

Client Alert

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What to Watch: Draft Export Control Law of China

The Ministry of Commerce ("**MOFCOM**") of the People's Republic of China ("**China**") published the draft Export Control Law ("**ECL**") for public comments via a circular on 16 June 2017. If enacted, the ECL will be the first set of comprehensive and unified export control legislation in China, which is aimed at upgrading the country's existing regime consisting of various administrative regulations and rules. The ECL is still in the draft form and no further update has been announced since its publication last year, but it is widely expected to be introduced in the National People's Congress within 2018.

1. Controlled Items, Blacklists and Embargoes

The draft ECL sets forth four categories of controlled items ("**Control Lists**"), including dual-use items which may be used for civilian and military purposes, military items, nuclear items, as well as other goods, technologies, services and items that are related to national security. Items outside the Control Lists could also be temporarily controlled for up to two years, subject to the approval of the State Council, the Central Military Commission and their designated authorities ("**Competent Authorities**"). In addition, activities subject to ECL control need not involve items on the Control Lists as long as the exporter knows or should know that the export may give rise to national security and terrorism concerns.

The Competent Authorities may also maintain blacklists of foreign importers and end-users that breach the ECL, and may prohibit the export of controlled items to such persons

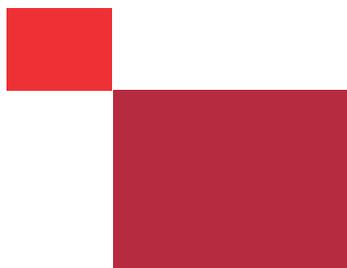
Furthermore, the draft ECL provides that if China is subject to any discriminatory export control measures by any country, the State may adopt retaliatory measures against such country. The State may also put in place any necessary controls over the export of any goods, technologies and services in order to safeguard security and interests during wartime or urgent situations concerning international relations.

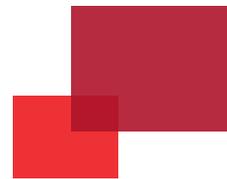
If the draft ECL is passed in its current form, companies must be prepared to regularly monitor dynamic updates to the scope of controlled items, countries and persons in order to ensure full compliance with the law.

2. Controlled Activities and Licensing

The draft ECL introduces the concepts of deemed export and re-export in China, which will bring China's system many steps closer to the export control regimes in western countries. Deemed exports include the provision of controlled items by a citizen, legal person or other organization in China to any foreign person; the item need not be physically exported from China. Re-export controls cover the export of controlled items (i.e. items comprising a prescribed amount of content controlled by China) from one overseas jurisdiction to another.

It remains unclear whether or precisely how China will implement provisions controlling deemed export and re-export transactions. Given their potentially extra-territorial reach, there may be practical challenges in enforcing such requirements. Furthermore, if ultimately adopted, the deemed export provisions may significantly impact multinational corporations with a presence





in China or with access to Chinese controlled items and technology outside of China. In view of the breadth of the draft legislation, even the sharing of information related to controlled items between colleagues (one of whom is employed by a Chinese subsidiary) may be included within the scope of the ECL's control regardless of whether there is actual cross-border transfer.

The ECL requires licences (categorized into General Licences and Individual Licences) to be obtained from the Competent Authorities for carrying out controlled activities. Additionally, exporters may also be subject to recordkeeping and monopoly qualification requirements.

3. End-Use Requirements

The Competent Authorities may request the exporters to submit end-use certificates or documents issued by the importers or the relevant agencies in the countries of import. The exporters are also under a positive obligation to review the end-users and uses of the exported items, and to immediately report to the Competent Authorities of any change in end-users or uses. Further, the importers shall undertake not to alter the ultimate uses of the imported items, or transfer the imported items to any third parties other than the end-users, without the approval of the Competent Authorities. In this regard, the Competent Authorities are empowered under the ECL to conduct on-site verifications on the end-users and end uses.

4. Enforcement and Penalties

The draft ECL grants Competent Authorities broad investigative powers. They may, for example, enter the business premises of parties under investigation, conduct interviews with relevant parties, access and copy relevant documents, examine the conveyance used for export, seize items and even freeze bank account of the export operators.

The draft ECL prescribes the following key penalties:

- Export without a Permit – The operator may receive a warning from the Competent Authorities, as well as administrative penalty of not more than 10 times the illegal business revenues and confiscation of any illegal gains derived from such activity. Persons directly in charge and other persons directly held liable (not expressly defined, but may include employees or agents of the exporter) may also be given a warning and fined up to CNY 300,000.
- Fraudulent Acquisition or Trading of a Permit – In addition to the above penalties, the Competent Authorities may withdraw the licence of any party that obtains it by fraud, bribery or other illegal means, or falsifies, alters, leases, lends, or trades a licence for the export of controlled items.

5. Implications

The ECL is still in the draft form and it remains to be seen how the legislative provisions will be enforced, whether any exemptions will be introduced, and if there will be any meaningful updates to the draft before it is introduced to the National People's Congress. Given the potentially wide-sweeping impact, multinationals that may be affected are well advised to start early to understand the implications of the new law on their compliance obligations, supply chains, and business operations.

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