

# BIS Tightens Export Controls to Counter Integration of Civil and Military Technology Development in China, Russia, and Venezuela

April 29, 2020

International Trade Controls

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On April 28, 2020, the U.S. Department of Commerce’s Bureau of Industry and Security (“BIS”) published two final rules and one proposed rule to modify certain license exceptions and definitions in the Export Administration Regulations (“EAR”) (15 CFR Parts 730 – 774), based on concern that sensitive products and technologies were being diverted to military uses or to further military technology development in countries of concern.

Specifically, BIS issued a [final rule](#) that significantly expands the restrictions on exports, reexports, and in-country transfers of certain items subject to the EAR for “military end use” and “military end users” in China, Russia, and Venezuela. BIS also issued a [final rule](#) removing License Exception Civil End-Users (“CIV”) and issued a [proposed rule](#) that would narrow License Exception Additional Permissive Reexports (“APR”).

These changes respond, in part, to the mandate in the 2018 Export Control Reform Act (“ECRA”) for BIS to review the EAR with respect to exports, reexports, and transfers to countries subject to U.S. arms embargoes, including China. The Administration continues to develop additional rules relating to the Chinese company Huawei, including a rule expanding the application of the EAR to certain advanced semiconductors made abroad and a rule regarding the ability of U.S. companies to participate in international standards development activities where Huawei is a member. However, proposals to change the EAR’s “*de minimis*” rules with respect to Huawei apparently are not proceeding.

## **New Restrictions on Military End Uses and Military End Users**

BIS amended Section 744.21 of the EAR to expand the licensing requirement for exports, reexports, and transfers (in-country) of items intended for certain military end uses and military end users in a number of significant ways. The new rule will take effect on June 29, 2020.

## **Background**

Since 2007, BIS has imposed a license requirement on exports, reexports, and transfers (in-country) of any item that is (a) subject to the EAR and (b) controlled pursuant to an Export Control Classification Number (“ECCN”) listed in Supplement No. 2 to EAR Part 744, if the exporter, reexporter, or transferor had “knowledge” (including both “positive knowledge” and “awareness of a high probability”) that the item was intended, entirely or in part, for a military

end use in China. Licenses were reviewed on a case-by-case basis to determine if such transactions would make a material contribution to Chinese military capabilities, and would result in advancing China's military interests contrary to the national security interests of the United States; if so, the license application would be denied.

"Military end use" was defined to include (a) incorporation into a military item described on the U.S. Munitions List ("USML") of the International Traffic in Arms Regulations (22 CFR Part 121) or the Wassenaar Arrangement Munitions List ("Wassenaar List"); (b) incorporation into items classified under ECCNs ending in "A018" or under "600 series" ECCNs; or (c) for the "use," "development," or "production" of military items described on the USML or the Wassenaar List, or items classified under ECCNs ending in "A018" or under "600 series" ECCNs.

Subsequently, in 2014, BIS extended the license requirements on exports, reexports, and transfers (in-country) of certain items to military end uses in Russia and Venezuela. At the same time, BIS broadened the restrictions imposed on Russia and Venezuela compared to the earlier China restrictions by prohibiting unauthorized exports, reexports, and transfers of listed items to "military end users." Military end users were defined as "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'". However, BIS did not extend the same license requirements to military end users in China.

### Revisions

As noted above, the 2018 ECRA mandated a review of EAR license requirements for exports, reexports, and transfers to countries subject to a comprehensive U.S. arms embargo, such as China. The mandated review included the scope of controls related to military end uses and military end users in such countries, as well as items on the Commerce Control List ("CCL") that are not subject to a license requirement for such countries.

With this final rule, BIS has adopted a single approach under Part 744 with respect to China, Russia, and Venezuela. The new rule extends the license requirement for exports, reexports, and transfers of items listed in Supplement No. 2 to Part 744 to *military end users* in China, regardless of whether the item is for a military end use. The term "military end users" is defined to include not only core military organizations such as the army, navy, marine, air force, or coast guard, as well as the national guard and national police, government intelligence, or reconnaissance organizations, but also any person or entity whose actions or functions are intended to support "military end uses." BIS stated in the Federal Register notice 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. In particular, given the potential involvement of many Chinese entities in the "support" of "military end uses," depending on the interpretation of this term, it is possible that a large number of Chinese entities will be considered as "military end users." Any export, reexport, or transfer of an item listed under Part 744, Supplement No. 2 (discussed below) to such entities would require a specific BIS license, regardless of whether the item itself is for a military end-use.

The potential impact of this final rule is further magnified by the fact that it broadens the definition of "military end use." As noted above, previously, items for "military end use" covered

items that were “for the ‘use,’ ‘development,’<sup>1</sup> or ‘production’<sup>2</sup> of military items described on the USML or the Wassenaar List, or items classified under ECCNs ending in “A018” or under “600 series” ECCNs.” As elsewhere in the EAR, “use” under this Part was limited to items for all six of the following functions: operation, installation, maintenance, repair, overhaul, *and* refurbishing. Once the new rule takes effect, any item that *supports or contributes* to the operation, installation, maintenance, repair, overhaul, refurbishing, development, or production of military items will be considered to have a military end use.

### Scope of Restrictions

The final rule also significantly broadens the scope of the items subject to license requirements in EAR Section 744.21. As discussed above, the license requirements of Section 744.21 apply to items listed in Supplement No. 2 to Part 744. The new rule adds 17 ECCNs to Supplement No. 2 to Part 744 and expands the range of items listed under three other ECCNs. Importantly, the rule adds, among other things, materials processing equipment controlled under ECCN 2B999; electronic devices, components, and general purpose electronic equipment controlled under ECCNs 3A991 and 3A992 (e.g. semiconductors); semiconductor manufacturing, inspection, and test equipment controlled under ECCNs 3B991 and 3B992; certain positive resists designed for semiconductor lithography controlled under ECCN 3C992; software controlled under ECCN 3D991, which includes software specially designed for the development, production, or use of certain electronic devices, parts, or components, general purpose electronic equipment, and manufacturing and test equipment; telecommunications test equipment controlled under ECCN 5B991; information security hardware and software controlled under ECCNs 5A992 and 5D992; optical sensors controlled under ECCN 6A992; avionics items controlled under ECCNs 7A994 through 7E994; and aircraft parts and components controlled under ECCN 9A991.

### Licensing Presumption of Denial

In contrast to the case-by-case review under the existing rule, the new rule states that BIS will review license applications with a presumption of denial.

### Restrictions on Exports, Reexports, and Transfers of Other Sensitive Items

The rule also includes some clarifying amendments to the general prohibition contained in EAR Section 744.21. Currently, paragraph (a)(2) of Section 744.21 prohibits unauthorized exports, reexports, or transfers of any 9x515 or “600 series” item, including items described in a .y paragraph of a 9x515 or “600 series” ECCN, to Russia or Venezuela. To streamline the

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<sup>1</sup> “Development” is defined in EAR Section 722.1 and refers to all stages prior to serial production, such as: design, design research, design analyses, design concepts, assembly and testing of prototypes, pilot production schemes, design data, process of transforming design data into a product, configuration design, integration design, and layouts.

<sup>2</sup> “Production” is defined in EAR Section 722.1 to mean all production stages, such as: product engineering, manufacture, integration, assembly (mounting), inspection, testing, and quality assurance.

regulations, the rule moves the existing restriction from Section 744.21 to the license requirements sections of the relevant ECCNs on the CCL.

BIS also declared that the controls on “600 series” .y and 9x515.y items are being imposed for “regional stability” reasons, and has added a description of these controls to a new Section 742.6(b)(8) of the EAR. In addition, the rule clarifies that the prohibition on unauthorized exports, reexports, and transfers of “600 series” .y and 9x515.y items also applies to items destined for China.

#### Expansion of Electronic Export Information Filing Requirements

Finally, this rule expands Electronic Export Information (“EEI”) filing requirements in the Automated Export System for exports to China, Russia, or Venezuela. Existing provisions exempt exporters from both filing EEI for many shipments valued under \$2,500 (unless an export license is required) and from entering the ECCN in the EEI when the reason for control is only anti-terrorism (AT). Under the new rule, the EAR will require filing EEI for items destined to China, Russia, or Venezuela regardless of the value of the shipment, unless the shipment is eligible for License Exception GOV. In addition, even if no license is required to ship an item to those destinations, the EEI filing must include the ECCN, regardless of the reason for control.

#### **License Exception CIV**

BIS issued a [final rule](#) to remove License Exception CIV from the EAR. A license exception is an authorization allowing the export, reexport, or transfer (in-country), under stated conditions, of items subject to the EAR that would otherwise require prior specific licensing.

Currently, License Exception CIV (EAR Section 740.5) authorizes exports, reexports, and transfers (in-country) of certain national security-controlled items, without prior review by BIS, to most civil end users for civil end uses in Country Group D:1,<sup>3</sup> except North Korea, provided the exporter does not “know” that the item would be or was intended to be exported, reexported, or transferred (in-country) in connection with missile proliferation; proliferation of chemical, biological, or nuclear weapons; or other military, intelligence, or law enforcement uses or applications. The removal of License Exception CIV will take effect on June 29, 2020.

BIS stated in the final rule that after reviewing export data from current License Exception CIV users, publicly available statements of economic development strategies of Group D:1 countries, and U.S. government enforcement actions, it has found evidence that Group D:1 countries are engaging in strategies to increase integration of civilian and military technology development. The Trump Administration has repeatedly expressed concern about civil-military fusion in China, and we understand that BIS’s concern regarding License Exception CIV related principally to China. Consequently, BIS decided to remove License Exception CIV so that in the future, transactions involving the national security-controlled items currently permitted under

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<sup>3</sup> Currently, Country Group D:1 includes Armenia, Azerbaijan, Belarus, Cambodia, China, Georgia, Iraq, Kazakhstan, North Korea, Kyrgyzstan, Laos, Libya, Macau, Moldova, Mongolia, Russia, Tajikistan, Turkmenistan, Ukraine, Uzbekistan, Venezuela, Vietnam, and Yemen.

License Exception CIV will be reviewed by the U.S. government through license applications prior to export, reexport, or transfer (in-country).

License Exception CIV has been a useful tool for some companies to engage in deemed exports of certain technology to foreign persons working in the United States. One potentially significant consequence of the new rule is that the deemed exports that were previously authorized by License Exception CIV will now require prior specific export licensing from BIS, unless another license exception applies.

### **License Exception APR**

BIS issued a [proposed rule](#), on which it is accepting public comments, on regulatory changes to limit the scope of License Exception APR, found in EAR Section 740.16.

Currently, paragraph (a) of License Exception APR authorizes the reexport of certain items from a country in Country Group A:1<sup>4</sup> or Hong Kong to destinations in Country Group D:1 other than North Korea, provided that the reexport is consistent with an export authorization from the country of reexport, and that the item is not subject to control for reasons described in EAR Section 740.16(a)(2), which includes missile technology and nuclear nonproliferation controls. Based on discussions with partner governments and U.S. companies, BIS stated that it has evidence of differences in licensing review standards for national-security controlled items destined to Country Group D:1, so that countries in Country Group A:1 or Hong Kong may be approving licenses for the reexport of a U.S.-origin item that would have been denied if the item had been exported directly from the United States. While BIS did not reference China expressly in the proposed rule, China is by far the largest economy in Country Group D:1 and poses significant national security concerns for the United States; and we understand that BIS's concerns, as with License Exception CIV, related principally to reexports to China.

To address these concerns, BIS is proposing to remove countries in Country Group D:1 from the category of eligible destinations for national security-controlled items under paragraph (a) of License Exception APR.

Notably, since License Exception APR relates to reexports, BIS does not currently require reports or other filings relating to items reexported or transferred under License Exception APR. Therefore, BIS issued this as a proposed rule, and is requesting comments on how the proposed change would impact persons who currently use or plan to use License Exception APR. Specifically, BIS is seeking information as to the volume of transactions affected by this proposed change; how the proposed change would affect the amount of time necessary to complete such transactions in the future; and how the proposed change would otherwise affect current business. Comments must be received by BIS no later than June 29, 2020.

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<sup>4</sup> Country Group A:1 includes Argentina, Australia, Austria, Belgium, Bulgaria, Canada, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, India, Ireland, Italy, Japan, South Korea, Latvia, Lithuania, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Romania, Slovakia, Slovenia, South Africa, Spain, Sweden, Switzerland, Turkey, United Kingdom, and the United States.

Covington's International Trade Controls practice is well-positioned to advise on the export controls issues related to these latest actions, and more broadly on the compliance dimensions of doing business internationally.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our International Trade Controls practice:

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