14 of the Act of the results of the Section 5(I) negotiations.

Senator GARN. Thank you.

Mr. O'Day, as you know, for a couple of years I have been very critical of Commerce in this area of export controls. Now we have a GAO report which certainly is not very complimentary in a number of areas. Can I ask you to respond in general to GAO's report. Are they accurate?

Mr. O'DAY. We have not seen the entire report, Mr. Chairman. It would be difficult to be specific.

Senator GARN. That's why I asked for a general statement. You sat here and listened to the same thing I did today.

Mr. O'DAY. In general, we appreciate the report. We think it will be helpful to us in improving a number of problems. There were a number of areas mentioned that we have already started to work on. We have begun increasingly to work with the FBI. We realize they have jurisdictional problems, but we have started to seek their advice and help more frequently. We have started weekend- and evening-inspection of cargo. Our inspectors, although they are few in number, are traveling far more now and their numbers run into thousands of cargo inspections now underway on an annual rate.

We are focusing on the compliance problems that they have mentioned in our budget. We are reorganizing resources available to us through ITA to make sure that compliance is carried out in a manner that is effective.

As I said, we are looking forward to examining the details and working with the other agencies to see what we can do.

One major area, one of the fundamental findings summarized by Mr. Conahan regarding low technology versus high technology. That is a subject that we have been looking at for some time. It is a very difficult one. We know we are putting a burden on exporters by requiring applications in far more cases than we ever seriously

considered for denial. On the other hand, perhaps we are tilting over too far in this regard.

There are low technologies that are militarily significant. We have to be careful, we think, in Commerce as we administer this program, to keep that particular taste before us as we decide to cut back the list. It is an issue we have been looking at carefully with other agencies and with the specific findings in the GAO report perhaps we can find ways to appropriately cut back the burden on exporters without threatening national security.

Senator GARN. You are screening a tremendous number of applications every year. That is one of my concerns. You are spending so much time screening routine applications that the very sensitive high-technology items in some cases are slipping through. Some 50 percent of your budget is for this screening, paperwork burden. Only 25 percent is for compliance. In many cases you are well over 30 days in granting the applications or approval for routine exports. Is there an imbalance there, with 50 percent of your budget compared to 25 percent in compliance?

Mr. O'DAY. The great majority of the resources go to the most difficult cases. The routine processing takes place on an average of 12 days per case, and we have to be sure that we have the right information and to be confident that we are not threatening military security by allowing the application.

In a recent check in the aircraft area we issued 500 licenses last year. They were issued on an average of 12 days each. In 40 of those cases we had requests for special processing because it was related to the opportunity for sale, and in those cases we issued the license within 2 days.

The real workload is in the most difficult cases. Consulting with the applicant, making sure that as we transfer the information to Defense we are giving them the proper information. It is in that area where most of our licensing effort is concentrated. It is the most difficult part of the program.

Senator GARN. Looking at 1980, you received almost 70,000 applications for exports to the Free World. Of that 70,000 only 80 were denied. Wouldn't it make some sense to try to screen out many of these applications to the Free World and concentrate more on those to the Communist-bloc countries?

Mr. O'DAY. That is a major management problem. In addition to the 80 that were denied there were some several thousands returned without action. So they have to be counted in the results of the review. It is the age-old problem of a very complicated system. We all know, for example, that we could perhaps remove half of the books or more from the Library of Congress and no one would ever know the difference. The question is which half.

We think in this case we are reviewing all of the low-technology cases that we should be sure that we do not miss any that would have military-security implications, and some of the most celebrated cases have come through this process.

We very much look forward to seeing the specific analysis results of the GAO report to whether or not there are ways suggested there for us to sort this out and remove the burden.

One additional factor is, as we looked at this last year, the problem of compliance follow-on should militarily significant diver-

sion occur after export from the United States—if we did not have the processing in place where exporters have to apply before they ship goods. Justice and Commerce had some serious questions there. We put that aside for further study.

It is a major problem, there is no question about it, Senator. We look forward to the GAO findings.

Senator GARN. I don't minimize the difficulty of sorting these things out. I'm not so sure that the Library of Congress is a good comparison. We are talking about massive amounts of routine applications, and we get the articles about silicon spies in the New York Times and some critical technology that they feel they have documented that are going to Communist-bloc countries.

Your burden is tremendous. You have been understaffed in the past. It seems to me, as an outsider—and I'm also waiting for the GAO report—there are a tremendous amount of routine things going on that in some way we ought to be able to draw that line more finely. There will always be something that slips between the cracks. I understand that.

It appears to me that you are doing a tremendous amount of what I would term "busy work" and letting bigger things slip through the cracks.

Mr. O'DAY. There are resources that could be used in other areas. But we put our priorities for the new resources in filling our vacancies and reprogramming into the much more critical area of compliance. With the new office on the west coast, we can get at some of the problems onsite, mentioned in the article you just displayed. Those are our priorities for the coming months. And we want to be sure that we reduce the low technologies applications.

Senator GARN. Do you agree with the Carter administration's decision to allow the Government to participate in the Yamal pipeline project? I will ask all three of you this question. [Laughter.]

So you don't need to confer with each other.

[Laughter.]

Mr. SKIDMORE. I would handle this question, Mr. Chairman, with your permission—which I may not have by being somewhat unresponsive. I think that is an issue that should be discussed by policy-level people, and as a civil servant, I implement the policy that is made. I take it that you are not asking for my personal opinion, but rather, for my official opinion.

Senator GARN. That's correct. And I understand. I understand you have some difficulties.

Mr. Kopp, you testified before the House committee. You stated: "We are now reviewing our own policy questions concerning the tolerable degree of dependence on the U.S.S.R. for natural gas."

What do you mean by "tolerable degree of dependence" on the Soviet Union? Is that a percentage? Is there a percentage that is all right?

Mr. KOPP. Our European allies are very heavily dependent on imports for energy. They get their imports primarily from the Middle East; also to some extent now from the Soviet Union; and coal from the United States, in some measure. And many of these countries are interested in diversifying their sources of supply. There is great concern about the reliability of Middle East, as well

as Soviet, supplies. These countries do not feel comfortable, needless to say, in their position.

The possibility of substantially increasing gas from the Soviet Union through the Yamal pipeline is something that we have talked to our allies about. We have talked to them in terms of their energy security, what possibilities they have to replace these supplies in the event of a cutoff should that deal go forward.

We are looking at alternate supplies within Europe as well as the possibility of supply of U.S. coal, and at the wisdom of arranging things so that plants that take Soviet gas can be rapidly converted to other forms of energy. We are looking at questions related to the final users of the gas that will come through that pipeline, whether residential or industrial. Residential is the hardest to give up. All in all, we are trying to work with our allies to assess, first of all, what they consider to be tolerable, that is, safe, in terms of gas imports from the Soviet Union; and to assist them in their analyses and in trying to arrange backup supplies, so that gas coming through the line, if the project goes forward, can be replaced.

As to the U.S. participation in that project, the Carter administration approved a license for shipment of pipelayers. That contract between the United States and the Soviet Union was not, in fact, concluded. We have before us a new application for amendment of the previous license, involving shipment of pipelayers for use in construction of other pipelines. We are examining that policy currently. We have the license application before us.

Senator GARN. That is a phrase that has no definition yet, in your words.

Mr. KOPP. It is really not up to the United States to define for Germany or for France what they consider to be "tolerable."

Senator GARN. I understand that. They have not made that decision yet for themselves.

Mr. KOPP. I don't think you can express it in terms of a percentage of supply. What is critically important is opportunities to replace Soviet supplies if they are cut off. If you have adequate backup facilities, in the event of a cutoff of Soviet supplies, then you are not really dependent; you have some safety net.

I think the concept of the safety net is more important than a single quantitative measure as to a percentage of total gas imports consumption, or total energy consumption, at least that is the way we have been working on the problem.

Senator GARN. Well, I would agree it is not just a percentage.

I happen to think it is a very dangerous thing for them to do. And our western allies, I think—I understand why they have been invaded century after century. They make accommodation after accommodation after accommodation, and wonder why they are involved in another war.

Mr. O'Day, has there been any attempt to have the technical advisory committees come up with advisory requirements for licensing that would eliminate some of the low-technology exports that we have already discussed, that are clogging up the system?

Mr. O'DAY. We expect to use the committees to do that as we get into the process of following up on the GAO report. We have been

using the committee for advice of that sort—the items we should be controlling.

Senator GARN. Would you support publishing of technical data to help determine what should be licensed?

Mr. SKIDMORE. I don't understand that question well enough to comment.

Mr. O'DAY. It would depend on what the publication of technical data actually contains.

Senator GARN. You are budgeting \$200,000 for the analysis of foreign availability. How specifically do you intend to establish this capability in future years?

Mr. O'DAY. This is a one-time request in the fiscal year 1982 budget. In the current year, we spent about \$60,000 on consultants in foreign availability studies. And the plan for the use of the \$280,000, should that come to us in the fiscal year 1982 budget process, we want to, in that process, to take a close look at several key technologies and see if we can develop a standard library, standard data system on availability, that would be useful to us in making decisions at that area.

I should say that we don't make very many decisions to allow exports because there is foreign availability. It is the last factor we look at, only after we examine the other criteria that dominate the system with regard to decisions in this area. Since there is some interest, both in the Congress and the private sector, that perhaps if we took a closer look at foreign availability, we would have the opportunity to allow a few more exports to flow we feel we need to look at that very closely and see if that could be a significant factor. We are looking at a technical consultant-based study of several key technologies that will allow us to factor that in.

Senator GARN. Have you considered using your technical advisory committees as sources on foreign availability?

Mr. O'DAY. Yes; we were using not only those committees, but individual companies, and we will use our posts abroad, use technical specialists wherever we can find them, to make sure that we have complete range of information on the technologies to assure that we understand just what foreign availability is in place, and see if we can factor that into the system.

Senator GARN. You mentioned that you have asked for 33 additional staffers who probably will be reprogrammed from other parts of Commerce.

I realize the need for additional staff, but considering the technical requirements of the job, will you be able to get the qualified people that you really need for this type of function?

Mr. O'DAY. We hope so, Senator. We will not know for sure until we actually put out the request for applications for employment. Obviously, some of our need is for very highly skilled technical people that are in short supply. In the compliance area, that makes up about one-half of the 33, we feel there is an adequate pool of individuals available to allow us to get some skilled investigators to allow us to beef that program up substantially.

Senator GARN. Fifteen of these new positions are going into compliance?

Mr. O'DAY. Yes.

Senator GARN. You mentioned you are working with the FBI, also with Customs?

Mr. O'DAY. Yes, very closely.

Senator GARN. And you have relationships of cooperation?

Mr. O'DAY. Yes, we have a reimbursement arrangement with Customs. We work with them not only on inspections, but investigations wherever we can combine our resources to get better and quicker results.

Senator GARN. You mentioned that you were having the inspectors travel more. GAO reported that Commerce had a total of seven export inspectors. Four are stationed at JFK. That seems a poor use of compliance personnel. You are sending more people around now?

Mr. O'DAY. Yes, sir, they are doing far more traveling than in the past, to a number of locations around the country.

In addition, we are adding another element to our system, which is the use of 47 field offices we have around the country. Whenever we need manpower in any one of those posts to go out and check on particular shipments, or with particular companies, we are going to develop the approach to use the several hundred people we have available in another element of Commerce under ITA. We will get leverage with existing resources—and not attempt to cover the 300 ports that Mr. Conahan mentioned with dedicated staff. We will use the available resources in high-priority areas.

Senator GARN. Have you considered sting-type operations?

Mr. O'DAY. I would rather not comment on that, sir.

Senator GARN. It is my understanding that an exporter, when selling goods on the COCOM list to other COCOM countries, must get a letter assuring that they will not reexport the goods without proper licensing. If the foreign purchaser decided to reexport the goods anyway, is there any way other than through government to government contacts that we can reach the foreign exporter? And of what value, then, is the letter of assurance, if we are not able to reach them?

Mr. O'DAY. That is a compliance question which I would like to ask Ms. Connelly to answer.

Ms. CONNELLY. We can bring an administrative action against the foreign party, and deny their export privileges. What that means is that they will no longer be able to deal with U.S.-originated commodities outside the United States.

Senator GARN. Is it effective? Does it work?

Ms. CONNELLY. It is very effective. We did bring actions against foreign parties. We placed them on our denial list. And the thing that makes it most effective is that it is a violation for a U.S. party to deal with that party. It makes it much harder for the foreign party to do business.

Senator GARN. How many are on the denial list? Just an idea.

Ms. CONNELLY. About 90 parties on the denial list. The majority of those are foreign parties. You will find that last year we placed more U.S. parties on the list than we have in previous years.

Senator GARN. Is the value of assurance really that good? Or would it make more sense with some of these countries to treat them like Canada and try to enforce the COCOM on them, rather

than go through all this type of procedure with letters of assurance?

Ms. CONNELLY. I'm not sure that I can comment on that.

Mr. KOPP. We have been examining the possibility of amending the regulations so that in fact things would operate as you suggest, that we would rely on COCOM countries to enforce COCOM controls. We are examining what enforcement problems that might create, what the risks are. I hope we can come to a conclusion that will permit us to lessen the burden on Commerce personnel on handling all of the paper.

Senator GARN. As more and more products combine technologies, such as the Apple computers, how do we limit access to our enemies? We cannot post a guard at every Radio Shack, or everyone who sells electronic equipment. What I am trying to get at is the technology, which obviously is advancing much, much faster than we can control access to it—should we try to protect the know-how, and perhaps focus less on the actual products. In the late 1940's and 1950's, military research in fields like avionics, led the commercial sector, and it was relatively easy to control technology. Now the reverse is true. Would there be some value in focusing on the technology itself, and the know-how, perhaps asking for registration by companies in these advanced areas, rather than try and control the Radio Shack?

Mr. O'DAY. We are not in a position to handle every commercial outlet that handles technologies.

With regard to specific proposals for registration, we would have to look at those carefully, and consider them in conjunction with the others. Defense is working on identifying the critical technologies. We look forward to the results of that process, and the reduction of it to items that we can put on the CCL list.

Senator GARN. Wouldn't it be easier to keep some controls—where you look at the technology? You see ads for the 64 K-RAM Apple computer and other ads like this. Obviously, you can't control all of those sales. But we really don't know what's going overseas.

Mr. O'DAY. That is a fair comment. Our jurisdiction starts at the border. In our own free market system, these goods flow without restraint, without reporting.

I don't have a good answer as to how one controls the millions of individuals who can buy these items, that are sometimes small enough to put in their pockets.

Senator GARN. You can't do that. That's why I'm looking for other ways to try to control the technology and the know-how, is there no way you can control the individual products in cases like the example that I used?

Mr. O'DAY. We are aware that it is a major problem. We don't have any good ideas on that right at the moment, how to assure that items available to all of the consumers in this country would not go offshore.

I am not aware personally of any specific recommendations for going back toward the producer, and trying to control at that level, in a way that would prevent the offshore selling of these goods.

We would be glad to examine any proposals.

Senator GARN. Dr. Lomacky, 80,000 validated licenses were received, and DOD received 3,000. Is that adequate? Do you think you should be looking at more?

Dr. LOMACKY. The bulk of the licenses, as you have already heard, are not to the Warsaw Pact or PRC. They are non-Communist destinations. I am not sure that we have to be so concerned about the numbers of these things. Some of them are controlled. Most of them are controlled—for a very simple reason. We want to be able to monitor the possibility of transfer to the block.

So, perhaps speedier processing of these applications would be helpful.

We are concerned about the retransfer problem. I am not too sanguine about making a tremendous impact on reducing the number of these products that we have to review. Most of them are the ones that are controlled by COMCOM.

Those countries where we might have one more reassurance that they are not retransferred—we simply want to keep track of those. I look at that mostly as a monitoring operation.

In terms of the applications to the Soviet Union and Warsaw Pact in general, I think perhaps we should be looking at more. As a result of the critical technologies project, we will be identifying some products on the CCL list which we would consider to be of marginal importance, in terms of the critical securities controls. We may decontrol some of those items entirely.

We should be looking at more important cases, perhaps more cases to the Soviet Union, than we have been looking at in the past.

Senator GARN. Do you feel that Congress is doing an adequate job of identifying significant cases for DOD review?

I agree that the numbers by themselves, 3,000 or 4,000, are not as important as your being aware and being able to review those that are significant.

Dr. LOMACKY. I am encouraged by the new team at Commerce. We are going to be working very closely in this area.

As you probably know, the delegations of authority on all cases going to the Soviet Union, which are controlled for national security—all of these cases are now being reviewed by the Department of Defense.

The cases going to Eastern Europe—not all of them are reviewed by the Department of Defense. We are working closely with Commerce, to make sure that we understand the concerns, both about “low technology” and “high technology” items. I am not sure that these distinctions are very helpful.

I think the low technology, by our standards, may be high technology by the Soviet standards, in their particular applications.

Senator GARN. There has been some concern and internal dispute within Defense on approval and denial of license applications, that have been hampered by inadequate technical review by the military commands.

Can you tell me the extent to which this has been a problem? And whether you are taking steps to supplement their technical reviews?

Dr. LOMACKY. We have been working closely with the services, after the reorganization of responsibilities in the Department of Defense, placing responsibility within my office.

The problem we have, essentially, is that many people in the services are not fully dedicated to this mission. They do it in addition to other tasks.

It is a question of trying to implement a new directive, which will be published very shortly, to make sure that services have this as a kind of a line responsibility, more than they have in the past.

The agreement that we have with the services is fairly rare. We tried to get the best technical judgment. Sometimes we do not have the response of the environment—real time environment in which we have to operate.

Senator GARN. What if you get a split decision? If the Army opposes the Air Force and the Air Force opposes the Navy, for example, how do you make a decision?

Dr. LOMACKY. We try to integrate their views and reach an agreement. If there is not such an agreement, then we give them a chance to reconcile. And then if we can't get an agreement, we may want to escalate to a higher policy level. That is how the decision process works.

Senator GARN. You're talking about within DOD?

Dr. LOMACKY. Within DOD. Yes, sir.

Senator GARN. There are some 33 items not on the COCOM list, unilaterally controlled by the United States. Can you tell me why we are controlling them, and why our allies refuse to go along?

Are these going to Communist bloc countries?

Dr. LOMACKY. I don't know which items GAO is referring to. Some of these—as a matter of fact, the unilateral controls—it is not simply the question of additional products being controlled by the U.S. Government. The technical data aspect is one where we have much broader controls than our COCOM partners. That is an area that is of some concern to us. We would like to have more of a common policy on that point.

Products—I would have to check these, based on the GAO findings—which products they are referring to. Some of them may be negotiated now, for additional COCOM coverage.

Senator GARN. Have the allies been cooperative in this effort?

Dr. LOMACKY. As far as the no exception policy, we are pleased that they have been cooperative. We have reached some agreement on items which we had proposed for additional controls in COCOM. Other items, we may have an uphill battle with. That will be decided this year.

Senator GARN. A recently established program of research and development on the very high-speed integrated circuits involves a number of universities. Presidents at five of the universities have complained that the controls on the research in this area violate academic freedom, to the extent that controls are placed on those who are participating in research.

Why do you think they need to be imposed?

Dr. LOMACKY. We try to make a very careful distinction between basic research and the application and know-how. There are some regulations on the book now which make that distinction fairly

clear. The kind of application know-how which may be involved in some of the university-sponsored work is subject to control.

In general, we do not want to control academic exchanges of a basic science nature. We are concerned possibly about some of the aspects of this program, which have military applications. Here, again, we are working on a program which would enable the control being administered—that we have the least amount of interference in these exchanges.

Senator GARN. Are there any other restrictions in this area?

Dr. LOMACKY. Not at this point. No, sir.

Senator GARN. What about control of foreign students' entry into certain courses?

Dr. LOMACKY. The foreign students, I believe, are those which come from Communist countries. And we have a program now where the Department of Defense reviews some of these visas of particular applicants from the Soviet Union.

I think that there has been too much made of DOD's alleged intent to control all foreign students. That is not our intention.

Senator GARN. The "Christian Science Monitor" reported that DOD has published guidelines to restrict foreign students in the high technology fields that we talked about.

Are these guidelines in effect?

Second, in other fields, aside from the integrated circuits are guidelines being formulated?

Dr. LOMACKY. I am not sure that they have been fully— what the status of implementation is at this point. I would like to answer that question for the record.

What we had in mind was the application—those applications which are essentially done for the DOD, in support of the DOD programs. So the defense contractors and defense-related research would be a matter of concern to us.

Senator GARN. Mr. O'Day, the same Christian Science Monitor article also reported that the Department of Commerce, in the interest of limiting export of U.S. technology, is moving to have universities restrict participation of foreign scientists in research which is sponsored.

Also, the Monitor continued that the Department already has excluded Eastern European experts from attending open science meetings in the United States.

Can you tell me the extent of the Department's efforts to restrict foreign scientists from Department-sponsored research? And whether they intend to continue excluding foreign scientists from open meetings?

And do you think that the exclusion of these scientists is effective in denying them information that is discussed at the meetings?

Mr. O'DAY. We have the letter from the five university presidents, and those problems relate to the Export Administration rules. We are consulting with the other agencies on guidelines on the problems they have raised.

We will also consult, of course, with the university community in that process, to come up with guidelines that will assist them in making their decisions in that particular area.

At the moment, that is all in process. I cannot give you any definitive answer.

Senator GARN. I would say to all of you that I don't ask those questions in an unfriendly manner. Because you may remember that we discussed this before; it was one of the things that I brought up that was really overlooked. We talked about computers, and I went through the list of specific Russian students, in many cases, attending MIT, and so on.

I'm on your side. I know some university professors that may scream "academic freedom." I would like to be able to maintain our academic freedom in this country. But if we do not limit some of this technology, we may find that academic freedom under Soviet rule is quite different.

I am supportive of efforts to cut off this area of technology transfer, as well.

Do you know how many exchange students from the Warsaw Pact countries will be coming here to study?

Mr. KOPP. I can get the figure for you.

Senator GARN. I would appreciate it if you would supply it for the record.

[The following information was received for the record:]

About 120 Soviet students and researchers come to the United States each year. Approximately 25 of these are on direct, university to university programs. Of the remainder, 25 come under an exchange agreement between the Academics of Science of the U.S.A. and of the U.S.S.R. and another 70 are on other government sponsored, but privately administered programs. All these latter exchanges are closely monitored by the U.S. Government.

For other Warsaw Pact countries, the following statistics show the number of persons who entered the United States on visas for exchange students, scholars, and researchers.

Country	1979	1980	1981 to date
Bulgaria	40	42	7
Czechoslovakia	68	59	12
German Democratic Republic	61	55	8
Hungary	212	188	71
Poland	890	982	330
Romania	116	99	24

License Applications Subject to National Security and Foreign Policy Controls
 Referred to the Department of State
 July 1, 1980 - April 15, 1981

Export Control	0-30 Days		31-60 Days		61 Or More Days		Total		Outstanding Cases		
	Recommended Approval	Denial	0-60 Days	61 Or More	Total						
NATIONAL SECURITY	252	66	15	14	2		269	80	10		10
FOREIGN POLICY	2,044	20	37	10	31	8	2,112	38	34	43	77
Human Rights	90	13	11	7	7	3	117	23	7	17	24
South Africa and Namibia	160	2	9		1		170	2		3	3
Anti-Terrorism	102	3	3		0		114	3	12	12	24
Regional Stability	3				4		7				
North Korea, Vietnam, Kampuchea, Cuba	9	2	3		3	3	15	5	1	1	2
USSR and Afghanistan	47		1				48		4		4
Nuclear Non-Proliferation	1,615		10	3	7	2	1,632	5	10	10	20
TOTAL	2,296	86	52	24	33	8	2,381	118	44	43	87

a. Includes all Commerce validated license applications to those countries designated as supporters of terrorism

b. 99% of these cases are for advanced computer exports.

Senator GARN. I have additional questions—some for Senator Heinz and possibly other members of the committee—that I would like to submit to you for written answers.

[Questions and responses can be found on p. 114.]

Are there any other comments that any of you would like to make before we close the hearing?

[No response.]

Senator GARN. I encourage you at Commerce to continue your attempts to tighten up the process. My interest in this all along has been the security of the country. I am very pro-business, but I am not concerned about their profits if it is going to help our enemies.

One of the reasons that I am sensitive to this is because of trying to deal with the MX issue, which could possibly be coming into my State. That is one of the major reasons we need the MX—as a result of the improved computer guidance systems in the Soviet SS-18, which we helped them very dramatically develop, because of the ball bearing machine sales.

I am a little bit sensitive that they will spend \$100 million, at least in part, because of the high technology transfer that was resisted and then finally sold to the Soviet Union. I do not think we differ in what we want to achieve.

I really don't think that the process has worked very well. Somehow, we have got to cooperate—and I say "we," the administration and the Department of Commerce—in tightening up this process as best we can, to eliminate high-technology sales to our enemies; and at the same time try to achieve a balance of where we are not burdened with so many routine export controls that we are putting too much of a paperwork burden on our business in this country.

Thank you very much for your testimony today.

Mr. O'DAY. Thank you.

Dr. LOMACKY. Thank you.

Senator GARN. The committee is adjourned.

[Whereupon, at 11:57 a.m., the meeting of the subcommittee was adjourned.]

[Material ordered inserted in the record follows:]

OFFICE OF THE UNDER SECRETARY OF DEFENSE

Answers to Subsequent Written Questions of Senators Garn and Heinz

GARN:

1. During the past decade, what entities within the Soviet Union have received U.S. computers?

The information required to answer this question must be supplied by the Department of Commerce and is expected within the next week. We will supply a response at the earliest possible time.

2. There have been reports from the computer industry claiming that up to 25% of computer time can be diverted without detection by the U.S. company representative. Is this true, and if so, what improvements can be made in computer safeguards?

In general, the performance level of computers licensed for export is limited to that which would be available from indigenous production in a proscribed country. This excludes the People's Republic of China where a more lenient policy is applied. Short of total operation and control by western personnel, no improvement in available safeguards can insure that no significant computer time is diverted to non-approved use. In addition, the figure of 25% raised in the question may be somewhat low.

3. Out of the approximately 80,000 validated license applications received last year, the Department of Defense reviewed only 3,000. Given the record of Soviet Bloc military diversion of so-called "dual-use" technology, do you feel that the Department of Defense should have more license cases referred to it?

Of the 80,000 validated license applications, less than 10%, about 7,500, involved exports to proscribed countries including the People's Republic of China. The Department of Defense reviewed about 40% (3,000) of the 7,500 cases to proscribed countries. The remainder were not reviewed by the Department of Defense because they involved exports to non-communist countries, spare parts, duplicative sales, national discretion cases and delegations of authority. The Department of Defense believes that earlier precedent and previous Department of Defense guidance is sufficient to allow Department of Commerce to identify potential diversions and review these cases in a responsible manner. However, the Department of Defense is concerned over the items which may be approved under Department of Commerce Bulletin 167. Bulletin 167 requires that products be evaluated according to the type of the assembled commodity. For example, an embargoed micro processor may be ordered as a spare part, without

Department of Defense review, if it is a subcomponent of a larger unembargoed product. The Department of Defense maintains that a one-time review of all such products should be required (1) to insure that there is no national security concern and (2) to establish acceptable parameters for the system being exported. An additional area of concern is the control of technical data exports even to non-communist countries. The Department of Defense may request tighter controls in this area and this will require additional license referral to the Department of Defense. We are now working with the Department of Commerce to solve these concerns.

4. Do you feel that Commerce is doing an adequate job of identifying significant cases for DoD review, and if not, what suggestions would you make?

For the most part, the Department of Commerce is doing an adequate job. However, increased communication between the Department of Defense and Department of Commerce is required to resolve some important differences such as the Bulletin 167 issue discussed above.

5. Do you agree with the Carter Administration decision to allow U.S. participation in the Soviet Yamal pipeline project designed to make Western Europe dependent in great part upon the Soviet Union for energy?

This office had serious concerns with the Carter decision to participate in the Yamal pipeline, due to the national security concerns outlined in the answer to question #7. As you know, the Reagan administration is reviewing the entire oil and gas policy to the Soviet Union at this time.

6. As I understand it, the U.S. still has no formal policy regarding Soviet energy development. No policy has been established as to whether we wish to aid in this development or not. Should the U.S. participate in such a project, in the absence of a clear policy on Soviet energy?

We should not participate in the trans Siberia pipeline project without a clear policy on Soviet energy development. An interagency review is underway in an effort to consolidate the differing views on energy related export policy toward the Soviet Union.

7. Would you agree with many experts that U.S. participation in the pipeline is much more than a foreign policy question, but a national security question as well?

Yes, U.S. participation in the trans Siberia pipeline project is far more than a foreign policy question. The national security question has a number of long term considerations. If such a pipeline does make a competitively priced source of natural gas available to our allies, we must be cognizant of the likelihood that the allies will become dependent on the Soviet Union. In such a situation, schisms may develop among the allies with respect to a unified policy toward the Persian Gulf. Such a possibility is wholly unacceptable to the U.S. In addition, this pipeline would have great utility for the Soviet Union in supporting military logistics. Approving the export of oil and gas cases to the Soviet Union prior to the completion of a cabinet level policy decision would undermine the strong position taken by Defense for stringent security controls over oil and gas technology transfers to the USSR.

8. Do you feel that such participation could jeopardize and undercut our technology sanctions against the Soviet Union, thereby making it much more difficult to obtain allied cooperation in future sanctions, should they be required?

We have taken a policy position with Commerce to withhold licensing of Oil and Gas technology to the Soviet Union. Yamal pipeline options papers are proceeding through the Interagency Group and Cabinet review process to establish a U.S. policy. Defense feels approval of any oil and gas cases to the Soviet Union prior to the IG and Cabinet level decision would undermine the strong position taken by Defense for stringent security controls over oil and gas technology transfers to the USSR. With respect to the Yamal pipeline, the greatest threat is to the allies who will likely become dependent on it. FRG, for instance, is currently dependent for 15% of its gas from the Soviet Union; this will increase by a factor of 2 at a minimum. While the U.S. will make its own policy decision, the final policy from the West must be coordinated between the U.S. and the West European Allies. The Soviet's ability to substantially increase leverage over the allies is the greatest determinate of future allied cooperation on technology control. It is likely, however, that should the U.S. provide equipment in support of the Yamal pipeline without prior agreement with the allies for a unified policy, the strategic credibility of our arguments for seeking more stringent controls over dual-use technology transfers to the Soviet Union would be seriously questioned by the allies.

HEINZ:

1. How would you react to a proposal that would limit the number of applications that Commerce screens so that they could better target those exports of strategic importance? For instance, raising the technical parameters on products needing licenses and publishing these new requirements.

Limiting the number of applications that Commerce screens under the present Commodity Control List (CCL) would not necessarily better target those cases of strategic importance. Most of the cases are COCOM controlled and have some strategic significance. A more effective option would be to ensure that control lists do not contain products of marginal strategic importance. This would be consistent with both improving export competitiveness (by expediting licensing requirements) and allowing more time to review the critical cases. Many of the items reviewed are COCOM list items that are processed without a great deal of energy or time. Due to the limited resources required, most of the effort is in fact expended on the difficult cases. Technical parameters are raised in the normal review of the COCOM list for obsolescent items. Technical parameters should not be raised to merely expedite licensing.

2. What about dropping licensing of product exports to COCOM countries while focusing on technology transfers and strengthening of COCOM controls?

Dropping the licensing of product exports to COCOM countries would not be in the best interest of U.S. national security. There have been a few instances of reexport violations, so we cannot relinquish our ability to remain knowledgeable of the destination of products. The audit trail created is essential in determining such violations and preventing them. In addition, not all COCOM countries have the same licensing procedures as the U.S. Downgrading the U.S. procedure on product controls would significantly reduce the level of COCOM control now operative.

With respect to focusing on technology transfers, we agree that this is an area that needs strengthening in COCOM. It is currently being pursued in the preliminary negotiations in COCOM and will be a major focus of the U.S. in the 1982 comprehensive list review. It may be possible to reduce the number of products on the COCOM list by tighter control of technology.



UNITED STATES DEPARTMENT OF COMMERCE
The Under Secretary for International Trade
 Washington, D.C. 20230

JUL 9 1981

Honorable Jake Garn
 Chairman, Committee on Banking, Housing,
 and Urban Affairs
 United States Senate
 Washington, D.C. 20510

Dear Senator Garn:

This is in response to your letter to Mr. Paul T. O'Day posing questions in addition to his testimony on April 30, 1981 before the Subcommittee on International Finance and Monetary Policy.

Our responses to your questions are as follows:

1. Under the Export Administration Act of 1979 (EAA), the Department regulates exports for reasons of national security, foreign policy and domestic short supply. Commodities and technologies controlled by the Department for national security reasons are by definition dual-use in nature. Items that are strictly military in nature are controlled by the Department of State, and items that have no military significance are not controlled, unless controlled for foreign policy or short supply reasons.

When an application for goods or technology controlled for national security reasons is received in the Office of Export Administration (OEA), it is screened immediately as to the commodity, level of technology, destination, and end-user. Then the application is analyzed by OEA's staff of 34 licensing officers, many of whom have advanced experience in engineering, who carefully review the characteristics of the equipment or technology involved and assess its potential for significant military applications. Applications having such potential are referred, as necessary, by our policy staff to other agencies for recommendations on the appropriateness of allowing the export.

2. OEA regularly consults with the intelligence community, technical and policy personnel in other agencies, and, as appropriate, members of the business community (particularly through the Technical Advisory Committees), on matters requiring their particular areas of expertise. Within the past year, we have taken steps to facilitate the flow of information from the intelligence community. We have upgraded the security clearances of designated OEA personnel and have begun a program of regular intelligence briefings.

3. Under section 379.4 of the Export Administration Regulations, technical data supporting prospective or actual bids for a given transaction do not require prior licensing by or notification to this Department, unless the data relate to specified strategic goods or reveal details of process or design. Data relating to internationally controlled strategic goods may not be disclosed to the Bloc, even for purposes of negotiation, unless a validated export license has been issued.

4. Although end-use statements and visitation requirements became an important facet of the overall export control function during the 1970's, there is a growing recognition that they have limited use as guarantees against diversion. End-use statements do provide a mechanism by which the applicant and the end-user certify that they are aware of and intend to abide by the provisions of the regulations of the United States concerning diversion to military use, and they can be used as evidence on which to base legal action against violators. Controls on the level of technology allowed to be exported provide at the outset a means of limiting the risk of diversion to a degree acceptable to the United States and our allies. Visitation requirements allow limited monitoring of the actual use of the exports after they are in place in the foreign country.

In response to Senator Heinz's questions:

1. The GAO findings closely reflect the conclusions reached by our own studies of the export licensing process. The problems cited by the GAO are of long standing and do not lend themselves to easy solution. We are in the process of instituting a number of managerial and procedural changes to improve our efficiency in processing export licenses and visitation reports. These center around bringing our personnel levels up to capacity, implementing a computerized license tracking system, and developing a data base on commodity characteristics. We are working on ways of standardizing the format for submission of data in support of applications while trying to avoid imposing burdensome requirements on exporters. (One example is the May, 1981 revision of the Computer System Parameters form to provide a step-by-step format for presenting information on a computer system's capabilities and configuration.) We have budgeted significant resources for

revamping the licensing procedures manual (see our response to your question seven). Incoming visitation reports are now reviewed by OEA's computer licensing division. In those instances where a diversion is apparent, the report is brought to the attention of the Compliance Division.

2. The Department coordinates closely with the Federal Bureau of Investigation and other branches of the Department of Justice, as well as other concerned agencies, in attempting to detect and prosecute violators of the export regulations. This involves analysis of information on suspected violations and cooperation as appropriate in investigations leading to preparation of criminal and administrative proceedings against violators, as warranted by the evidence.

3. As part of an FY 1981 reprogramming request and our FY 1982 budget request, we have asked for an additional fifteen positions for our compliance staff. This would allow us to open a compliance office with both investigators and inspectors on the West Coast. These personnel would be hired through public announcement of position vacancies.

4. OEA presently employs 170 personnel, and processed approximately 76,000 license applications in FY 1980. We feel that the present staffing is inadequate to handle all of the day-to-day procedural requirements set by the EAA, particularly as the case load is constantly increasing, both in terms of numbers and complexity. Other, long-range requirements such as development of the Militarily Critical Technologies List cannot be given the comprehensive attention that they merit. As part of an FY 1981 reprogramming request and our FY 1982 budget request, we are asking for an additional eighteen licensing positions.

5. There are licensing requirements for the export to CoCom nations of certain particularly sensitive technologies. Less sensitive technical data may be exported to CoCom member nations without a requirement for a validated export license, although a written assurance against reexport of the data or its direct product may be required.

6. Many particularly sensitive technologies are under licensing control because of their significance to our national security. Controls on products are maintained to aid in prevention of diversion of particular pieces of equipment,

including products for which the technical data may not be controlled for export to CoCom destinations. This function is maintained in coordination with the CoCom countries' respective export control systems, which exercise similar controls, including controls over the reexport of U.S.-origin equipment and over exports of the direct products of U.S.-origin technology. Several of our CoCom allies, however, lack legal authority to control technical data unless the product of the data is also controlled. Therefore, certain products are maintained on the CoCom list specifically to assure control of the technical data.

7. We have budgeted approximately \$280,000 to develop a system to study foreign availability. Additionally, about \$900,000 is to be divided among: redrafting the export regulations, instituting a computer system to track licenses in process and maintain a commodity characteristics data base (which will include data on foreign availability), and redrafting the licensing procedures manual. Although the redrafting of the regulations and the procedures manual is of great importance to improved case processing and thus to OEA and to the exporting community, we do not anticipate that it will claim the share of resources you cite, but that much of that allocation will be devoted to development of the computerized systems.

8. When export licenses are received at OEA, they are immediately screened as to the commodity, level of technology, destination and end-user. The applications are then forwarded to licensing officers for review and analysis of the characteristics of the equipment. The types of cases to be referred to Defense are established in prior interagency conferences, with Commerce licensing the others without referral to Defense. For those falling into categories that the Department of Defense has requested to review (or special cases that OEA feels should be referred to Defense), the licensing officer will prepare a summary report on pertinent details of the application for Defense's information. Approximately 3,000 applications involving Soviet Bloc destinations and the People's Republic of China and about 2,500 applications for Free World destinations were referred to Defense in 1960. When Defense requires additional information, they request it of OEA, which either provides it from the material available, or gathers it from the applicant. Under

the EAA, the deadline for bringing license applications to the attention of our advisory agencies, including Defense, is 30 days. We are required to inform the applicant within ten days of receipt that we anticipate interagency review will be necessary. We are attempting with the resources available to meet all deadlines established by the EAA.

I hope this information meets your needs.

Sincerely,



Lionel H. Olmer

cc: Honorable John Heinz
Committee on Banking, Housing,
and Urban Affairs
United States Senate

[From the Congressional Record, April 2, 1981]

COMPETITIVE EXPORT FINANCING ACT OF 1981

Mr. HEINZ. Mr. President, financing is a vital part of any national export strategy. Particularly in the developing world, which receives 40 percent of our exports, financing has become a more critical factor in securing a sale than price, quality, and reliability of delivery.

The multilateral trade negotiations, concluded in 1979, have increased opportunities for U.S. exporters by clarifying the rules of the game which define and limit unfair trade competition. One major area of competition, however, remained outside the coverage of the Tokyo round of trade agreements. The United States did not attempt to have officially subsidized export credits included under the subsidies code, because it was claimed that such a subsidy was being handled within the OECD (organization for economic cooperation and development) export credit arrangement.

The arrangement, however, is little more than a gentlemen's agreement which has done little to restrain subsidies and predatory practices in export financing by our trade competitors. The current minimum rate of 7.75 percent is absurdly low in a period which the prime rate has been averaging 10 points higher. Still worse, the arrangement does not effectively cover the most predatory of all export credit practices, "mixed credits," which are device through which foreign aid and export credits are combined to offer rates even lower than the minimum set in the arrangement. Countries such as Mexico and Argentina recently have been offered "mixed credits," so it would be difficult to argue that such credits serve a legitimate foreign aid function. Indeed, U.S. law expressly forbids this practice. Yet, it is an increasingly popular credit package among OECD exporters—particularly the French.

For 3 years the U.S. Government has been trying to negotiate a new, more sensible and workable international arrangement on officially supported export credits. And for 3 years our good faith efforts have been rebuffed.

In 1980 the issue of subsidized export credits was raised repeatedly in international forums by the Secretary of State and the Treasury Secretary. Finally, at the July economic summit conference in Venice, President Carter was able to obtain a commitment from his counterparts to satisfactorily resolve the question by the end of the year. Regrettably, that promise proved empty, as the December OECD conference on official export credits broke up with no progress whatsoever having been made.

The European Community under the Treaty of Rome is bound to speak with one voice on all trade issues when negotiating with nonmembers of the EC. But since all decisions within the EC must be reached by consensus, any obstinate member can exercise a veto over EC negotiating positions. Historically, on the issue of export credits, the French have exercised the veto. That was the case in December, as a French hard line against any sort of a comprehensive new arrangement prevailed.

Particularly when viewed from the perspective of the Venice summit commitment to resolve the issue, the OECD talks were a tremendous disappointment. The interest rate floor remains at 7.75 percent, without even the modest increase to 8.55 percent, which was at one time a part of the EC proposal. There was no progress on the U.S. proposal to revise the guidelines on "mixed credits." There was not even a commitment to try to resolve these issues at the next meeting in May.

I believe that our trade competitors—and the French Government in particular—have refused to reach an agreement to end the cutrate and cutthroat competition in the subsidized export credits because they have concluded that the United States is not serious about defending its legitimate interests in the international trade arena.

Mr. President, the bill I introduce today, together with Senators GARN, INOUE, WILLIAMS, and CRANSTON, will provide Eximbank with resources to meet the predatory export credit subsidies of our foreign competitors. The \$1 billion authorized for the purpose of meeting such competition should serve to disabuse our trade competitors of any illusions they hold about our seriousness.

I am sure that I speak for my colleagues when I say we would prefer to see a firm, workable international agreement to end unfair official export credit subsidies. And that is our purpose.

Mr. President, this bill is designed to foster negotiations. It would not take effect for 1 year after adoption, and the effective date could be postponed another 6 months if the President determines that an effective international agreement is near conclusion.

As I said in recent letter to the President:

"The \$1 billion authorized by this bill would be a dramatic signal to our export competitors that we are dead serious when we say that we want to end predatory

financing once and for all. I would hope . . . that our allies—particularly the French—would see the logic and advantage of reaching a firm, workable agreement to end wasteful export credit subsidies. But I firmly believe that the best way to convince them of our seriousness is not with more rhetoric but with action—by putting subsidy money into our own export credit program if no agreement is reached. In other words, the best way to bring peace to the export credit arena is by making clear our willingness to wage an export credit war as the alternative to an agreement."

Mr. President, I sincerely hope this bill achieves its objective. There is really no justification for the current cutthroat and cut-rate competition in export credit subsidies. It is foolish. It is destructive of trust and amity among trading partners. Yet it persists. Hopefully, the message of this legislation will be heard abroad: That Congress is unwilling to accept continued foot-dragging and obstructionism on the part of our trade competitors, that now is the time for serious negotiations.

S. 868

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Competitive Export Financing Act of 1981".

SEC. 2. (a) The Congress hereby finds that—

(1) there is a growing tendency by the major trading partners of the United States to resort to the use of predatory financing arrangements to gain competitive advantage for their exporters;

(2) other major trading countries have been unwilling to negotiate an end to such practices and have rejected a series of United States proposals to strengthen provisions of the International Arrangements on Export Credits; and

(3) as a consequence of the unsuccessful conclusion of the export credit negotiations within the Organization for Economic Cooperation and Development in December 1980, measures to strengthen programs of the Export-Import Bank of the United States are required to insure continued United States export competitiveness and to bring other major trading countries back to the bargaining table for serious negotiations.

(b) It is the purpose of this Act to provide the authority for the Export-Import Bank of the United States to engage in the use of extraordinary measures of export finance to counter and ultimately discourage the use of such measures by other major trading countries.

SEC. 3. Section 2(b)(1)(A) of the Export-Import Bank Act of 1945 is amended by inserting after the third sentence thereof the following: "The Bank shall provide programs of export finance which are comparable in structure to those extraordinary official export credit measures offered by the principal countries whose exporters compete with United States exporters. Pursuant to such programs, the Bank shall offer export credit on rates, terms, and conditions competitive with those offered by other major trading countries. The Bank, at its discretion, shall use such programs to meet foreign official export credit competition until such time as the use of extraordinary measures of official export credit financing is proscribed in international agreements to which the United States is a party. For the purpose of this subsection, the term 'extraordinary measures of official export credit financing' shall include, but not necessarily be limited to, programs of highly concessional mixed credits, local cost financing, foreign currency financing, and lines of credit arrangements."

SEC. 4. (a) There are authorized to be appropriated without fiscal year limitation, not to exceed \$1,000,000,000 to achieve the purposes of the amendment made by section 3 of this Act.

(b) Within sixty days after section 3 of this Act becomes effective, and annually thereafter, the Export-Import Bank of the United States shall report to the Congress as to whether any additional appropriations or increases in overall commitment authority or annual ceiling levels are necessary to achieve the purposes of the Act.

SEC. 5. Section 3 shall take effect twelve months after the date of enactment of the Act. The President may defer the effective date of section 3 for an additional period of not to exceed six months if (1) he determines that international agreements have or will be concluded which put United States and foreign exporters in a substantially equal competitive position with respect to official export finance, and (2) he reports to Congress prior to and following such deferral period as to progress achieved in negotiating an end to predatory export financing.

SECTION-BY-SECTION ANALYSIS

Section 1 provides that the legislation may be cited as the competitive Export Financing Act of 1981.

Section 2 contains Congressional findings concerning the use by foreign governments of predatory financing practices, the failure of negotiations to limit such practices, and the need to strengthen the programs of the Export-Import Bank to insure continued U.S. export competitiveness. Section 2 further states the purposes of the Act to be to authorize the Bank to use extraordinary export finance measures to counter and ultimately to discourage the use of such measures by other countries.

Section 3 would amend the Export-Import Bank Act to require the Bank to provide export finance programs comparable in structure and competitive in other respects to the extraordinary official export credit measures offered by foreign competitor countries. The Bank would be authorized, at its discretion, to use such programs to meet extraordinary measures of official export credit financing, including, but not limited to, programs of highly concessional mixed credits, local costs financing, foreign currency financing and lines of credit, until the use of such financing is proscribed in international agreements to which the United States is a party.

Section 4 would authorize an appropriation of \$1 billion to the Bank to achieve the purposes of section 3, and would require the Bank to report annually to Congress on the need for appropriations or increases in authority in order to achieve the purposes of the Act.

Section 5 provides that section 3 would take effect 12 months after enactment of this Act unless the President deferred the effective date an additional 6 months by determining that international agreements have or will be concluded which put U.S. and foreign exporters in a substantially equal competitive position with respect to official export finance, and reporting to Congress prior to and following such deferral period as to progress achieving in negotiating an end to predatory export financing.

U.S. SENATE,
Washington, D.C., March 19, 1981.

The PRESIDENT,
The White House,
Washington, D.C.

DEAR MR. PRESIDENT: While I support the economic program you submitted to Congress, I believe it is important that the full consequences of the proposed budget cuts be clearly understood so that other appropriate actions can be taken. One cut which particularly concerns me is the proposed reduction in the direct credit authority of the Export-Import Bank, although I believe there are a number of ways in which we can ameliorate the consequences of that proposal.

The importance of exports in improving our national economic picture is often ignored in policy discussions, and therefore it would be useful to review a few key facts.

We can point with pride to the fact that U.S. merchandise exports have grown twice as fast as the gross national product since 1972. As a result, the ratio of exports to GNP rose from 4.2 percent in 1972 to 7.5 percent in 1979. U.S. imports grew equally as fast, however, increasing in importance relative to GNP from 5.1 percent to 8.7 percent in the same years. Because imports have expanded since 1972 from a higher base than exports, the trade deficit has expanded sharply, with an aggregate deficit over the past five years exceeding \$110 billion.

Our nation can ill-afford to relent in the fierce competition for international market shares. During the decade of the 1970's, our share of world industrial exports (outside the U.S.) declined from over 21 percent to 17.5 percent. This was the most serious loss for any major industrial exporter, including the United Kingdom.

While Export-Import Bank financing is used in only 7 percent of our exports (compared to 35 percent for the Japanese and 29 percent for the French official export credit facilities), it can be critical in protecting our basic comparative advantage and market position in key high technology industries. Currently, the United States is losing significant numbers of exports to foreign subsidized industries, including aerospace, nuclear and conventional power generators, and machine tools. Particularly in the developing world, which received 40 percent of our exports, financing has become a more critical factor in securing a sale than price, quality, and reliability of delivery.

I am concerned, therefore, that inadequate credit limits for the Export-Import Bank over the next few years will do irreparable harm to the competitiveness of key

U.S. industries. Since the Eximbank's credit restraint is not likely to be shared by our trade competitors, a number of consequences can be expected.

In order to take advantage of foreign export credit support, U.S. companies are likely to adopt one or more of the following strategies: (1) a shift to foreign procurement for major components of large capital goods; (2) long-term, off-shore subcontractor relationships, particularly in the case of airframe and aircraft engine manufacturers, and, (3) a shift to off-shore facilities for entire projects, which many multinational manufacturing and construction companies already have and more are likely to acquire.

What these likely corporate strategies add up to is a significant loss of U.S. jobs and tax revenue. Ironically, although large corporations are recipients of the majority of Eximbank support, it is the smaller U.S. subcontractors who are likely to be hurt the most. Boeing, for example, placed nearly \$6 billion in subcontracts for parts and equipment to 3500 subcontractors and suppliers in 44 states during 1979. Approximately \$3 billion of those purchases were for foreign aircraft sales.

The Congressional Budget Office has estimated that every \$1 billion in export sales generates 40,000 to 50,000 jobs. The complement to that calculation is that every 50,000 unemployed Americans costs the Treasury \$1 billion in lost revenue and transfer payments.

The French Government understands those calculations only too well. The OECD has estimated that France committed \$2.34 billion to export credit subsidies in 1980.

Since 1978 the United States Government has been negotiating within the OECD to reach a multilateral agreement to end the cut-rate and cutthroat competition in officially-subsidized export credits. The aim has been to set new market-related minimum interest rates for government-supported export credits and to limit predatory export financing practices.

In 1980, that effort nearly bore fruit: every OECD country except France was ready to agree to a major strengthening of the International Arrangement on Export Credits in a way which would sharply reduce export subsidies. Unfortunately, the structure of the European Community enabled France alone to block such a step.

Mr. President, export credit subsidies are a wasteful burden on taxpayers in all major nations. We should be continuing our efforts to reach an international agreement to that end. But we need leverage to achieve that objective. To reduce Eximbank credits at this time, without some other compensatory action on our part, would be a signal to our foreign competitors that the United States is no longer serious about obtaining an international agreement and is not willing to press other countries, particularly France, on the point by matching their credit offers.

I would no more counsel unilateral disarmament as an approach to negotiating trade issues with our allies than I would recommend it for dealing with the Russians on global security; yet that is precisely what we are doing.

The OECD negotiations on export credit resume in May, and it is essential that we have the resources to maintain a strong position.

Bearing all these considerations in mind, including your credit limits for the Export-Import Bank, I would suggest the following strategy to strengthen the hand of our negotiating team:

(1) The United States Eximbank ought to pursue a strategy of derogating on term from the export credit Arrangement, with particular targeting on French export sales. The original Arrangement was basically a tradeoff for the United States in which it gave up the advantage of its ability to finance long-term obligations in the U.S. bond market in return for a European and Japanese agreement to set minimum interest rates at a reasonable level; that is, not to subsidize. Obviously, the non-subsidy floor of 7.75 percent in 1976 is no longer a non-subsidy in 1981. In the meantime, the U.S. had maintained its export credit maturities at 10 years. One vehicle to get leverage, therefore would be to derogate and extend maturity on a selected basis on export cases where we are in competition with the French.

We also ought to try, to the degree possible, to concentrate available Exim credit to the French. Both of these measures are designed to put significant pressure on the French, with the view of getting them to agree to reducing export credit subsidies.

(2) During the recently concluded Tokyo Round of Multilateral Trade Negotiations, the United States did not attempt to have officially-subsidized export credits included under the Subsidies Code, because it was claimed that such a subsidy was being handled within the OECD export credit Arrangement. However, with the failure of the European Community—particularly the French—to bargain in good faith on this issue, I believe a strong case should be made that subsidized official exports credits are an unfair trade practice that adversely affects us in third markets and that our government should seriously consider bringing a case against

the offending parties, particularly the French, pursuant to Articles XXII and XXIII of the GATT and Section 301 of the Trade Act of 1974 as amended by the Trade Agreement Act of 1979.

(3) On March 26 I intend to introduce the Competitive Export Financing Act of 1981 which would authorize the appropriation of a special billion dollar contingency fund to be available for the Export-Import Bank's use in matching predatory export credit offers by U.S. trade competitors if no international agreement barring subsidy financing is reached within one year. The effective date could be further postponed another six months if the President determines that an effective international agreement is near conclusion.

The \$1 billion authorized by this bill would be a dramatic signal to our export competitors that we are dead serious when we say that we want to end predatory financing once and for all. I would hope that this money will never have to be appropriated, that our allies—particularly the French—would see the logic and advantage of reaching a firm, workable agreement to end wasteful export credit subsidies. But I firmly believe that the best way to convince them of our seriousness is not with more rhetoric but with action—by putting subsidy money into our own export credit program, if no agreement is reached. In other words, the best way to bring peace to the export credit arena is by making clear our willingness to wage an export credit war as the alternative to an agreement.

Mr. President, I sympathize with your desire to cut the budget and to reduce the level of federal borrowing. But, I also believe that exports are simply too important to the U.S. economy to be left exposed to predatory financing ploys by our trade competitors. To reduce Eximbank's credit limit without also taking steps to induce our trade competitors to do likewise would be counterproductive to the long-range goals of employment and balanced growth for our economy which we both share.

I urge you to endorse the strategy I have suggested. I stand ready to assist you in every possible way to insure that your trade policy, as well as your economic policy, is a success.

Sincerely,

JOHN HEINZ.

RESPONSE TO QUESTIONS OF SENATOR GARN

Q. Do you agree with the Carter Administration decision to allow U.S. participation in the Soviet Yamal pipeline project, designed to make Western Europe dependent in great part upon the Soviet Union for energy?

A. The Administration is very concerned about the prospects of Western European dependence on Soviet energy resources, and the possibility that our Allies would become vulnerable to Soviet energy leverage. In this context, we are particularly concerned about the proposed Siberian gas pipeline which would increase the volume of Soviet gas exports to Europe.

We have shared our assessment of the project with our Allies and intend to consult closely with them as they consider whether in fact to proceed in this endeavor.

Q. It has been reported that there is a proposal under discussion at State for a three to four year trade agreement with the Soviet Union as was envisioned in the 1973 detente trade proposals. Do you feel that the agreement should be reciprocal in terms of key U.S. products and technology in return for the Soviet promise of more responsible global behavior; or do you feel this reciprocity, were such an agreement in accordance with the President's national security objectives, should be in terms of a more realistic exchange of significant quantities of high grade Soviet strategic minerals for U.S. goods? Should any such agreement be concluded, in your view, while Soviet troops continue to occupy Afghanistan and remain mobilized and poised to invade Poland at any time they choose?

A. The State Department does not have under consideration any trade agreement with the USSR of the sort negotiated (but never brought into force) in 1973.

The Administration is considering whether any successor arrangement to the long-term grains agreement, which expires September 30, would be in the U.S. interest.

Q. How many so-called exchange students and academics from the Soviet Union and other Warsaw Pact countries will be coming to the U.S. to study or visit in high technology fields?

A. In 1980, the following numbers of Soviet exchange students and academics visited the United States in what could generally be called "high technology fields" (these numbers should be taken as approximate due to the imprecision of the term):

- official exchanges: 140;
- by agreement between the National Academy of Sciences and the Soviet Academy of Sciences: 32;
- through IREX programs:
 - graduate students or young faculty: 30
 - senior researchers: 10
 - individuals sponsored by the American Council of Learned Societies: 10;
- as Fulbright lecturers in the U.S.: 15; and
- through private agreements, an estimated 5-10.

All but the handful of private-agreement students are subject to official U.S. approval (including review from the standpoint of security concerns for acceptability of their studies).

While it is difficult to give a precise figure for future exchange students and academic visitors from the Soviet Union, (due to the effect which our bilateral relations has on such exchanges), we believe that the figures for 1981 will approximate those given above.

Regarding exchange students and academics from non-Soviet Warsaw Pact countries, the State Department, extrapolating from recent experience, estimates that over the next 12 months as many as 360 East European exchange visitors could come to the U.S. in "high technology fields", broadly defined.

The visitors would be divided approximately as follows:

- 200, Poland
- 70, Hungary
- 30, Czechoslovakia
- 20, Bulgaria
- 20, German Democratic Republic
- 20, Romania

There has been a general upward trend in the number of visitors in high-technology fields from the non-Soviet Warsaw Pact countries. In all cases, we look closely at the question of possible technology loss in this regard; obviously we must balance the question of possible losses against possible benefits to us from such visits. Given the development of our trade with Eastern Europe and a trend toward increased complexity in many industrial products, we would expect that the 1981 figures will show an overall increase of several per cent in exchange visits in high technology fields. We will continue to monitor the situation closely as regards visits by exchange students and academics from the Soviet Union and non-Soviet Warsaw Pact countries so that their potential access to those specific technology sub-areas of concern will be appropriately circumscribed.

RESPONSE TO QUESTIONS OF SENATOR HEINZ

Q. I understand that COCOM Lists are comprehensively reviewed approximately every three years but that between revisions "definitional discussions" are held on specific embargo items so that updating does not have to wait for the next list review. Given the rapid advances in technologies, do you think that "definitional discussions" are enough to properly protect our technology from Soviet acquisition? Do you believe that the interests of our nation might better be served by having yearly COCOM reviews instead of the present practice of one final review every three years?

A. Regarding the efficacy of holding yearly COCOM List Reviews, the scope of preparations necessary would make this task impracticable. Slower-moving and procedural, a List Review is appropriate for going through scores of pages of highly technical definitions (the last List Review took 11 months in position preparation and lasted for 13 months), but it is not a vehicle for swift action on individual items. Instead, where interim U.S. review of a technical area shows redefinition of controls to be advisable, the definitional discussions can provide more rapid attention by COCOM to a U.S. proposal. For smaller groupings of proposals on faster-moving technologies, these definitional discussions are the appropriate tool for use in achieving redefinition.