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Report to Congressional Committees

September 2006

CONFLICT DIAMONDS

Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act

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Highlights

Highlights of GAO-06-978, a report to congressional committees

CONFLICT DIAMONDS

Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act

Why GAO Did This Study

In 2003, the United States and other countries began implementing the Kimberley Process Certification Scheme (KPCS) to curtail the trade of rough diamonds that had fueled severe conflicts in Africa, known as conflict diamonds. CDTA provides the statutory framework for U.S. implementation of the KPCS. As mandated in CDTA, this report (1) describes the institutional framework established to implement the act, (2) examines implementation of the domestic provisions of the act and challenges it faces, and (3) examines how the United States has helped to strengthen the KPCS and challenges it faces.

What GAO Recommends

This report contains recommendations to the Secretaries of the Departments of State, the Treasury, Homeland Security, and Commerce. It recommends improvements in the (1) accuracy of U.S. rough diamond trade data; (2) processes for importing and exporting rough diamonds, including conducting periodic physical inspections and confirmation of rough diamond import receipts with foreign exporting authorities; (3) oversight of the activities of USKPA and its licensees who issue Kimberley Process certificates; and (4) approach for providing some of the U.S. diamond-related assistance. The departments reviewed a draft copy of this report and concurred with GAO's recommendations.

www.gao.gov/cgi-bin/getrpt?GAO-06-978.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Loren Yager at (202) 512-4347 or yagerl@gao.gov.

What GAO Found

The United States has used multiple U.S. agencies and a private, not-for-profit entity to implement the domestic and international provisions of the Clean Diamond Trade Act (CDTA). The Departments of State and the Treasury have led U.S. efforts to implement the domestic provisions of the act; State has led the U.S. efforts to curtail trade in conflict diamonds abroad. Domestically, the Departments of State, the Treasury, Homeland Security, and Commerce, and the private entity, called the U.S. Kimberley Process Authority (USKPA), have been responsible for controlling U.S. imports and exports of rough diamonds. Internationally, State, the U.S. Agency for International Development (USAID), and the U.S. Geological Survey have helped to strengthen KPCS.

Domestically, the U.S. systems for reporting rough diamond statistics and for controlling imports and exports of these diamonds are vulnerable to illicit trade. The United States has enhanced the quality of its rough diamond trade data by improving its collection processes, but work remains to be done. Also, the United States does not periodically inspect rough diamond imports or exports to ensure that the contents of the rough diamond parcels match the Kimberley Process certificates. In addition, the United States lacks an effective system for confirming receipt of imports—a Kimberley Process requirement for avoiding possible diversions of rough diamond imports. Finally, the United States has not had a plan for monitoring USKPA, but is developing and testing one.

Internationally, the United States has helped to strengthen KPCS by participating in KPCS activities and providing assistance to Sierra Leone and Liberia in their efforts to comply with KPCS, but donor assistance to these countries faces challenges. Donors and diamond producing countries are considering a regional approach to help enhance the effectiveness of donor diamond-related assistance because this assistance is constrained by the limited capacity and resources of these countries and the need to harmonize diamond policies among countries vulnerable to illicit cross border diamond trading.

Diamond Mining Site in Sierra Leone—A Recipient Country of U.S. Assistance

Source: GAO.

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Abbreviations

AES	Automated Export System
CBP	Customs and Border Protection
CDTA	Clean Diamond Trade Act
DIPAM	Diamond Policy and Management Project
IDMP	Integrated Diamond Management Program
KPCS	Kimberley Process Certification Scheme
MSI	Management Systems International
PDA	Peace Diamond Alliance Support Project
UN	United Nations
USAID	United States Agency for International Development
USGS	United States Geological Survey
USKPA	United States Kimberley Process Authority
WTO	World Trade Organization

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United States Government Accountability Office
Washington, DC 20548

September 27, 2006

The Honorable Charles E. Grassley
Chairman
The Honorable Max Baucus
Ranking Minority Member
Committee on Finance
United States Senate

The Honorable Richard G. Lugar
Chairman
The Honorable Joseph R. Biden, Jr.
Ranking Minority Member
Committee on Foreign Relations
United States Senate

The Honorable Henry J. Hyde
Chairman
The Honorable Tom Lantos
Ranking Minority Member
Committee on International Relations
House of Representatives

The Honorable William M. Thomas
Chairman
The Honorable Charles B. Rangel
Ranking Minority Member
Committee on Ways and Means
House of Representatives

When legitimately traded, rough diamonds (uncut and unpolished diamonds) can make a major contribution to the economies of producing, exporting, and importing countries, especially developing countries. In the 1990s, however, rough diamonds that became known as conflict diamonds fueled severe conflicts and humanitarian crises in countries such as Liberia, Sierra Leone, the Democratic Republic of the Congo, and Angola.[1]

[1]The United Nations (UN) General Assembly defines conflict diamonds as rough diamonds used by rebel movements to finance efforts to undermine or overthrow legitimate governments. UN General Assembly Resolution 55/56 (Jan. 29, 2001).

Although many of these conflicts have now ended and the international community has taken steps to gain control of the rough diamond trade, the United Nations (UN) and other sources report that illicit trading of rough diamonds still exists and could potentially finance civil conflicts as well as criminal and terrorist activities.[2]

In November 2002, diamond producing and diamond trading countries launched a voluntary global system, called the Kimberley Process Certification Scheme (KPCS), to control the trade of rough diamonds and to assure consumers that the diamonds they purchase have not helped to finance violent conflicts.[3] Implementation of KPCS began on January 1, 2003. The United States and other KPCS participants are responsible for ensuring that the integrity of the certification scheme is upheld and that the Kimberley Process works towards preventing conflict diamonds from entering the legitimate trade of rough diamonds. In instances of noncompliance, KPCS can expel or suspend a participant from the certification scheme. For example, in July 2004, the Chair of KPCS expelled the Republic of Congo from participation because this country could not account for the origin of large quantities of rough diamonds.[4]

The United States has a major interest in KPCS because the certification scheme helps ensure the protection of the legitimate trade in these diamonds by breaking the link between conflict and rough diamonds. Although the United States is not a producer of rough diamonds, it is a significant global trader of rough and polished diamonds and the world's largest consumer market for diamond jewelry. In 2003, the United States was the seventh largest exporter of rough diamonds among non-mining KPCS participants (exporting about $227 million worth), and the fifth largest exporter of polished diamonds.[5]

[2]In November 2005, KPCS adopted a resolution on the subject of illicit diamond production in Côte d'Ivoire that outlined a series of measures to prevent the introduction of conflict diamonds from Côte d'Ivoire into legitimate trade, including a detailed assessment of the import and export volumes. The assessment will be carried out in cooperation with the UN.

[3]In mid-2002, GAO reported on the efforts to develop KPCS. See GAO, *International Trade: Critical Issues Remain in Deterring Conflict Diamond Trade*, GAO-02-678 (Washington, D.C.: June 14, 2002); and GAO, *International Trade: Significant Challenges Remain in Deterring Trade in Conflict Diamonds*, GAO-02-425T (Washington, D.C.: Feb. 13, 2002).

[4]For additional details regarding KPCS, see www.kimberleyprocess.com.

[5]Appendixes II and III contain additional rough- and polished-diamond-related information.

The United States enacted the Clean Diamond Trade Act (CDTA) in April 2003 to provide the statutory framework for implementing KPCS.[6] As mandated in CDTA, this report (1) describes the institutional framework the U.S. government has created to implement CDTA, (2) examines how the United States has implemented the provisions of CDTA domestically and what principal challenges it faces, and (3) examines how the United States has helped to strengthen KPCS and what principal challenges it faces.

To meet these objectives, we examined documents relevant to the Kimberley Process and CDTA implementation from the UN, KPCS, U.S. and foreign government agencies, the diamond industry, and non-governmental groups. Additionally, we conducted audit work in the United States (Washington, D.C., and New York City); Canada; Belgium; Russia; Italy; Sierra Leone; and Liberia. We also met with representatives from the Department of State (State), the Department of the Treasury's (the Treasury) Office of Foreign Assets Control (OFAC), the Department of Homeland Security's (Homeland Security) Bureau of Customs and Border Protection (CBP) and Bureau of Immigration and Customs Enforcement (ICE), the Department of Commerce's (Commerce) Bureau of the Census (Census), the Department of the Interior's U.S. Geological Survey (USGS), the U.S. Agency for International Development (USAID), the Office of the U.S. Trade Representative (USTR), and the U.S. Kimberley Process Authority (USKPA); as well as non-governmental groups, the diamond industry, foreign governments, and the UN and other international organizations. Furthermore, we analyzed Census data submissions to KPCS. We conducted our work from September 2005 through September 2006 in accordance with generally accepted government auditing standards. Appendix I contains a more detailed description of our scope and methodology.

Results in Brief

The United States uses multiple U.S. agencies and a private, not-for-profit entity (USKPA) to implement the domestic and international provisions of CDTA. State and the Treasury lead U.S. efforts to implement the domestic provisions of the act; State leads the U.S. efforts to curtail trade in conflict diamonds abroad. Domestically, State, the Treasury, Homeland Security,

[6]Pub. L. 108-19. The act directs the President to prohibit imports and exports of rough diamonds that are not controlled through KPCS. The act defines the term "controlled by the Kimberley Process Certification Scheme" to include any system that substantially meets standards, practices, and procedures of KPCS.

Commerce, and USKPA are responsible for preparing and sharing statistics on the U.S. trade of rough diamonds, and for controlling U.S. imports and exports of rough diamonds. State and the Treasury coordinate and lead U.S. agency efforts by convening and co-chairing regular interagency meetings, as well as ongoing informal discussions with other U.S. agencies, in which CDTA and KPCS-related implementation issues are discussed. For example, State and other U.S. agencies recently met to discuss, among other things, U.S. plans for providing additional diamond-related technical assistance; U.S. comments on recommendations made to KPCS on the preliminary results of the 3-year review of the certification scheme that is currently under way on issues such as creating and financing a KPCS Secretariat; and the issues raised at the June 2006 KPCS intersessional meeting in Gaborone, Botswana, including enhancing KPCS monitoring and statistics. State is also responsible for overseeing USKPA, which, through 17 licensed private entities, issues the Kimberley Process certificates that must accompany U.S. export shipments of rough diamonds. Internationally, State leads U.S. participation in KPCS. State and USAID have helped Sierra Leone's efforts to comply with KPCS. State has recently worked with USGS to help Liberia become a member of KPCS.

Domestically, the U.S. systems for reporting rough diamond statistics and for controlling imports and exports of these diamonds have improved but are still vulnerable to illicit trade of rough diamonds. Through Census, the United States has enhanced the accuracy and reporting of its rough diamond trade data, but work remains to be done. Despite improving the accuracy of its trade data on rough diamonds, resulting in a significant reduction in the excess of exports over imports—from almost 3 million carats in 2003 to less than 300,000 carats in 2005—the United States does not know what factors, such as diamond stockpiles, account for the remaining excess in exports. The United States does not periodically or regularly inspect rough diamond imports or exports, a control feature that allows participants to match the contents of the rough diamond parcels and Kimberley Process certificates and deters illicit trade in rough diamonds. The United States does not have an effective system for confirming the receipt of rough diamond import shipments, a control feature that allows participants to track shipments and prevent their diversion. For example, by relying on importers to confirm imports and having no U.S. agency to track these confirmations, the United States did not confirm most import shipments originating from four key U.S. trading partners—Canada, Belgium, Israel, and the United Kingdom—in 2004 and 2005, and it does not know the extent to which it has not confirmed imports with other countries. Despite recent U.S. efforts to improve the

process for confirming receipt of imports, the percentage of confirmations remains low. The United States has not implemented a plan for overseeing the activities of USKPA and its licensees but, according to State officials, the department is developing and testing such a plan—a control feature that would allow the United States to conduct periodic or regular, independent, and systematic oversight of USKPA activities to make sure that they conform with KPCS standards.

Internationally, the United States has helped to strengthen KPCS by participating in KPCS activities and providing assistance to help Sierra Leone and Liberia in their efforts to comply with KPCS; however, donor assistance to these countries faces challenges. The United States has helped strengthen KPCS by participating in the activities of its working groups and committees, such as the working groups on monitoring and statistics. For instance, U.S. officials including geological experts have participated on several Kimberley Process peer review teams to help monitor implementation of the certification scheme among participants. Also, the United States has recently assumed lead roles within KPCS by leading a peer review visit to Brazil and offering to identify and coordinate donor assistance to countries seeking to implement or strengthen KPCS. The United States has provided approximately $7.57 million in assistance to support Sierra Leone ($6.13 million) and Liberia's ($1.44 million) efforts to implement systems for controlling their trade in rough diamonds. The United States has helped Sierra Leone develop and implement a system for controlling rough diamond exports. The United States is currently helping Liberia to, among other things, build and equip a secure facility and train personnel for the Liberian authority that will be responsible for controlling the rough diamond trade. The effectiveness of donor assistance in both countries is constrained by their limited capacity and resources for implementing KPCS, and the need to harmonize diamond policies among these countries and other countries in the region vulnerable to illicit cross-border trading. For example, officials in both Sierra Leone and Liberia noted their lack of resources for monitoring large mining areas and highly porous borders, which contributes to illicit mining and trading. Donors and diamond producers are considering a regional approach to help enhance the effectiveness of donor assistance. This regional assistance would complement country-specific assistance provided to diamond-producing countries within a region.

This report contains recommendations to the Secretaries of State, Homeland Security, the Treasury, and Commerce. Specifically, it recommends improvements in (1) the accuracy of U.S. rough diamond trade data to improve the effectiveness of these data as a tool for detecting

illicit trade in rough diamonds; (2) the processes for importing and exporting rough diamonds, including conducting physical inspections periodically or regularly and confirming rough diamond import receipts with foreign exporting authorities; (3) the oversight of the activities of USKPA and its licensees; and (4) U.S. diamond-related assistance by developing and implementing a regional approach for providing some of this assistance.

We received written comments on a draft of this report from State, the Treasury, Homeland Security, Commerce, and Interior (see apps. VI, VII, VIII, IX, and X) indicating that they concurred with our recommendations. We also received technical comments on this draft from State, the Treasury, USAID, and USTR, which we have incorporated where appropriate.

Background

KPCS participants produce and trade the vast majority of rough diamonds in the world. However, the nature of diamonds and the lack of effective control systems create opportunities for illicit trade, including trade in conflict diamonds. By deterring potential illicit trading, effective control mechanisms could help prevent illicit diamonds from entering the legitimate trade. For example, without systems to accurately capture and analyze rough diamond trade data, KPCS participants cannot readily identify anomalies in imports and exports that could indicate illicit activity. Also, without effective systems for inspecting imports and exports or confirming import receipts, illicit rough diamonds could enter the legitimate trade.

On November 5, 2002, 37 ministers and heads of official delegations launched KPCS, which contained elements for participants to consider in establishing control systems for monitoring the production and trade in rough diamonds. These elements included, among other things, systems for collecting and sharing data on production and trade of rough diamonds, inspecting the contents of import and export shipments to verify the details declared on the Kimberley Process certificate, and

confirming import receipts with the foreign exporting authority.[7] Implementation of KPCS began on January 1, 2003. Currently, 46 participants, including the European Community, voluntarily participate in KPCS and account for approximately 99.8 percent of the global production of rough diamonds. (See appendix IV for a timeline of KPCS and CDTA-related events and appendix V for the list of KPCS participants.) Consistent with KPCS provisions, the United States enacted CDTA on April 25, 2003, to establish an institutional structure for controlling and monitoring U.S. imports and exports of rough diamonds.[8]

Kimberley Process Certification Scheme

The structure of KPCS includes a Chair and Vice-Chair, a Secretariat serving under the Chair, working groups, and committees; KPCS participants also hold an annual plenary meeting. Figure 1 depicts KPCS's structure and the responsibilities of the Chair, Secretariat, working groups, and committees. In addition to participants, only applicants and official observers—including representatives from the diamond industry, non-governmental groups, and international organizations—can participate in KPCS meetings and activities.

[7]To complement worldwide KPCS implementation efforts, the international diamond and jewelry industry initiated a voluntary system of warranties. This system requires that for every diamond transaction—rough, polished, or diamond jewelry—the seller must affirm on the invoice that the diamonds have been purchased through authorized channels that are not involved in funding conflict. While the system is voluntary, the industry views the system as a requirement for all its members involved in the diamond trade. Noncompliance with the system of warranties can result in expulsion from diamond trade organizations. The U.S. industry adopted this system of warranties.

[8]Several KPCS participants, including the United States (through the U.S. Trade Representative) obtained a 4-year waiver needed for implementing KPCS and CDTA from the World Trade Organization (WTO) in 2003. These participants are currently trying to obtain a 6-year waiver extension from WTO and expect to get it in November 2006, according to USTR officials. In the absence of a waiver, WTO could impose sanctions on KPCS participants if WTO deemed the certification scheme an unauthorized trade barrier. Also, without a waiver, CDTA might lapse because the act requires that the President certify the existence of either a WTO waiver or a binding resolution of the UN Security Council for its provisions to remain in effect. See Pub. L. 108-19, sec. 15.

Figure 1: KPCS Structure and Responsibilities

Chair (Botswana)

- Oversees implementation of KPCS.
- Oversees the operations of the working groups and committees.
- Oversees the general administration of the Kimberley Process.

Secretariat

- Schedules meetings of the working groups.
- Circulates documents between participants and maintains the Kimberley Process web site.
- Performs all other duties designated by the Chair.

Working groups

Monitoring - Chair, European Community
- Monitors and assesses the implementation of the KPCS by all participants.

Statistics - Chair, Canada
- Ensures timely reporting and analysis of statistical data on the production and trade of rough diamonds in order to identify anomalies, and to ensure the effective implementation of the certification scheme.

Diamond experts - Chair, World Diamond Council
- Identifies solutions to technical problems in the implementation of the KPCS.

Committee

Participation Committee - Chair, Russian Federation
- Assists the Chair of KPCS in handling the admission of new participants in the KPCS.

Selection Committee - Chair, Botswana
- Reviews and assesses the credentials of the candidates for the Vice-Chair position and submits findings to the Chair of KPCS. The KPCS Plenary selects the Vice-Chair. When the Chair's term expires, the Vice-Chair becomes the new Chair. The European Community is the current Vice-Chair.

Source: GAO analysis of KPCS information.

The Chair is responsible for overseeing the implementation of KPCS, leading the annual plenary meeting, overseeing the operations of three working groups and two committees, and the general administration of the Kimberley Process. Under the Chair, a Secretariat is responsible for scheduling meetings, circulating documents among participants, maintaining the KPCS Web site, and all other duties the Chair designates. The Secretariat does not have permanent staff. The country chairing the certification scheme is responsible for staffing the Secretariat. Currently,

Botswana chairs KPCS and the Vice-Chair is from the European Community.

KPCS holds a plenary meeting normally once per year, in which participants and official observers typically discuss and assess the implementation of the certification scheme. KPCS participants and official observers work together in monitoring, statistics, and diamond experts working groups, and in the Participation Committee and the Selection Committee, to strengthen the certification scheme.

KPCS's key provisions require participants to:

- enact or amend appropriate laws or regulations to implement and enforce the certification scheme, and maintain dissuasive and proportional penalties for transgressions;
- designate importing and exporting authorities;
- establish control systems designed to eliminate the presence of conflict diamonds from the rough diamond trade, such as systems for physically inspecting rough diamond import and export parcels;
- ensure that a Kimberley Process certificate accompanies each import and export shipment of rough diamonds;
- acknowledge the receipt of rough diamond import parcels to the foreign export authority;
- ensure that rough diamonds are imported and exported in tamper-resistant containers; and
- collect and maintain rough diamond data on production, imports, and exports; and collate and exchange such data with KPCS.

Clean Diamond Trade Act

CDTA provides the institutional structure for implementing its domestic and international provisions.

Regarding domestic implementation, key CDTA provisions

- designate importing and exporting authorities,

- establish an interagency Kimberley Process Implementation Coordinating Committee for coordinating U.S. implementation efforts,
- give the U.S. government responsibility for overseeing any entity involved in the issuance of the certificates that must accompany each shipment of rough diamonds exported from the United States,
- impose civil and criminal penalties to enforce implementation of CDTA, and
- support the collection and exchange of U.S. import and export data on rough diamonds.

Regarding international implementation, key CDTA provisions

- urge the U.S. government to strengthen KPCS by monitoring the effectiveness of the certification scheme and by sharing statistics, and
- allow U.S. agencies to make technical assistance available to countries seeking to implement KPCS.

Several U.S. Agencies and USKPA Have Implemented CDTA

Consistent with the provisions of CDTA, the United States has used several U.S. agencies and USKPA to implement the domestic and international provisions of the act.

U.S. Agencies and USKPA Have Implemented CDTA's Domestic Provisions

State, the Treasury, Commerce, Homeland Security, and USKPA have had responsibilities for implementing the domestic provisions of CDTA. State and the Treasury have led these U.S. implementation efforts.[9]

- *State:* The department co-chairs the U.S. interagency group for implementing CDTA. State is responsible for reviewing the activities of USKPA and its licensees and for annually reporting to the Congress the results of its review.[10]

[9]Controlling imports and exports of rough diamonds involves at least four entities in the United States. A number of countries, including some of those we visited (Belgium, Canada, and Sierra Leone) have used a single government entity for controlling their trade of rough diamonds.

[10]State has submitted three reports on USKPA activities to the Congress covering 2003, 2004, and 2005 respectively.

- *The Treasury*: The department co-chairs the interagency group for implementing CDTA. OFAC is responsible for promulgating the rough diamond regulations to implement CDTA. One of these regulations designates the final recipient of the shipment (i.e., the ultimate consignee) with the responsibility of confirming, with the foreign exporting authority, the receipt of a rough diamond import shipment.[11]

- *Homeland Security*: Under CDTA, Homeland Security's CBP is the importing authority responsible for regulating U.S. rough diamond imports. The department's Bureau of Immigration and Customs Enforcement is responsible for pursuing criminal investigations related to violations of CDTA and its regulations.

- *Commerce*: Under CDTA, Census is the exporting authority responsible for regulating U.S. rough diamond exports. Also, Census is responsible for collecting and analyzing data on the U.S. trade of rough diamonds and reporting it to KPCS.

- *USKPA*: Unlike most KPCS participants, the United States has assigned the responsibility of issuing Kimberley Process certificates to a private entity rather than to a government agency. USKPA produces these certificates and currently relies on 17 licensees for issuing them.

- *Interagency Coordination Committee*: State and the Treasury co-chair an interagency committee, the Kimberley Process Implementation Coordinating Committee, that CDTA created for coordinating U.S. government activities on rough diamonds. Aside from convening and leading committee meetings, State and the Treasury have no formal authority over the actual activities of the other agencies in carrying out their assigned CDTA roles. Nevertheless, U.S. officials noted that the formal and informal interagency coordination processes have effectively addressed many operational issues. For example, State and other U.S. agencies recently met to discuss topics such as U.S. options for providing additional diamond-related technical assistance; U.S. comments on recommendations made to KPCS on the preliminary results of the 3-year review of the certification scheme that is currently under way on issues such as creating and financing a KPCS Secretariat; and the issues raised at

[11]In the United States, issuing Kimberley Process certificates and confirming import receipts involves private entities (USKPA and the ultimate consignee). These activities are a government responsibility in a number of countries, including the three countries we visited (Canada, Belgium, and Sierra Leone).

the June 2006 KPCS intersessional meeting in Gaborone, Botswana, including enhancing KPCS monitoring and statistics.

U.S. Agencies Have Implemented the International Provisions of CDTA

State, Census, USAID, and USGS are involved in implementing the international provisions of the act. See table 1 for a brief description of the responsibilities of these agencies. Consistent with KPCS, the key international provisions of the act cover the United States' participation in KPCS and the U.S. technical assistance to participants seeking to implement KPCS.

Table 1: U.S. Agency Responsibilities for Implementing CDTA's International Provisions

Agency	Unit	Responsibilities
State	Economic Affairs Bureau	Leads U.S. efforts in KPCS.
	Africa Bureau	Funded technical assistance to support Sierra Leone and Liberia's KPCS-related efforts.
Census	Foreign Trade Division	Analyzed rough diamond data for KPCS Statistics Working Group.
USAID	Office of Transition Initiatives/Bureau for Africa	Funded technical assistance to support Sierra Leone's KPCS-related efforts.
USGS	Middle East and Africa Section	Under an agreement with State, provided KPCS-related technical assistance to Liberia.
		Analyzed rough diamond data for KPCS Monitoring Working Group.

Source: GAO analysis of U.S. agency information.

State leads U.S. efforts in KPCS and works with other U.S. agencies to, among other things, strengthen KPCS by monitoring its effectiveness in preventing trade in rough diamonds. State and other U.S. agencies participate in various aspects of KPCS, including attending annual (and other) KPCS meetings, and serving on KPCS working groups and committees. For example, State serves on the KPCS working group on monitoring, which is mandated to monitor and assess implementation of KPCS by all participants. Also, State and Census serve on the KPCS statistics working group and USGS has done statistical analysis of rough diamond trade data for the monitoring working group.

The CDTA authorizes federal agencies to provide technical assistance to countries seeking to implement KPCS. Thus far, State and USAID have

provided diamond-related assistance to Sierra Leone, and State and USGS have provided this assistance to Liberia. Specifically, through Management Systems International,[12] USAID has provided technical assistance to Sierra Leone to help the country gain control of its trade of rough diamonds. State has recently funded USGS to provide, through Constella Futures International,[13] technical assistance to Liberia for implementing KPCS.

U.S. Agencies Have Improved Systems for Implementing CDTA's Domestic Provisions but Are Still Vulnerable to Illicit Trade

U.S. entities responsible for implementing the domestic provisions of CDTA have improved the system for collecting and sharing U.S. trade data on rough diamonds and have established systems for controlling the U.S. trade in these diamonds, yet these systems are still vulnerable to illicit trade. Because most of these vulnerabilities involve limited government monitoring or oversight, U.S. control systems cannot help deter illicit rough diamonds from entering the legitimate trade.[14]

Census Has Improved Collection and Reporting of Rough Diamond Data, But Some Work Remains to Be Done

Since the enactment of CDTA in 2003, Census has steadily improved its system for capturing and reporting U.S. rough diamond trade statistics in response to KPCS concerns. However, this system needs further improvement to assure that the rough diamond trade does not include illicit diamonds. CDTA recommends that the executive branch keep and publish statistics on rough diamond imports and exports, recognizing that reliable and comparable data on the international trade in rough diamonds are an essential tool to effectively implement the certification scheme. These data can help to identify any irregularities or anomalies that might indicate the presence of conflict diamonds in the legitimate trade in rough diamonds. For example, because the Republic of Congo was not able to explain its reports of rough diamond exports that were far in excess of its

[12]Management Systems International is a USAID contractor.

[13]Constella Futures International, formally known as Futures Group International, is a USGS contractor.

[14]Monitoring is an internal control standard that focuses on assessing— through ongoing monitoring activities and separate evaluations—the quality of performance over time to ensure that the government promptly identifies and addresses any problems. See *Internal Control Management and Evaluation Tool*, GAO-01-1008G (Washington, D.C.: Aug. 2001).

known production capacity or imports, KPCS decided to ban this country from participation in the certification scheme in 2004.

KPCS has expressed several concerns about the trade data the United States has submitted. Subsequent to the enactment of CDTA, Census reported U.S. rough diamond trade data to KPCS that contained a greater volume of exports than imports. For example, it reported that the United States had exported about 3 million carats more than it imported in 2003. As a non-producing nation, this excess in exports was not plausible and raised concerns about the accuracy of the U.S. trade data and the potential laundering of rough diamonds through the United States. In fact, because the United States does not produce rough diamonds and cuts and polishes some rough diamonds, exported carats should, on average, be lower than imported carats. In 2005, the KPCS peer review visit to the United States recommended that Census identify all anomalies within the systems for recording data and correct them as necessary, that the United States provide explanations for the large differences between exports and imports in 2003 and 2004 to the KPCS Working Group on Statistics, and that the group follow up on this issue with the U.S. authorities.

To improve the quality of its data and to comply with KPCS data requirements, Census made a number of changes, including the following:

- Census officials indicated they had identified anomalies that affected the accuracy of the data, including the misclassification of shipments by individual filers and the Census' use of a method that altered some shipments by recalculating quantities of exports or imports based on historical price data.

- Census continues to pursue potential causes of inaccuracy in U.S. rough diamond import and export data. Specifically, Census officials told us of their efforts to determine how many carats of rough diamonds are entering the United States under the generic U.S. Goods Returned Code.[15] In addition, Census officials also reconcile U.S. trade data bilaterally with

[15]According to officials at Census, the U.S. Goods Returned code may be used when diamonds that were exported from the United States are returned, for example, following a trade show or a failed transaction. Since this generic code is used for a variety of commodities, it is difficult to identify rough diamond imports classified under this code, which could bias the level of imports down.

other trading partners, as this can also help to identify any data anomalies.[16]

- In early 2006, Census started collecting and reporting data from Kimberley Process certificates. This change harmonized the U.S. system for data collection with the vast majority of other KPCS participants. Before this change, Census used data from its traditional customs-based method to report to KPCS, which can be different from data collected based on Kimberley Process certificates.[17]

- Census now checks its own data against the monthly data it receives from USKPA on the disposition of certificates issued each month. This extra step has helped Census to identify errors involving quantities or shipments that were misclassified as rough diamonds.

- Census and CBP modified the Automated Export System (AES) and the Automated Broker Interface (ABI), so that these computer systems, through which filers enter export and import shipment data, require Kimberley Process certificate numbers when entering information on rough diamond exports and imports. With these changes, filers will now receive an error if they do not provide a Kimberley Process certificate number after entering a rough diamond tariff code. Prior to these modifications, polished diamonds and diamond jewelry could be (and were) misclassified as rough diamonds.

- Census stopped estimating the quantity for shipments that fell outside of a reasonable price range.[18]

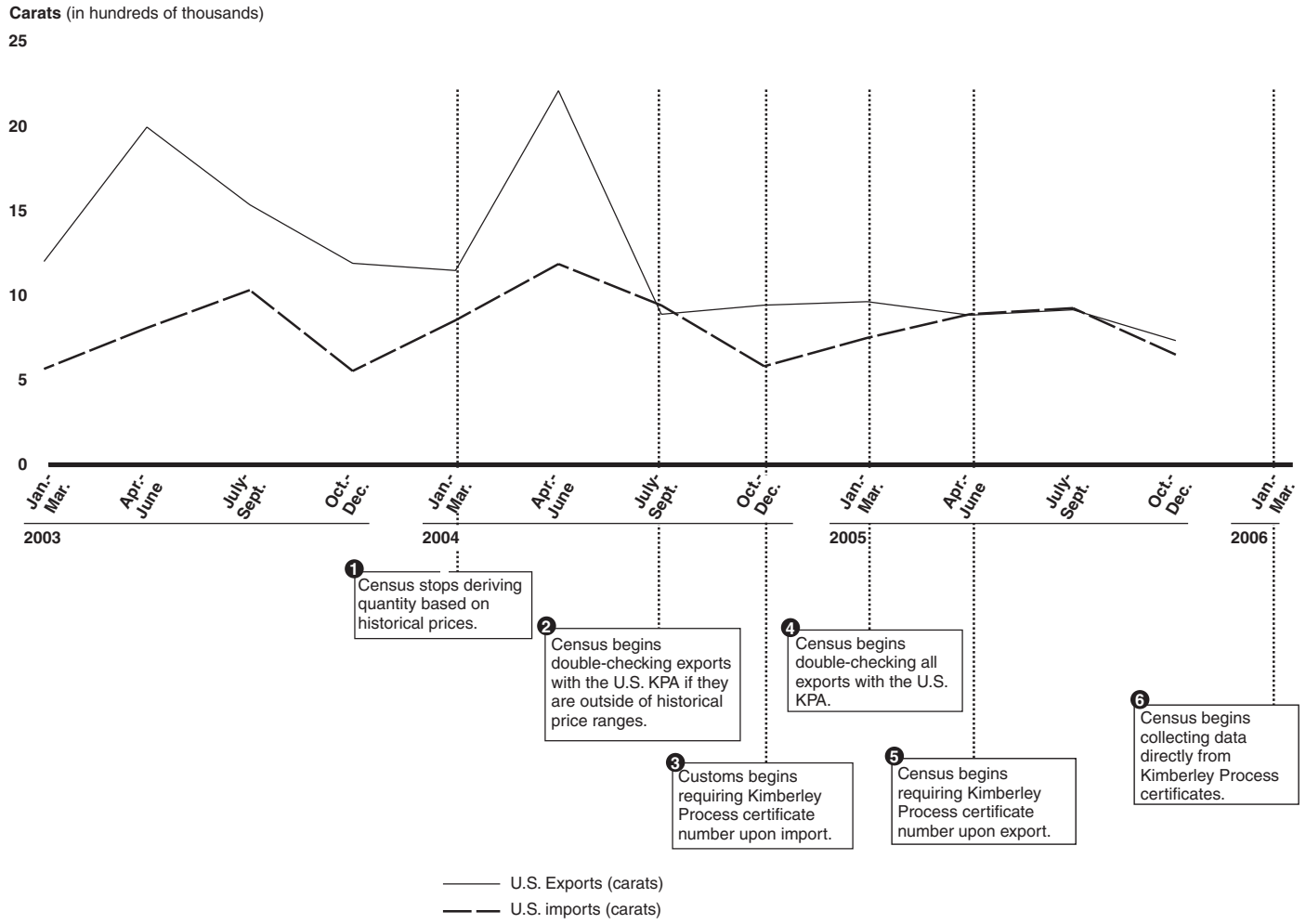
[16]If Census detects differences in bilateral trade data, it will ask the trading partner to send information on specific shipments. Then Census can check if it has the Kimberley Process certificate for the shipments in question and can also check ABI to see if the shipment was filed at all. However, Census is constrained by Title XIII, which prohibits it from discussing individual shipments with other countries; this makes it more challenging to perform these reconciliations.

[17]The Kimberley Process Working Group on Statistics conducted a study comparing 2004 KPCS-based data with non-KPCS-based data. They found fewer differences between export and import transactions derived from KPCS-based data than non-KPCS-based data.

[18]This method, which used historical prices to estimate a new quantity, relied on assumptions that could bias the quantity estimate. The procedure, known as imputation, assumes that the quantity was recorded incorrectly, and that the shipment value was recorded correctly. However, if the shipment value was incorrect, scaling it by a historical price will not produce the correct quantity.

As figure 2 shows, Census' actions resulted in a significant reduction in the reported discrepancies between U.S. rough diamond export and import data. Compared to the nearly 3 million carat discrepancy reported between imports and exports in 2003, by 2005 Census reported an excess in exports of less than 300,000 carats compared to imports. However, Census has not determined whether this annual excess of U.S. exports compared to imports is reasonable for a non-mining country and, thereby, does not involve illicit rough diamonds. Factors that might contribute to this annual excess include the levels of inventories held and the volume of cutting and polishing done in the United States.

Figure 2: Discrepancy in U.S. Rough-Diamond Trade Volume and Census Data Improvements



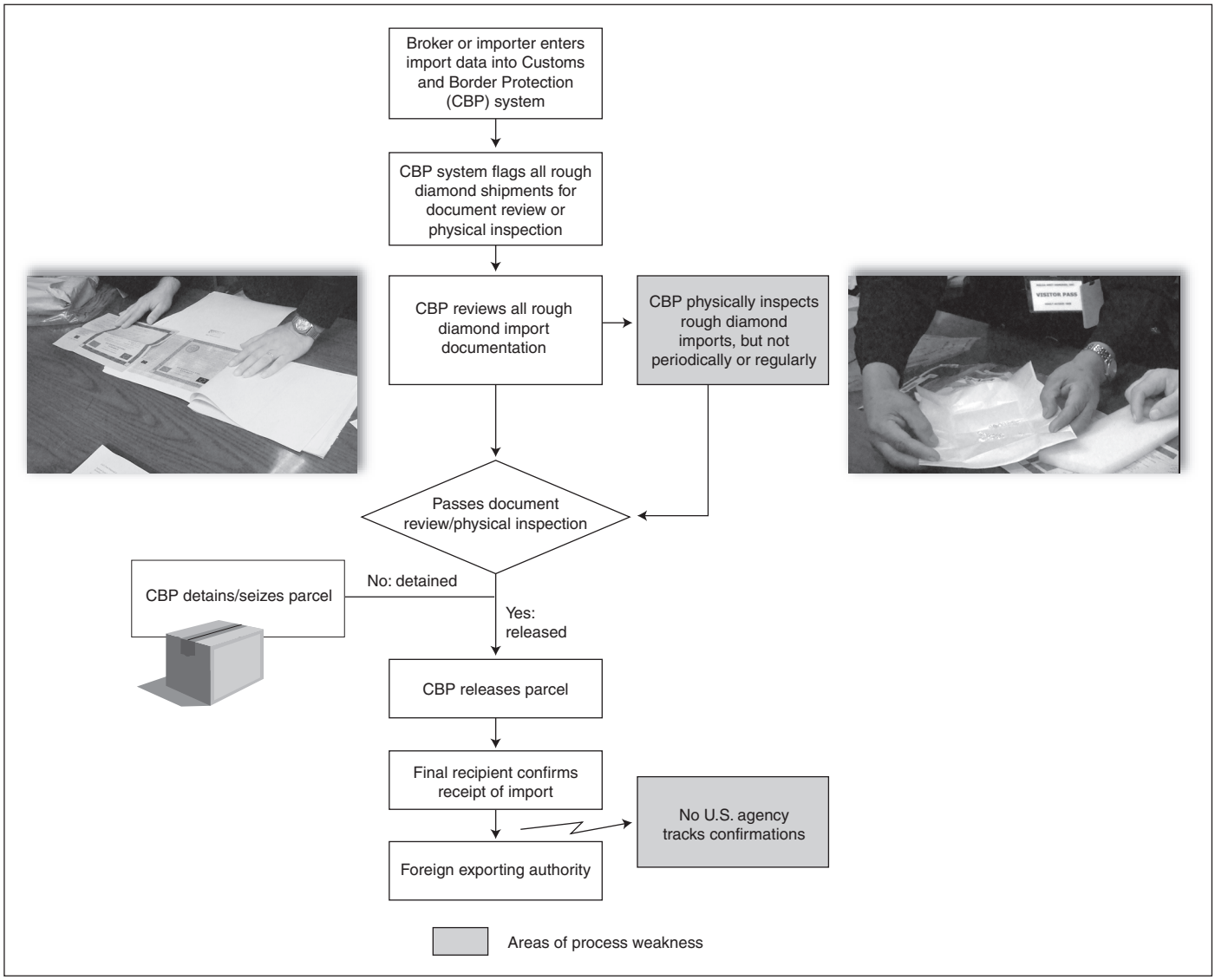
Source: GAO analysis of Census and CBP information.

CBP's System to Control Rough Diamond Imports Has Weaknesses

CBP has established a system for controlling U.S. rough diamond imports through documentation review and physical inspections. However, because these physical inspections do not occur periodically or regularly, the system cannot ensure that illicit shipments of rough diamonds are not entering the country. Furthermore, since 2003, U.S. importers have failed to confirm rough diamond import receipts with foreign exporting authorities, resulting in U.S. non-compliance with this KPCS standard. See

figure 3 for a graphic depiction of the import control process and weaknesses in U.S. government oversight.

Figure 3: U.S. Import Control Process and Weaknesses



Source: GAO analysis of CBP and OFAC information.

CBP's Import Control Process Involves Documentation Review of All Imports and Physical Inspections

CDTA prohibits the importation into the United States of any rough diamond that has not been controlled through KPCS, which details a number of requirements to control imports of rough diamonds. For example, the United States must:

- require imports to contain a valid Kimberley Process certificate;
- ensure that no shipment of rough diamonds is imported from a non-participant;
- ensure that rough diamonds are imported in tamper-resistant containers; and
- establish a system of internal controls designed to eliminate the presence of conflict diamonds from rough diamond import shipments.

To implement CDTA import provisions, CBP created a system that selects all rough diamond import shipments for documentation reviews. Depending on the approach CBP uses for physical inspections, the system might choose all or some of these shipments for physical inspections, although not periodically or regularly. CBP controls about 300 ports of entry into the United States. Although rough diamonds come into the United States through multiple ports of entry, about 85 percent of them come through one port of entry—John F. Kennedy (JFK) Airport in New York City. Under the current system, after a rough diamond import arrives at a port of entry, the customs broker sends the hard-copy entry documentation to the CBP office at the port, at which time the information is entered into CBP's computer system for review.

All rough diamond shipments must, at least, receive a document review by an import specialist, who verifies that the Kimberley Process certificate is authentic and ensures that the information on the certificate (such as the certificate number, and the value and quantity of the rough diamonds) matches the information on the invoice accompanying the shipment. If the reviewing import specialist detects a problem with the documentation, the shipment is detained until CBP obtains the necessary documentation to release the shipment. The shipment may be seized if the information is not obtained within a certain time frame.

CBP has used four approaches to select imports of commodities for physical inspections. In the case of rough diamonds, this means physically opening and examining the content of import parcels. First, given the large number of imports arriving into the United States every day, CBP uses an

approach to identify high risk import shipments for physical inspections. According to CBP documentation, this approach enables CBP to balance its efforts to enforce CDTA with the agency's Priority Trade Issues and other responsibilities.[19] Second, CBP has a compliance measurement program that randomly selects shipments for physical inspection across all ports. Less than 1 percent of rough diamond shipments each year are selected for a physical inspection through this program, according to CBP. Third, physical inspections occur at the discretion of the ports. At JFK, for instance, CBP physically inspects shipments for different reasons, including (1) intelligence information entered into CBP's computer system before the shipment arrives at port; (2) suspicious discovery in the documentation review; (3) shipments from unknown importers; or (4) other information. Finally, CBP inspected all rough diamond imports that came into JFK on two occasions in 2004 and 2005. According to CBP documentation, on these two occasions, inspections found a high rate of importer compliance with U.S. requirements regarding declaration of rough diamond imports.

Since 2003, CBP has seized seven shipments for violations of CDTA. One case involved a rough diamond import without a valid Kimberley Process certificate that was not packed in a sealed tamper-resistant container. Of the remaining six cases, three closed cases were resolved through the administrative process, with one resulting in a fine. Three cases are open and proceeding through the administrative process.

CBP Does Not Have a Policy or Plan for Conducting Physical Inspections Periodically or Regularly

Although CBP has used four approaches for selecting rough diamond import shipments for physical inspections, none of these approaches results in periodic or regular physical inspections. According to accepted government internal control standards, control activities such as periodically or regularly reviewing assets—in this case, rough diamond shipments—should be evaluated periodically or regularly to ensure that they are still appropriate and working as intended.[20] While the total inspection of rough diamond imports at JFK, referred to above, helped CBP to assess the effectiveness of its import control systems during two periods of time, the agency has no policy or plan for conducting these total

[19]CBP's Priority Trade Issues include risks to the economic interests of the United States or the health and safety of the American public. Specifically, these issues include Penalties, Revenue, Antidumping/Countervailing Duties, Agriculture, Intellectual Property Rights, and Textiles.

[20]See *Internal Control Management and Evaluation Tool*, GAO-01-1008G.

inspections periodically or regularly in any of its ports of entry. Furthermore, CBP has no policy or plan for conducting other physical inspections periodically or regularly. Without these types of physical inspections, the United States cannot ensure that its import control system deters illicit rough diamond shipments.

The United States Has Confirmed Few Import Receipts with Foreign Exporting Authorities

The United States has not fully complied with the KPCS standard that requires KPCS participants to confirm rough diamond import receipts to the relevant foreign exporting authority. The 2005 KPCS peer review reported that the implementation of this requirement has been sporadic and recommended that the United States take steps to ensure that it enforces this provision. During our fieldwork, we found that the United States had not confirmed receipt of most import shipments to foreign exporting authorities of four KPCS participants, which are key U.S. trading partners, and the United States did not know the extent to which it had not confirmed import receipts with the rest of the participants. For example, the United States confirmed receipt of 2 percent of rough diamond import shipments from Belgium in 2004, and 18 percent of these shipments in 2005. All other countries confirmed receipt of 95 percent of rough diamond import shipments from Belgium in 2004, and 97 percent of these shipments in 2005. See table 2 for U.S. confirmation of import receipts to four countries, and all other countries' confirmation of import receipts to three of these four countries in 2004 and 2005.

Table 2: U.S. Import Confirmations to Select Countries Compared to All Other Trading Countries, 2004 and 2005

		2004			2005		
Country reporting	KPCS participant	Number of certificates sent	Number of imports confirmed	Percentage confirmed	Number of certificates sent	Number of imports confirmed	Percentage confirmed
Canada	United States	32	7	22%	44	7	16%
	All other trading countries	139	126	91%	149	134	90%
United Kingdom	United States	224	35	16%	262	132	50%
	All other trading countries	1,523	1,415	93%	1,490	1,370	92%
Belgium	United States	1,466	36	2%	1,333	236	18%
	All other trading countries	3,1778	30,191	95	31,722	30,710	97%
Israel	United States	235	3	1%	286	41	14%
	All other trading countries	7,476	N/A[a]	N/A[a]	7388	N/A[a]	N/A[a]

Source: GAO analysis based on data from Canada, the United Kingdom, Belgium, and Israel.

[a]Israel could not provide specific numbers, but indicated that all other countries confirm most imports from Israel.

The United States has delegated the responsibility for confirming rough diamond import receipts to importers. Through OFAC, the Treasury clarified this requirement in its September 2004 revisions to the Rough Diamond Control Regulations by making the ultimate importer (i.e., the ultimate consignee instead of the importer-of-record) responsible for confirming rough diamond import receipts to the relevant foreign exporting authority. The revised regulation also requires that the ultimate importer send the confirmation within 15 calendar days of the import's arrival at the U.S. port of entry, and clarifies that the confirmation may be in any form and may be submitted electronically, by mail, or by courier. The regulations include civil and criminal penalties for any person who violates, or attempts to violate, any order or regulation issued under CDTA.

The United States has not made any U.S. agency responsible for tracking these import confirmations, and has only learned about the U.S. failure to confirm import receipts when exporting authorities from other countries have complained about this problem. In response to these complaints, the United States has recently taken steps to improve the compliance of U.S. importers with this KPCS requirement. Between April and June 2006, State sent letters to about 150 U.S. importers reminding them of the requirement under the rough diamond control regulations to confirm receipt of rough diamond imports to foreign exporting authorities. Based on information provided by State to OFAC, in August 2006, OFAC opened investigations

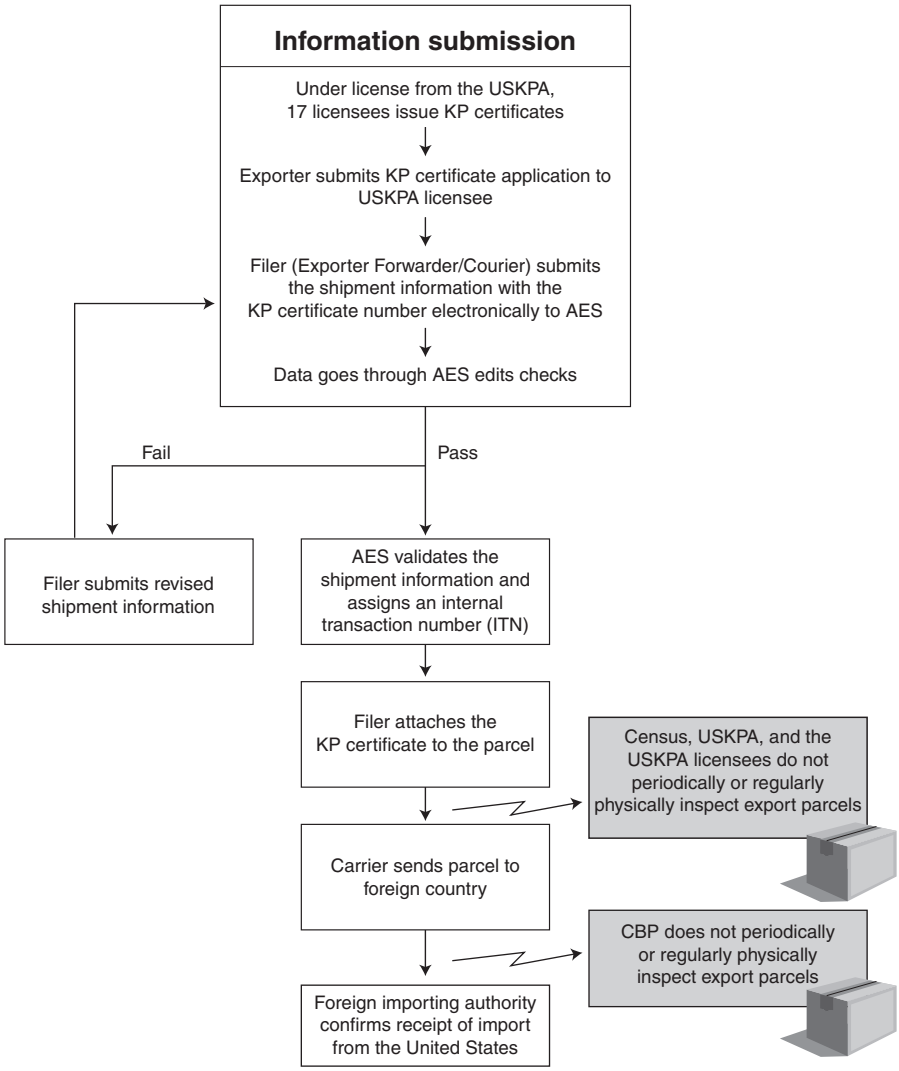
and started to issue administrative subpoenas to importers who had not confirmed import receipts. If any importer continues to fail to confirm import receipts, that is, fail to comply with the regulation, civil penalties may result.

These enforcement efforts have had a positive effect on U.S. compliance with this requirement, but the United States is not yet fully compliant. As of June 2006, for instance, Belgium reported receiving confirmations of import receipts for 35 percent of its shipments to the United States, compared to 18 percent in 2005. Likewise, Canada reported receiving confirmations of import receipts for 33 percent of its shipments to the United States compared to 16 percent in 2005. Despite these improvements, the United States is far from fully complying with this requirement. Because the United States has not assigned an agency to track confirmation of import receipts by importers, it cannot monitor the compliance of importers with this KPCS standard and also is not able to detect possible diversions of rough diamond import shipments. See figure 3 for a depiction of the rough diamond import process and existing weaknesses.

U.S. System to Control Rough Diamond Exports Shows Weaknesses

State, Census, and USKPA have established a system for controlling U.S. rough diamond export shipments. However, the system shows weaknesses because it involves little direct U.S. government monitoring, thereby preventing the United States from being sure that illicit shipments are not leaving the country. See figure 4 for a depiction of the export control process and weaknesses in U.S. government oversight.

Figure 4: U.S. Export Control Process and Weaknesses



Areas of process weakness

AES Automated Export System
CBP Customs and Border Protection
USKPA U.S. Kimberley Process Authority

Source: GAO analysis of CBP and USKPA information.

Census, State, and USKPA Have Established System to Control Rough Diamond Exports

CDTA requires exportation of any rough diamond from the United States to be substantially consistent with KPCS, which details a number of requirements to control rough diamond exports. For example, the United States must:

- ensure a Kimberley Process certificate accompanies each shipment of rough diamonds on export, and that the certificates meet the minimum requirements set out by KPCS;
- ensure that no shipment of rough diamonds is exported to a non-participant;
- ensure that rough diamonds are exported in a tamper-resistant container; and
- establish a control system designed to eliminate the presence of conflict diamonds from export shipments of rough diamonds.

Under the oversight of State, USKPA, through its licensees, issues Kimberley Process certificates. According to a State report to Congress, USKPA, which is comprised of representatives of the diamond industry, was established in 2003 to issue and control Kimberley Process certificates for rough diamond exports from the United States.[21] To issue U.S. Kimberley Process certificates, USKPA subcontracted out to 17 licensees. These licensees represent companies that ship on behalf of third parties, as well as companies engaged in the business of buying and selling rough diamonds that agree to fulfill the requirements of KPCS and all relevant U.S. laws and regulations.[22] Each licensee also agrees, through contractual agreements, to a set of fixed procedures in order to qualify to obtain and use Kimberley Process certificates when exporting rough diamonds. Under these procedures, licensees agree to maintain a supply of Kimberley Process certificates in safekeeping, keep records for 5 years for each shipment where a Kimberley Process certificate is issued, and submit to an

[21]The USKPA has three directors who serve without compensation, selected by consensus by representatives of the diamond industry. The directors are persons familiar with the requirements of KPCS, and are not engaged in the buying or selling of diamonds or jewelry containing diamonds. The activities of the USKPA are funded through fees paid by USKPA licensees. The USKPA designed and produced the Kimberley Process certificate in consultation with the U.S. government.

[22]According to the 2004 USKPA annual report to State, in order to qualify as a licensee each entity has to be authorized as a "known shipper" under AES.

audit by USKPA. Also, licensees/shippers agree to complete an application form.[23]

Licensees submit monthly and annual reports to USKPA with all of the certificates issued in that period. These reports are forwarded to State and Census. See table 3 for the number of certificates issued by the United States from 2003 to 2005.

Table 3: Number of U.S. Kimberley Process Certificates Issued, 2003–2005

Year	Number of U.S. certificates issued
2003	1,516
2004	1,864
2005	1,970

Source: GAO analysis of State data.

CDTA requires that State conduct an annual review of the standards, practices, and procedures of USKPA to determine whether these activities are in accordance with KPCS, and that State report the results of the review to Congress. State has reported as required; however, the content of the annual report is more descriptive than evaluative. According to State, it has not used a formal plan for overseeing USKPA and its licensees. State is currently developing this plan and has tested some of its elements in 2006, according to State officials. The implementation of this plan would help State to conduct periodic or regular, independent, and systematic oversight of USKPA and its licensees to make sure that they conform with KPCS standards.

U.S. Export Process Involves Limited U.S. Government Monitoring

The U.S. government monitors the export process using electronic data checks rather than physical inspections of rough diamond shipments. While USKPA reviews licensees, it does not have a plan for conducting these reviews. Finally, KPCS participants reported to us that they had

[23]The application form that licensees/shippers complete must contain: the names, addresses, and tax identification numbers of the applicant, exporter, and importer; the carat weight of the shipment; the value in U.S. dollars; the number of parcels in the shipment; and the relevant Harmonized Commodity Description and Coding System number. In addition, the following warranty statement must appear on the application: "The applicant hereby asserts that the rough diamonds intended for export referenced in this application have been handled in accordance with the provisions of the Kimberley Process International Certificate Scheme for Rough Diamonds."

received U.S. Kimberley Process certificates that did not comply with the certification scheme requirements.

Monitoring of Export Operations Limited to Electronic Data Checks with No Physical Inspections

Direct government involvement in the operational export process is limited to Census' electronic data checks through AES. Once Census validates a shipment for export based solely on data submitted through AES, no other government agency reviews the shipment. The contents of the parcels are never physically inspected by any government agency, USKPA, or its licensees. According to a senior official at CBP, no one at CBP physically inspects rough diamond export shipments before they are sent, and no requirement exists for submitting a Kimberley Process certificate to CBP for these export shipments.[24] In its final report, a peer review team sent by KPCS to the United States to assess implementation of the certification scheme found that the U.S. export regime would benefit from a more hands-on approach by the government and recommended conducting physical inspections of exports periodically or regularly to ensure that, among other things, the description on the certificate matches the contents of the shipment.

The private sector, through USKPA and its licensees, plays a significant role in the U.S. export process, yet these private entities do not verify the contents of rough diamond exports either. According to a co-director of USKPA, the agency takes no responsibility for the information on the certificate; the licensee and exporter assume this responsibility. Likewise, a senior official from State maintained that the licensees are responsible for providing truthful data—thus ensuring that the contents meet the information on the documentation.

However, according to two USKPA licensee freight forwarders responsible for issuing about half of the U.S. Kimberley Process certificates in 2005, they also do not examine the contents of rough diamond parcels they ship. For rough diamonds, they rely on the warranty the exporters sign on the application attesting that the shipment has been handled in accordance with KPCS. The licensees maintain that the exporters are responsible for collecting and retaining documentation showing that the diamonds were legally imported into the United States. Without an effective monitoring strategy that includes a plan for conducting physical inspections

[24]According to other CBP officials, CBP uses an approach for exports that focuses on inspecting high-technology items that could be used by potential U.S. enemies. Under this approach, rough diamond shipments do not get flagged for inspection.

periodically or regularly, the United States cannot be assured that its internal controls for exports sufficiently prevent export of illicit shipments. This weakness of the U.S. export process could allow illicit diamonds to enter the legitimate trade.

USKPA does not have a plan to conduct reviews of licensees

Under its licensing agreement, USKPA can review a licensee's books, records, and other documents to verify compliance with the agreement. According to a USKPA co-director, USKPA has visited five licensees. However, USKPA does not have a plan to conduct these monitoring visits, nor does it have any protocol for selecting which licensees will receive a visit. The visit might include a review of the security measures used to store the certificates, packing procedures, and record-keeping for every application received, as well as interviews with the employees involved in these processes and those who prepare monthly or annual reports. USKPA gave us visit summaries from its annual reports to State. USKPA did not give us any other documentation regarding these reviews. Without an established monitoring strategy, plan, criteria, and documentation, USKPA cannot be sure that its licensees are meeting their requirements to prevent illicit exports of rough diamonds from the United States.

U.S. Trading Partners Report Problems with U.S. Kimberley Process Certificates

Some countries have reported quality control problems with U.S. Kimberley Process certificates. For example, in 2005, one country reported receiving 26 U.S. Kimberley Process certificates with corrections (correction fluid such as Liquid Paper or Wite-Out had been used to amend errors on them). Also, 10 certificates had typographical errors, and 5 had incorrect dates. In the same year, another country reported receiving 21 U.S. Kimberley Process certificates with typographical errors and 5 certificates with correction fluid. These quality issues raise the possibility that the certificates have been tampered with and, thus, do not meet KPCS requirements. In the absence of physical inspections of U.S. rough diamond exports, foreign importing authorities have alerted U.S. officials of these problems. In response, these officials began conducting outreach efforts to exporters to address these issues.

The United States Has Helped to Strengthen KPCS Internationally, but Assistance-Related Efforts Face Challenges

Internationally, the United States has helped to strengthen KPCS by participating in KPCS activities and providing assistance to help Sierra Leone and Liberia comply with KPCS, but this assistance faces challenges. The United States has helped strengthen KPCS by participating in the activities of its working groups and committees and assuming lead roles; for instance, the United States led a peer review visit to Brazil and offered to identify and coordinate donor assistance to countries seeking to implement or strengthen KPCS. Also, the United States has provided approximately $7.57 million in assistance to the diamond producing countries of Sierra Leone and Liberia to implement systems for controlling their trade in rough diamonds. However, the effectiveness of assistance-related efforts in Sierra Leone and Liberia is constrained by the limited capacity and resources of these countries to implement KPCS and the need to harmonize diamond policies among these countries and other countries in the region. Donors and diamond producers are considering a regional approach to help enhance the effectiveness of donor assistance.

The United States Has Participated in KPCS Activities and Recently Led Two of Them

With State leading U.S. efforts, the United States has helped strengthen KPCS by regularly attending KPCS-related meetings and serving on the three KPCS working groups and the two KPCS committees. CDTA expresses the sense of the Congress that the United States should strengthen KPCS by monitoring the effectiveness of the certification scheme in stemming trade in rough diamonds not controlled by KPCS. To this end, the United States has taken the following actions:

- The United States regularly attends KPCS meetings, which aim to strengthen the certification scheme and assess its effectiveness. According to U.S. officials, the United States has regularly participated in KPCS meetings, including the annual KPCS plenary and intersessional meetings, to discuss and assess KPCS implementation. Also, it crafted compromises and negotiated solutions to disagreements among KPCS participants.

- The United States serves as a member of the Statistics Working Group and, according to U.S. officials, through diplomatic channels has encouraged and assisted several participants to provide required statistical reports to KPCS in a timely manner. Also, the United States, through Census, has analyzed production and trade data for the Statistics Working Group and, through USGS, has done it for some of the KPCS peer review teams.

- The United States serves as a member of the Monitoring Working Group, which monitors how individual participants implement KPCS. The primary

activity of the Monitoring Working Group has been to conduct peer reviews, which include peer review visits to examine participants' efforts to implement KPCS. Since the first peer review visit to the United Arab Emirates in May 2004, KPCS has conducted 31 review visits, including the KPCS peer review visit to the United States in 2005. Officials from State and other U.S. entities have participated in KPCS peer review visits to the following ten participants: United Arab Emirates, Russia, Guinea, India, Sierra Leone, Sri Lanka, Ghana, Togo, Brazil, and Guyana. The United States also participated in the recent Kimberley Process special mission to Liberia.

- The United States serves on two KPCS committees: the Participation Committee, which assists the Chair of the Kimberley Process in handling the admission of new participants to KPCS; and the Selection Committee, which reviews and assesses the credentials of candidates for the position of Vice-Chair.

- The United States has recently led two KPCS activities. Specifically, the United States offered to identify and coordinate donor assistance for implementing KPCS at the plenary meeting in Moscow, Russia, in November 2005. Also, the United States led the KPCS peer review visit to Brazil in April 2006.

The United States Has Helped Two Countries in Their Efforts to Implement KPCS and Is Considering a Regional Approach to Enhance the Impact of Its Diamond-Related Assistance

The United States has provided about $7.57 million in assistance to help Sierra Leone ($6.13 million) and Liberia ($1.44 million) implement KPCS, but the limited capacity and resources of these two recipient countries and the need to harmonize diamond policies with other countries in the region have restricted the effectiveness of this assistance. Donors, including the United States, are considering using a regional approach to enhance the impact of diamond-related assistance. Table 4 shows the U.S. diamond-related assistance to these two countries.

Table 4: U.S.-Funded Diamond-Related Projects Supporting the Implementation of KPCS in Sierra Leone and Liberia

Implementing U.S. agency/contractor	Country/program title	Amount of disbursement[a] (dollars in millions)
	Sierra Leone	
USAID/Office of Transition Initiatives/Management Systems International	Diamond Management Program	$1.26
	Subtotal	**$1.26**
USAID/Management Systems International	Diamond Project	$0.06
	Diamond Policy and Management Project (DIPAM)	$0.94
	Peace Diamond Alliance Support Project (PDA)	$1.08
	Integrated Diamond Management Program (IDMP)	$2.79[b]
	Subtotal	**$4.87**
	Total for Sierra Leone	**$6.13**
	Liberia	
USGS/Constella Futures International	Kimberley Process Implementation Program	$1.44[b]
	Total for Liberia	**$1.44**
	Total for Sierra Leone and Liberia	**$7.57**

Source: GAO analysis of USAID and USGS data.

[a]Disbursements are outlays for programs completed. State has provided $2 million and USAID provided $0.79 million.

[b]These amounts represent obligations for programs not yet completed. State has fully funded this program.

U.S. Diamond-Related Assistance Helped Sierra Leone Comply with KPCS

The United States, as part of its support to the Lome Peace Accord in 1999, helped Sierra Leone initiate diamond policy reform. From September 1999 to March 2007, USAID, through five rough diamond-related projects, plans to provide about $6.13 million in assistance to support Sierra Leone's efforts to control rough diamonds at the national and local level. Between 1999 and 2001, USAID's Office of Transition Initiatives (OTI) provided, through Management Systems International (MSI), about $1.26 million in funding under one project to support government efforts to gain control of its production of and trade in rough diamonds. Between 2002 and 2007, USAID plans to provide, again through MSI, about $4.87 million in assistance under four projects to further enhance the country's efforts to gain control over its rough diamonds. The specific programs are outlined below.

Diamond Management Program

Between 1999 and 2002, OTI, through MSI, provided about $1.26 million, under the Diamond Management Program, to support Sierra Leone in its efforts to develop and implement diamond policies and a system for controlling the trade in rough diamonds. The two primary objectives of the program were to (1) help Sierra Leone bring diamonds under control of the government and (2) cut the trade in conflict diamonds to diminish this trade's financing of warfare. According to a USAID-sponsored evaluation, the primary achievement of the program was to assist the government in establishing a Certificate of Origin system that the country needed to have in place to be able to export rough diamonds. Although this program was largely advisory, it also included providing training and equipment to the Ministry of Mineral Resources' monitoring staff. The evaluation considered the program a success because legitimate exports of rough diamonds increased from $1.2 million in 1999 to $26 million in 2001.

The Diamond Project

At the end of the OTI-funded Diamond Management Program, USAID granted about $62,000 to MSI, under the Diamond Project, to continue working on rough diamonds from August 2002 to November 2002. This funding helped MSI get ready to start a larger program, called the Diamond Policy and Management (DIPAM) program.

Diamond Policy and Management Project

From 2002 to 2004, USAID, through MSI, provided $940,000, under the DIPAM program, to further help Sierra Leone control its rough diamonds at both the national and local level. According to MSI's project closeout report, DIPAM had five policy objectives, and successfully implemented programs in support of each of them:

- *Legitimize policy reform.* MSI, through DIPAM, worked with the government of Sierra Leone to apply economic incentives to shape the behavior of both domestic and international actors in the diamond sector, and promote legitimate mining and marketing. For example, the project explored ways to reward citizens for mining rough diamonds legally and for ensuring that their neighbors also did so.

- *Increase community benefits from mining.* DIPAM focused on increasing community benefits in two ways: by maximizing direct income within the country from the production and sale of rough diamonds, and by encouraging the government to return a portion of rough diamond export tax revenues to communities through the Diamond Area Community Development Fund (DACDF). DACDF distributes one-fourth of revenue earned from export taxes on rough diamonds to communities holding mining licenses. In 2005, over $900,000 in DACDF funds were turned over

to these communities. In one community we visited, these funds helped to build a police facility and a town hall.

- *Engage civil society with government in mining policy deliberations and monitor the government's performance.* DIPAM worked to strengthen community-based institutions to help them more explicitly represent community interests with respect to diamond mining and alternative development activities.

- *Establish dialogue among communities, the government, and the private sector in industrial mining.* DIPAM established forums where community voices could be heard. For example, project officials worked directly to help property owners express their grievances regarding the mining practices of a large mining company.

- *Improve environmental management of artisanal mining.* In September 2004, DIPAM succeeded in getting the government of Sierra Leone to release funds to reclaim land at an illegal mining site that was shut down. The government had set aside a portion of the revenue that it had received from selling mining licenses to pay for environmental reclamation. However, the government had never released it before.

Peace Diamond Alliance Support Project

From 2003 to 2004, USAID, through MSI, provided about $1.08 million, under the Peace Diamond Alliance Support Project (PDA), to help Sierra Leone establish a public/private partnership for mining rough diamonds. MSI implemented this project in an integrated manner with the DIPAM cooperative agreement discussed above. The approach of the PDA has been to remove diamonds from the smuggling chain by providing incentives for legal export, chiefly by increasing benefits at the local level. Specifically, PDA worked to improved diamond management in mining communities by encouraging cooperation among government, businesses, and civil society.

The PDA offered training for members of mining cooperatives (which are largely made up of unskilled workers) on a number of issues, such as valuing stones and improving environmental and safety practices. Figure 5 shows diggers working at a diamond mining site in Sierra Leone. In addition, the PDA helped to organize 35 mining cooperatives between 2003 and 2004, mainly in the Kono District, which is one the main diamond mining areas in Sierra Leone. However, only five of these cooperatives mined rough diamonds in 2005 and only one of them continues to mine rough diamonds in 2006.

The measure of success for the DIPAM/PDA programs was the degree to which legal diamond exports increased and the degree to which benefits were returned to communities. By the above measures, the DIPAM/PDA projects were successful, according to MSI's project closeout reports. For instance, legal diamond exports have increased from $10 million in 2000 to over $140 million in 2005. U.S. and Sierra Leone government officials view the increase in legal diamond exports as an indicator that more diamonds are being traded licitly.

Figure 5: Diamond Mining Site in Sierra Leone—A Recipient Country of U.S. Assistance

Source: GAO.

Integrated Diamond Management Program

From 2004 to 2006, USAID, through MSI, has implemented the Integrated Diamond Management Program (IDMP), to support Sierra Leone efforts to improve the management of Sierra Leone's diamond sector at both the national and local levels. State has provided about $2 million to support this program. In July 2006, USAID approved about $790,000 in additional funding to extend this program until March 2007. At the national level, IDMP continues to help the High-Level Diamond Steering Committee (HLDSC) and its ad hoc Technical Committee in their efforts to support the government of Sierra Leone formulate diamond-related policy. At the local level, IDMP continues to support the PDA, described above, and other local initiatives.

Sierra Leone agreed to create HLDSC to advise the government on the effective management and control of the country's rough diamond

resources. HLDSC members include Sierra Leonean government ministers as well as the U.S. Ambassador and equivalent representatives from the United Kingdom, the European Community, and the UN. The committee formed a technical advisory group to address issues raised by the government or donors in early 2004. The committee and its ad hoc technical committee serve as key policy forums for enhancing national diamond-sector policy development and implementation. They analyze strategic policy issues and advise the government on important diamond-sector policy. For example, recent discussions focused on the establishment of diamond cutting and diamond polishing legislation and procedures, and policies for transparent land allocation to diamond companies. MSI serves as the secretariat for both committees. For this reason, these committees have relied on U.S. assistance for guidance, recommendations, and support, according to recent program status reports.

U.S. Diamond-Related Assistance Is Helping Liberia in Its Efforts to Comply with KPCS

In 2005, State asked USAID to transfer funds to USGS for developing and implementing a program to help Liberia move toward compliance with KPCS.[25] With this funding, from September 2005 to December 2006, USGS, under an agreement with State and through Constella Futures International, plans to provide about $1.44 million in rough-diamond-related assistance under one project to help Liberia in its efforts to comply with KPCS.

The U.S. assistance focuses on developing and implementing a capacity-building and a technical training program in a broad range of rough diamond activities, such as improving the government capacity for controlling the production and trade in rough diamonds and related geological and commercial activities. For instance, this program includes funding for building a secured annex behind the Ministry of Lands, Mines, and Energy to house Liberia's rough diamond exporting and importing authority, as well as for buying vehicles and equipment needed to support this authority and the ministry's efforts to monitor rough diamond mining activities.

In Monrovia, Liberia, we observed a subcontractor working on the secured annex that will house the exporting and importing authority. Figure 6

[25] The UN Security Council imposed sanctions on the export of rough diamonds from Liberia in 2001 for its role in the armed conflict in neighboring Sierra Leone. Compliance with KPCS is one of the key conditions for lifting the sanctions on diamond exports.

shows the secured annex under construction. Recent status reports on the U.S.-funded assistance effort in Liberia indicate that the U.S program is helping Liberia make progress in different areas. For example, the construction of the annex is almost finished, Kimberley Process certificates are under development, and training of different staff needed to implement KPCS is under way.

Figure 6: Liberian Ministry of Lands, Mines, and Energy Building and Secured Annex under Construction for Housing Liberia's Rough Diamond Exporting and Importing Authority

Source: GAO.

U.S. and program officials noted that, despite the progress made through the support of the U.S. assistance program, Liberia still does not have an effective system for controlling its production and trade in rough diamonds, which is needed to comply with KPCS. In May 2006, the UN completed an assessment of the status of Liberia's efforts to comply with KPCS and a second Kimberley Process Expert Mission visited Liberia to independently assess the status of these efforts.[26] The UN reported that

[26]In February 2005, the first Kimberley Process Mission to Liberia found that, while Liberia had enacted the necessary law to implement KPCS and designated the Ministry of Lands, Mines, and Energy as the focal point for national implementation, this country lacked the means to enforce internal controls, including monitoring the activities of diamond-producing regions.

Liberia still did not comply with KPCS. The UN report, for instance, noted that the components needed for a credible, internationally-accredited certification scheme for rough diamonds were still some months away. In June 2006, the UN decided to extend its rough diamond-related sanctions on Liberia for another 6 months, with the option of assessing the country's efforts to comply with KPCS again in another 4 months. In August 2006, the Kimberley Process Expert Mission to Liberia reported that Liberia had made some progress towards establishing a system of internal controls, which is crucial to the effective implementation of KPCS. However, it also noted that Liberia still lacks, for instance, a system of internal controls that will ensure that conflict diamonds are not entering its production.

Donor Assistance Faces Challenges, But a Regional Approach for Providing Some Assistance Would Enhance Impact of This Assistance

Sierra Leone and Liberia's limited capacity and resources to fully implement KPCS, and the countries' need to harmonize diamond policies with other countries in the regions, constrains the effectiveness of donor assistance. Although U.S. assistance has provided training, equipment, and vehicles to help Sierra Leone monitor diamond mining areas and borders to prevent illicit activities, government officials told us during our visit to that country that they did not have enough capacity and resources to accomplish their mission. For instance, these officials emphasized that they did not have enough vehicles for monitoring large diamond mining areas under their jurisdiction. Because these vehicles included many motorcycles, these officials also noted that they faced many difficulties reaching many mining areas given the bad conditions of the roads and remoteness of mining sites. According to U.S. and Liberian officials, without the U.S. and other donor assistance that is providing training, equipment, and vehicles to help Liberia comply with KPCS, the country would not be able to implement the control systems needed for monitoring trade in rough diamonds, large mining areas, and highly porous borders. Also, the UN Mission in Liberia (UNMIL) in March 2006 noted that the problem of porous borders and insecurity in the Mano River Basin area—which includes Liberia, Sierra Leone, Guinea, and Cote d'Ivoire—has contributed to difficulties in effectively dealing with illicit trading of diamonds.

Donors and diamond producers are considering a regional approach to help enhance the effectiveness of donor assistance because this assistance is constrained by the limited capacity and resources of these countries and the need to harmonize diamond policies among countries vulnerable to illicit cross border diamond trading. In February 2006, at a meeting of alluvial diamond producers, participants encouraged regional and subregional cooperation by harmonizing and reinforcing mechanisms to fight more efficiently the illicit cross border trade of diamonds. Also, the

reports of the KPCS peer review visits to Sierra Leone and Liberia stress the importance of harmonizing diamond-related policies of these (and other) countries in the Mano River region to avoid the illegal transfer of rough diamonds across borders. For instance, when Sierra Leone significantly raised its diamond-related tax rate above the tax rate of other countries in the region in early 2006, it experienced a drop of rough diamond exports that led it to rescind the tax rate increase. Public and private officials have stated that employing a regional approach for some rough diamond-related assistance would improve the impact of this assistance, thereby further deterring illicit diamond trading. These officials have noted that harmonization of taxation and other laws among countries within a region is needed to dissuade people from illegally moving diamonds across borders. In June 2006, representatives from Sierra Leone, Liberia, Guinea, and Cote D'Ivoire, along with representatives from the United States and other donors, met to discuss rough diamond-related issues—including policy areas for potential regional harmonization. According to U.S. officials, the conference highlighted the importance of regional harmonization, as well as the complexity—given the differences in national laws—of trying to find common positions that could be adopted by all the countries within a region. The United States is considering using a regional approach to enhance the impact of some of its diamond-related assistance. This regional assistance would complement country-specific assistance provided to diamond-producing countries within a region.

Conclusions

A system for controlling the trade in rough diamonds will be effective only if it has control mechanisms designed to curtail or deter the trade in conflict diamonds. The United States has established a multi-agency system aimed at controlling trade in rough diamonds (thereby curtailing trade in conflict diamonds) but, because of weaknesses of the system, the United States cannot ensure that illicit rough diamonds are not traded. To succeed, KPCS depends on all participants having strong control systems and procedures for collecting and sharing trade data on rough diamonds, for inspecting imports and exports of these diamonds, and for tracking confirmations of import and export receipts.

Since implementing CDTA, the United States has made significant improvements to its system and procedures for collecting and sharing data and for controlling the rough diamond trade. However, a continual excess of exports over imports raises concerns because the United States is not expected to have such excess of exports over time (it does not produce rough diamonds and polishes some rough diamonds domestically) and

because U.S. agencies have not conducted an analysis that might help to explain a persistent excess of exports. Also, the United States has not had a policy and plan for periodically or regularly physically inspecting imports and exports of rough diamonds to ensure that illicit rough diamonds do not enter the legitimate U.S. trade of these diamonds. In addition, the United States has failed to confirm most rough diamond import receipts to foreign export authorities, thereby failing to comply with a KPCS standard. The United States relies on the ultimate recipients to confirm import receipts, but it has not tracked whether these recipients do so. Moreover, although State and Census have received annual activity reports from USKPA, and State has reported to Congress on USKPA activities, State has not had a plan for overseeing the activities of USKPA and its licensees, who issue the U.S. Kimberley Process certificates. Although USKPA has reviewed the activities of 5 of its 17 licensees, it has not had a plan and protocols for conducting these reviews. These weaknesses diminish the effectiveness and deterrent effect of the U.S. and international systems for controlling imports and exports of rough diamonds.

The United States has helped to enhance KPCS by, among other things, participating in the decision making and operational aspects of the certification scheme, and has supported the adoption of KPCS by providing technical assistance to two African diamond-producing countries, Sierra Leone and Liberia. The United States has participated in KPCS since its inception, and has recently assumed leadership roles, by identifying and coordinating donor assistance to diamond producing countries, and leading a peer review visit to Brazil. The United States has helped Sierra Leone and Liberia in their efforts to meet the minimum KPCS requirements, but the limited capacity and resources of both countries—and the need to harmonize diamond policies among these countries and other countries in the region—has presented a major challenge to U.S. assistance efforts and the countries' ability to control their trade in rough diamonds and monitor large mining areas and highly porous borders. To enhance the impact of its diamond-related assistance and further curtail illicit rough diamond trading, the United States, other donors, and diamond producers are considering using a regional approach for providing some diamond-related assistance, which would help to address diamond issues of a regional nature.

Recommendations for Executive Action

To help the United States ensure that it has a more effective system for preventing the importation or exportation of conflict diamonds, we are making seven recommendations.

- To improve the accuracy of U.S. rough diamond trade data—if U.S. rough diamond exports continue to exceed imports—-we recommend the following:
  - The Secretaries of State and the Treasury direct the U.S. Kimberley Process Implementation Coordinating Committee to perform such analysis as is necessary to determine what constitutes a normal excess of exports over imports based on a variety of factors, including market factors such as rough diamond stockpiles and domestic diamond cutting and polishing capacities.
- To enhance the U.S. process for inspecting rough diamond imports and exports, we recommend the following:
  - The Secretary of Homeland Security direct the Commissioner of CBP to develop and implement a plan for conducting physical inspections of both imports and exports of rough diamonds periodically or regularly, including inspecting the quality of U.S. Kimberley Process certificates.
- To enhance the U.S. process for confirming the receipt of U.S. imports with foreign exporting authorities, we recommend the following:
  - The Secretaries of State and Homeland Security develop and implement a plan for confirming the receipt of imports—currently the responsibility of individual importers—and for tracking these confirmations. The system for tracking import confirmation receipts would help enhance Census' data on rough diamond imports and exports.
  - The Director of OFAC revise the pertinent rough diamond trade regulations to reflect the above change.
- To enhance the U.S. process for reviewing the activities of USKPA and its licensees who issue Kimberley Process certificates, we recommend the following:
  - The Secretary of State direct the Assistant Secretary, Bureau of Economic and Business Affairs, to implement a plan for reviewing the activities of USKPA and its licensees.

- The Secretary of State direct the Directors of USKPA to develop and implement a plan for reviewing the activities of its licensees.

- Finally, to enhance the impact of U.S. diamond-related technical assistance and further curtail illicit rough diamond trading, we recommend the following:

  - The Secretary of State direct the Assistant Secretary, Bureau of African Affairs, to develop and implement a plan for providing some of the diamond-related assistance using a regional approach so that countries within a region can harmonize aspects of their systems for controlling the rough diamond trade across porous borders.

Agency Comments and Our Evaluation

We provided a draft of this report to State, the Treasury, Homeland Security, Commerce, Interior, USAID, and USTR. We obtained written comments from State, the Treasury, Homeland Security, Commerce, and Interior (see apps. VI, VII, VIII, IX, and X). They concurred with our recommendations. We also received technical comments on this draft from State, the Treasury, USAID, and USTR, which we have incorporated where appropriate.

We are sending copies of this report to interested congressional committees, State, the Treasury, Homeland Security, Commerce, Interior, USAID, and USTR. We will also make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at http://www.gao.gov.

If you and your staff have any questions about this report, please contact me at (202) 512-4347. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix XI.

Loren Yager, Director
International Affairs and Trade

Appendix I: Objectives, Scope, and Methodology

As mandated by the Clean Diamond Trade Act (CDTA), this report focused on (1) describing the institutional framework the U.S. government has created to implement CDTA, (2) examining how the United States has implemented the provisions of CDTA domestically and what principal challenges it faces, and (3) examining how the United States has helped to strengthen the Kimberley Process Certification Scheme (KPCS) and what principal challenges it faces.

To address all of these objectives, we interviewed key officials from multiple U.S. agencies and the U.S. Kimberley Process Authority (USKPA). The agencies we interviewed included:

- the Department of State (Bureau of Economic Affairs and United States Mission to the United Nations),
- the Department of the Treasury (Office of Foreign Assets Control),
- the Department of Homeland Security (Bureau of Customs and Border Protection and Bureau of Immigration and Customs Enforcement),
- the Department of Commerce (Bureau of the Census),
- the Department of Interior (U.S. Geological Survey),
- the U.S. Agency for International Development, and
- the Office of the U.S. Trade Representative.

To address our first objective of describing the institutional framework the U.S. government has used to implement CDTA and our second objective of examining how the United States has implemented the provisions of CDTA domestically and what principal challenges it faces, we reviewed documents from the U.S. government and USKPA, including relevant laws, regulations, reports, and briefing documents. Also, we interviewed representatives and collected documentation from diamond industry organizations and non-governmental groups that have been involved in the implementation of CDTA. In addition, we interviewed representatives from private organizations that have been involved in trading rough diamonds to and from the United States. We analyzed Census' rough diamond import and export flows in conjunction with data collection improvements to determine the factors contributing to excess exports. These data have limitations, as discussed in the report. We assessed the quality of data the Census, the UN, and the KPCS used to describe international trade in

diamonds, and determined that they were sufficiently reliable for our purposes. Finally, we used data provided to us by foreign governments to analyze U.S. import receipt confirmations. Based on interviews with foreign government officials we determined that these data were sufficiently reliable to support our findings.

To address our third objective of examining how the United States has helped to strengthen KPCS and what principal challenges it faces, we reviewed UN, KPCS, and U.S. and foreign government documents, including relevant legislation, reports, and briefing documents. Also, we interviewed officials and collected documentation from the UN and other international organizations, KPCS, diamond industry organizations, non-governmental groups, and the U.S. and foreign governments involved in the development and implementation of KPCS. In addition, to identify, describe, and assess U.S. diamond-related assistance efforts, we interviewed U.S., UN, and foreign government officials and non-governmental groups and private organizations representatives involved in the development and implementation of the diamond-related assistance the United States has provided to Sierra Leone and Liberia. We did not independently verify the U.S. assistance data.

We conducted our work in Washington, D.C.; New York, New York; Moscow, Russia; Ottawa, Canada; Brussels and Antwerp, Belgium; Catania, Italy; Freetown and Koidu, Sierra Leone; and Monrovia, Liberia. We conducted our work from September 2005 through September 2006 in accordance with generally accepted government auditing standards.

Appendix II: U.S. and Global Trade In Rough Diamonds

Tables 5 to 8 show information related to the U.S. and global trade in rough diamonds, including the top destinations for U.S. rough diamond exports, top sources of U.S. rough diamond imports, top (non-mining) rough diamond exporting KPCS participants, and the economic importance of diamond mining for selected countries. We assessed the quality of data from the Census, the UN, and the KPCS, and, despite limitations, we determined that they were sufficiently reliable for our purposes.

Table 5: Top Destinations for U.S. Rough Diamond Exports, 2005 (value > 1 percent of U.S. exports)

KPCS participant	Value of exports	Percent of U.S. exports
Israel	$204,486,572	40.0%
European Community	$157,386,752	30.8%
United Arab Emirates	$42,320,452	8.3%
South Africa	$32,243,114	6.3%
India	$19,648,240	3.8%
Switzerland	$14,578,528	2.8%
China	$13,116,880	2.6%
Japan	$8,786,284	1.7%
Namibia	$6,805,390	1.3%
Mauritius	$6,032,302	1.2%

Source: GAO analysis of Census data.

Table 6: Top Sources of U.S. Rough Diamond Imports, by Exporting Participant, 2005 (value > 1 percent of US imports)

KPCS participant	Value of imports	Percent of U.S. imports
European Community	$581,379,013	64.7%
Israel	$215,579,636	24.0%
South Africa	$33,102,427	3.7%
United Arab Emirates	$21,775,428	2.4%
Canada	$12,305,324	1.4%
Guyana	$10,803,495	1.2%

Source: GAO analysis of Census data.

Table 7: Top (Non-Mining)[a] Rough Diamond Exporting KPCS Participants, 2003 (exports > $200 million)

KPCS participant	Value of rough diamond exports
European Community	$9,760,320,078
Israel	$2,948,141,887
United Arab Emirates	$1,006,991,024
Switzerland	$795,914,964
Armenia	$486,569,182
Japan	$299,162,740
United States	$227,286,017
Thailand	$225,365,729

Source: GAO analysis of KPCS data.

[a]The KPCS did not record diamond mining for these countries in 2003.

Table 8: Economic Importance of Mining for Selected Countries, 2003

Country	Value of mining	Mining as a percentage of gross domestic product	Mining as a percentage of exports
Botswana	$2,225,275,390	29%	65%
Democratic Republic of Congo	$910,833,462	16%	64%
Namibia	$421,312,014	9%	24%
Sierra Leone	$76,700,000	8%	44%
Angola	$788,100,104	6%	8%
Guyana	$20,626,850	3%	Not available.

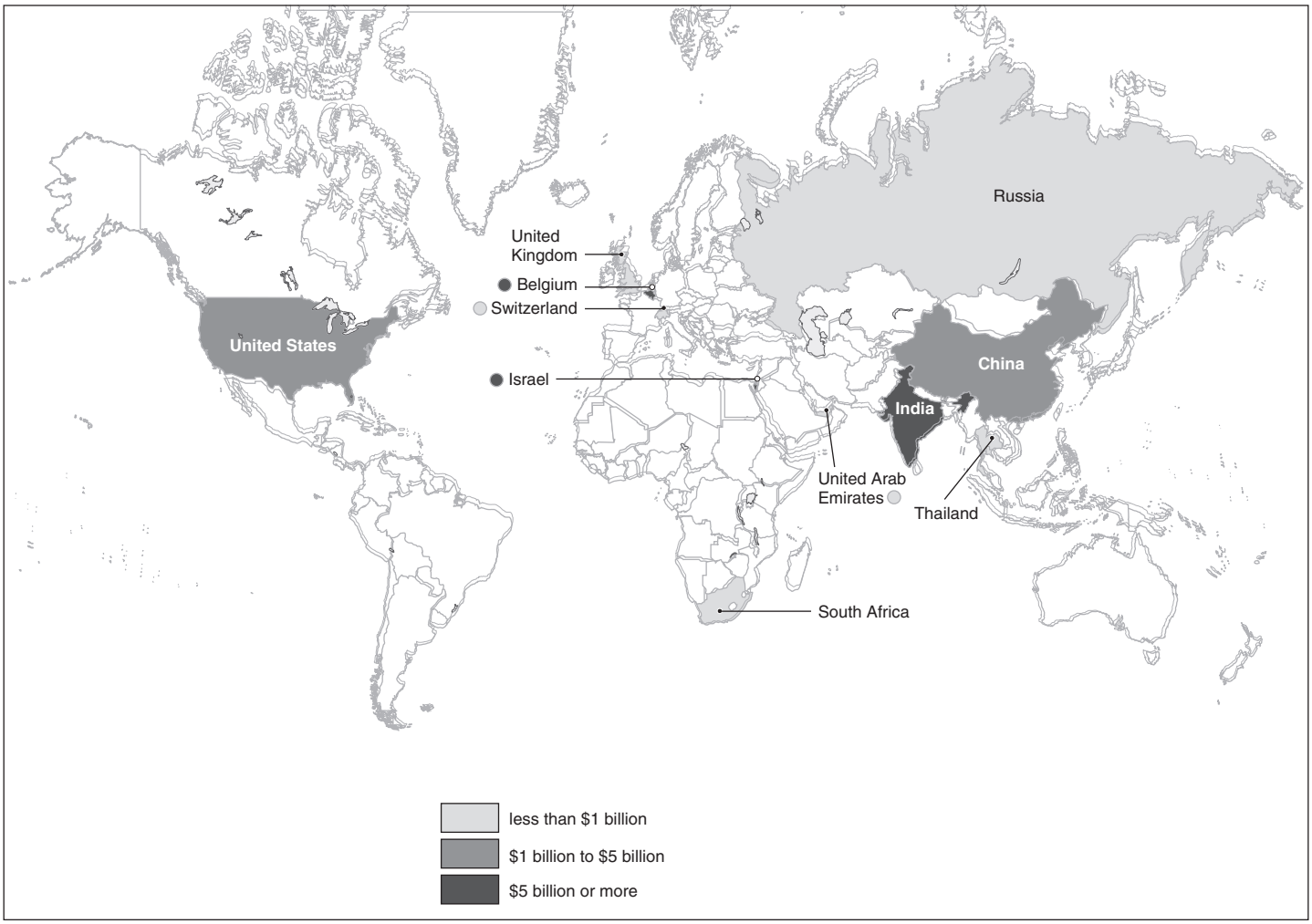
Source: GAO analysis of KPCS, United Nations, World Bank, and U.S. Geological Survey data.

Note: Shares of gross domestic product and exports rounded to the nearest percent.

Appendix III: Top Polished Diamond Exporting and Top Diamond Mining Countries

Figures 7 and 8 depict the top polished diamond exporting countries and the top diamond mining countries.

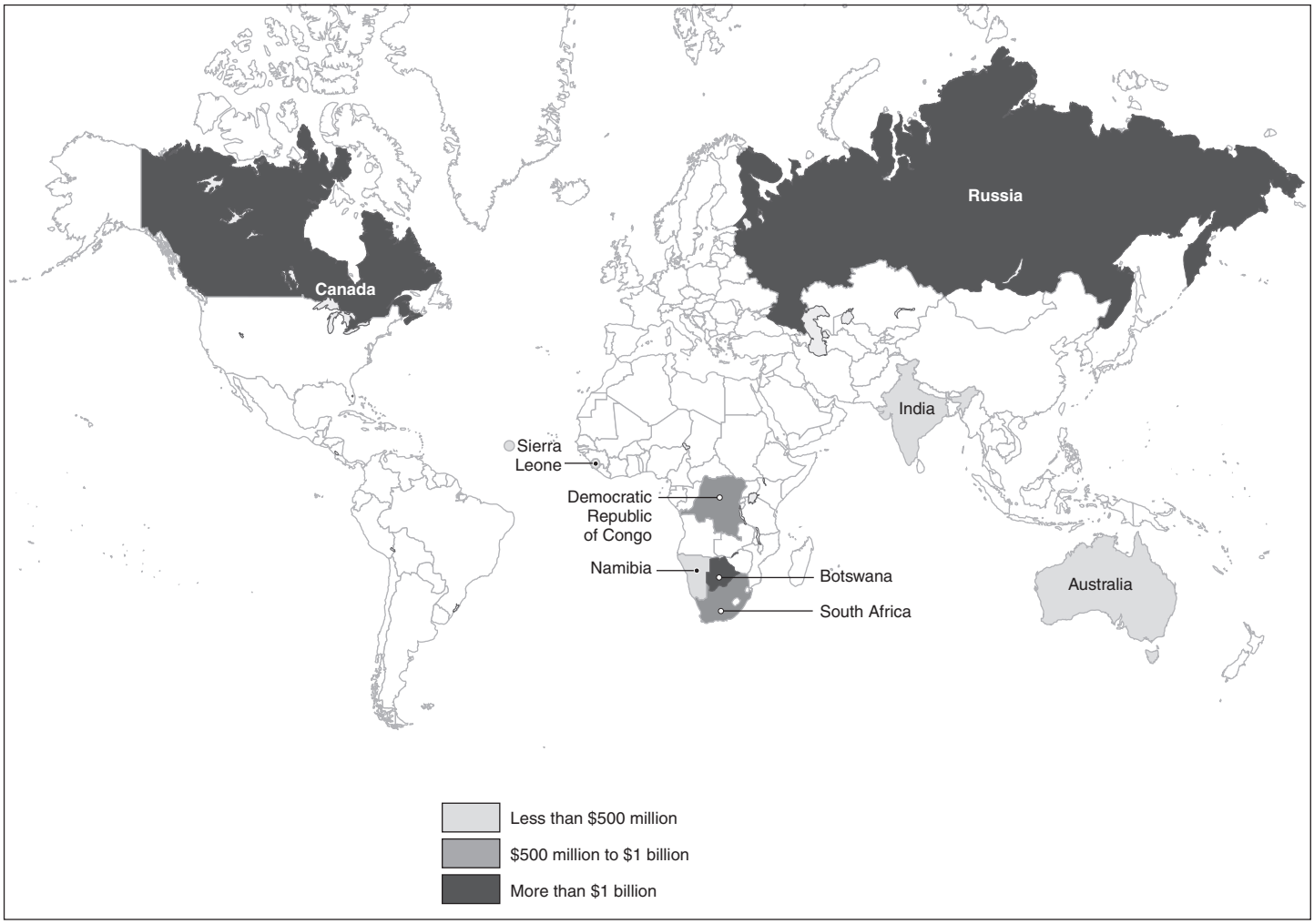
Figure 7: Top Polished Diamond Exporting Countries, 2004 (estimated exports > $200 million)



Sources: GAO analysis of UN data and MapArt (map).

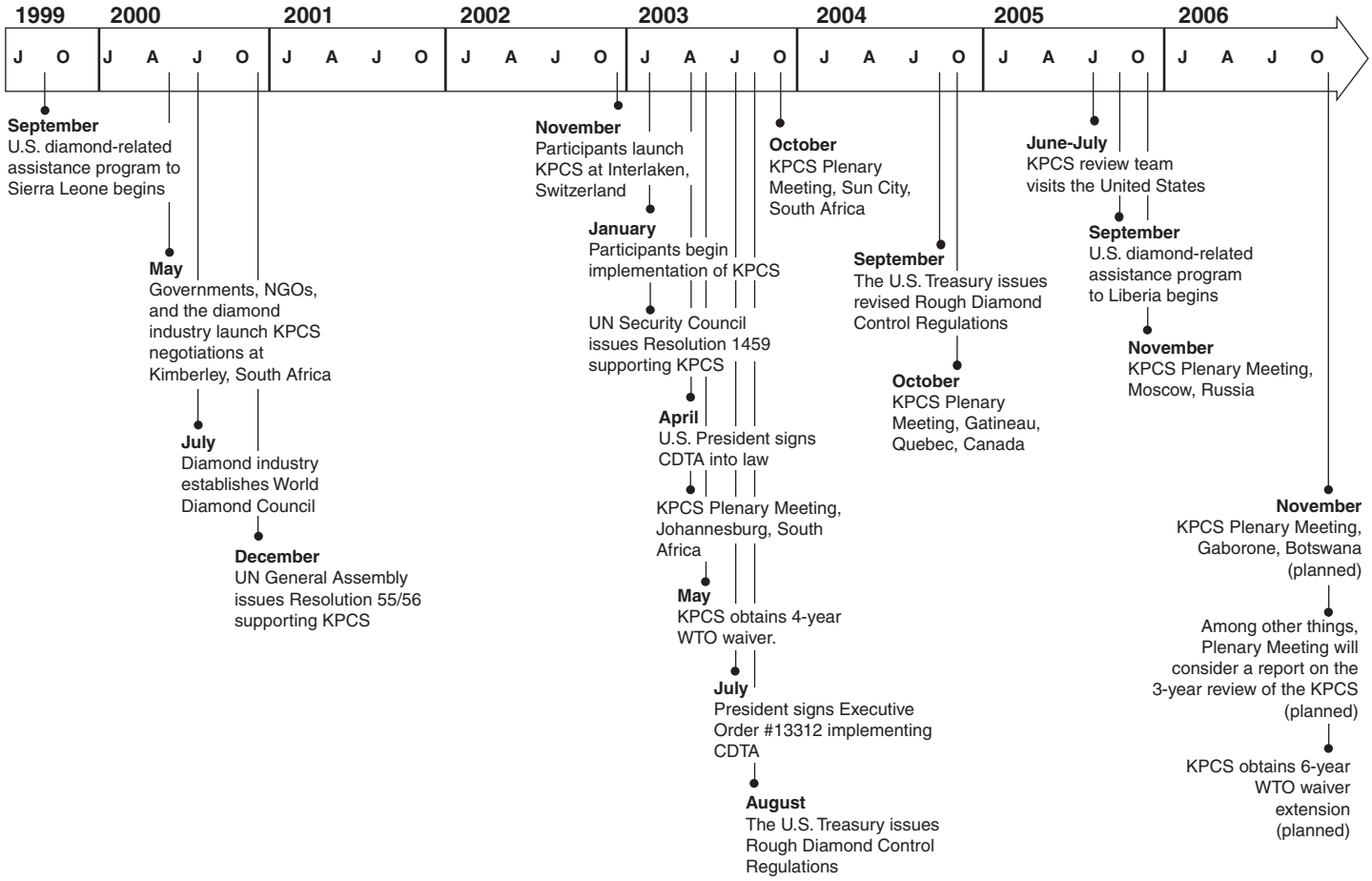
Note: Exports are estimated as the sum of partner imports. China's estimated exports include Hong Kong.

Figure 8: Top Diamond Mining Countries, 2003 (mining value > $50 million)



Sources: GAO analysis of KPCS and US Geological Survey data, media reports, and MapArt (map).

Appendix IV: Timeline of KPCS and CDTA-Related Events



Source: GAO analysis of UN, WTO, KPCS, diamond industry, and U.S. government information.

Appendix V: List of KPCS Participants

States and regional economic integration organizations who have met the minimum requirements of KPCS are:

1. Angola
2. Armenia
3. Australia
4. Belarus
5. Botswana
6. Brazil
7. Bulgaria
8. Canada
9. Central African Republic
10. China, People's Republic of
11. Congo, Democratic Republic of
12. Cote D' Ivoire
13. Croatia
14. European Community
15. Ghana
16. Guinea
17. Guyana
18. India
19. Indonesia
20. Israel
21. Japan
22. Korea, Republic of
23. Lao People's Democratic Republic
24. Lebanon
25. Lesotho
26. Malaysia
27. Mauritius
28. Namibia
29. New Zealand
30. Norway
31. Romania
32. Russian Federation
33. Sierra Leone
34. Singapore
35. South Africa
36. Sri Lanka
37. Switzerland
38. Tanzania
39. Thailand
40. Togo
41. Ukraine

42. United Arab Emirates
43. United States of America
44. Venezuela
45. Vietnam
46. Zimbabwe

Source: GAO analysis of KPCS information.

Note: The rough diamond-trading entity of Chinese Taipei has also met the minimum requirements of KPCS.

Appendix VI: Comments from the Department of State

United States Department of State
Washington, D.C. 20520

SEP 12 2006

Ms. Jacquelyn Williams-Bridgers
Managing Director
International Affairs and Trade
Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548-0001

Dear Ms. Williams-Bridgers:

We appreciate the opportunity to review your draft report, "CONFLICT DIAMONDS: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade," GAO Job Code 320351.

The enclosed Department of State comments are provided for incorporation with this letter as an appendix to the final report.

If you have any questions concerning this response, please contact Sue Saarnio, Economic Advisor, Bureau of Economic and Business Affairs, at (202) 647-1713.

Sincerely,

Bradford R. Higgins

cc: GAO – Zina Merritt
EB – Elizabeth Dibble
State/OIG – Mark Duda

Department of State Comments on GAO Draft Report:

CONFLICT DIAMONDS: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade (GAO-06-978, GAO Code 320351)

Thank you for allowing the Department of State the opportunity to respond to the report entitled *Conflict Diamonds: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade (GAO-06-978, GAO Code 320298).*

We appreciate the GAO's thorough review of the Clean Diamond Trade Act, its recognition of the positive steps the Department of State has taken to strengthen international cooperation on conflict diamonds and its recommendations to strengthen controls over the rough diamond trade. We share GAO's concerns about the need to prevent conflict diamonds from fueling the kinds of conflicts they financed in Africa in the 1990s. The Kimberley Process Certification Scheme has made great strides since 2003 in efforts to control the international trade in rough diamonds. We are pleased that GAO has recognized U.S. contributions to those efforts through the Kimberley Process and technical assistance to Sierra Leone and Liberia.

Since the April 25, 2003, passage of the Clean Diamond Trade Act, the July 29, 2003, signing of the Executive Order implementing the Act and the September 23, 2004, publication of Rough Diamonds Control Regulations, U.S. government agencies have dealt promptly with the challenges that have emerged in the operation of this program. There has been tremendous interagency cooperation to deal with the types of issues which are described in the GAO review. We are strongly committed to continue to improve the U.S. government's internal controls over rough diamonds in order to prevent their use in fueling future conflict.

Our responses to the GAO's specific recommendations follow:

Recommendation 1: To improve the accuracy of U.S. rough diamond trade data—if U.S. rough diamond exports continue to exceed imports---we recommend the following:

The Secretaries of State and the Treasury direct the U.S. Kimberley Process Implementation Coordinating Committee to perform such analysis as is necessary to determine what constitutes a normal excess of exports over imports based on a variety of factors, including market factors such as rough diamond stockpiles and domestic diamond cutting and polishing capacities.

As the GAO report notes, improvements in record keeping have dramatically improved U.S. rough diamond trade statistics in the past three years. If U.S. rough diamond exports continue to exceed imports, the Departments of State and Treasury will continue to coordinate interagency efforts to refine the accuracy of our reports.

Recommendation 3: The Secretaries of State and Homeland Security develop and implement a plan for confirming the receipt of imports – currently the responsibility of individual importers – and for tracking those confirmations. The system for tracking import confirmation receipts would complement Census' system for tracking export confirmation receipts and would help enhance Census' data on rough diamond imports and exports.

While we have made significant improvements in the past year in private sector compliance with the confirmation process, we are prepared to assume greater governmental responsibility for this Kimberley Process obligation. In this regard, the Department of Homeland Security has agreed to provide monthly reports to the Department of State on imports of rough diamonds. The Department of State will then forward the confirmations of receipt to the appropriate foreign exporting authority. Implementation will begin immediately following the conclusion of appropriate disclosure agreements between the two agencies.

Recommendation 5: The Secretary of State direct the Assistant Secretary, Bureau of Economic and Business Affairs, to develop and implement a plan for reviewing the activities of the USKPA and its licensees.

As the GAO report notes, the Bureau of Economic and Business Affairs in early 2006 developed a plan to review the USKPA and its licensees. Implementation of the plan, which includes quarterly visits to USKPA licensees, diamond importers and exporters and regular meetings with the USKPA board, began in March 2006. We will continue to refine this oversight plan and work with the interagency committee to ensure compliance with Kimberley Process standards.

Recommendation 6: The Secretary of State direct the Directors of the USKPA to develop and implement a plan for reviewing the activities of its licensees.

The Bureau of Economic and Business Affairs will direct USKPA Directors to prepare a formal plan to review the activities of its licensees.

Recommendation 7: The Secretary of State direct the Assistant Secretary, Bureau of African Affairs, to develop and implement a plan for providing some of the diamond-related assistance using a regional approach so that countries within a region can harmonize aspects of their systems for controlling the rough diamond trade across porous borders.

The Department of State supports the efforts of regional organizations such as the Economic Community of West African States, the Mano River Union, the West African Economic and Monetary Union, and the Central African Economic and Monetary Community to promote regional harmonization and economic integration in Africa. Kimberley Process Economic Support Funds appropriated through FY06 are committed to projects to support strengthening of land tenure and property rights systems. If additional funds are appropriated by the Congress, we will consider funding programs with a regional focus.

Thank you for the opportunity to respond to this report.

Appendix VII: Comments from the Department of the Treasury

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

SEP 14 2006

Loren Yager
Director, International Affairs and Trade
United States Government Accountability Office
Washington, DC 20548

Dear Mr. Yager:

Thank you for the opportunity to respond to GAO's draft report entitled "*CONFLICT DIAMONDS: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act.*"

The Department of the Treasury's Office of Foreign Assets Control (OFAC) takes its responsibility to contribute to the effective implementation of the Clean Diamond Trade Act, P.L. 108-19 (CDTA), very seriously. I share GAO's concern about the need to prevent conflict diamonds from entering the legitimate trade of rough diamonds. As you correctly point out in the draft report, OFAC's primary role in ensuring the integrity of the Kimberley Process Certification Scheme for rough diamonds (KPCS) is through the promulgation of the Rough Diamonds Control Regulations, 31 C.F.R. part 592 (RDCR), which implement the CDTA and the KPCS. In addition, together with the Department of State, OFAC co-chairs the Kimberley Process Implementation Coordinating Committee established pursuant to the CDTA. OFAC works closely with other U.S. agencies, principally the Department of State and the Department of Homeland Security's Bureau of Customs and Border Protection (CBP), to ensure that U.S. importers and exporters of rough diamonds comply with the requirements of the RDCR, including the requirement that importers of rough diamonds confirm receipt of shipments of rough diamonds imported into the United States to the appropriate foreign Exporting Authorities.

I have reviewed the draft report and submit two technical comments for your consideration. These edits are as follows:

1) On page 23, 1st paragraph, line 6, following the words, "in August 2006, OFAC", please delete the last three words "also sent letters" on that line and instead insert "opened investigations and started to issue administrative subpoenas" before the words "to importers who had not confirmed import receipts." We would suggest rewording the next sentence, beginning on line 7 of that same paragraph, as follows: "If any importer continues to fail to confirm import receipts--that is, fails to comply with the regulation—civil penalties may result."

2) On page 43, we have a technical comment with respect to GAO's recommendation, set forth in the first bullet, that the Secretary of the Treasury direct the Director of OFAC to revise the regulations with respect to confirmation of receipt of rough diamond shipments. The Secretary of the Treasury has already delegated to the

Director of OFAC his full authority to issue regulations or take any other action that he is authorized to take relating to the Clean Diamond Trade Act. *See* 31 C.F.R. § 592.702. Therefore, there is no need to recommend that the Secretary "direct OFAC" to amend the RDCR, and this sentence should simply read: "OFAC amend the Rough Diamonds Control Regulations to reflect the above change." Finally, with regard to the substance of this recommendation, at such time as OFAC is advised by the Departments of Homeland Security and State that a new system for confirming receipts is in place and that the RDCR should be revised, OFAC will issue a conforming amendment.

I hope these comments are helpful in clarifying the above points and again, thank you for the opportunity to comment. I look forward to reading the final Report.

Sincerely,

Adam J. Szubin
Director,
Office of Foreign Assets Control

Enclosure

Appendix VIII: Comments from the Department of Homeland Security

U.S. Department of Homeland Security
Washington, DC 20528

Homeland Security

September 8, 2006

Mr. Loren Yager
Director
International Affairs and Trade
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Yager:

Thank you for the opportunity to review and comment on the Government Accountability Office's (GAO's) draft report entitled *CONFLICT DIAMONDS: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act* (GAO-06-978).

GAO identified key issues in the report and they are being addressed. The report contains several recommendations, one of which is directed to U.S. Customs and Border Protection (CBP), and one of which is directed to a collaborative effort by the Department of Homeland Security and the Department of State.

The Department agrees with the recommendations and will take the appropriate steps needed to implement them. Key actions are listed below:

Recommendation 2: To enhance the U.S. process for inspecting rough diamond imports and exports, GAO recommended that the Secretary of Homeland Security direct the Commissioner of CBP to develop and implement a plan for conducting physical inspections of both imports and exports of rough diamonds periodically or regularly, including inspecting the quality of U.S. Kimberley Process certificates.

Corrective Action

For imports, CBP will create intensive cargo criteria that will require the examination of rough and polished diamond shipments on a periodic basis. Using a random selection process, a specific percentage of diamond shipments will be subject to examination before release. That percentage will either be increased or decreased depending on an annual evaluation of the examination results. The examination will include a full document review to ensure that a valid and original Kimberly Process Certification Scheme (KPCS) certificate has accompanied the shipment. It will also include an examination of the packaging for compliance with the KPCS and a verification of its contents.

www.dhs.gov

For exports, CBP will establish a process to target diamond shipments. The process will produce regular, random targets for verification. The Bureau of the Census has confirmed that all rough diamonds are excluded from Option 4 filing in the Automated Export System (AES) and the U.S. Principal Party in Interest must transmit the export information prior to departure. The time frame for reporting cargo information for air shipments is two hours prior to aircraft departure from the last U.S. port.

Recommendation 3: To enhance the U.S. process for confirming the receipt of U.S. imports with foreign exporting authorities, GAO recommended that the Secretaries of State and Homeland Security develop and implement a plan for confirming the receipt of imports--currently the responsibility of individual importers--and for tracking these confirmations. The system for tracking import confirmation receipts would complement Census' system for tracking export confirmation receipts and would help enhance Census' data on rough diamond imports and exports.

Corrective Action

On a monthly basis, CBP will electronically provide the U.S. Department of State with the following information regarding the receipt of confirmation for each import of rough diamonds: KPCS Certificate Number, country of export, import date, value of the shipment, tariff number, manufacturer/exporter name, importer name and quantity in carats.

The U.S. Department of State will forward the confirmations of receipt to the appropriate exporting authority. Implementation will begin immediately upon establishment of appropriate disclosure law agreements between the two agencies.

Thank you again for the opportunity to comment on this draft report and we look forward to working with you on future homeland security issues.

Sincerely,

Steven J. Pecinovsky
Director
Departmental GAO/OIG Liaison Office

Appendix IX: Comments from the Department of Commerce

THE DEPUTY SECRETARY OF COMMERCE
Washington, D.C. 20230

September 19, 2006

Mr. Loren Yager
Director
International Affairs and Trade
United States Government Accountability Office
Washington, DC 20548

Dear Mr. Yager:

The U.S. Department of Commerce appreciates the opportunity to comment on the United States Government Accountability Office draft report entitled *Conflict Diamonds: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act* (GAO-06-978). I enclose the Department's comments on this report.

Sincerely,

David A. Sampson

Enclosure

U.S. Department of Commerce
Comments on the United States Government Accountability Office
Report Entitled *Conflict Diamonds: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act* (GAO-06-978)

The U.S. Census Bureau supports the Kimberley Process Certification Scheme (KPCS) and is working with the KPCS authorities to provide the most accurate statistics possible. The Census Bureau recognizes there are concerns when the United States has greater volumes of rough diamond exports than imports. As stated in the report, the Census Bureau made several changes to the export processing and collection systems to help minimize this trade difference. The Census Bureau also started capturing the Kimberley Process (KP) certificates in January 2006 and is reporting this information to the KPCS. The Census Bureau has not received additional funding for the KPCS implementation and relies on current resources and funding to perform the required tasks for the KPCS.

The Census Bureau will continue to monitor the trade of rough diamonds and reconcile trade with other KP participants. If there continues to be a substantial amount of exports over imports, the Census Bureau will work with the U.S. Kimberley Process Implementation Coordinating Committee to research this issue.

Finally, a correction is needed on page 25, last paragraph, first sentence. The Census Bureau does not provide oversight to the U.S. Kimberley Process Authority (USKPA). The State Department is responsible for monitoring the USKPA.

Appendix X: Comments from the Department of Interior

United States Department of the Interior

OFFICE OF THE SECRETARY
Washington, D.C. 20240

SEP 1 5 2006

Ms. Loren Yager
Director, International Affairs and Trade
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Ms. Yager:

Thank you for providing the Department of the Interior the opportunity to review the U.S. Government Accountability Office (GAO) draft report entitled, "*CONFLICT DIAMONDS: Agency Actions Needed to Enhance Implementation of the Clean Diamond Trade Act*" (Report Number GAO-06-978).

The GAO staff is to be commended for conducting a thorough, well-researched examination of the Clean Diamond Trade Act. The report shows the U.S. Geological Survey technical assistance to Liberia in a favorable light. We have no substantive comments on the report.

Sincerely,

Mark Limbaugh
Assistant Secretary for
Water and Science

Appendix XI: GAO Contact and Staff Acknowledgments

GAO Contact

Loren Yager, (202) 512-4347

Staff Acknowledgments

Zina Merritt served as Assistant Director responsible for this report, and Juan Tapia-Videla was the Analyst-in-Charge. In addition to those named above, the following individuals made significant contributions to this report: Kate Blumenreich, Leah DeWolf, David Dornisch, Mark Dowling, and Michael Hoffman. The team benefited from the expert advice and assistance of Joe Carney, Randall Cole, Karen Deans, Etana Finkler, Chanetta Reed, Kendall Schaefer, Jena Sinkfield, and Mark Speight.

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