

U.S. Government Sanctions Chinese and Russian Entities and Creates New Military End User List

by Lawrence Ward, Dave Townsend, and T. Augustine Lo

Rounding out an already-intense 2020, the U.S. Department of Commerce's Bureau of Industry and Security ("BIS") issued three notices in December that expanded export sanctions and restrictions against Chinese, Russian, and other enterprises and institutions accused of engaging in activities contrary to U.S. interests. On December 18, BIS announced export sanctions against Semiconductor Manufacturing International Corporation ("SMIC"), the largest semiconductor producer in the People's Republic of China ("PRC"), along with 76 other entities, the vast majority of which are PRC enterprises and research institutes. On December 23, BIS created a new Military End User ("MEU") List that designates specific PRC and Russian entities for more stringent export licensing requirements under the MEU rule expanded by BIS earlier in the year. Finally, also on December 23, BIS officially terminated Hong Kong's status as a jurisdiction separate from the PRC under the U.S. Export Administration Regulations ("EAR"), meaning that U.S. exports to Hong Kong will now be treated as if they are exports to the PRC itself.

Addition of SMIC and Other PRC Companies to BIS Entity List

BIS's addition of SMIC and other PRC enterprises and institutions to the "Entity List" caps a year of intensified export control sanctions against major PRC entities because of their alleged participation in "military-civil fusion," a PRC national strategy to migrate civilian and commercial technology innovations as rapidly as possible to serve the PRC's military forces and its growing defense industrial sector. The U.S. Government is concerned that PRC civilian entities are compelled under this strategy to participate in the country's military modernization programs to benefit different branches of the People's Liberation Army ("PLA"). Following similar sanctions against other PRC electronics producers, the Entity List sanction against SMIC prohibits the transfer to SMIC of any commodity, software or technology that is subject to the EAR unless authorized by BIS. However, as detailed below, on closer examination, the BIS sanctions against SMIC were not quite as broad as some had previously expected.

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This latest BIS action was part of the outgoing Trump Administration's broader efforts to slow the growth of PRC "national champions" competing globally to supply high-end telecommunications and digital products while bolstering the PLA's modernization. In 2019, BIS had added Huawei Technologies Co., Ltd., a major producer of smartphones and other telecommunications devices, and a large number of its affiliates to the Entity List because of their alleged violations of various U.S. economic sanctions and export control laws. Huawei's Entity List sanction imposed an export license requirement on the transfer of items that are subject to the EAR. In May 2020, BIS expanded that Huawei export sanction to cover items made abroad using certain U.S.-origin software and technology.

Underscoring BIS's intent to target more advanced technologies, the BIS move against Huawei subjects only items capable of supporting 5G wireless technology to a stringent "presumption of denial" of export licenses, while BIS applies a more lenient "case-by-case" review of export licenses for items that are only capable of supporting 4G or older mobile communications technology. Because of these BIS sanctions, it has become increasingly difficult for Huawei to obtain much-needed U.S. origin items for the continued development and production of its latest and most sophisticated smartphones and other kinds of telecommunications equipment.

In its December action, BIS expanded the Entity List to include SMIC, the largest PRC producer of semiconductors, and ten of its affiliates, including one in Hong Kong. This Entity List designation means that anything supplied to SMIC that is "subject to the EAR," whether from a U.S. or non-U.S. company, will now require a BIS export license. Notably, because SMIC supplies Huawei and other leading PRC electronics companies with many key microelectronics components for their products, by restricting exports and transfers of EAR-regulated items to SMIC, BIS will also likely further hobble the product development and manufacturing by Huawei and other major PRC high tech producers who rely upon SMIC semiconductors.

BIS's Entity List designation for SMIC also again targets items that would advance the development of cutting-edge technology. The Entity List treatment for SMIC and its affiliates only creates a presumption of BIS denial of export licenses for the supply of items that are "uniquely required to produce semiconductors at advanced technology nodes 10 nanometers or below." That explicit criterion allows SMIC to continue importing U.S.-origin technology to support the design and production of semiconductors above that critical 10 nanometer floor. Moreover, SMIC may already possess and use a good deal of the targeted design or manufacturing technology for sub-10 nanometer semiconductors, thus attenuating the Entity List sanction's potential impact.¹

At the same time, BIS also added 66 other companies and institutions to the Entity List, the vast majority of which are other PRC entities. It is significant that these other entities were listed for a diverse range of U.S. foreign policy concerns. For example, BIS included four PRC high-tech firms engaged in the production of items contributing to the PRC's alleged violations of human rights through electronic surveillance of its population, particularly in Xinjiang, and BIS also listed China Communications Construction

Company, Ltd. (“CCCC”) and several other firms that have been involved in the construction of military outposts and assertion of PRC’s maritime claims in the South China Sea.

Notably, these Entity List designations include not only large PRC enterprises but also state-affiliated academic institutions that allegedly contribute to the PLA’s modernization through the military-civil fusion strategy. In particular, BIS added a large number of research institutes affiliated with China State Shipbuilding Corporation, Ltd. (“CSSC”), which is deeply involved in the PLA Navy’s research and development programs. BIS added Beijing Institute of Technology, Nanjing University of Science and Technology, and Nanjing University of Aeronautics and Astronautics because of their alleged efforts in procuring U.S.-origin items to benefit the PLA. BIS also named Tianjin University and several persons associated with that institution because of their alleged involvement in economic espionage and trade secrets theft to obtain military and civilian dual-use items to benefit the PLA. The full list of BIS’s recently sanctioned entities is [here](#).

MEU List

BIS has created for the first time a “MEU List” containing 102 entities from the PRC and Russia. The creation of the MEU List is in furtherance of a major EAR Part 744 revision earlier in 2020 to prevent certain items subject to the EAR from going to military end users and military end uses in the PRC, Russia, and Venezuela.

BIS has long restricted the export of certain items to the PRC and Russia, and more recently BIS also added restrictions for exports to Venezuela if those items were for a military end use or to MEUs. In April 2020, BIS expanded its existing MEU rule in EAR Part 744 to cover MEUs in China, in addition to MEUs in Russia and Venezuela. In addition, the expanded MEU rule covers not only obvious military, national police, and intelligence agencies in the PRC, Russia, and Venezuela, but also non-government entities in those countries that could use certain sensitive items to support the “operation, installation, maintenance, repair, overhaul, refurbishing, development, or production” of military items. Exports of certain items on the Commerce Control List (“CCL”) to any entity subject to this expanded MEU rule would require a BIS license.

However, in April 2020, BIS did not name any specific PRC, Russian, or Venezuelan MEUs in its expansion of the MEU rule, forcing a rather open-ended and ambiguous degree of due diligence upon U.S. exporters to determine for themselves who should be covered by the revised MEU rule. Under the MEU rule announced in April, BIS considers any Chinese, Russian, or Venezuelan company to be an MEU if it produces any defense articles. The obvious difficulty is that a U.S. company often does not know if a nominally civilian PRC, Russian or Venezuelan buyer could use an exported U.S.-origin item in a defense article or to support military uses when that buyer is not self-evidently part of any defense or security agency. In spite of that difficulty, BIS insisted that U.S. exporters should bear the responsibility to conduct due diligence to ensure that EAR-controlled items do not end up with MEUs or go into restricted military end uses.

BIS’s latest action on December 23 now provides a certain measure of clarity with

respect to some PRC and Russian companies and institutes that BIS has declared meet the BIS definition of an MEU. In creating the MEU List, BIS noted that it had received over 80 requests for clarification since the MEU rule expansion in April, including requests to confirm whether 34 different entities are or are not subject to the MEU rule. While the creation of a MEU List does not eliminate a U.S. exporter's compliance burden under the MEU rule because the list is non-exhaustive, it does at least remove any ambiguity or uncertainty with respect to all the named entities on the MEU List.

At this time, the MEU List contains 57 PRC entities and 45 Russian entities. BIS may well add more entities to this list, potentially including Venezuelan entities as well. The entities appearing on this initial version of the MEU List are deemed to be MEUs, whether as direct military end users or as persons who engage in activities that support military end uses in the PRC or Russia. All entities on the MEU List are subject to a BIS export license requirement for the items subject to the MEU rule, which includes a variety of commodities, software, and technology on the EAR CCL, and export license applications are reviewed with a stringent presumption of denial. The current MEU List is available [here](#).

Hong Kong Loses Status Separate from PRC under EAR

BIS also acted on December 23 to eliminate Hong Kong's status as an export territory separate from the PRC for purposes of the EAR. In doing so, BIS implemented Executive Order 13936 ("EO 13936") that the President had issued in July 2020. Citing Hong Kong's perceived loss of autonomy to the PRC, EO 13936 requires U.S. Government agencies to terminate Hong Kong's preferential treatment under U.S. law as a jurisdiction that is distinct from the PRC.

Even before the issuance of EO 13936, BIS had already stated its intent to revoke EAR license exceptions for certain exports to Hong Kong. Citing Hong Kong's loss of autonomy, that BIS policy ensured that any exported item bound for Hong Kong and subject to an export license requirement if it were exported to the PRC would be subject to that same PRC licensing requirement. That policy change was only limited to the elimination of EAR license exceptions for Hong Kong, and so that had left in place a number of other EAR provisions that were more lenient towards Hong Kong and, indeed, had allowed certain exports to Hong Kong at the same level as to a number of U.S. allies.

With the latest BIS rule shift announced in December, Hong Kong's parity with the PRC now extends to the entirety of the EAR. All items that are subject to the EAR bound for Hong Kong are now subject to the same degree of restriction as to the PRC. As a result of this latest change, items to Hong Kong are now subject to significantly more stringent controls, including the MEU rules summarized above. For example, Hong Kong's Government Flying Service, which performs maritime search and rescue and police functions, has now been named and included on that MEU List, which was apparently due to its recent role in arresting a number of pro-democracy activists who had been seeking to flee Hong Kong by sea to carry on their protest against the new National Security Law put into effect at the insistence of the PRC government.

Ongoing Developments

Finally, although EO 13936, expansion of the Entity List and creation of the MEU List were all products of the Trump Administration, there has been relatively strong bipartisan support in Congress for a firmer U.S. posture toward the PRC. The incoming Biden Administration will therefore likely reflect that stern consensus in its own foreign policy and national security strategy vis-à-vis the PRC, and so it probably will not reverse EO 13936 or these other EAR-based sanctions, at least in the near term. Indeed, with the Democrats' new control of the U.S. Senate after the two recent run-off elections in Georgia, there could be even more legislation driven by human rights and democracy issues in regard to the PRC and Hong Kong and forcing yet harsher measures.

Accordingly, within the current EAR regulatory framework, BIS could well designate more PRC or Hong Kong entities under the MEU List or Entity List. Such further U.S. export control restrictions would then place more compliance burdens on American companies seeking to sell their goods and services to customers in the PRC or Hong Kong or to support and expand their own company operations in the PRC or Hong Kong. In turn, potential PRC customers (including many state-owned enterprises) will then likely be more reluctant to select and rely on U.S.-origin inputs for their own products and services as they worry about possible instability in their own supply chains in light of these U.S. actions taken against other PRC companies such as Huawei and SMIC.

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¹ www.bloomberg.com/news/articles/2020-12-22/how-chinese-chip-giant-smic-can-evade-trump-s-newest-crackdown.