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Assessing the Impacts of Executive Order 13936 on Hong Kong's Status, One Month Later

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Introduction

by Ali Burney, Wendy Wysong, Nick Turner

On July 14, the president issued Executive Order (EO) 13936, directing US federal agencies to revoke or suspend the Hong Kong Special Administrative Region's (HKSAR) special status from mainland China under select laws and regulations.[1] EO 13936 specifies a wide range of differential treatment historically granted to Hong Kong by regulation and program inclusion, implemented by various US government agencies, from economic sanctions and export controls, to immigration and academic exchanges. As of August 15, several agencies have announced rule changes or proposed changes to implement the president's directive.

After one month, what are the major impacts of EO 13936 on individuals and companies doing business or investing in Hong Kong?

Background

On May 28, Secretary of State Mike Pompeo submitted the 2020 Hong Kong Policy Act Report to Congress, certifying that the HKSAR "does not continue to warrant treatment under US laws in the same manner as US laws were applied to Hong Kong before July 1997." The secretary's certification was pursuant to section 301 of the United States-Hong Kong Policy Act of 1992 (HKPA), as amended, which requires the Department of State to certify to Congress annually whether Hong Kong continues to warrant differential treatment under US law.

On May 29, the president announced that his administration would "begin the process" of revoking the HKSAR's separate treatment from mainland China under US laws, a status afforded to the HKSAR under the Hong Kong Policy Act of 1992. Furthermore, he said that his administration would sanction Chinese and Hong Kong officials "directly or indirectly involved in eroding" the HKSAR's autonomy.

On July 2, Congress passed the Hong Kong Autonomy Act (HKAA), authorizing sanctions on foreign persons responsible for certain actions in Hong Kong and financial institutions that knowingly engage in significant transactions with them. On July 14, the president signed the HKAA into law and issued EO 13936.

Scope of EO 13936

Section 3 of EO 13936 directs the heads of relevant agencies to "commence all appropriate actions [within 15 days] to further the purposes" of EO 13936 on 11 topics including export controls, immigration, and extraditions. Section 3 will also end Hong Kong's separate participation in the Fulbright exchange program and training of members of Hong Kong's Police Force at the State Department's International Law Enforcement Academies, among other actions.

The order excludes mutual legal assistance, civil aviation, and financial services regulation, and a handful of other areas where the HKSAR differs from mainland China. However, section 3 also directs agencies to recommend "further actions deemed necessary and prudent to end special conditions and preferential treatment for Hong Kong," leaving the door open to further changes.

Section 4 of EO 13936 authorizes the Treasury and State Departments to impose blocking sanctions on foreign persons in relation to certain events in Hong Kong. For discussion of economic sanctions under EO 13936, refer to Steptoe's July 15 client alert, "US Executive Order Implements, Strengthens Hong Kong Sanctions" and Steptoe's August 14 International Compliance Blog post, "Financial Institutions Watch and Wait as OFAC Sanctions Top Hong Kong Officials."

This client alert provides a summary of EO 13936's impact on export controls, arms controls, investigations and white-collar defense, immigration, and trade, with contributions from Steptoe's cross-border teams based in Washington, DC, New York, and Hong Kong.

1 https://www.federalregister.gov/documents/2020/07/17/2020-15646/the-presidents-executive-order-on-hong-kong-normalization

Export Administration Regulations (EAR)

by Alexandra Baj, Meredith Rathbone, Anthony Pan

Until EO 13936, the HKPA permitted the Commerce Department to treat Hong Kong and China differently under the Export Administration Regulations (EAR), including by granting Hong Kong access to license exceptions for exports of dual-use goods controlled under the EAR, which were not available for exports to the PRC. These exceptions allowed for license-free exports to Hong Kong that otherwise would have required a license from the Commerce Department's Bureau of Industry and Security (BIS).

Section 3(c) of EO 13936 mandates the revocation of "license exceptions for exports to Hong Kong, reexports to Hong Kong, and transfers (in-country) within Hong Kong of items subject to the [EAR] that provide differential treatment."

The Commerce Department announced, on June 29, that it would revoke Hong Kong's special status under the EAR. Following the issuance of EO 13936, BIS published a final rule, on July 31, implementing the decision.[2] As a result, license exceptions for exports, re-exports, and transfers to and within Hong Kong of items subject to the EAR are available only to the extent such exceptions apply to China.

Summary of Changes Under the EAR

The change affects 13 license exceptions that could impact US exporters in sectors including aviation and shipping, manufacturing, and technology. Humanitarian donations could also be impacted. The 13 now suspended exceptions are:

1. Shipments of Limited Value (LVS in §740.3)
2. Shipments to Group B Countries (GBS in §740.4)
3. Technology and Software under Restriction (TSR in §740.6)
4. Computers (Tier 1 only, APP in §740.7(c))
5. Temporary Imports, Exports, Reexports, and Transfers (in-country) (TMP in §740.9(a)(11), (b)(2)(ii)(C, and (b)(5))
6. Servicing and Replacement Parts and Equipment (RPL in §740.10(a)(3)(viii), (a)(4), (b)(1) except as permitted to Country Group D:5, and (b)(3)(i)(F) and (ii)(C))
7. Governments (GOV in §740.11(c)(1) – Cooperating Governments only)
8. Gift Parcels and Humanitarian Donations (GFT in §740.12)
9. Technology and Software Unrestricted (TSU in §740.13)
10. Baggage (BAG in § 740.14, except as permitted by §740.14(d))
11. Aircraft, Vessels, and Spacecraft (AVS in §740.15(b)(1), (b)(2), (c))
12. Additional Permissive Reexports (APR §740.16(a) and (j))
13. Strategic Trade Authorization (STA in §740.20)

2 85 Fed. Reg. 45,998 (July 31, 2020), available at https://www.federalregister.gov/d/2020-16278

BIS' final rule contains two savings clauses. The first allows covered items to proceed to their destination if they were in shipment by June 30. The second allows for "deemed" exports and reexports involving Hong Kong persons to continue until August 28, as long as the exporter can document that the Hong Kong persons were hired and provided access to relevant technology prior to June 20.

Economic Impact

According to trade data, EAR license exceptions applied to only USD 432.7 million out of the total USD 50.1 billion of US exports to Hong Kong in 2018 (less than 1%), most involving items related to encryption, software, and technology.[3] The impact of BIS' rule change may be limited because the most used license exceptions—such as the encryption license exception "ENC" in §740.17—are still available for most exports of hardware and software items to Hong Kong (as they are for China).

Despite the seemingly limited impact today, there may be long-term implications. Companies doing business with, through, or in Hong Kong should reassess export policies and procedures (and in-house automated export operations) to account for fewer EAR license exceptions for Hong Kong and monitor for further restrictions in light of ongoing US-China tensions.

For more information about BIS' rule change, see Steptoe's July 30 International Compliance Blog post, "BIS to Publish Rule Suspending License Exceptions for Hong Kong under Export Administration Regulations."

3 *See* https://ustr.gov/countries-regions/china-mongolia-taiwan/hong-kong

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International Traffic in Arms Regulations (ITAR)

by Brian Egan, Edward J. Krauland, Hena Schommer

Sections 2(c) and 3(d) of EO 13936 address defense-related export controls under the International Traffic in Arms Regulations (ITAR) and require that Hong Kong be treated the same as China for the purposes of the Arms Export Control Act (AECA) and the ITAR, with limited exceptions.

As a result, Hong Kong is now subject to the same US arms embargo as China, prohibiting most activity that is subject to ITAR jurisdiction. The US Department of State's Directorate of Defense Trade Controls (DDTC), which administers the ITAR, has issued a notice and FAQs confirming that "Hong Kong is now considered to be included in the entry for China under section 126.1(d)(1) of the ITAR and therefore subject to a policy of denial for all transfers subject to the ITAR."[4] This includes instances "where a Hong Kong person is named as an end-user, licensee (signatory) or sublicensee, or where Hong Kong appears as a marketing, transfer, re-transfer, re-export, sales, or distribution territory."[5] Technical data that are subject to the ITAR and stored in Hong Kong will not be eligible for the new cloud computing rules issued by DDTC on December 26, 2019.[6]

Carve Outs and Past Authorizations

Section 3(d) of EO 13936 carves out from these restrictions "Hong Kong persons who are physically located outside of Hong Kong and the PRC and who were authorized to receive defense *articles* prior to" July 14, 2020. In FAQ guidance, DDTC explains that exports of defense *services* to Hong Kong persons who meet these criteria will be reviewed on a case-by-case basis[7] and that "exporters may continue to rely on available exemptions." The DDTC guidance is silent as to whether it will consider any further license applications for defense articles to Hong Kong persons who meet these criteria.

Previously-issued authorizations are not being revoked or rescinded, but new requests for authorizations will be subject to a policy of denial under section 126.1(d)(1) of the ITAR. Section 126.1(a) provides for limited exemptions (applicable to all Section 126.1 countries), such as the section 123.17(g) exemption for supplies of personal protective gear.

Cloud Computing

Changes under EO 13936 impact more than licensing policy. They also affect companies that may have taken advantage of the new cloud computing rules under the ITAR and stored their ITAR-controlled technical data on a cloud server located in Hong Kong. Under the cloud rule technical data may not be stored on a server located in a Section 126.1 country, which now includes Hong Kong.[8]

These changes to Hong Kong's treatment under the ITAR could disrupt new export authorizations for defense articles and services, especially renewals of current authorizations. Exporters of technical data, in particular, should also carefully review any cloud computing agreement to ensure that data is not stored in Hong Kong.

4 *See* DDTC, July 15, 2020 Notice and FAQs at https://www.pmddtc.state.gov/ddtc_public
5 *See* DDTC, July 15, 2020 Notice and FAQs at https://www.pmddtc.state.gov/ddtc_public
6 *See* Fed. Reg. 70887, December 26, 2019.
7 *See* DDTC, July 15, 2020 Notice and FAQs at https://www.pmddtc.state.gov/ddtc_public
8 *See* ITAR Section 120.54(4).

by Jeff Beatrice, Michelle Levin, Patrick Linehan, Martin Willner

In 1996 and 1997, the United States entered into three treaties with Hong Kong that provide law enforcement officials in both jurisdictions with tools to investigate, prosecute, and punish individuals for certain crimes committed in each other's respective jurisdiction: an extradition treaty, a treaty on the voluntary transfer of prisoners, and a mutual legal assistance treaty (MLAT).

EO 13936 directs US federal agencies to take steps to suspend and terminate the first two of these treaties, thereby limiting US cooperation with Hong Kong with regard to extradition and the transfer of sentenced persons. On August 19, 2020, the State Department announced that it had notified the Hong Kong government of the suspension or termination of the agreements.[9]

EO 13936 does not directly address the MLAT. Therefore, the United States and Hong Kong could continue to cooperate on obtaining evidence supporting the investigation and prosecution of criminal cases.

Extradition Treaty

EO 13936 takes steps to suspend the US-Hong Kong Agreement for the Surrender of Fugitive Offenders, which requires each jurisdiction to extradite individuals for most offenses that are punishable by imprisonment of at least one year in both jurisdictions. Like many extradition treaties, the US-Hong Kong agreement requires "dual criminality," meaning that the United States is not obligated to extradite persons for offenses under Hong Kong law that would not be offenses under US law and vice versa.

The extradition treaty's termination clause permits either party to withdraw on six months' notice. Rather than terminating the agreement, EO 13936 directs agencies to give notice of "suspension," an option not contemplated under the treaty itself, and a step that appears to fall short of permanent withdrawal but which nonetheless will have the effect of suspending the US-Hong Kong extradition treaty for an unspecified period of time.

Despite this action, Hong Kong nationals may still be subject to extradition to the United States in certain circumstances. For example, should a Hong Kong national who has been indicted in a US federal court be detained in a jurisdiction with a robust US extradition treaty (the UK and the EU, among other jurisdictions) extradition proceedings may very well proceed. Similarly, US citizens could still be subject to extradition to Hong Kong from a jurisdiction with an operative Hong Kong extradition agreement.

Transfer of Prisoners Treaty

EO 13936 also calls for the termination of the US-Hong Kong Agreement for the Transfer of Sentenced Persons, which authorizes each jurisdiction, with the other's consent, to transfer prisoners to their home jurisdiction to carry out sentencing.

9 https://www.state.gov/suspension-or-termination-of-three-bilateral-agreements-with-hong-kong/

Mutual Legal Assistance Treaty

EO 13936 does not order suspension or termination of the US-Hong Kong Agreement on Mutual Legal Assistance Treaty in Criminal Matters, which provides for a broad range of cooperation, including securing physical, documentary, and testimonial evidence to be used in criminal proceedings.

Although the US government's ability to extradite individuals from Hong Kong has been suspended, at least temporarily, the legal mechanism for investigating cross-border cases in Hong Kong was not targeted by EO 13936. Still, EO 13936 could have the practical effect of causing Hong Kong officials to choose not to comply with requests under the mutual legal assistance treaty or ignore them altogether. Indeed, on August 20, the Hong Kong government announced it had notified the United States that Hong Kong would suspend implementation of the MLAT and the extradition treaty.

Trade

by Eric Emerson, Zachary Simmons, Jacob Nelson (International Trade Assistant)

On August 11, US Customs and Border Protection (CBP) issued a notice requiring that goods imported into the United States from Hong Kong be marked as originating in "China." Recognizing that affected parties will need time to implement this change, the notice provides that "unless excepted from marking, goods produced in Hong Kong, which are entered or withdrawn from warehouse for consumption into the United States after September 25, 2020, must be marked to indicate that their origin is 'China'..." The notice implements section 2(f) of EO 13936, which suspends the application of section 201(a) of the HKPA (*i.e.*, Hong Kong's special trade status) to Section 304 of the Tariff Act of 1930, as amended (the marking statute). 19 U.S.C. § 1304. The value of Hong Kong's goods exports to the United States in 2019 was USD 4.7 billion.

Tariff Act of 1930

Section 304 of the Tariff Act of 1930, as amended, requires that foreign-origin articles imported into the United States "be marked in a conspicuous place as legibly, indelibly, and permanently as the nature of the article (or its container) will permit, in such a manner as to indicate to the ultimate purchaser in the United States the English name of the country of origin of the article."

On June 5, 1997, pursuant to the HKPA, the US Customs Service issued a notice that goods produced in Hong Kong should continue to be marked as Hong Kong-origin following the territory's handover to China on July 1, 1997.

Failure to mark an article in accordance with the Act and CBP marking rules (19 C.F.R. § 134) can result in the assessment of a duty of 10% *ad valorem*.

Tariffs and Duties

Notably, section 2(f) of EO 13936, and the CBP notice issued pursuant thereto, will not meaningfully impact the assessment of duties on products imported to the United States from Hong Kong. In guidance published by CBP following the August 11 notice, the agency clarified that the notice "does not affect country of origin determinations for purposes of assessing" ordinary or temporary duties under Chapter 1-97 and Chapter 99 of the Harmonized Tariff Schedule of the United States (HTSUS), respectively.[11] According to CBP, "goods that are products of Hong Kong should continue to report International Organization for Standardization (ISO) country code 'HK' as the country of origin when required." As a consequence, although goods exported from Hong Kong to the United States will be marked as originating in "China," their treatment for tariff purposes will be no different than prior to the change introduced by the August 11 notice. This includes with respect to tariffs imposed under Section 301 of the Trade Act of 1974 on goods from China.

Hong Kong's Response

On August 11, the Hong Kong government issued a statement responding directly to the notice issued by CBP, indicating the potential for response at the World Trade Organization. During the pendency of any such challenge, it is likely that the requirements imposed by CBP's notice would remain in effect.

11 https://www.cbp.gov/trade/rulings/frequently-asked-questions-guidance-marking-goods-hong-kong-executive-order-13936

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Immigration

by Elizabeth (Liz) Laskey LaRocca, Dana J. Delott

Prior to EO 13936, Hong Kong had important preferential treatment under US immigration law. EO 13936 directs federal agencies to take actions to eliminate distinctions between China and Hong Kong to the detriment of Hong Kong nationals.

For more information on these distinctions, read Steptoe's June 9 International Compliance Blog post, "Six Ways Hong Kong is Different from China Under US Immigration Laws."

Immigrant Visas

Immigrant visa numbers needed to obtain US permanent resident ("green card") status are limited annually and allocated based upon country of chargeability. With the loss of differentiation between China and Hong Kong, persons born in Hong Kong will face the same multi-year backlogs in immigrant visa availability typically experienced by mainland Chinese. This translates to significantly longer green card process time frames for Hong Kong nationals in many categories, including the EB-5 investor category.

EB-5 Investors

The EB-5 investor category is one of the most notable immigrant visa categories affected by EO 13936. This investment-based path to US permanent residence is used heavily by nationals of mainland China and Hong Kong. However, prior to EO 13936, Hong Kong was categorized separately from mainland China. As a result, Hong Kong nationals avoided the multi-year or decade-long backlogs applicable to China. Hong Kong will now be included within the Chinese quota and subject to extended backlogs. Unless this dissuades Hong Kong nationals from pursuing EB-5 visas, the addition of these applicants could worsen the existing China backlogs.

Visa Duration

Within visa categories, the duration and other terms of visas issued at US consulates are established by the State Department on a reciprocal basis. The validity duration, number of admissions (multiple or single entry) and fee structure is based upon treatment of US citizens by the foreign country. Under EO 13936, Hong Kong nationals—previously granted the maximum allowable visa validity periods-- will be limited to the generally more restrictive visa terms applicable to Chinese nationals.

Travel Suspensions

EO 13936 contains a security-related Hong Kong travel ban applicable to those who have been involved with implementing new national security laws imposed on Hong Kong. This is broadly worded to include those involved indirectly or who provided material assistance as well as certain family members of those subject to this ban.

Additionally, the COVID-19-related travel suspensions applicable to China, which specifically excluded Hong Kong, could be equalized.

Diversity Lottery

Eligibility to participate in the US Diversity Visa (DV) lottery program extends to countries with low US immigration rates. Hong Kong has historically qualified for the DV lottery; China has historically not qualified for the DV lottery. Under the EO, Hong Kong and China are treated identically and, thus, will not qualify for the DV lottery program.

Humanitarian Relief

The EO directs the reallocation of the refugee ceiling to residents of Hong Kong, "based upon humanitarian concerns," to the extent feasible and permitted by law.

Tourism

Since November 2016, Chinese nationals holding 10-year multiple entry visitors (B-1/B-2) visas have required a valid Electronic Visa Update System (EVUS) enrollment.[10] EVUS registration was not required for Hong Kong passport holders prior to EO 13936. The EO also suspends provisions relating to Hong Kong-specific eligibility for visa-free tourist travel to Guam and the Northern Mariana Islands.

Exchange Visitors

EO 13936 directs the termination of China and Hong Kong from eligibility to participate in the Fulbright exchange (J-1) program. This bears watching, as the J-1 program is important to academic and research institutions, as well as hospitals.

10 https://www.cbp.gov/faqs/what-electronic-visa-update-system-evus; https://www.steptoe.com/en/news-publications/chinese-business-and-tourist-travelers-must-enroll-in-visa-system-beginning-november-29.html.

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Conclusion

The US government's recent shift in policy toward the HKSAR is part of a broader effort to target actions by the PRC government perceived to threaten US national interests. While Hong Kong remains distinct from mainland China in many ways, there is a growing expectation in Hong Kong that the central government in Beijing could increase its oversight of certain activities in the HKSAR following the adoption of the Law of the People's Republic of China (PRC) on Safeguarding National Security in the HKSAR, in July 2020. Such changes could provoke new US responses.

With strong support in Congress for its recent actions, the White House is unlikely to reverse course on the HKSAR absent significant improvements in other areas of the US-China relationship. Companies doing business or investing in Hong Kong can therefore expect some or all of the changes under EO 13936 to be permanent.

For more information about how these changes impact your business, contact a member of Steptoe's Hong Kong team or its broader export controls, white-collar, immigration, and international trade teams.

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