

The logo for Hogan Lovells, consisting of the words "Hogan" and "Lovells" stacked vertically in a serif font, set against a solid green square background.

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BIS v. Beijing – conflict through the prism of export controls

The WorldECR Virtual Forum 2021



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Agenda

- U.S. national security approach to China
- U.S. export controls restrictions
- Chinese counter measures
- Looking ahead



U.S. National Security
Approach to China

China as a Strategic Competitor



United States Strategic Approach to the People's Republic of China

Our competitive approach to the PRC has two objectives: first, to improve the resiliency of our institutions, alliances, and partnerships to prevail against the challenges the PRC presents; and second, to compel Beijing to cease or reduce actions harmful to the United States' vital, national interests and those of our allies and partners.

U.S. National Security Concerns Regarding China

- In May 2015, China announced its “Made in China 2025 Policy”
 - Policy shift toward higher-tech production in China
 - Emphasized ten key industries, including, among others, artificial intelligence in information technology, robotics, green energy/vehicles, aerospace
- DoD Defense Innovation Unit January 2018 report on China’s Tech Transfer
 - Explored risks from Chinese venture capital investment in innovative dual-use technologies
 - Advocated for curbing tech transfer to preserve U.S. ability to “win the wars of the future”
- March 2018 USTR Section 301 Report on China
 - Highlighted threats to U.S. intellectual property
 - China state policy of systemic investment in cutting-edge U.S. industries
- November 2020 State Department “Elements of the China Challenge”
 - Argues that the Chinese Communist Party is a challenge to the established world order
 - Looks at China’s efforts around the world as a part of great-power competition and highlights China’s authoritarian government



Current U.S. National Security Toolkit

Export Controls

Military End Use /
End User Rule

License Exceptions
(CIV, APR)

Deemed Exports

De Minimis Rule

Emerging and
Foundational
Technologies

Entity List

Foreign-Produced
Direct Product
Rule

Enforcement
Priority

Other Export
Control Regimes
(*e.g.*, DOE)

Hong Kong
Decertification

Sanctions

SDN Designations
(*e.g.*, human rights)

Hong Kong
Sanctions

EO on Investment
in Chinese Military
Companies

Other Measures

CFIUS / FIRMMA

Immigration

Chinese App
Executive Orders

IP Theft
Prosecutions

ICT / Bulk Energy
Executive Orders

National Security
Tariffs

Xinjiang Customs
Orders

DoD Lists Under
NDAA FY99

Escalating Trade Controls Restrictions on China

- Presidential action
- Commerce/BIS action
- Treasury/OFAC action
- Defense Department action

May-Nov 2019

- EO and proposed rules on information and communications technology (ICT)
- Huawei and others added to Entity List (28+)

April – May 2020

- EO on bulk power system
- BIS military end use/user (MEU) rule
- BIS eliminates CIV
- Foreign-Produced Direct Product (FPDP) rule expanded for Huawei
- Entity List additions (30+)

June-July 2020

- EO on Hong Kong
- BIS suspends certain license exceptions for HK
- BIS FAQs for MEU rule
- Entity List additions (11 including XPCC)
- OFAC sanctions XPCC
- DOD issues list of Chinese military companies

Aug-Sept 2020

- EOs on TikTok / WeChat
- BIS tightens Huawei FPDP rule
- Entity List additions (24)
- OFAC Hong Kong designations
- DOD expands list

Nov-Dec 2020

- EO on investment in Chinese Communist Military Companies
- BIS issues list of companies for MEU Rule
- Entity List additions (75+ including SMIC)
- BIS removes HK from Commerce Country Chart
- OFAC Hong Kong designations
- DOD expands list

Jan 2021

- EO on certain Chinese payment and other apps
- OFAC FAQs for EO on investment in Chinese Communist Military Companies



U.S. Export Control Restrictions

The background of the slide is a blurred image of green text, likely representing code or data. The text is out of focus, but some words like 'function', 'document', and 'trigger' are visible. A dark green, semi-transparent rectangular box is positioned in the lower right quadrant of the slide, containing the title text in white.

Entity List & Huawei Restrictions

Use of the Entity List



- Frequent use of BIS Entity List to target Chinese companies, government entities, research institutions and individuals
 - Diversion to sanctioned countries / terrorism / violations of export control laws
 - More recently, human rights, allegations of IP theft, and involvement with Chinese military
- Listed entities are prohibited from receiving some or all items subject to the EAR unless the exporter secures a license.
 - Generally, a license is required for all items subject to the EAR, even unlisted items (EAR99)
 - Generally, license exceptions are unavailable (unless specified in Supp. 4)
- Applies to exports, reexports or transfers (in country) of items subject to the EAR
 - Not an SDN designation; for instance, does not apply to imports or purchases *from* Entity List parties
 - But, beware of any General Prohibition Ten (“**GP10**”) violations involving items subject to the EAR
 - Example: U.S. company purchases a commodity that is subject to the EAR from Huawei
 - This is not *per se* prohibited if Huawei obtained the item prior to its designation or received the item under a license
 - If Huawei obtained the item in violation of the EAR, any purchase of that item would be a violation of GP10

Background: Huawei Technologies Co., Ltd.

- May 16, 2019 - Huawei and 66 non-US affiliates added to Entity List
 - Persons are prohibited from exporting, re-exporting, or otherwise transferring to Huawei and its designated affiliates any hardware, software, source code or technology subject to the EAR without an export license from BIS.
 - License exceptions under the EAR are no longer available for exports, reexports, or transfers to Huawei. License applications to engage in such exports, reexports, or transfers to Huawei or its designated affiliates are generally subject to a presumption of denial by BIS (certain transactions that do not involve 5G technology are subject to a case-by-case review).
 - Effective May 20, 2019 – temporary general license permits certain narrow transactions with Huawei
- August 19, 2019 –Additional 46 non-US affiliates added to Entity List
- May 19, 2020 Interim Final Rule
 - General Prohibition 3: Foreign-Produced Direct Product (FPDP) Rule expansion for Huawei
- August 17, 2020 Final Rule
 - 38 non-U.S. affiliates added to Entity List
 - Removed a temporary general license for Huawei and its non-U.S. affiliates and replaces those provisions with a more limited authorization
 - Further tightening of the FPDP Rule for Huawei



Huawei Foreign-Produced Direct Product Rule

- You may not reexport, export from abroad, or transfer (in country) without a license certain foreign-produced items when there is “knowledge” that:
 - The foreign-produced item will be incorporated into, or will be used in the “production” or “development” of any “part,” “component,” or “equipment” produced, purchased, or ordered by Huawei; or
 - When Huawei is a party to any transaction involving the foreign-produced item, *e.g.*, as a purchaser, intermediate consignee, ultimate consignee, or end-user.
- Covers the following foreign-produced items:
 - Direct product of “technology” or “software” subject to the EAR and specified in certain Category 3, 4 or 5 ECCNs (next slide); or
 - Direct product of a plant or major component of a plant located outside the United States, when the plant or major component of a plant (whether made in the United States or foreign country) itself is a direct product of U.S.-origin technology or software specified in Category 3, 4 or 5 ECCNs (next slide).

Huawei Foreign-Produced Direct Product Rule

- The relevant ECCNs for purposes of this rule (certain U.S. software or technology) are listed in Categories 3, 4 and 5 of the Commerce Control List (“CCL”) and include items subject to National Security (“NS”) and/or AT controls:
 - Technology or software controlled under 3E001, 3E002, 3E003, 4E001, 5E001, 3D001, 4D001, or 5D001 (subject to NS and AT controls);
 - Technology controlled under 3E991, 4E992, 4E993, or 5E991 (subject to AT controls only); or
 - Software controlled under 3D991, 4D993, 4D994, or 5D991 (subject to AT controls only).

Foreign-Produced Direct Product Rule

- Key FAQs issued on December 18, 2020 take an **expansive view** of the FPDP's application
 - **FAQ #13** - Company A is selling items subject to FPDP rule to Company B, which will incorporate a percentage of Company A's items into products that are not subject to FPDP rule (or otherwise subject to the EAR). Company A knows that its items will be incorporated into some of Company B's products that are destined to Huawei.
 - **If Company A knows that its items are destined for incorporation into Company B's products that will be sold to Huawei, a license is required even though Company B's products are not subject to the EAR.**
 - **If a percentage of Company A's items are destined for incorporation into Company B's products that will be sold to Huawei, a license is required for the export, reexport or transfer of those items to Company B – regardless of the percentage of Company A's items are used to make products destined for Huawei.**
 - **If Company A doesn't know that the item it is selling will be incorporated into products destined for Huawei in some quantity, it should ask for that information from Company B. If Company B does not provide that information, Company A will need a license to sell to Company B.**





Expansion of
Military End Use /
End User Rule

Summary of Military End Use / End User Rule

- *Purpose is to prevent the transfer of certain technology and items to military in China, Russia and Venezuela*
 - Particular concern about civil-military fusion in China
- Expands licensing requirements for China to include “military end users” in addition to “military end uses”
- Expands the definition of “military end use” to include “support” or “contribution” to certain military applications
- Expands the items subject to the rule to include certain low level items
- Final rule effective on **June 29, 2020**



Overview of Military End Use / End User Rule



- You may not export, reexport, or transfer (in country) certain items subject to the EAR and listed in **Supplement 2 to Part 744** to China, Russia, or Venezuela if, at the time of export:
 - You have “knowledge” that the item is intended entirely or in part for:
 - “military end use” or
 - New rule includes any item that **“supports or contributes”** to the operation, installation, maintenance, repair, overhaul, refurbishing, development, or production of military items described on the USML, or classified under Export Control Classification Numbers (ECCN) ending in “A018” or under “600 series” ECCNs
 - to “military end users”
 - “End user” = (1) national armed forces, national guard and national police, government intelligence and reconnaissance; or (2) **any person or entity “whose actions or functions are intended to support ‘military end uses’”**
- or
 - You have been informed by BIS that the items may be intended for military end use or military end users.

Items Subject to the Expanded MEU Rule

- The expanded rule also adds a number of new ECCNs to the list of items covered by the MEU rule, including items that are controlled for only anti-terrorism reasons. Currently, the following items are subject to the MEU Rule (listed under EAR Supplement No. 2 to part 744)
 - Category 1 Materials, Chemicals, Microorganisms, and Toxins : 1A290, 1C990, 1C996, 1D993, 1D999, 1E994
 - Category 2 Materials Processing: 2A290, 2A291, 2A991, 2B991, 2B992, 2B996, 2B999, 2D290
 - Category 3 Electronics Design, Development and Production: **3A991**, 3A992, 3A999, 3B991, 3B992, 3C992, 3D991, 3E991
 - Category 4 Computers: **4A994**, 4D993, 4D994
 - Category 5 (Part 1) Telecommunications and Category 5 (Part 2) Information Security: 5A991, 5B991, 5D991, 5E991, **5A992**, **5D992**,
 - Category 6 Sensors and Lasers: 6A991, 6A993, 6A995, 6A996, 6C992
 - Category 7 Navigation and Avionics: 7A994, 7B994, 7D994, 7E994
 - Category 8 Marine: 8A992, 8D992, 8E992
 - Category 9 Propulsion Systems, Space Vehicles and Related Equipment: 9A991, 9B990, 9D991, 9E991

BIS Issues FAQs

- On June 26, 2020 BIS issued FAQs addressing the MEU Rule, including the following:
 - **Military end user**
 - Provincial/municipal police departments (as distinct from national police) are not military end users
 - Clarified that “other end users whose activities are intended to support military end uses” include national government organizations, state owned enterprises, and other entities that develop, produce, maintain or use certain military items.
 - **Military end use** – BIS clarified that an item that "supports or contributes to" means an item that provides "direct facilitation" of the specified activities related to the defined military items, such as installation, inspection, or test equipment and related software and technology.
 - **Due diligence** – FAQs indicate that BIS expects a high level of due diligence for even civil companies located in China (and Russia and Venezuela); fact-specific inquiry with no threshold for volume of military activities



BIS MEU List



- On December 23, 2020, BIS published a final rule by adding a new Military End User (MEU) List that identifies companies that have been determined to be “military end users” and notified to public
- Adds 102 companies to the MEU List, including 57 Chinese companies
- Not being listed does not mean a company is not subject to MEU Rule – still need to conduct diligence when engaging with China (and Russia and Venezuela)
- Rule states that companies not on the BIS MEU List but set forth on the DoD Lists created pursuant to the NDAA of FY1999 raise “red flags” that require additional due diligence

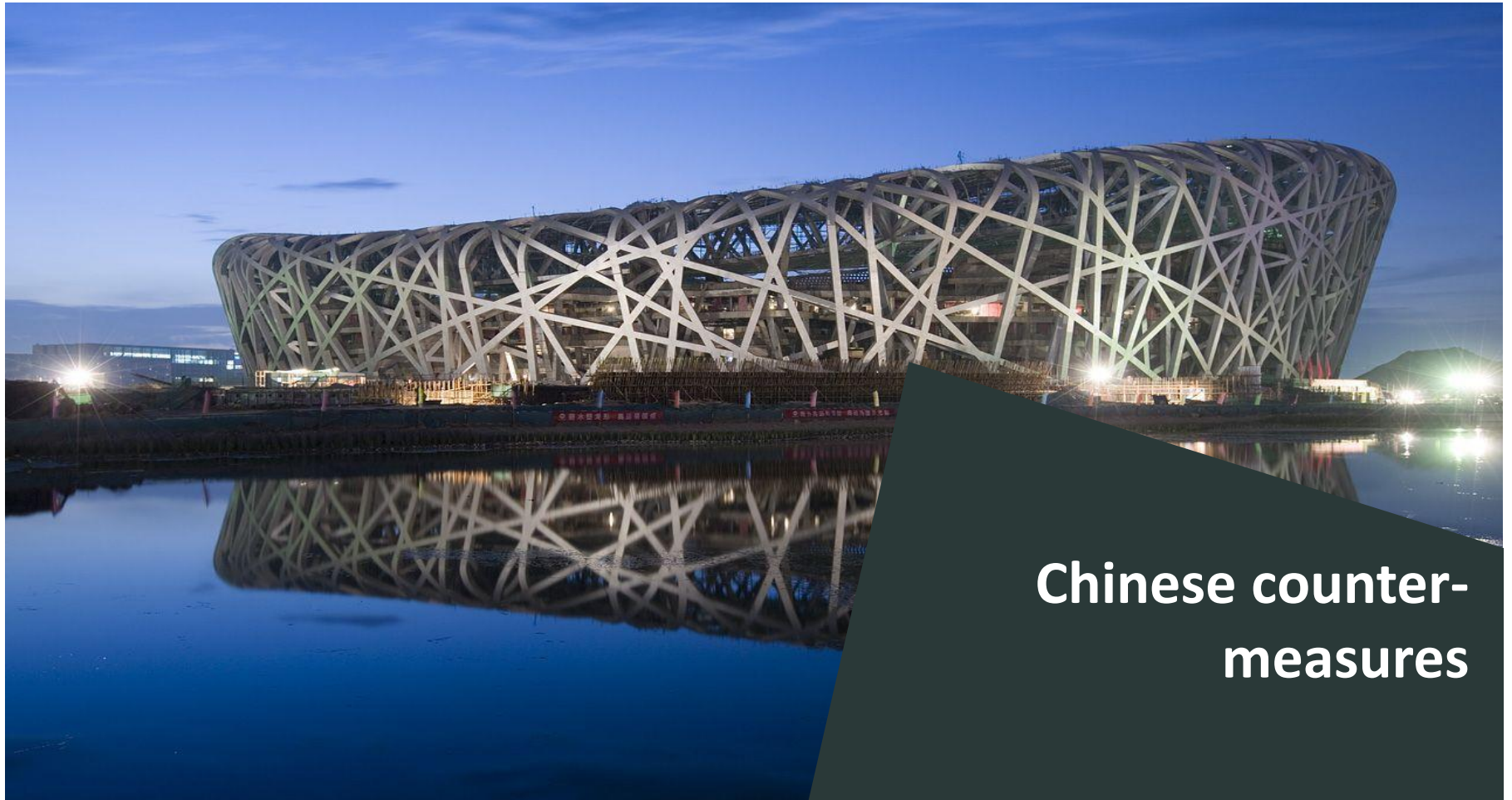


Elimination of License
Exception CIV

License Exception CIV was Eliminated on June 29, 2020

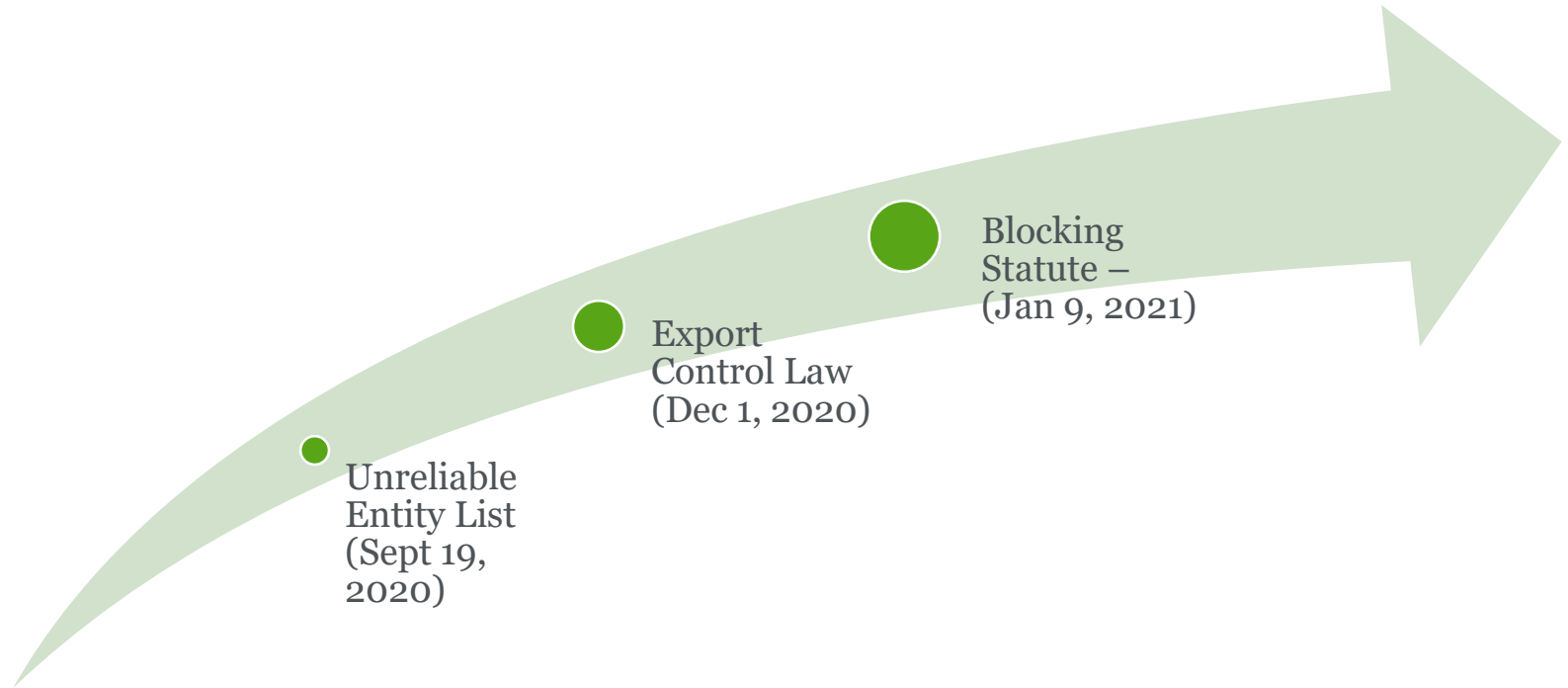
- Before the elimination 15 CFR § 740.5 authorized the export, reexport, and in-country transfer of NS controlled items on the CCL that would otherwise require a license, provided that the items are destined to ***civil end-users and civil end-uses*** in countries in Country Group D:1 (except North Korea). Includes China, Russia, Venezuela, and other countries.
- Elimination of License Exception CIV took effect on **June 29, 2020**
 - Any such exports, reexports, or in-country transfers will require a BIS license.
 - Includes any reexports of items previously exported pursuant to License Exception CIV that are in the foreign recipient's inventory after 29 June 2020





**Chinese counter-
measures**

Chinese counter-measures



PRC “Blocking Statute” Summary

- January 9, 2021 - the Ministry of Commerce of the PRC (“MOFCOM”) issued “Rules on Counteracting Unjustified Extraterritorial Application of Foreign Legislation and Other Measures” (the “Blocking Statute”)
 - Prevent Chinese entities and persons from complying with the extraterritorial application of certain foreign sanctions laws and regulations
 - Effective immediately but not “self-executing”
- Allows Chinese Government to issue “prohibition orders” to companies to prevent them from complying with certain sanctions (including potentially restrictions under U.S. export control regulations) if it has concluded that such sanctions are “unjustified extra-territorial application.”
- Companies that suffer financial losses from non-compliance with such sanctions may apply to the Chinese government for support and compensation and seek legal remedies in Chinese courts.

PRC “Blocking Statute” Key Points

Application Scope: The Blocking Statute will apply when the extraterritorial application of foreign laws and measures violate international law and basic principles of international relations, and improperly prohibit or restrict Chinese entities and persons from engaging in normal economic and trade activities with a person or entity from a third nation.

Working Group: Chinese government will establish a Working Group that is composed of relevant central departments.

Considerations of Improper Extraterritorial Application of Foreign Legislation: Improper extraterritorial application of foreign legislation is not defined in the Blocking Statute. Instead, the Blocking Statute provides discretion to the Working Group to make determination regarding such improper applications.

Reporting Obligation and Injunction: Chinese individuals or entities are required to report to the Ministry of Commerce within 30 days when their business with third-country entities are affected by the foreign laws and measures. If Working Group determines unjustified extra-territorial application of foreign legislation and other measures exist, the Ministry of Commerce will issue a prohibition order restricting the recognition, enforcement or compliance with the foreign laws and measures at issue.

Exemption of Injunction and Penalty: The Statute allows Chinese individuals and entities to apply for an exemption to the injunction. The penalties provided in Article 13 of the Blocking Statute could also apply where a Chinese person or entity fails to truthfully report situations to the working mechanism.

Compensation and Legal Proceedings: It provides that Chinese persons and entities can sue in Chinese courts for compensation of losses incurred from other parties’ (including foreign companies located outside of China) compliance with the foreign laws and measures prohibited in the injunction and foreign rulings made in accordance with those foreign laws and measures.

Government Support and Actions: It authorizes the Chinese government to provide financial support to Chinese persons and entities when they suffer severe losses in non-compliance of a sanction or measure.

PRC Unreliable Entity List (“UEL”)

- On 19 September 2020, China’s Ministry of Commerce (“**MOFCOM**”) published the *Provisions on the Unreliable Entity List (Order No. 4 of 2020)* (the “**UEL Provisions**”), which came into effect immediately upon promulgation.
- No parties have been named under the UEL yet, and there is no clear timeline for the release of potential candidates.
- The purpose of the UEL is to designate foreign entities that have put China’s national sovereignty, security and development interests in danger by suspending transactions with Chinese entities or applying discriminatory treatment against Chinese entities.
- The UEL Provisions establish list-based sanctions through which specific foreign entities may be added to the UEL.
- It is possible that UEL provisions may be applied extraterritorially, such that penalties could be imposed for conduct of foreign entities outside China.

PRC Export Control Law

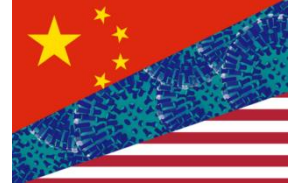
- Comprehensive legal framework for export controls implemented on December 1, 2020
- Key points:
 - Tightens exports control regime through strict monitoring, penalties, and extraterritorial application of export control provisions
 - Article 43 of the Law provides that exporting Controlled Items, which are prohibited from export or without a license in violation of the Law, will face criminal charges.
 - The Law includes provision on reciprocity: “where any country or region which abused export control measures that jeopardize the national security and interests of China, China may, depend on the circumstances, take reciprocal measures”.
 - Extraterritorial reach: Article 44 explicitly provides that organizations and individuals outside China will be held liable if they violate export control rules, impede China's fulfilment of its international obligations, or otherwise endanger China's national security.



Looking Ahead

President-Elect Biden's Approach to China

- **Short-term:** Biden will maintain status quo.
- **Medium-term:** New actions will reflect China as a strategic competitor/adversary.
- **Long-term:** not yet clear if Biden will find an off-ramp or take the relationship from bad to worse.
- **Other considerations:**
 - Biden likely to take a more “traditional” approach to foreign policy;
 - Executive action expanded under Trump Administration;
 - U.S. Congress very active on China policy;
 - Onshoring, nearshoring and the rise of industrial policies, particularly for critical technologies;
 - Areas of cooperation - climate change, North Korea, nuclear non-proliferation, counter-terrorism.



U.S.-China Trade War: What could happen next?

GREEN (Tensions Cool)	YELLOW (Tensions Continue to Slowly Rise)	RED (Crisis Occurs)
<ul style="list-style-type: none">• Gradual and low-key tariff reductions• Suspension of further export controls on China and the United States• Phase 2 Deal• Cooperation on global issues• Return to rules-based trade disputes• Less pressure on MNCs	<ul style="list-style-type: none">• Tension between US/China gradually increases• More list-based sanctions• Expanded export controls on U.S., Chinese and EU technology• Expanded immigration restrictions• More Chinese responses in export controls, MEU• More pressure on MNCs/executives	<ul style="list-style-type: none">• Comprehensive embargo• Chinese rules force MNCs out• Impact on other countries (i.e. EU, Japan/Korea)



Questions?

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