

INTERNATIONAL BUSINESS ALERT

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BIS further tightens export control on China and other countries

A lot of changes are happening in the export control area lately. Since April 28, 2020, the U.S. Department of Commerce Bureau of Industry and Security (BIS) has made at least five announcements altering export control policy. This article will explain these changes in detail, but the complexity of these new export control rules will certainly generate interpretive questions and compliance challenges for anyone in the export businesses. We will continue to monitor export control developments and analyze the implications of such challenges for our client community.

BIS expands its military use license requirement

On April 28, 2020, the BIS published the [Expansion of Export, Reexport, and Transfer \(in-Country\) Controls for Military End Use or Military End Users in the People's Republic of China, Russia, or Venezuela Final Rule](#), effective June 29, 2020. Notwithstanding the "Final Rule" designation, on June 3, 2020, the BIS further published the [Expansion of Export, Reexport, and Transfer \(in-Country\) Controls for Military End Use or Military End Users in the People's Republic of China, Russia, or Venezuela \(corrected\)](#) (Military Use Final Rule), effective June 29, 2020, correcting a portion of the Export Control Classification Numbers (ECCNs) on the CCL, but with no change to the Military Use Final Rule published on April 28, 2020.

The goal of the Military Use Final Rule is "broadening the United States government's visibility into and ability to deny or condition exports, re-exports, and transfers (in-country) involving certain items on the CCL (Supplement No. 1 to part 774 of the EAR) that are destined to military end users or end uses in China, Russia, or Venezuela."

Specifically, this rule does the following:

1. Expands the licensing requirements under Section 744.21 of the

EAR (15 CFR parts 730–774) for China to include “military end users” and “military end use” and adds additional items to the list of items subject to the military end-use and end-user license requirements in Supplement No. 2 to part 744

2. Adopts a license review policy of presumption of denial
3. Further expands the definition of “military end use.”

While the EAR’s current definition of military end use refers both to direct use (for parts, components or subsystems of weapons and other defense articles) and indirect use (weapon design and development, testing, repair and maintenance), this Military Use Final Rule broadens the definition of military end use beyond any item for the “use,” “development,” or “production” to include any item that supports or contributes to the operation, installation, maintenance, repair, overhaul, refurbishment, “development,” or “production” of military items. This expansion will require increased diligence with respect to the evaluation of end users in China.

The rule also creates a new reason for control and the associated review policy for regional stability for certain items exported to China, Russia, or Venezuela, modifying existing text related to this policy. It also adds Electronic Export Information (EEI) filing requirements in the Automated Export System for exports to China, Russia, and Venezuela. The current rule exempts exporters from both filing EEI for many shipments valued under \$2,500 (unless an export license is required), and from entering the Export Control Classification Numbers (ECCN) in the EEI when the reason for control is only anti-terrorism. However, with the Military Use Final Rule, all items destined to China and/or Russia must complete an EEI filing, regardless of the value of the shipment. In addition, even if no license is required to ship an item to those destinations, the EEI filing must include the correct ECCN regardless of reason for control.

BIS eliminates the license exception for civil end users

On April 28, 2020, the BIS published the [Elimination of License Exception Civil End Users \(CIV\) Final Rule](#) (CIV Final Rule), effective June 29, 2020. In it, the BIS amended the EAR by removing CIV § 740.5 and requiring a license for national security to export controlled items on the CCL for certain civil end users for civil end use in countries listed in Country Group D:1 (countries of national security concern). To conform with this CIV Final Rule, the BIS also removed the CIV paragraph from the List-Based License Exceptions section wherever it appears in the ECCN on the CCL. ([Supp. No. 1 to part 774](#)). The BIS states that it is the policy of the BIS to approve license applications on a case-by-case basis provided that the items are for civilian use or would otherwise not make a significant contribution to the military potential of any countries of national security concern listed in Country Group D:1. To date, those countries include 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.

BIS amends its foreign-produced direct product rule

On May 15, 2020, the BIS announced in a [press release](#) that it plans to further restrict Huawei's ability to use U.S. technology and software to design and manufacture its semiconductors abroad by amending its longstanding foreign-produced direct product rule and the Entity List. On May 19, 2020, the BIS issued an interim final rule and request for comment for the [Export Administration Regulations: Amendments to General Prohibition Three \(Foreign-Produced Direct Product Rule\) and the Entity List](#) (Foreign-Produced Direct Product Final Rule", effective May 15, 2020. This new rule imposes a new control over certain foreign-produced items, when there is knowledge that such items are destined to a designated entity on the Entity List. A foreign-produced item is subject to the new control if the entity for which the item is destined has a footnote 1 designation in the Entity List.

What is the Entity List?

Pursuant to Parts 744 and 746 of the EAR, the BIS has the authority to place entities on the Entity List that are reasonably believed to be involved, or to pose a significant risk of being or becoming involved, in activities contrary to U.S. national security or foreign policy interests. Entities placed on the Entity List are generally prohibited from receiving some or all items subject to the EAR unless an export license is obtained, with some exceptions, as specifically described in the notice that the BIS publishes in the Federal Register relating to the addition of the entity to the list. While this Foreign-Produced Direct Product Final Rule can apply to any of the companies, so far only Huawei Technologies Co., Ltd. (Huawei) and its affiliates (such as HiSilicon) have been listed in footnote 1, so there are beliefs in the industry that this amendment is specially created and targeted for Huawei.

Background for Huawei being added to the Entity List

On May 16, 2019, the BIS posted a [proposed rule](#), adding Huawei Technologies Co. Ltd. and 68 non-U.S. affiliates located in 26 destinations (all identified by company name and location) to the Entity List. In its notice relating to this determination, the BIS stated that Huawei and the 68 affiliates would generally be subject to a license requirement for the export, re-export or transfer of all items "subject to the EAR." Importantly, most goods, software and technology located in or originating from the United States are considered subject to the EAR (as that term is defined under the EAR), and certain items outside of the United States may also be subject to the EAR if they incorporate more than de minimis controlled U.S.-origin content or are produced as the "direct product" of certain controlled U.S.-origin technology. The notice further explained that license applications will be reviewed under a presumption of denial, and that no license exceptions set forth under the EAR could be used for the export, re-export or transfers of items subject to the EAR to Huawei or the 68 affiliates. Subsequently, on

August 19, 2019, the BIS added additional 46 non-U.S. affiliates of Huawei to the Entity List. On May 19, 2020, Huawei and its affiliates have been added as a footnote 1 designation in the Entity List.

What is the Foreign-Produced Direct Product Rule?

The Foreign-Produced Direct Product Rule is set forth in the EAR's General Prohibition Three. This rule prohibited the re-export and export from abroad of certain foreign-produced direct products of U.S. technology and software to certain countries considered to pose risks to U.S. national security and countries that were found to support terrorist activities. In general, a foreign-made item is defined as a "direct product of U.S. technology" when it is the "direct product of technology or software that requires a written assurance as a supporting document for" authorization from the BIS (such as through licenses or license exceptions) and when it was subject to national security controls on the CCL. This prohibition also applied to a limited set of foreign-made items that were the direct product of a complete plant or any major component of a plant.

New amendment to the Foreign-Produced Direct Product Rule

Under the current Foreign-Produced Direct Product Rule, a foreign-made product would be considered a "direct product" of U.S. technology only when it was based on certain U.S.-origin technology that was subject to the control of the CCL for national security reasons. The Foreign-Produced Direct Product Final Rule amends the EAR's General Prohibition Three Foreign-Produced Direct Product Rule to include two sets of items as "direct product" of U.S. technology. The first set of products includes "[i]tems, such as semiconductor designs, when produced by Huawei and its affiliates on the Entity List . . . that are the direct product of certain . . . CCL . . . software and technology." The second set of products includes "[i]tems, such as chipsets, when produced from the design specifications of Huawei or an affiliate on the Entity List . . . that are the direct product of certain CCL semiconductor manufacturing equipment located outside the United States." Among the "direct products" thus restricted are the foreign direct products of U.S. technology or software classified under ECCN 3E001, 3E002, 3E003, 4E001, 5E001, 3D001, 4D001, 5D001, 3E991, 4E992, 4E993, 5E991, 3D991, 4D993, 4D994 and 5D991.

Going forward, companies that ship or transfer foreign-made commodities, software or technology outside the United States with "knowledge" that they are destined to any of the designated Huawei entities will need to determine whether the items: (1) were "produced or developed" by any of the designated Huawei entities; and (2) are the "direct product" of software or technology subject to the EAR that is described in ECCN 3E001, 3E002, 3E003, 4E001, 5E001, 3D001, 4D001, 5D001, 3E991, 4E992, 4E993, 5E991, 3D991, 4D993, 4D994 and 5D991.

The Foreign-Produced Direct Product Final Rule took effect on May 15, 2020, immediately upon publication of the interim final rule. However, the BIS is providing companies impacted with a limited grace period

and exempts companies with license requirements within 120 days from the effective date of the final rule, until September 14, 2020, in order to “prevent immediate adverse economic impacts on foreign foundries utilizing U.S. semiconductor manufacturing equipment that have initiated any production step” for these two sets of items.

The BIS is requesting comments on the impact of this rule. Comments must be submitted on or before July 14, 2020. Impacted companies and industry organizations are encouraged to submit comments through the Federal Rulemaking Portal: [regulations.gov](https://www.regulations.gov) (docket number BIS 2020-0011 or RIN 0694-AH99) prior to the deadline.

BIS adds additional entities to the Entity List

On May 22, 2020, the BIS issued the press release that [Commerce Department to Add Two Dozen Chinese Companies with Ties to WMD and Military Activities to the Entity List](#), announcing that it will add 24 Chinese entities to the Entity List, for engaging in activities contrary to the national security or foreign policy interests of the United States. On the same day, the BIS issued the press release [Commerce Department to Add Nine Chinese Entities Related to Human Rights Abuses in the Xinjiang Uighur Autonomous Region to the Entity List](#), stating that it will add nine Chinese entities to the Entity List, for alleged complicity in human rights abuse in the Xinjiang Uighur Autonomous Region. The EAR imposes additional license requirements on, and limits the availability of most license exceptions for, exports, re-exports, and transfers (in-country) to listed entities.

On June 5, 2020, the BIS published the Final Rule [Addition of Entities to the Entity List, Revision of Certain Entries on the Entity List](#) [Docket No. 200407-0100], formally amending the rule to add 24 entities that have been determined by the U.S. Government to be acting contrary to the national security or foreign policy interests of the United States, effective June 5, 2020. The entities are located under the destination of the People’s Republic of China (China), Hong Kong and the United Kingdom (U.K.). This rule also modifies three existing entries on the Entity List under the destination of China. Also on June 5, 2020, the BIS published the Final Rule Addition of Entities to the Entity List, and Revision of Entry on the Entity List [Docket No. 200407-0099], adding nine entities to the Entity List for alleged complicity in human rights abuse in the Xinjiang Uighur Autonomous Region. This rule also modifies two entries and revises one entry on the Entity List under the destination of China.

Take away

These changes signal the BIS’s increasing efforts to tighten the U.S. export control to China and other countries that the U.S. considers to be a threat to its national security. These actions will have significant implications for U.S. and non-U.S. companies that have business relationships with Huawei and many of its affiliates, identified entities on the Entity List, companies which previously relied upon the CIV license exemption, and other



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companies that export, re-export, and transfer items intended for military end use or military end users. Companies in the export business should be aware of the changes and their implications, and vigorously examine their own export compliance program to ensure compliance.

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