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## Exports to China Must Comply with New Commerce Department Licensing Rules

On June 19, 2007, the Department of Commerce's Bureau of Industry and Security (BIS) published in the Federal Register a final rule revising its export controls for the People's Republic of China. The new rule updates U.S. licensing policy for dual-use exports to China by removing license requirements for exports to trusted customers while imposing new restrictions on a targeted list of items that could enhance China's military capabilities. The new rule:

- establishes a validated end-user (VEU) program to permit the transfer of certain items without a license to qualified end-users in China;
- imposes new licensing requirements for certain items destined for "military end-use";
- adopts a presumption against the export of certain items that would make a "direct and significant contribution" to China's military capabilities; and
- requires end-user statements from the Chinese government for export transactions.

The rule became effective upon publication, but items en route to a port of export that would become subject to license requirements under the new rules retain their previous eligibility if they are exported before July 19, 2007.

### Validated End-User Authorization

The rule establishes a VEU program, which allows U.S. exporters and reexporters to transfer eligible items to approved end-users without a license. Either a Chinese company or U.S. exporter, or non-U.S. reexporter on behalf of its Chinese customer, may file a request for

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VEU status. Among other things, the request must include:

- a description of the entity's ownership structure, business activities and relationship with government or military organizations;
- a list of the items to be transferred and their intended end-uses;
- a description of the entity's record-keeping system and how it will ensure compliance with the VEU requirements; and
- a certification that the entity:
  - understands that use or diversion of the items it receives under VEU authority contrary to the Export Administration Regulations is prohibited;
  - understands and will abide by all VEU end-use restrictions, including the requirement that items received under VEU authority will be used only for civil end-uses;
  - will comply with VEU record-keeping requirements; and
  - agrees to allow on-site compliance reviews by U.S. government officials.

Requests will be submitted to a new End-User Review Committee (ERC) made up of representatives from the Departments of State, Defense, Energy, Commerce and other agencies as appropriate. The ERC will make determinations by unanimous consent no later than 30 days after the VEU candidate's complete application is circulated to all ERC agencies. The ERC will consider a range of factors in evaluating VEU requests, including:

- the entity's record of exclusive civil end-use activities;
- its compliance with U.S. export controls;
- its ability to comply with the VEU requirements;
- its agreement to continuing on-site reviews;
- its relationship with U.S. and foreign companies; and
- the need for an on-site review by U.S. government officials prior to approval.

Denial of a request for VEU status will not preclude future grant of such status, and the export or reexport of dual-use items to that entity

will require a traditional license under the existing scheme.

BIS will publish the list of VEUs and associated eligible items in Supplement No. 7 to Part 748. Prior to an export of eligible items to a VEU, exporters and reexporters must obtain certifications from the VEU regarding end-use and compliance with the VEU requirements. In addition, exporters must submit annual reports to BIS identifying each VEU to which eligible items were transferred and the quantity and value of such items.

### **Items Destined for Military End-Use**

The new rule identifies 20 products and associated technologies described in 31 full or partial Export Control Classification Numbers (ECCNs) for which licenses are now required for export or reexport if they are intended for military end-use in China. These items include items such as aircraft and aircraft engines, underwater systems, lasers, depleted uranium, certain composite materials, airborne communications systems and inertial navigation systems, and certain highly specialized telecommunications equipment useful for electronic warfare, space communications or air defense.

For purposes of the rule, “military end-use” means incorporation into:

- items on the U.S. Munitions List (USML);
- items on the International Munitions List (IML);
- items listed under ECCNs ending in “A018” on the Commerce Control List (CCL); or
- items for the use, development or production of items described on the USML, the IML or items listed under ECCNs ending in “A018” on the CCL.

“Military end-use” also means deployment of items classified under ECCN 9A991 as set forth in Supplement No. 2 to Part 744.

Under the rule, applications to export military end-use items will be reviewed on a case-by-case basis to determine whether the export, reexport or transfer would make a “material contribution to the military capabilities of [China] and would result in advancing the country’s military activities contrary to the national security interests of the United States.”

### **Presumption against Export of Items That Would Make “Direct and Significant Contribution” to China’s Military Capabilities**

The final rule adopted by BIS incorporates a presumption against the export of items controlled for reasons of national security, biological

and chemical weapon proliferation, nuclear nonproliferation and missile technology if those items would make a “direct and significant contribution” to China’s military capabilities. Thus, license applications for such items generally will be denied. Items controlled for national security reasons include major weapons systems such as certain tanks, armored combat vehicles, artillery systems, combat aircraft and warships; missiles, missile launchers, rocket systems and man-portable air-defense systems; unmanned aerial vehicles; offensive space weapons; command support systems; precision guided munitions; and night-vision equipment.

### **Chinese Government End-User Statements**

BIS increased the dollar value threshold for licensed exports that require an end-use statement from China’s Ministry of Commerce (“MOFCOM”). Companies applying for a license to export, reexport or transfer items to China are now required to obtain an end-use statement from MOFCOM for any transaction that exceeds \$50,000 in value. For certain cameras, an end-user statement is required if the transaction value is greater than \$5,000. In addition, an end-user statement must be obtained to export certain high-performance computers regardless of transaction value. BIS believes that the increased transaction value will offset the expansion of items requiring a license so that there will be no incremental administrative burden for U.S. exporters.

### **Conclusion**

The new China export control rule presents both challenges and opportunities. It will likely take some time to understand the operation and impact of the new military end-use restrictions, and exporters and reexporters may need to expand their due diligence efforts to confirm that no military end-use exists for newly covered items. At the same time, exporters, reexporters and Chinese end-users may be able to take advantage of the new VEU program to eliminate licensing requirements. Although VEU candidates must adopt record-keeping and other procedures compliant with U.S. requirements and agree to on-site audits by U.S. government personnel, eliminating the need for individual licenses for covered items may outweigh the procedural burdens.

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*If you have any questions concerning the information discussed in this Alert or any other international trade or export control topic, please contact one of the attorneys listed below or your primary contact with the firm who can direct you to the right person. We would be delighted to work with you.*

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