Update on PRC Restrictions on Technology Export: High-tech may be restricted from being exported from China

By Xun Yang | Vera Zhao

China has a long-standing technology import and export control system. Under the Technology Import and Export Regulation (the "**Regulation**") effective in 2002, technologies which fall within a "restricted catalogue" ("**Restricted Technologies**") must seek an approval before contracts for exporting those technologies can be executed and technologies which fall within a "prohibited catalogue" ("**Prohibited Technologies**") must not be exported. The Ministry of Commerce and the Ministry of Science and Technology published the first *Catalogue of Technologies Prohibited or Restricted from Export* (the "**Catalogue**") in 2001, which was later amended in 2008.

The issuance of the Catalogue during the last a couple of decades triggers very little attentions because, at the time of issuance, these Restricted and Prohibited Technologies are not very advanced in the world or they are too "special" to have a worldwide usage (such as techniques related to herbal medicine). However, the issuance of the second amendment to the Catalogue (the "**Second Amendment**") on 28 Aug 2020 attracted huge attentions. Does the Second Amendment suggest that China is closing down the door for the export of high technology?

1. Historical Review of Catalogue and Second Amendment

Under the PRC technology export regime, generally speaking, there are three types of technologies which are either prohibited or restricted from being export: (1) military technologies; (2) dual use technologies; and (3) Restricted and Prohibited Technologies. The export of military technologies and dual use technologies are restricted or prohibited primarily to implement UN conventions regarding non-proliferation of massive-destruction weapons and the

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national legislations of the same nature. The restrictions to and prohibitions on the export of Restricted and Prohibited Technologies are largely to protection national interest.

When the Regulation and the first Catalogue were issued in 2001, for a period of more than 10 years thereafter, China was primarily a technology importer. China government had very little concerns over technology export. Even when the Catalogue was amended in 2008, neither domestic companies nor foreign players had many concerns. However, China has been undergoing a fast development in its technology during the last a few years so that the Catalogue becomes obsolete. Moreover, with the increasingly intensified economic relationship between China and the western world, export of technology which may have an impact on national interest has become an issue.

The Second Amendment was issued when US forced the sale of Tiktok's US business. As a result, many people believe that the Second Amendment was released in response to it. The timing which is selected to release the Second Amendment is, of course, not a coincident. However, the legislative intend for the Second Amendment is far beyond the Tiktok case. Rather, the Second Amendment is a necessary consequence of China's technological development and of its lack of trust in the western world.

Generally speaking, the Second Amendment removed some obsolete technologies and add some technologies in which China has leading positions or which otherwise have a national security concerns. In particular,

- 4 items are removed from Prohibited Technologies List, including microbial fertilizer technology(微生物肥料技术), chemical synthetic and semisynthetic caffeine production technology(化学合成及半合成咖啡因生产技术), VB2 production technology(核黄素(VB2)生产工艺) , and chemical synthetic and semi-synthetic medicine production technology (two-step fermentation production of Vitamin C intermediate 2-keto-l-colonic acid) (化学合成及半合成药物生产技术：维生素 C 中间体 2－酮基－L－古龙酸二步发酵制备技术);
- 5 items are removed from Restricted Technologies List, including Newcastle disease vaccination technology(新城疫疫苗技术), chemical synthetic and semi-synthetic medicine production technology (preparation of rifapentine, preparation of rifampicin, etc.) (化学合成及半合成药物生产技术：利福喷丁制备工艺、利福定制备工艺等), natural medicines production technology (天然药物生产技术), preparation and processing technology of functional polymer materials with biological activity(带生物活性的功能性高分子材料制备和加工技术), and cybersecurity firewall software technology(信息安全防火墙软件技术);
- 23 items are added to the Restricted Technologies List, including genetic engineering (genes and vectors)(基因工程(基因及载体)), 3D printing technology (3D 打印技术), design and construction technology of large high speed wind tunnel(大型高速风洞设计建设技术), strategic new product design technology for heavy machinery industry(重型机械行业战略性新产品设计技术), UAV technology(无人机技术)， laser technology(激光技术), encryption technology (密码安全技术), etc;
- The control points and technical parameters of 21 items are revised. Customized information push

service technology based on data analysis (基于数据分析的个性化信息推送服务技术) is included as a control point of information processing technology under the Restricted Technologies List.

In these technical areas, China companies have comprehensive cooperation with foreign parties, with extensive technological collaborations and exchanges. How does the Regulation and the Second Amendment affect the business?

2. Overview of Technology Export Administrative Regime in PRC

2.1 Scope of Technology Export

According to Article 2 of the Regulation, technology export refers to transfer of technology from the territory of PRC to overseas via trade, investment or economic and technical cooperation. Aforesaid technology transfer includes patent assignment, transfer of patent application rights, patent licensing, transfer of tech secrets, technical services and other forms of technology transfer. In other words, the scope of technology export defined under the Regulation not only includes transfer of ownership of intellectual properties, but also includes licensing of intellectual properties, release of technical secrets, and transfer of technologies in other forms to overseas.

2.2 Administrative Procedures for Export Restrictions

The export of Restricted Technologies is subject to a licensing requirement. The exporter must seek a letter of intent for technology export before the substantive negotiation process of an export contract.[1] After an export contract is executed, the exporter must apply for a license for technology export.[2]

According to Article 33 of the Regulation and the *Measures on Work Relating to Transfer of Intellectual Property to Overseas Parties (Trial Implementation)* (the "**Measures**") effective in March 2018, the foreign economic and trade administration will examine the technology subject to an export after receiving the application for technology export license, jointly with other departments below, to decide whether a license will be issued:

(1) where export involves transfer of intellectual property such as patent right, exclusive rights to integrated circuit layout design etc. to overseas parties, IP administration should review the transfer;
(2) where export involves transfer of computer software copyright, science and technology administrative should review the transfer;
(3) where export involves transfer of plant variety rights, agricultural administration and forestry administration should review the transfer.

1 *Regulation of the PRC on the Administration of the Import and Export of Technology,* Article 33, 34
2 *Regulation of the PRC on the Administration of the Import and Export of Technology,* Article 14

2.3 Consequence of Violation

According to Article 44 of the Regulation, export of Prohibited Technologies or export of Restricted Technologies without a license will be subject the exporter to administrative warnings, confiscations of illegal incomes, administrative fines ranging from one to five times the amount of illegal incomes, or even revocation of the foreign trade permits. In series cases, a violation of technology export control may constitute criminal offences, including crime of smuggling, crime of illegal business operations, and crime of divulging State secrets, depending on the detailed circumstances.[3]

3. Implications and development trend

3.1 Geographic Applications

Currently, the technology export controls under the Regulation only applies to cross-border exports but not "deemed export."

Different from the counterpart in the US, the Regulation applies only to the transfers of technologies from the territory of PRC to overseas. Technology transfers within PRC between companies having beneficiary owners in different countries are not governed under the Regulation. For example, foreign-invested companies incorporated in the PRC are allowed to receive Restricted Technologies from Chinese companies without licenses. However, the transfers of these Restricted Technologies to their overseas affiliates are subject to export controls under the Regulations. This gives flexibilities for foreign-invested companies to enter into technological collaborations with Chinese domestic companies as far as these technologies are retained in the hand of the foreign-invested companies. However, foreign investors are not allowed to share the technologies with their subsidiaries; or otherwise, the subsidiaries will be in a violative situation.

3.2 Expansion into a Foreign Direct Investment Regime

Technology export controls are expanding to apply to a wider circumstance, not only in a technology trading scenario but also a foreign-investment context. According to Section 3.2 of the Measure, during a national security review for foreign acquisition of domestic business, if a transfer of intellectual property is involved, the transfer will be reviewed as part of the national security. This section suggests that technology transfers are not only controlled in trading deals but also in equity transactions.

3.3 The Trend: Draft Export Control Law

With the increasing "protective" economic environment in the world, China is contemplating the legislation of a comprehensive Export Control Law. The Standing Committee of the National

3 *Regulation of the PRC on the Administration of the Import and Export of Technology,* Article 44

People's Congress released a draft *Export Control Law* in December 2019, and the second draft was released in July 2020, where the scope of export control is no longer limited to transfer of goods and technologies from the territory of the PRC to overseas, it also includes transfer from a PRC citizen, entity, or organization to a foreign organization or individual at any location.[4]

It remains unclear if foreign-invested companies in PRC constitute "foreign organizations" under the draft *Export Control Law*. If this is the case, once this *Export Control Law* comes into effect, foreign-invested companies will not be allowed to acquire Prohibited Technologies from PRC companies no matter if the technologies are transferred within the PRC or to overseas, and a license will be required for foreign-invested companies to acquire Restricted Technologies from PRC companies.

This draft *Export Control Law* also includes restrictions on end users and on subsequent transfers of exported technologies. In other words, the China government is drawing on the experience of the US in reforming its technology export system and requires that the exporter contractually restrict the end users and subsequent transfers. As a result, foreign companies and foreign-invested companies will likely be required to make commitments to restricting the end users of products using Chinese technologies and to restrict subsequent transfers of Chinese technologies. They may also face the requirements to disclose downstream commercial arrangements where Chinese technologies are involved, which may have a trade secret protection concern.

[4] *Export Control Law (2nd Draft for Public Comments)* ,Article 2

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