

China Releases Second Draft of Export Control Law for Public Comment

January 14, 2020

Trade Controls

On December 28, 2019, China released a second draft of the PRC Export Control Law (“Second Draft”), which contains significant revisions to the initial draft released in June 2017 (“First Draft”; see our summary [here](#)). The drafts build upon China’s existing export control regulations, which are scattered across multiple laws, administrative regulations, and implementation rules, with the goal of creating a unified export control system to promote China’s commitment to nonproliferation and national security interests. While the Second Draft retains key provisions of the First Draft, it revises the list of factors for regulators to consider in reviewing a license application, requires exporters to develop an internal compliance review system, imposes an obligation on exporters and importers to self-report both likely and actual changes to the end-user or end-use, and increases the potential penalties for violations.

Comments may be submitted before January 26, 2020.

Key Structure, Definitions, Licensing, and Agencies Retained from First Draft

Given that the Second Draft retains most of the structure and definitions of the First Draft, the underlying purpose of the proposed law remains the same: to establish a robust and cohesive export control system, similar to that of other countries, to replace the current patchwork of laws, regulations, implementation rules, and lists.

The Second Draft also retains the concept of deemed export, i.e., a Chinese citizen, legal representative, or entity providing a controlled item to a non-Chinese natural person, legal representative, or entity inside China. Similar to how the concept of deemed exports under U.S. law can affect information sharing among employees of different nationalities working in the United States or on U.S.-origin technologies, the PRC Export Control Law, if enacted as drafted, could affect information sharing among employees of different nationalities working in China or on Chinese-origin technologies.

The Second Draft also retains the key licensing framework in the First Draft, although with certain changes, as discussed below.

Key Changes from the First Draft

The Second Draft retains many of the core concepts and structure of the First Draft, but changes certain details, most notably how the regulators develop and operationalize the lists, and the obligations on exporters when applying for licensing.

Definitions and Jurisdiction

Definition of “Exporter” Added

The Second Draft adds a definition of “exporter” (also translated as “export operator,” 出口经营者), which is defined as “a citizen, legal representative, or other organization that is engaged in exporting controlled items in accordance with the rules of laws and administrative regulations.”

Definition of Re-Export Deleted

The First Draft included a rule on re-exporting “a controlled item or a foreign product that contains a certain percentage of value of China’s controlled items” from a country outside of China to a third country. The Second Draft deletes this provision, but adds the term “re-export” to the provision regulating other situations where export controls may apply, such as transshipments. The purpose of the change is unclear, but given the importance of re-exports in export controls, we may see this rule reintroduced in future drafts or in implementing regulations.

Retaliation Provision Deleted

The First Draft contained a provision that authorized China to take reciprocal measures against countries that impose “discriminatory export control measures on China.” The Second Draft deletes that provision. However, other laws and regulations, such as the PRC Foreign Trade Law, contain similar provisions that allow China to take retaliatory actions against foreign countries for laws perceived as discriminatory.

Provisions Related to Taiwan, Hong Kong, and Macau Deleted

The First Draft provided that the Export Control Law would apply to exports to Taiwan, Hong Kong, and Macau. The Second Draft deletes this provision.

“Development Interests” Removed

The First Draft stated that one of the purposes of the law was to “safeguard national security and development interests.” The Second Draft drops the term “development” to focus the law on China’s international obligations and national security concerns.¹

¹ Comments on the First Draft, particularly by non-Chinese companies and governments, had noted that the text of the First Draft could be read to support use of export control licensing as a means of industrial policy that would be inconsistent with China’s other international obligations.

Regulators, Lists, and Controls

Regulators

The First Draft provided that departments under the State Council and the Central Military Commission would be responsible for enforcing export control laws, but it did not specify which departments and how these agencies would perform their duties.

The Second Draft states that departments under the State Council and the Central Military Commission would be involved in regulating export control matters based on their portfolios, which likely will make the Ministry of Commerce and the General Administration of Customs as the main regulators for dual-use items, and the Central Military Commission responsible for military items. The Second Draft also adds that a mechanism shall be established for coordinating major export control matters, and that the local governments at the provincial level would be responsible for the day-to-day work related to export controls.

Lists and Controlled Items

The First Draft required regulators to develop two control lists: a list for dual-use items and a list for military items. The Second Draft adds that regulators will develop a third list for nuclear items.

The Second Draft is unclear whether controlled items would include only products, technologies, or services that are developed within China. It is therefore possible that products or technologies developed outside of China and then imported into China may be subject to export control requirements when (re)exported out of China.

The Second Draft also clarifies a catch-all provision: an exporter must still apply for an export license, even if the item is not included on a control list, if the exporter knows or should know that the export of a product, technology, or service likely would:

- affect China's national security;
- be used to design, develop, produce, or employ weapons of mass destruction and their means of delivery; or
- be used to develop nuclear, biological, or chemical weapons for the purpose of terrorism.

(The Second Draft adds that the regulator should respond "in a timely manner" to inquiries regarding whether an item is subject to control.)

Temporary Controlled Items

The First Draft allowed regulators to place temporary controls on unlisted items for up to two years. The Second Draft adds that such temporary designations must be justified by the "need to fulfill international obligations and to safeguard national security" and clarifies that the temporary control should not last more than two years.

Licensing and Obligations on Exporters

Factors to be Considered in License Applications Revised

The First Draft listed seven factors that regulators should consider when reviewing a license application. The Second Draft removes two factors (market availability and internal compliance systems of the exporter), revises a factor (removes “development interests” from “national security and development interests”), and adds three new factors (export type, export destination, and the exporter’s social credit record). The revised list of factors is:

1. international obligations and external commitments undertaken by China
2. national security (*removed “development interests”*)
3. export type (*new factor*)
4. degree of sensitivity of the item
5. export destination (*new factor*)
6. end-user and end-use
7. exporter’s social credit record² (*new factor*)
8. other circumstances prescribed by laws and regulations

Notably, the First Draft allowed regulators to issue different types of licenses such as general licenses and licenses for individual items, and license exceptions. The Second Draft deletes this language.³

Mandatory Internal Compliance Review System

The First Draft encouraged, but did not require, exporters to establish an internal compliance review system in order to be eligible for certain licensing. The Second Draft makes it mandatory for exporters to establish such a system. Further, exporters with “well-functioning” systems and

² China’s social credit system (“SCS”) establishes a system by which the Chinese government collects information and rates companies across a wide range of areas (e.g., tax, environment) and then can reward or sanction companies based on that information and rating. Notably, SCS functions as an information-sharing system among government agencies, which means that non-compliance in one area, such as bribery and corruption, will be more quickly reported, publicized, and shared with other government agencies, and, in many cases, with the public. For more on SCS, see [here](#).

³ In the First Draft, national security was listed first and international obligations was listed second in the list of factors to be considered when reviewing a license application; the Second Draft switches the order of these two factors, placing international obligations first. Similar changes are also seen in the purpose of the law (placing international obligations before national security and interests) and the scope of the law (adding items that are related to fulfilling China’s international obligations to the scope). Somewhat contrary to these changes, the Second Draft deletes the provision that required export control rules for fulfilling China’s international obligations and external commitments to take precedence, as well as deleting and the provision that exempted military aid from the scope of the law.

no significant violations may be eligible for unspecified “licensing convenience,” which potentially a streamlined licensing procedure.

The Second Draft does not, however, specify how regulators should evaluate an internal compliance review system and what would constitute a significant violation. We anticipate that the regulators may release additional guidance in more detailed implementation rules.

End-User and End-Use Certifications

The First Draft allowed regulators to request exporters or importers to provide end-user and end-use certifications, depending upon the items to be exported and the sensitivity. The Second Draft obliges the end user (or the government of the end user) to provide the certification, and for exporters to proactively supply such documents to the regulators, presumably as part of the application process.

Reporting Obligation

The First Draft required exporters to report identified changes to an end-user or end-use *after* the item had been exported. The Second Draft changes the obligation to require reporting immediately after exporters discover that the end-user or end-use “may have a possibility of changing.” The Second Draft imposes this same obligation on importers as well as exporters. However, the Second Draft does not specify the consequences for failing to self-report or the procedure for self-reporting. We anticipate that subsequent implementing regulations may contain these details.

Investigation and Penalties

Investigative Powers

The Second Draft retains most of the earlier powers to investigate potential violations, including the power to enter business premises, review and copy documents, seize assets, and review bank account activity. The Second Draft removes regulators’ power to freeze exporters’ bank accounts during an investigation and limits collectible electronic data to those that could be used to authenticate that transactions occurred.

More Severe Penalties

The Second Draft substantially revises and increases penalties for violations, such as heavier fines and adding the potential penalty of suspending/revoking an exporter’s business license for “serious” violations, although Second Draft does not specify what would constitute a “serious” violation.

Certain penalties are deleted in the Second Draft:

- Penalties for individuals responsible for export control violations
- Penalties for circumventing export controls
- Penalties for providing untrue materials in a license application

The revised penalties are summarized in the chart below.

Violation	Penalty
Exporting in violation of specialty business qualification (“专营资格”; applicable to military items)	<ul style="list-style-type: none"> • Confiscation of illegal gain • Where illegal revenue is RMB 500,000 (about USD 70,000) or above, a fine of no less than five times, but no more than ten times, of the illegal revenue • Where illegal revenue is below RMB 500,000 (about USD 70,000), a fine between RMB 500,000 (about USD 70,000) and 5,000,000 (about USD 700,000)
Exporting without a license	<ul style="list-style-type: none"> • Confiscation of illegal gain • Where illegal revenue is RMB 500,000 (about USD 70,000) or above, a fine of no less than five times, but no more than ten times, of the illegal revenue
Exporting outside the scope of a license	<ul style="list-style-type: none"> • Where illegal revenue is below RMB 500,000 (about USD 70,000), a fine between RMB 500,000 (about USD 70,000) and 5,000,000 (about USD 700,000) • Where the violation is “serious,” an additional order to suspend business and ultimately revocation of the exporting business license
Exporting items that are prohibited from being exported	<ul style="list-style-type: none"> • Revocation of license • Confiscation of illegal gain • Where illegal revenue is RMB 200,000 (about USD 30,000) or above, a fine of no less than five times, but no more than ten times, of the illegal revenue • Where illegal revenue is below RMB 200,000 (about USD 30,000), a fine between RMB 200,000 (about USD 30,000) and 2,000,000 (about USD 300,000)
Obtaining an export license via fraud, bribery, or other improper means	<ul style="list-style-type: none"> • Confiscation of illegal gain • Where illegal revenue is RMB 50,000 (about USD 7,000) or above, a fine of no less than five times, but no more than ten times, of the illegal revenue • Where illegal revenue is below RMB 50,000 (about USD 7,000), a fine between RMB 50,000 (about USD 7,000) and 500,000 (about USD 70,000)
Falsifying or buying/selling an export license	<ul style="list-style-type: none"> • Confiscation of illegal gain • Where illegal revenue is RMB 100,000 (about USD 15,000) or above, a fine of no less than three times, but no more than five times, of the illegal revenue • Where illegal revenue is below RMB 100,000 (about USD 15,000), a fine between RMB 100,000 (about USD 15,000) and 500,000 (about USD 70,000)
Facilitation of another’s violation	<ul style="list-style-type: none"> • Confiscation of illegal gain • Where illegal revenue is RMB 500,000 (about USD 70,000) or above, a fine of no less than ten times, but no more than 20 times, of the illegal revenue
Conducting business with controlled end-users in violation of the Export Control Law	<ul style="list-style-type: none"> • Confiscation of illegal gain • Where illegal revenue is RMB 500,000 (about USD 70,000) or above, a fine of no less than ten times, but no more than 20 times, of the illegal revenue

Violation	Penalty
	<ul style="list-style-type: none"> Where illegal revenue is below RMB 500,000 (about USD 70,000), a fine between RMB 500,000 (about USD 70,000) and 5,000,000 (about USD 700,000) Where the violation is “serious,” an additional order to suspend business and ultimately revocation of the exporting business license
Obstruction of government inspection/investigation	<ul style="list-style-type: none"> A fine between RMB 100,000 (about USD 15,000) and 300,000 (about USD 45,000) Where the violation is “serious,” an additional order to suspend business and ultimately revocation of the exporting business license

The Second Draft also makes additional changes to the penalty provisions:

- The Second Draft deletes a laundry list of situations in which an exporter could receive reduced penalties.
- The provision on facilitation removes “abetting” and “conspiring” as violations.
- The First Draft provided that an exporter could be prohibited from obtaining export licenses for a period of three years for export control violations. The Second Draft extends the ban to five years and adds that the exporter’s responsible individuals could also be banned from engaging in an export business for five years; the ban could be permanent if the responsible individuals were criminally penalized for export control violations.

Conclusion

The Second Draft does not clarify whether the Export Control Law will replace the existing patchwork of regulations, although we assume that those regulations will continue in force until implementing regulations and the different elements of the new export control regime are established.

Along with the recently enacted Encryption Law (see our summary [here](#)) and other laws such as the Cybersecurity Law, National Security Law, and Counterterrorism Law, the drafts of the Export Control Law evidence China’s efforts to roll out a more robust legislative framework to support its national security priorities. The changes in the Second Draft likely represent efforts among the various stakeholders in the Chinese bureaucratic system to align interests and priorities.

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