

28.10.2020

## FOREIGN TRADE LAW

### THE NEW CHINESE EXPORT CONTROL LAW

The Standing Committee of the National People's Congress has recently codified China's export control law for the first time in a single piece of legislation with effect as of 1 December 2020 and significantly expanded its scope. With new, far-reaching powers of control and threats of fines, the reforms will have a significant impact on export business, regardless of whether companies have a subsidiary or branch in China.

#### Summary

- › Companies with and without subsidiaries or branches in China will be subject to comprehensive Chinese export control policies in the future. The new Export Control Law ("ECL") is broad in scope and, in particular, extraterritorial in reach.
- › Chinese export control policies now extend to all goods that could endanger China's national security and national interests.
- › Exporters and other parties involved in the export business face heavy fines for violating the provisions of the ECL.
- › Companies should take a critical look at the compliance measures for their Chinese business and adjust them if necessary.

#### China's previous export control legislation

Until now, Chinese export control policies have been regulated in numerous laws, executive orders and explanatory regulations. Export operations were, among other things, subject to foreign trade law, customs law and criminal law. The export control regulations focused mainly on standard military goods. In recent years, however, trade in sensitive goods has been increasingly restricted and controlled. With the ECL, China is now codifying the existing regulatory regime for the export of military and dual-use items, thereby significantly extending its scope and the State's powers of control. The aim of the ECL is to safeguard national interests and security, prevent proliferation of weapons of mass destruction, regulate export business and enhance export control (Article 1 ECL). The ECL will enter into force on 1 December 2020.

The extraterritorial scope of the ECL and the restrictions on re-exports are reminiscent of US export control law. Even though the law has not yet been implemented as such, companies doing business with China should take steps now to review their compliance strategies in light of the new requirements.

#### Key points of the new ECL

- › Export control under the ECL will continue to be managed centrally by the departments of the State Council and Central Military Commission, which were already responsible for export control (the competent authorities are collectively referred to as the State Export Control Administrative Departments, "SECADs"). In terms of the actual implementation, China has however kept the existing decentralised control system run by the provinces. At the same time, new mechanisms and agencies should ensure a better exchange of information and expertise and establish new opportunities for cooperation (Article 5 ECL).
- › The *material* scope of the ECL is broadly defined. Application of the new Export Control Law is not restricted

- › to the control of military, dual-use and nuclear goods, but instead also covers all “*other goods, technologies and services relating to the maintenance of national security and national interests, performance of anti-proliferation and other international obligations*” (Article 2 ECL). Re-exports of controlled items are also covered by the material scope of the ECL.  
However, given the broad definition of controlled items, the exact scope of the control is unclear. This will likely only become clearer through the implementing regulations, the control and item lists and the practical application of the ECL by the SECADs.
- › The same applies to the *territorial* scope of the ECL: Companies with registered office in and outside China will have to comply with the new regulations. As such, the ECL is extraterritorial in reach.
  - › Article 2 ECL states that export control not only covers the export of controlled items out of China but also the transfer of controlled items by citizens, legal persons or non-corporate organisations based in China to foreign organisations and individuals. This means that even the transfer of sensitive technologies or data by subsidiaries based in China to subsidiaries and branches outside China may be regarded as an export within the meaning of the ECL.
  - › Pursuant to Article 45, the ECL also applies to the “*transit, transshipment, through shipment and re-export of controlled items as well as to the export of controlled items from bonded areas, export processing zones and other areas [...]*”.
- › An export licence is required for the export of controlled items. It is not only the goods specified in the general lists of controlled items or goods that are subject to temporary control for which such a licence must be obtained. Exporters must also apply for a licence if they *are or should be aware* that an (unlisted) item for export poses a risk to China’s national interests or national security, is used for the development and production of weapons of mass destruction or serves terrorist purposes. This means that the mere negligent failure to recognise a security risk or a potential violation of Chinese interests already exposes a company to the risk of sanctions. A large number of criteria is used to assess whether an export licence will be granted. In addition to the sensitivity of the items, the destination country and the intended end use, the past reliability of the exporter also plays a role. The decision not to grant a licence may also be based on a violation of national interests or the endangering of national security.
- › Exporters are obliged to submit documentation to the SECADs regarding the intended end use of the controlled items as well as the end users. End users may not deviate from the intended end use, and any such deviation must be reported to the SECADs. The latter will place any end users that have violated the requirements or that may endanger the national interests or national security of China or use the controlled items for terrorist purposes on a “blacklist” of untrustworthy companies. Exporters are prohibited from entering into any transactions with companies on the list, with violations being subject to fines.
- › The new ECL lays down far-reaching official powers to investigate and intervene in order to implement the export control provisions. These include searching business premises and questioning the employees of all the companies involved in the export transaction, accessing bank accounts, seizing the goods intended for export, inspecting transport vehicles and examining and copying all business records relevant for the investigation. In addition, all other persons and companies connected to the transaction may also be interviewed and their business records scrutinised. German and European end customers may also be affected by this.
- › Violations of the ECL’s provisions are punishable by heavy fines. Should an obligation to apply for an export licence be violated, the authorities have the power – insofar as the export has resulted in income of RMB 500,000 (approx. EUR 63,000) or more – to confiscate this income and impose a fine of between five and ten times the turnover. If the violation results in income of less than RMB 500,000, a fine of between RMB 500,000 and RMB 5 million (approx. EUR 630,000) is to be imposed. In the case of serious violations, a company may be ordered to temporarily suspend business, may be given a negative entry in China’s social credit system or may even be generally barred from exporting goods. Natural persons directly responsible for violations may be generally prohibited from engaging in any activities relating to export operations. Criminal penalties may moreover apply as well if a violation of the provisions of the ECL also constitutes a criminal offence, e.g. smuggling, illegal business operations or the disclosure of state secrets.
- › Article 48 ECL is also potentially significant given the current geopolitical and economic tensions between China and the US: This provides that retaliatory measures may be taken by China if export control provisions are abused or its national security is endangered by other countries.

## Implications and consequences

The new Chinese Export Control Law has a much broader scope than the previous legislation. The use of vague legal terms such as “national interests and national security”, in particular, gives the authorities a broad margin of discretion. Ultimately, time will tell to what extent the authorities will make use of their powers of control and intervention when applying the rules in practice. Guidelines in the form of detailed implementing regulations and explanations from the SECADs and the decentralised export control authorities have been announced and are generally to be welcomed. Nevertheless, the expanded export control powers increase the risk of sanctions. Companies face heavy fines or even being de facto barred from the export business for simply violating the rules through negligence. Because of the extraterritorial scope, the new regulations have an equal impact on companies with and without a subsidiary or branch in China. Companies that do business with China would therefore be well advised to carry out a careful risk assessment of their supply chains and commercial channels at this stage already, and to bring these in line with the new requirements if necessary.

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