Overview

On April 28, the US Department of Commerce’s Bureau of Industry and Security (BIS) published a new set of regulations tightening export controls on China, Russia, and Venezuela (the new rule). The new rule will take effect on June 29, and will apply to goods, software and technology subject to US export controls jurisdiction. The new rule will not be limited to US persons.

The most significant parts of this new rule will increase the licensing requirements and due diligence expectations that apply to trade with China, Russia, and Venezuela under the US Export Administration Regulations (EAR) when “military end users” or “military end uses” are involved. However, in light of the way these terms are defined, industry should note that the impact of this new rule will extend beyond the defense sector into many areas of commercial technology and trade with these countries.

Restriction on Items that "Support or Contribute to" Military Applications in China, Russia, or Venezuela

China’s defense sector has long been subject to a broad US arms embargo. In addition, since 2007, BIS has imposed a licensing requirement on trade with China when the exporter has knowledge or reason to know that the products are intended for a “military end use” in China. BIS subsequently extended that requirement to Russia and Venezuela. This licensing requirement applies (under Part 744 of the EAR) even when a license would not generally be required to export a particular type of product to these countries. However, this restriction has had a limited practical impact on trade with China because (1) it has been based on a narrow definition of “military end use,” and (2) it applies only to a limited number of products (in Supplement No. 2 to Part 744 of the EAR).

The new rule expands the scope of the licensing requirement by redefining “military end use” more broadly and by increasing the number of products now subject to the restriction. We anticipate that this expanded military end use restriction will have a significant impact on trade with China and associated export control compliance burdens in many areas of commercial technology, including the technology and telecommunications sectors. Below we discuss the two major changes made by the new rule.

Expanded Definition of "Military End Use"
First, the new rule expands the definition of "military end use," which will capture a greater scope of trade with China, Russia, and Venezuela within this licensing requirement. The pre-existing military end use restriction applied when covered items were exported to these countries for "incorporation into a military item...or for the 'use,' 'development,' or 'production' of military items..." (Military items include defense articles as described on the US Munitions List or the Wassenaar Arrangement Munitions List, along with items described under the EAR's "600 series" and "A018" classifications.) Under that pre-existing provision, the term "use" was defined as "operation, installation (including on-site installation), maintenance (checking), repair, overhaul and refurbishing" (emphasis added). The restriction only applied when the exported item was "for" all such applications relating to military items.

The new rule applies when the exported item "supports or contributes" to the operation, installation, maintenance, repair, overhaul, refurbishing, 'development,' or 'production,' of military items." (emphasis added). The use of the term "or" rather than "and" means that an exported item used in connection with any one of these applications may now trigger this licensing requirement.

As BIS stated, the new rule identifies "each element of the definition of 'use' so that any one of the six elements, standing alone, is sufficient." Moreover, the new rule applies to exports that merely "support or contribute to" such activity relating to military items. These terms are undefined, and the risk of proceeding with certain exports to China in particular without a license from BIS could be elevated in light of broad statements by US government officials regarding China's "civil-military fusion" efforts. Also, this restriction applies when an export may only "in part" "support or contribute to" such an end use. This new rule may call for expanded due diligence regarding potential end uses of exported products in China, and in some cases, may call for seeking other protections such as contractual safeguards around restricted end uses.

**Expanded List of Product Types**

Second, the new rule applies this military end use restriction to a longer list of product types (in Supplement No. 2 to Part 744 of the EAR). Specifically, it adds the following Export Control Classification Numbers (ECCNs) relating to materials processing, electronics, telecommunications, information security, sensors/lasers, and propulsion: ECCNs 2A290, 2A291, 2B999, 2D290, 3A991, 3A992, 3A999, 3B991, 3B992, 3C992, 3D991, 5B991, 5A992, 5D992, 6A991, 6A996, and 9B990, and an expanded range of items in ECCNs 3A992, 8A992, and 9A991. Some of these product categories are very broad.

For example, "mass market" hardware or software incorporating limited encryption functionality, which includes many types of basic electronics and consumer software applications, will now be covered by this new rule. In addition, telecommunications testing equipment, and many basic types of industrial and electronics production equipment and software will now be subject to this restriction.

When an exporting party determines that the expanded licensing requirement under this new rule applies, any application for a license will be subject to a "presumption of denial," such that applying for a license would generally be futile. Tellingly, BIS stated in this rulemaking that it has only received approximately two to three license applications per year under this provision of the EAR in the past, and "BIS believes that the reason for this small number is the likelihood that such applications will be denied." BIS stated that it does not expect any significant change in license applications, "due to continuing likelihood of denials."

**Related New Restriction on Exports to Certain Parties in China**

The new rule adds a licensing requirement for exports to "military end users" in China, in addition to the expanded licensing requirement applicable to "military end uses" in China discussed above. (A "military end user" licensing requirement has previously been in place for Russia and Venezuela.) This new military end user restriction for China applies to the same list of product types as under the military end use restriction (In Supplement No. 2 to Part 744 of the EAR). Also like the military end use provision, this end user restriction applies when the exporter has knowledge or reason to know that the products are intended "entirely or in part" for a military end user in China.

The relevant definition of "military end user" under the EAR includes "the national armed services (army, navy, marine, air force, or coast guard), as well as the national guard and national police, government intelligence or reconnaissance organizations, or any person or entity whose actions or functions are intended to support 'military end uses'" (emphasis added), as discussed in the preceding section. So, under this new rule, licenses will now be required when an exporter has reason to know that its products may be used, even "in part," by Chinese armed services, police, intelligence, and similar agencies. While that may include a significant amount of trade with China in light of the expanded list of covered product types, it is a reasonably well-defined regulatory obligation. The more troubling aspect may be in trying to understand or ascertain whether a customer or end-user in China may engage in "actions or functions [that] are intended to support" the broadly-defined set of activities discussed above that are now considered restricted "military end uses" in China.

Additional clarification on the scope of this new rule from BIS would be welcome. For example, it is unclear whether a customer in China whose unrelated activities support these broadly-defined "military end uses" in China, would be treated as a "military end user" for the purpose of all exports covered by this new rule.
BIS has so far provided scant guidance in its announcement of the new rule, stating that “This expansion will require increased diligence with respect to the evaluation of end users in China, particularly in view of China’s widespread civil-military integration.” Companies will need to make risk-based decisions in construing this new rule in light of its potentially broad scope.

**Broader AES Filing Requirement**

The new rule requires exporters to China, Russia and Venezuela to file Electronic Export Information (EEI) in the Automated Export System (AES) for all items on the EAR’s Commerce Control List (CCL) and to state the applicable ECCN in these filings, except for intangible exports and shipments eligible for License Exception Governments and International Organizations (GOV) in § 740.11 of the EAR.

For exports to China, Russia, and Venezuela, the new rule eliminates the previous provision that allowed exporters to forego AES filings when the value of a shipment was $2,500 or less and when a license was not required. For many companies that do not make specific EAR classification determinations for each product or sale, this new requirement could significantly increase their export compliance burden when exporting to China, Russia, or Venezuela, as these determinations will now be mandatory even when no license is required.

More broadly, this expanded requirement to submit AES filings will increase the risk of possible errors or misstatements, and will also provide increased visibility for the US government into trade with China, Russia, and Venezuela.

**Removal of License Exception CIV and Proposed Modification of License Exception APR**

Also effective on June 29, 2020, BIS is removing License Exception CIV. Thus, BIS will require a license for national security-controlled (NS) items on the CCL to countries of US national security concern, specifically those in EAR Country Group D:1, including China, Russia, Venezuela, and others. Currently, License Exception CIV authorizes exports or reexports of certain items (as specifically designated on the CCL) destined to civil end-users or for civil end-uses that would otherwise require a license from BIS for NS reasons.

BIS notes that its decision to remove License Exception CIV is based on, among other things, strategies implemented by these countries for the integration of civil and military industries. This integration strategy can make it difficult for a US exporter to determine if an NS item is being exported or reexported for a civil end use or a civil end user (or instead will be for a military end user or end use). In support of this decision, BIS also cited “US government enforcement actions identifying diversion of US-origin items to military end uses and military end users by purported civil end users in these countries.”

In addition, BIS is requesting comments on a proposed rule to revise License Exception APR by removing a provision that authorizes reexports from certain countries of certain NS-controlled items to countries in Country Group D:1, aligning it with the removal of License Exception CIV. Currently, License Exception APR authorizes reexports of certain items from a country in Country Group A:1 or Hong Kong to certain destinations (including Country Group D:1), provided that the reexport is consistent with an export authorization from the country of reexport, and that the item is not subject to other reasons for control under the EAR. BIS states that “even Wassenaar participating states in Country Group A:1 may have export authorization policies that do not align with the national security or foreign policy interests of the US government.” Comments must be received by BIS no later than June 29.

**Conclusion**

As we covered in a publication last year, the new rule appears to respond to a requirement enacted into law by Congress for BIS to review existing controls on “military end users” and “military end uses” in China and other countries subject to a US arms embargo by May 2019. Coming nearly a year after this statutory deadline, the new rule illustrates the complexity of crafting some of the broad new export controls on China that Congress has called for.

Other congressionally-mandated export controls on China that have not yet been issued include the new general rules relating to “foundational technologies,” along with the specific rules that BIS is planning to issue covering “emerging technologies.” In addition, there have been reports that BIS is working on a new set of rules expanding the jurisdiction of the EAR when it comes to certain types of exports to China, such as the “foreign direct product” rule (and potentially also the “de minimis” rule). Industry should remain on alert for these continuing developments.

 Practices
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