

Decoding the new Chinese Export Control Law

In brief

The recent couple of years have been a compliance roller coaster ride for businesses with supply chains involving China. China went on a major legislative revamp and rolled out a series of new laws, including the new Export Control Law (ECL) of the People's Republic of China (PRC), which came into force on 1 December 2020.

In our past client alerts (see the links below), we wrote about the status of the implementation of the ECL and the principles that form the backbone of the ECL. Half a year after the ECL came into force, we are pleased to provide an update incorporating what we learnt from working with various clients in understanding this new law and how to comply with it.

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The ECL's key principles

1. The framework

The ECL is the first comprehensive and consolidated export control law in China that provides for export controls in respect of dual-use items; military products; nuclear products; and other goods, technologies, services and items that relate to protecting national security and interests and fulfilling international obligations relating to non-proliferation, etc. ("**Controlled Items**"). As the controlled items and technologies sought to be addressed under the ECL were traditionally regulated under various independent regimes, the ECL is expected to, over time, streamline the relevant rules under one legislative framework.

The ECL defines "export control" to mean prohibitive or restrictive measures taken by the state on the transfer of Controlled Items from within the Chinese territory to a place outside of the China territory, as well as the provision of Controlled Items by a PRC citizen, legal person or unincorporated organization to any foreign organization or individual.

2. Controlled goods and technology

Items under the control lists. Relevant departments designated by the State Council and the Central Military Commission ("**National Export Control Authorities**" or NECA), such as the Ministry of Commerce (MOFCOM), are responsible for the administration of the ECL. According to the ECL, the NECA will publish relevant control lists for the purposes of the ECL.

However, instead of issuing a fresh ECL control list, the MOFCOM has, effective from 1 January 2021, adopted the catalogue of dual-use items and technologies ("**DUI List**") (traditionally issued pursuant to the Administrative Measures for the Import and Export License of Dual-Use Items and Technologies ("**Dual-use Measures**")), effectively bringing the DUI List within the scope of the ECL. The DUI List is updated on a yearly basis and the latest list covers items and technologies adopted from regulations relating and applicable to, amongst others, nuclear products; non-nuclear materials used for nuclear materials; nuclear equipment and reactors; missiles; biological products; controlled chemicals; precursor chemicals; radioisotopes and radiation devices; encryption items; specific civilian items; as well as related equipment and technologies.

We would also highlight that there has been a revamp to the list of encryption items and technologies subject to import and export controls. Encryption items and technologies, which were regulated separately under the encryption regime, have now been incorporated into the DUI List effective from 1 January 2021, thereby bringing encryption items and technologies within the purview of the ECL. We will discuss the rules around encryption in greater detail below.



Although the controlled items and technologies under the DUI List have some semblance to those covered under the Wassenaar Arrangement, China's controlled items and technologies are identified based on PRC tariff codes accompanied by certain technical description or parameters. Because of this, a common challenge faced by businesses in complying with the ECL lies in the product screening process; the Export Control Classification Number (ECCN) for dual-use items that multinational businesses are accustomed to using is not applicable in China. It remains to be seen whether China intends to update its regime to adopt ECCN classification in the future for greater alignment with international regimes and standards.

It is also important to note that while certain technologies are included in the DUI List, the ECL stops short of incorporating the control measures in respect of the import and export of technologies set out under a separate set of regulations, i.e., the Regulations for the Administration of the Import and Export of Technology ("**Technology Regulations**"). The Technology Regulations recently garnered significant attention when the control lists were updated last year (the first time since 2008). As a result of the amendments, the export of artificial intelligence interactive interface technologies; speech synthesis and evaluation technologies; scanning and photo recognition technologies; cryptographic security technologies; information countermeasure and defense technologies; laser technologies; and space and aerospace-related technologies, amongst others, are now subject to licensing requirements. It is therefore of paramount importance for companies dealing with technologies to understand and consider the scope and requirements of the Technology Regulations, in addition to the ECL.

The ECL also makes specific reference to control measures in respect of the export of military items or technologies. However, as at the time of writing, no military item or technology has been incorporated into the ECL framework as they remain regulated under separate regulations.

Temporary controls. The ECL provides for the imposition of temporary controls on unlisted items for the purposes of protecting national security and interests and fulfilling international non-proliferation obligations. Such controls can be implemented for up to two years and can be cancelled or extended upon the expiry of the term.

Catch-all provision. In addition to the above, if an exporter knows or should know, or is notified by the authorities that there is a risk of the relevant goods, technologies and services: (i) endangering national security and interests; (ii) being used to design, develop, produce or use weapons of mass destruction and their delivery vehicles; or (iii) being used for terrorist purposes, the relevant exporter will be subject to controls.

3. Export licensing

Licensing regime. The ECL requires exporters to obtain licenses to export Controlled Items. The ECL further notes that the licensing authorities will consider the following factors when deciding whether to grant a license: (i) national security and interests; (ii) international obligations and commitments to foreign parties; (iii) type of exports; (iv) sensitivity of Controlled Items; (v) destination country or region; (vi) end-users and end-uses; (vii) export operator's relevant credit records; and (viii) other factors stipulated by laws and regulations. At the time of writing, we note that the application procedure under the ECL is still based on the existing dual-use and military regimes. The application processes under these two regimes are separate from one another, and license applications should be submitted to the MOFCOM and the State Administration of Science, Technology and Industry for National Defence (SASTIND), respectively, accompanied by the relevant supporting documents.

Export control compliance program. The ECL also underscores the importance of internal compliance by specifically providing for the issuance of export control guidelines to guide exporters in establishing sound internal compliance programs. In this regard, the MOFCOM issued Announcement No. 10 of 2021, on "Internal Compliance Guidelines on the Export of Dual-Use Items" ("**Guidelines**"), which sets out and elaborates on nine key elements that establish an effective internal compliance program with respect to dual-use goods and technology. The elements are: (i) enactment of a policy statement; (ii) establishment of an organizational structure; (iii) comprehensive risk assessment; (iv) establishment of review procedures; (v) formulation of emergency measures; (vi) training and education; (vii) compliance audits; (viii) recordkeeping; and (ix) management manual preparation. The Guidelines also discusses practical tips on how each of the key elements can be incorporated into an export operator's compliance processes and sets out, amongst others, template commitment statements and sample red flag considerations.

It should be noted that the Guidelines has no force of law. However, consistent with the ECL, the Guidelines promises certain licensing facilitation for exporters that establish and maintain sound and well-implemented internal compliance programs.

4. End-user and end-use controls

End-user and end-use certificate. Compared to the Dual-use Measures, the ECL further strengthens controls over end-users and the end-use of Controlled Items. An exporter must submit end-user and end-use certificates, and the end-user must make the commitment that without permission from the Chinese authorities, it will not alter the end-use of the Controlled Item or transfer it to a third party. Exporters that learn of changes in the end-user or the end-use must promptly notify the authorities.



Importer and end-user blacklisting. The ECL also provides for the establishment of a control list for importers and end-users who: (i) breach their end-user and end-use control requirements; (ii) may do harm to national security and interests; or (iii) use the Controlled Items for terrorism purposes. Importers and end-users listed on the control list may be subjected to certain export prohibitions or restrictions.

5. Export prohibitions in respect of specific countries, entities or persons

Export prohibitions. The ECL permits the Chinese authorities to impose export prohibitions in respect of Controlled Items to safeguard national security interests and to fulfil international non-proliferation obligations, etc. The export prohibitions may also be imposed in respect of specific countries, regions, organizations or individuals.

Reciprocal measures. The ECL also provides the Chinese government with the power to take reciprocal measures against any country or region that abuses export control measures to endanger the national security and interests of the PRC.

Much of the above measures are speculated to have been incorporated to provide the Chinese authorities with a mandate to respond to certain trade policies taken by foreign countries that may adversely impact China, particularly policies that result from the US-China trade conflict. That said, there is no evidence of the authorities exercising these powers to date.

It is also noteworthy that the Chinese government has published the Unreliable Entity List Regulations ("**UEL Regulations**"), which took effect on 19 September 2020. The UEL applies separately and is entirely independent from the ECL. According to the UEL Regulations, the Chinese government may impose restrictions on foreign enterprises, organizations or individuals that engage in certain activities that endanger China's national sovereignty, security or development, or that cause serious damage to the legitimate rights and interests of Chinese enterprises, organizations and individuals. Such activities may include the application of discriminatory measures or the suspension of normal business transactions by disregarding market-based trading principles. Entities on the UEL may be subject to a variety of restrictions (import and export, investment, travel, etc.) and may be liable for fines and penalties. At the time of writing, no entity has been listed on the UEL.

6. Deemed export, re-export and extraterritorial reach

Deemed export. The ECL not only applies to the cross-border transfer of Controlled Items from China, but also in respect of the provision of Controlled Items by PRC entities and individuals to foreign entities and individuals either within or outside of China. In this regard, the Guidelines issued by the MOFCOM (which is not legally binding) may shed some light on how deemed export controls may be applied. Circumstances where: (i) a company engages foreign employees in the research and development of controlled technologies; and (ii) a company publishes information regarding controlled technologies in an open trade fair, are provided as examples of a possible occurrence of a "deemed export." Notwithstanding this, we would highlight that there may be practical challenges in complying with the deemed export control rules as we understand that the current licensing regime does not appear to cater for "deemed exports" at this time.

Re-export. The definition of "re-export" (i.e., the export of items containing a *de minimis* amount of PRC-controlled content from one foreign country to another foreign country), which was initially included in the first draft of the ECL, was removed from the final version of the law. For now, references to "re-export" are still included within the context of Article 45, where the ECL applies in respect of transshipment and transit activities, as well as the transfer of goods from customs-supervised zones in China to a place overseas.

Extra-territorial application. Article 44 further provides that organizations and individuals outside of the territory of China that violate the ECL may be held legally liable.

Encryption regime

Background. In 1999, the China State Council issued the Regulations for the Administration of Commercial Encryption ("**Commercial Encryption Regulations**"). These regulations, along with subsequently issued notices, set out the regulatory framework and restrictions applicable to the import, export, use, sale, production and research of commercial encryption products and technologies in China, under the administration of the State Cryptography Administration (SCA).

New Encryption Law. About two decades since the Commercial Encryption Regulations were issued, China passed the Encryption Law (EL), its first national law (as opposed to regulations) to systematically regulate three categories of encryption: core encryption; ordinary encryption; and commercial encryption. Core and ordinary encryptions are used to secure state secrets; commercial encryptions, on the other hand, deal with information that are not state secrets. The EL came into effect on 1 January 2020. Under the new EL, there is a notable change of tone in respect of China's approach as regards the use of commercial encryption. In



particular, it introduces a non-discrimination principle in the application of the EL, including in respect of foreign invested enterprises that engage in the scientific research, production, sale, service, import and export of commercial encryption. The EL also provides that a list of encryption items subject to import and export control is to be published. A general licensing exemption for commercial encryptions used in mass consumption products is also incorporated into the EL. However, the application of such an exemption has been challenging, given the lack of clarity or guidance on how and when this exemption may apply. On 8 August 2020, SCA released a revised draft of the Commercial Encryption Regulations for public consultation, with the period for public consultation ending on 19 September 2020. However, no further announcements have been made to date.

New encryption list. Pursuant to the EL, the MOFCOM, SCA and General Customs Administration (GAC) jointly issued Announcement [2020] No. 63, which sets out new catalogues of encryption products that are subject to import and export controls. The announcement took effect from 1 January 2021 and repealed the previous Announcement [2009] No. 18. It is interesting to note that the control list for import only contains four tangible items, which in effect means that no intangible encryption technology is subject to import controls. In contrast, the control list for exports is notably more comprehensive and covers both tangible and intangible items. It is also worth noting that the items set out in the export control list bear descriptions that are now generally more aligned with the international standards for encryption control.

Licensing under ECL / dual-use regime. As mentioned above, the catalogue of encryption products set out in Announcement [2020] No. 63 has been incorporated in its entirety into the DUI List. This means that encryption products subject to import or export licensing requirements are caught under both the EL and ECL. In practice, however, only one dual-use license under the ECL would be required. Consistent with the DUI List, encryption items and technologies are also identified based on tariff codes and technical descriptions.

Key compliance challenges and risks

Given that the ECL was enacted recently, we note that there exist areas (i) where the practical implementation of the ECL is slowly catching up with legislative changes; and (ii) where additional guidance on the interpretation of requirements is much needed. To help our readers better identify and navigate risks arising from export control law developments, we have set out below some common pitfalls and challenges that we identified from working with clients across industries:

- a. challenges in implementing reliable product screening processes and accurately determining the control status of items and technologies, especially given that the ECCN classification adopted in other jurisdictions cannot readily be applied in China
- b. challenges in relying fully on the tariff classification and control status determination made by manufacturers or freight forwarders, noting that the responsibility to obtain an export license generally lies with the exporter of record
- c. challenges in bridging legal interpretation and practical administration/enforcement, particularly where an item is caught by a tariff code of a Controlled Item but does not fall within the technical parameters of the same, noting that GAC, the key enforcement agency for import and export control, is primarily guided by the tariff classification of exported goods
- d. end-use and end-user-related non-compliance due to a lack of appreciation of the increased controls under the ECL and the dual-use regime
- e. potential transfers of technologies without proper assessment of restrictions under the ECL and Technologies Regulations
- f. potential risks of "deemed exports" occurring without an appropriate license where business engages foreign employees to work with Controlled Items, coupled with the uncertainty around licensing requirements and process for "deemed exports"

Conclusion

Businesses doing business in and with China are encouraged to carry out a holistic evaluation of the implications of the new ECL on their operations in order to manage their risks. As the implementation of the ECL progresses, more guidance, including in the form of implementing regulations, are expected to be published in the near future. As such, businesses should keep their fingers on the pulse of the latest developments in this area to ensure timely responses in the increasingly sophisticated compliance environment in China.



Useful Links

ECL

- [China – What to Watch: Draft Export Control Law of China](#)
- [Updates to China's Draft Export Control Law - What You Need to Know](#)
- [China Publishes Revised Draft of Export Control Law, Solicits Public Comments](#)
- [People's Republic of China enacts new Export Control Law](#)
- [PRC Ministry of Commerce Announce Export Control Internal Compliance Guidelines](#)

Technology Regulations

- [China Amends Catalogue of Technologies Prohibited or Restricted from Export](#)

UEL

- [China Issues the Regulations on Unreliable Entity List](#)

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