

CHINA EXPORT CONTROL LAW – 2020 DRAFT

A. Background

In 2017, the Ministry of Commerce led the drafting of the *Export Control Law of the People's Republic of China (Draft for Comment)*, which was published for public comment on June 16, 2017. This draft was subsequently reviewed on December 28, 2019 by the 15th meeting of the 13th National People's Congress ("**NPC**") Standing Committee, resulting in the full text of the draft being published on the same day for public comment ("**2019 Draft ECL**"). The *2019 Draft ECL* was submitted to the 20th meeting of the 13th NPC Standing Committee on June 28, 2020. The *Export Control Law of the People's Republic of China (Draft after 2nd Review)* ("**2020 Draft ECL**") was released for another round of public comment on July 3, 2020.

Key differences between the *2020 Draft ECL* and *2019 Draft ECL* are as follows:

- The *2020 Draft ECL* reiterates that all parties in the supply chain, including trade agents, freight forwarders, customs brokers, financial service providers and e-commerce platform operators etc. must ensure compliance with the *2020 Draft ECL*.
- The *2020 Draft ECL* includes an evaluation process for temporary measures which will occur before the expiration of the 2-year temporary period to determine whether to extend or repeal the measures or add the item into the export control list ("**Control List**").
- The *2020 Draft ECL* provides that exporters shall not enter into transactions with parties in the entity lists.
- The *2020 Draft ECL* also penalises organisations and persons outside China who violate the *2020 Draft ECL*, obstruct the implementation of international non-proliferation obligations, and harm China's national security and interests.
- The *2020 Draft ECL* removes the mandatory requirement for exporters to set up internal compliance programmes. It also lists the issuance of a general license as one type of simplification of license requirements.
- The *2020 Draft ECL*, however, removed certain provisions in the 2019 Draft ECL resulting in less clarity. Some examples include the removal of the definition of exporters and specified timeframes for processing dual use items license applications.

B. Stated Objectives

The stated objectives of China's new export control law as set out in the *2020 Draft ECL* are as follows:

- Perform China's international non-proliferation obligations;
- Protect national security and interests; and
- Strengthen her export control regime.

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The 2020 Draft ECL covers the following areas: (a) scope of application and competent agencies; (b) control policy and measures; (c) supervision and administration; and (d) statutory liabilities and penalties.

An analysis of the 2020 Draft ECL is set out as follows.

C. Export Control Agencies

The State Council and the Central Military Commission perform the managing functions as the national export control authorities ("**NECA**"). The relevant departments under the State Council and the Central Military Commission would be involved in dual use, military and nuclear items export control matters based on their division of responsibilities.

D. Controlled Activities

The 2020 Draft ECL applies to the following controlled activities:

- The export and re-export of controlled items from China to overseas, including from Customs Supervised Zones (e.g., bonded zones, export processing zones, bonded logistics centres, export bonded warehouses, etc.).
- Provision of controlled items by Chinese citizens, legal persons or non-legal person organisations to foreign organisations or individuals ("**Deemed Exports**").
- Transit and transshipment of controlled items through China's territory.

E. Controlled Items

Controlled items include (i) dual use items; (ii) military items; (iii) nuclear items; and (iv) any other items that are goods, technologies, or services related to the performance of international obligations and protection of national security. The specific items that are subject to control are defined in: (i) the control list, (ii) prohibition orders and temporary controls; and (iii) the "catch-all" provision.

The scope of controls includes exports of controlled items in the form of goods, technologies and services.

(a) Control List

The Control list is to be drafted by the NECA in consultation with the relevant departments and shall be approved by the State Council (and the Central Military Commission) before official publication.

Apart from items which are controlled due to national security concerns, we expect the control list to reflect the items that are controlled under the non-proliferation treaties that China is a member of as well as treaties that China is not a member to base on the existing framework of relevant laws and regulations.

In this regard, China is a party to the Treaty on the Non-Proliferation of Nuclear Weapons ("**NPT**"), the Biological Weapons Convention ("**BWC**") and the Chemical Weapons Convention ("**CWC**"). China is currently not a member of the Australia Group ("**AG**"), Missile Technology Control Regime ("**MTCR**"), Nuclear Suppliers Group ("**NSG**") and the Wassenaar Arrangement ("**WA**").

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(b) *Prohibition Orders and Temporary Controls*

The *2020 Draft ECL* also provides for prohibition orders that prohibit the export of certain controlled items or prohibit exports to certain designated countries / regions or organisations / individuals.

It also allows for temporary controls to be imposed on the export of items that are not listed in the control list for no longer than two years. The *2020 Draft ECL* includes a new provision which allows the NECA to evaluate any temporary controls imposed before the expiry of the two-year period. The NECA may thereafter decide to extend the temporary controls, rescind the temporary controls, or include the relevant item(s) in the control list.

(c) *Catch-All Provision*

The *2020 Draft ECL* also includes a "catch-all" provision. The "catch-all" provision applies to items which the exporter either knows, ought to have known or has been informed by the NECA that the relevant items may (i) endanger national security; (ii) be used in the design, development, production or use of weapons of mass destruction and their means of delivery; or (iii) be used for nuclear, biological or chemical terrorist purposes.

The *2020 Draft ECL* also restricts organisations and individuals within China from providing overseas parties with any information that may endanger national security. This is a new provision in the *2020 Draft ECL*.

(d) *Pre-Classification Process*

The *2020 Draft ECL* provides for a pre-classification process. This requires the NECA to respond in a timely manner to any pre-classification enquiry if the exporter / applicant is unable to determine whether the goods, technologies or services fall within the scope of controlled items. This draft also provides for the establishment of an expert committee to address pre-classification queries.

We expect details on the application process as well as the binding nature of the pre-classification advice to be elaborated upon when the final version of the law is issued or in subsequent administrative issuances.

F. Entities Subject to Export Control Regime

The *2020 Draft ECL* imposes legal obligations on exporters of controlled items. Where previously in the *2019 Draft ECL* exporters had been defined broadly to include citizens, legal persons or other organisations engaged in the export of controlled items, the definition of exporters has notably been removed from this draft.

Apart from exporters, the *2020 Draft ECL* also imposes obligations on organisations / individuals that are involved in export activities such as export agents, logistics providers, couriers, third party electronic trading platforms, financial service providers, etc. to prevent violation of the *2020 Draft ECL*.

The *2020 Draft ECL* provides that only specially designated exporters may export military items in the control list. Records and other less restrictive measures to determine the eligibility of exporters to export controlled items have been removed for the *2020 Draft ECL*.

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The *2020 Draft ECL* also has extraterritorial application. It expressly provides that organisations and individuals outside China may also be liable for export control violations. This is a notable development which was not previously set out in the *2019 Draft ECL*.

G. Licensing Regime

(a) Export Licenses and Licensing Considerations

The *2020 Draft ECL* provides that the export of items in the control list or subject to temporary controls will require export licenses. We expect that the licensing regime will also apply to Deemed Exports, transit and transshipment transactions.

To determine whether to issue export licenses, the following factors will need to be considered:

- international obligations and external commitments;
- national security;
- nature of export transaction;
- degree of sensitivity of the item controlled;
- export destination;
- end-user and end-use;
- exporter's relevant trustworthiness record; and
- any other circumstances prescribed by laws and regulations.

(b) Dual Use Items Export Licenses

On top of the general considerations and factors listed above, the *2020 Draft ECL* also stipulates that an export license will be issued to the applicant once the license application is approved. Nevertheless, the specific timeframe for the processing of applications in the previous *2019 Draft ECL* has been removed. We expect that more clarity will be provided in the final draft or in administrative regulations.

(c) Military Items Export Licenses

With regard to military items, only specially designated exporters for military items can apply for the examination and approval of contracts for the sale and export of military items. These exporters must be endorsed as "Military Items Transportation Enterprises" before being allowed to engage in the export of military items.

(d) End-User End-Use Certifications and End-User Undertakings

The *2020 Draft ECL* provides that exporters are required to submit End-User End-Use Certifications to the NECA. The End-User End-Use Certification may take the form of certifications by the End-User or certifications by the relevant government agency where the End-User is located. We expect that for certain types of exports, China's NECA will require exporters to procure import delivery verifications from the countries where the End-User is located.

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Furthermore, the *2020 Draft ECL* also requires that End-User Undertakings be provided. Such End-User Undertakings require end-users to undertake not to change the end-use of the controlled item or transfer the controlled item to third parties without consent from the NECA. Exporters, distributors of imported goods (presumably in the end-user destination) are required to notify the NECA immediately if they discover that the end-user or end-use has changed.

The *2020 Draft ECL* also requires the NECA to set up a risk assessment procedure to evaluate the End-User and End-Use Certifications submitted by exporters and reinforce the management of End-User End-Use matters.

(e) *Simplification of License Requirements*

The NECA may at its discretion allow simplification of license requirements for exporters who (i) have proper internal compliance programmes; and (ii) have operated such programs properly. Please note that under the *2020 Draft ECL*, an internal compliance programme is not mandatory.

One specified license simplification measure provided in the *2020 Draft ECL* is the issuance of general licenses. This was not specified in the previous *2019 Draft ECL*.

H. Entity Lists

The NECA is empowered to create entity lists for exporters and end-users who:

- violate the end-user and end-use compliance requirements;
- may endanger national security; or
- use controlled items for purposes of terrorism.

Importers and end-users who are added into the entity list may be designated as denied parties or restricted parties. They could also be subject to prohibition orders (i.e., prohibited from importing controlled items). Exporters are prohibited and restricted from entering into any transactions with parties on the entity list.

I. Supervision Powers

The *2020 Draft ECL* also empowers the NECA's with various powers to implement and administer the export control regime.

(a) *Investigation Powers*

The *2020 Draft ECL* grants the NECA powers to investigate potential violations, including:

- Search and entry into business premises of the subject of investigation and related premises;
- Interviewing and taking statements from relevant organisations / individuals that are the subject of the investigation, interested parties, or other related parties;
- Review and taking copies of documents, invoices, agreements, accounts, electronic data and other information;
- Search transport vehicles or equipment;

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- Prohibit the loading of suspicious controlled items and order the return of illegally exported items;
- Seal or detain suspicious items; and
- Review bank accounts of the subject of the investigation.

To ensure that there is proper accountability in the exercise of these investigative powers, the responsible person of the NECA must provide written approval in order to seal or detain suspicious items or review the investigation subjects' bank accounts.

(b) *Confidentiality Obligations*

Under the *2020 Draft ECL*, officers from the investigation team are required to keep confidential any national secrets, commercial secrets and / or personal information acquired during the investigation process.

(c) *Pre-emptive Measures*

The NECA may take pre-emptive measures, including conducting regulatory talks and issuing warning letters to the relevant exporters to prevent any potential breaches.

(d) *Whistle Blowers*

The *2020 Draft ECL* also has provisions relating to whistle blowers. The NECA shall promptly investigate the cases raised by whistle blowers and must keep the identity of whistle blowers confidential. The provision regarding non-anonymous whistle blowers being informed of investigation results has been removed in the *2020 Draft ECL*.

J. Statutory Liabilities and Penalties

The *2020 Draft ECL* imposes stringent penalties on non-compliant exporters for a wide variety of offences, which will result in different types of monetary, non-monetary administrative penalties and / or criminal liabilities (if convicted of criminal charges). These are elaborated on below.

(a) *Types of Offences*

Penalties will be imposed for

- Violation of eligibility requirements;
- Exporting without a license;
- Exporting beyond the permitted scope of a license;
- Exporting prohibited items;
- Obtaining an export license via fraud, bribery, or other improper means;
- Falsifying or buying/selling an export license;
- Providing agency services, freight, delivery, customs declaration, e-commerce platform, financial services or other services to facilitate export control violations;

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- Conducting business with end-users on the Entity List; and
- Obstructing an investigation.

(b) *Administrative and Criminal Liabilities*

The *2020 Draft ECL* stipulates a range of penalties such as

- Warnings;
- Confiscation of illegal proceeds;
- Fines of up to twenty (20) times of illegal proceeds;
- Revocation of export licenses;
- Suspension of business suspension;
- Cancellation of eligibility to export;
- Record violation in the trustworthiness record system;
- Prohibition from obtaining export licenses for a period of five years.

Personal liability may also be imposed on persons who are in-charge of or who are directly responsible for the export violations. Such liability could include being banned from engaging in export business for five years or a permanent ban if criminal penalties are imposed.

Please note that the *2020 Draft ECL* also provides that criminal liability may also be imposed if there are violations of other laws and regulations.

(c) *Appeals*

The *2020 Draft ECL* provides for an appeal process whereby exporters may challenge decisions by the NECA through administrative reconsideration, results of which shall be final.

K. Roles and Responsibilities of Customs

China's Customs will play an important role in the enforcement of the *2020 Draft ECL*. The *2020 Draft ECL* stipulates that exporters / consignors must produce an export license to Customs before controlled items are allowed to be exported. Should there be a failure to produce a required export license, Customs is required to raise a query with the exporter / consignor, and may submit a verification request to the NECA. During the period of the query and verification, Customs shall not release the items for export.

In light of this, Customs has been empowered with the right to investigate potential violations or impose penalties based on the *2020 Draft ECL*.

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L. Our Observations

The Chinese authorities are still seeking comments to the *2020 Draft ECL* before promulgating the law. The draft is open for public comment from July 3 to August 16, 2020.

Companies operating in China need to review the *2020 Draft ECL* very carefully. Apart from the expansive controls that are contemplated in the draft, several areas should remain of concern to businesses.

- **Adoption of WA classification codes** – It is unclear whether the control list will adopt the WA classification codes. The current export control lists in the various regulations do not adopt these classification codes, which hamper the ability of global businesses to ascertain the control status of their products and technologies in China. This is especially so if these products have been classified overseas pursuant to regimes that adopt the WA classifications.
- **Tariff classification codes in the control list** – Given that Customs is to play a prominent role in the enforcement of the *2020 Draft ECL*, it remains to be seen whether the control list will have a table which seeks to correlate the controlled items to tariff classification codes. Such a correlation table has in the past been problematic where Customs has relied heavily on the tariff classification codes as opposed to the descriptions in the control list.
- **Removal of timeframes for license applications** – The removal of the timeframes for license applications creates uncertainty to businesses seeking to fulfil commercial orders within contractual timeframes. Businesses should consider pushing for clarity on application time frames or include provisions in their supply agreements which exempts them from liability for delay resulting from export license applications.
- **Extra-territoriality** – The extra-territorial reach of the *2020 Draft ECL* may impose obligations for exporters in China to monitor changes to the end-uses and end-user of exported items or their transfer or disposal post-exportation from China. Likewise, parties overseas will need to monitor compliance with the Chinese export control laws to avoid inadvertently exposing themselves to liabilities under the *2020 Draft ECL*.
- **Ensuring that parties on the entity list are identified clearly** – Given the potentially dire consequences of transacting with parties listed on the entity list, it is important to ensure that entities listed are identified with clarity, especially where the names and contact details of these entities are not in Chinese.
- **Presence of Deemed Export rules** – Businesses in China will need to take note of the Deemed Export rules. Proper controls will need to be put in place to ensure that only authorised personnel have access to controlled items in China and the necessary licenses are obtained to allow foreign individuals to access such items in China.
- **Appeal Processes** – Currently, challenges to administrative decisions made under the *2020 Draft ECL* can only be pursued through administrative reconsideration presumably before an NECA body that is superior to the NECA body that made the decision being reviewed. There is currently no further appeal to the administrative reconsideration results. This removes the judiciary from reviewing the decisions made under the *2020 Draft ECL*. Given the potential liabilities which may result from violations, businesses may wish to consider the merits of further recourse to the judiciary.

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Please note that the *2020 Draft ECL* aims to introduce a comprehensive export control regime. It should also be viewed in light of the current mosaic of different laws and administrative regulations which deal with specific aspects of export controls. Some of these regulations will be consolidated within the legal framework set out in the *2020 Draft ECL*. However, we expect that the *2020 Draft ECL* will co-exist with other laws and regulations controlling other aspects of exports of controlled goods and technologies from China.

For further consultations on the impact of China's export control laws and regulations to your business or for further inquiries regarding this alert, please contact:

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