TRADE WITH CHINA: CURRENT REGULATIONS AND TOOLS FOR MANAGING TRADE AND PREDICTING THE FUTURE

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ACC Association of Corporate Counsel
NATIONAL CAPITAL REGION

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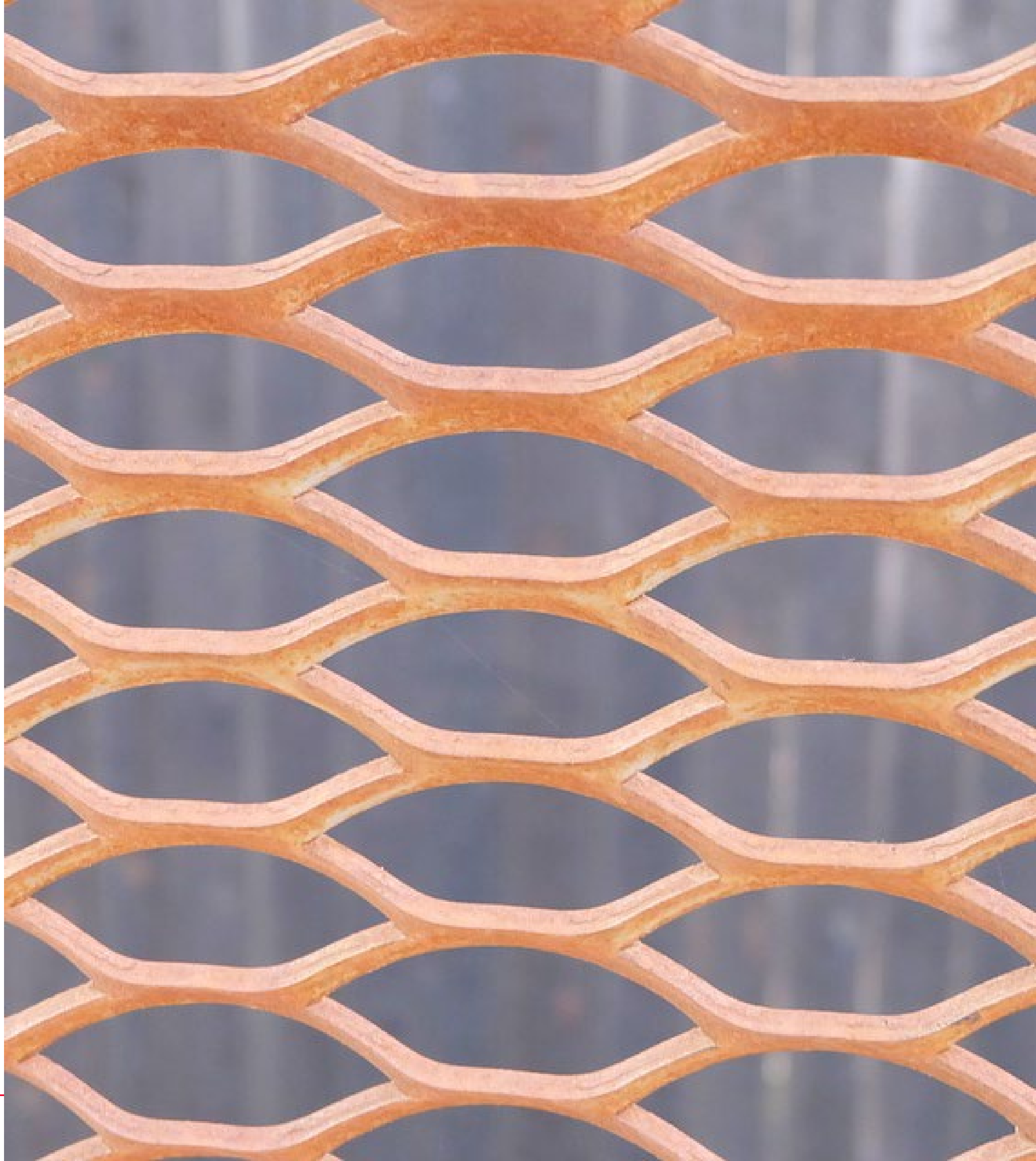
AGENDA ITEMS

- Current Restrictions on Trade with China
  - Import Restrictions
  - Export Restrictions
  - Economic Sanctions
  - Foreign Direct Investment

- Potential Legal Changes that Could Impact Trade with China



IMPORT RESTRICTIONS

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- Generally, there are no import restrictions on most products imported from China
  - However, all imports must comply with agency regulations that apply
- Section 301 tariffs remain in force – 7.5-100 percent, depending on the product
  - Some exemptions from the tariffs
- Steel and aluminum tariffs
- Antidumping and countervailing duty tariffs
- U.S. government is prohibited from contracting with companies that use certain telecommunications equipment produced by Huawei and ZTE or video surveillance and telecommunications equipment produced by Hytera, Hangzhou Hikvision, Dahua or their affiliates
  - Check your supply chain!

REGULATORY REQUIREMENTS/TARIFF MITIGATION

- **CLASSIFICATION:**
  - Customs regulations require merchandise to be classified in accordance with the Harmonized Tariff Schedule of the United States ("HTSUS"): The HTSUS is based on a single internationally recognized classification system shared by virtually all significant trading nations. Complex Customs precedent (Rulings) often govern the classification of certain types of products.
  - Tariff misclassifications can result in the overpayment or underpayment of duties, failure to satisfy import restrictions, and monetary penalties.

- **VALUATION:**
  - As part of the entry process, importers are required to report the value of the goods to Customs. It is important to report accurate values because most duties are assessed on an ad valorem basis. Underreporting the value could result in the underpayment of duties and fees, subjecting a Company to retroactive duty liability and penalties.

- **COUNTRY OF ORIGIN:**
  - Along with the HTSUS classification and the valuation of the product, the country of origin is the other factor used to determine the amount of general duties owed on an entry.
  - Along with the HTSUS classification of a product, its country of origin is also used to determine whether any special additional duties like "Section 301" duties on certain imports from China or antidumping/countervailing duties apply.
  - A country of origin determination is based on where the last "substantial transformation" occurred in the manufacturing process to create a product with a new "name, character, and use". Under the certain FTA's like the USMCA a "tariff shift" analysis is required.

SECTION 301 TARIFFS ON CHINA

- USTR will institute the following Section 301 tariff additions/increases as a result of its 4-Year Section 301 Review:

Battery parts (non-lithium-ion batteries)	Increase rate to 25% in 2024
Electric vehicles	Increase rate to 100% in 2024
Facemasks	Increase rate to 25% in 2024
Lithium-ion electrical vehicle batteries	Increase rate to 25% in 2024
Lithium-ion non-electrical vehicle batteries	Increase rate to 25% in 2026
Medical gloves	Increase rate to 25% in 2026
Natural graphite	Increase rate to 25% in 2026
Other critical minerals	Increase rate to 25% in 2024
Permanent magnets	Increase rate to 25% in 2026
Semiconductors	Increase rate to 50% in 2025
Ship to shore cranes	Increase rate to 25% in 2024
Solar cells (whether or not assembled into modules)	Increase rate to 50% in 2024
Steel and aluminum products	Increase rate to 25% in 2024
Syringes and needles	Increase rate to 50% in 2024

- Tariffs will become effective on August 1, 2024, for the year 2024, and on January 1st for the years 2025 and 2026.
- The 4-Year Section 301 Review also introduced:
  - A new exclusion process targeting machinery used in domestic manufacturing (only certain HTS codes in Chapters 84 and 85 are eligible)
  - 19 temporary exclusions for certain solar manufacturing equipment
  - Increased enforcement of Section 301 duty payments
- The Federal Register Notice (FRN) provides an Annex containing 382 HTSUS subheadings within the product categories referenced by the USTR and President Biden.
- The FRN establishes a public comment period from May 29, 2024, to June 28, 2024

IMPORT RESTRICTIONS - UFLPA

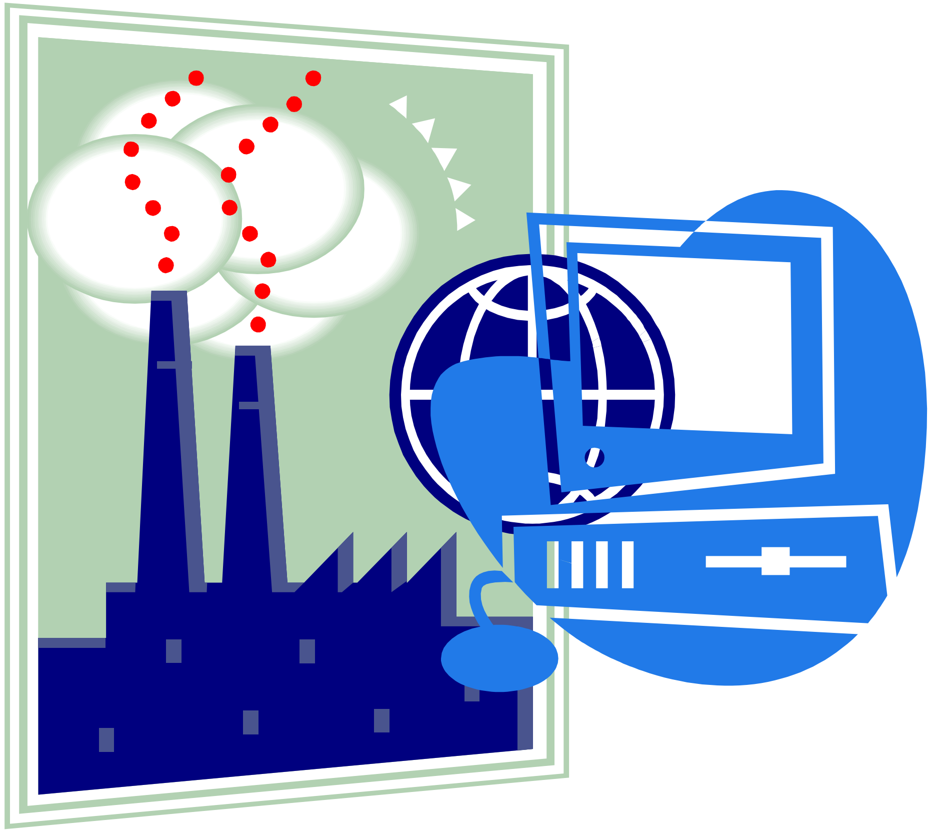
- Uyghur Forced Labor Prevention Act
  - Establishes a rebuttable presumption that the importation of any goods, wares, articles, and merchandise mined, produced, or manufactured wholly or in part in the Xinjiang Uyghur Autonomous Region of the People's Republic of China, or produced by certain entities, is made with forced labor and unfit to enter the United States
  - Effective since June 2022
  - DHS maintains a UFLPA Entity List
  - CBP has created a process for rebutting the presumption of the use of forced labor
  - Starting March 18, 2023, all shipments manufactured in China were required to enter the U.S. with the postal code of the factory
  - Process of rebutting the presumption is tedious

AGAIN, check your supply chain!

EXPORT RESTRICTIONS

EXPORT LAW BASICS – WHAT IS AN EXPORT?

- Send or Carry items/information out of the country
- Re-Export items/information from the original country of export to a third country
- Provide Defense Services outside of the country
- “Deemed Exports”; And
- Brokering



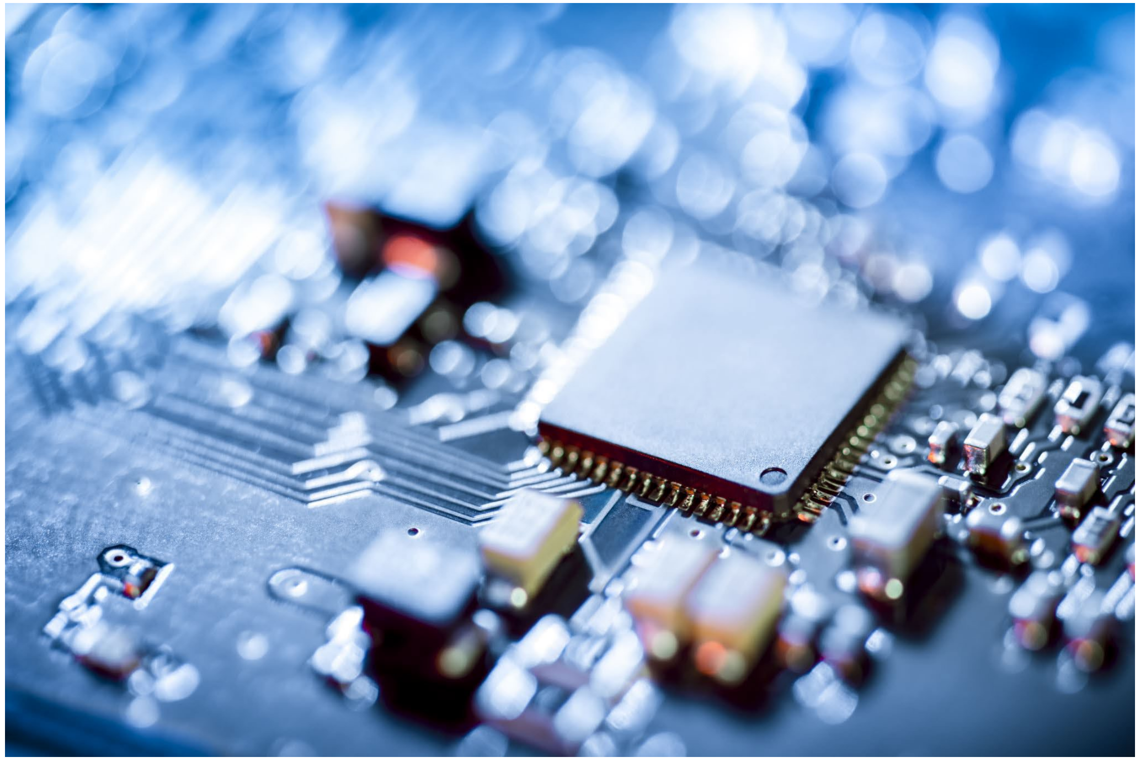
EXPORT RESTRICTIONS – FOCUS ON CHINA

- Export regulations establish licensing requirements based on the product, recipient, and destination
- All military goods are prohibited for export to China – ITAR §126.12 debarred country
- Export Administration Regulations (EAR) administered by Dept. Of Commerce, Bureau of Industry and Security (BIS)
  - Contains many licensing requirements for export, reexport, or in-country transfers of goods to/within China
  - Contains heightened restrictions on many commercial and dual-use items to China
  - Contains restrictions on certain services to China – UNIQUE!
  - Contains restrictions on parties located in China
    - Entity List
    - Unverified List
    - Denied Persons List
    - Military End-User List

EXPORT RESTRICTIONS – CHINA FOCUS (CONT.)

- Many Chinese parties added to the Entity List
- Revocation of Hong Kong's special status – U.S. export controls no longer distinguish between Hong Kong and China
- Military-intelligence end-use, end-user, and support activities to China restricted
- Miliary end-use and end-user export restrictions to China for specific identified export classifications
- Exporters may be notified by BIS "Is Informed" letter that exports, reexports, or transfers require licensing because there is "unacceptable risk" of diversion to China
- Policy of denial for certain license requests

EXPORT CONTROLS – SEMICONDUCTORS AND CHINA



- New Restrictions in Place 2022/2023/2024
  - New export classifications created for certain advanced computing items
    - Includes new controls for less powerful ICs used in the aggregate to provide high level processing power = "Performance Density"
  - Controls on supercomputers
  - Controls on semiconductor manufacturing equipment (SME)
  - Restriction of Advanced ICs and SME to end-users headquartered in, or if their ultimate parent company is headquartered in China or Macau
  - New end-use controls for supercomputing, Advanced ICs, and SME
  - New license exceptions
    - New notification requirement for specified exception
  - Diligence requirements for U.S. sellers
  - Restriction on U.S. Person support of restricted activities
    - EUV masks and associated software and technology

EXPORT ENFORCEMENT

- **Office of Export Enforcement – What are they looking for?**
  - Willful negligence
  - Continuous violations
  - Disregard of export controls and regulations

- **Risks of violations:**
  - Civil penalties to $353,534 per violation or twice the value of the transaction, whichever is greater.
  - Criminal penalties up to 20 years imprisonment and $1 million per violation
  - Debarment from federal contracting
  - Denial of export privileges: Violators may be subject to the denial of their export privileges, prohibiting participation in any transaction subject to the EAR.
  - Impact on individuals and institutions: Violations can have severe consequences, affecting both the individual(s) involved and the institution.

CASE STUDIES – SEAGATE TECHNOLOGY LLC

- April 2023: Seagate Technology LLC
  - Seagate Technology LLC received a $300 million civil penalty from BIS
  - The penalty was imposed for violating U.S. export controls by selling hard disk drives (HDDs) to Huawei Technologies Co. Ltd., breaching the foreign direct product (FDP) rule
  - This represents the largest standalone administrative penalty ever imposed by BIS
  - The case introduced a historic foreign direct product enforcement case, a multi-year audit requirement, and a five-year suspended Denial Order
  - Seagate's continued HDD supply to Huawei, despite sanctions and competitors' withdrawal, positioned it as Huawei's exclusive HDD provider
  - The case highlights the complexity of international trade restrictions and emphasizes the importance of stringent compliance measures in today's regulatory environment, including criminal reviews

CASE STUDIES – 3D SYSTEMS CORP.

- February 2023: 3D Systems Corp.
  - 3D Systems Corp. received a $2.77 million penalty from BIS for exporting controlled aerospace technology and metal alloy powder to China and controlled technology to Germany without the required licenses.
  - The settlement requires 3D Systems to retain a third-party consultant and complete two audits of its export controls compliance program, resolving 19 violations of EAR.
  - Violations included exporting military electronics blueprints and metal alloy powder to China and controlled technology to Germany, bypassing EAR requirements.
  - 3D Systems also entered into settlement agreements with the Department of State and the Department of Justice.
  - The enforcement action was triggered by a defense contractor's report and involved joint investigation by multiple federal agencies, including the Department of Defense and NASA.
  - The case underscores the critical need for compliance with export controls to protect U.S. national security and the importance of coordinated government enforcement.

ECONOMIC SANCTIONS

DEPARTMENT OF TREASURY

Office of Foreign Assets Control (OFAC)

- OFAC administers a series of laws that impose economic sanctions against hostile targets to further U.S. foreign policy and national security objectives. These targets include:
  - foreign governments/countries (i.e., Iran, Syria, and Cuba),
  - individuals (i.e., terrorists and narcotics traffickers),
  - groups (i.e., drug front companies and charities linked to terrorist groups), and
  - practices (i.e., cyber crimes, trade in non-certified rough diamonds and proliferation of weapons of mass destruction)

JURISDICTION - WHO IS SUBJECT TO U.S. SANCTIONS?

- "U.S. Persons:"
  - U.S. citizens
  - U.S. permanent resident
  - A Person Granted Asylum
  - A Refugee
  - A Temporary Resident Granted Amnesty
  - Any other person **located** in the U.S.
- Entities that are:
  - Organized in or doing business in the U.S.
  - Foreign branches of U.S. entities
  - Owned or controlled by a U.S. Person
  - Trading in U.S. goods
  - Trading in U.S. dollars
  - Causing another entity to violate sanctions

❖ OFAC has recently been extending its jurisdiction

SCREENINGS - OFAC SANCTIONED & EMBARGOED LOCATIONS

- Balkans
- Belarus
- Burma
- Central African Rep.
- China: Hong Kong and Xinjiang
- Cote d'Ivoire
- Cuba
- Democratic Republic of the Congo
- Crimea, Donetsk People's Republic and Luhansk People's Republic regions of Ukraine
- Iran
- Iraq
- Lebanon
- Libya
- Mali
- North Korea
- Nicaragua
- Russia
- Somalia
- Sudan
- South Sudan
- Syria
- Venezuela
- Yemen

* OFAC sanction programs are in constant flux; countries may be added or removed at any time.

ECONOMIC SANCTIONS

- Evolving situation
- Intersecting prohibitions with other U.S. government agency controls to create a broad and expanding regulatory regime
- No general embargo, but precise prohibitions focused on the Chinese military/intelligence-industrial complex, government activities, persons undermining democracy in Hong Kong, and other specific industries and activities that are deemed to conflict with U.S. foreign policy or national security aims:
  - Prohibitions on investing in securities and derivatives of Chinese Communist Military Companies or “CCMCs” (OFAC and DOD)
  - List-based broad prohibitions on transacting with designated Chinese entities/SDN list/50% rule (OFAC)
  - Sanctions related to aid to war in Russia
  - Sanctions related to fentanyl precursors

FOREIGN DIRECT INVESTMENT

FOREIGN DIRECT INVESTMENT-CFIUS

- Foreign Investment Risk Review Modernization Act of 2018
- Largely directed at China
- Some filings are mandatory
- Jurisdiction for investments in certain industries if foreign owners have certain rights
- Jurisdiction for property transactions
- TID U.S. businesses – technology, data, infrastructure
- Increased resources for non-notified process
- Chinese transactions are among the most reported
- Special concerns about data and surveillance opportunities
- Mitigation and enforcement concerns

FOREIGN DIRECT INVESTMENT (CFIUS) – EXPANDING JURISDICTION

- Foreign Investment Risk Review Modernization Act – August 2018
- Expansion of CFIUS jurisdiction:
  - **Real estate** transactions — sale, lease or concession near sensitive facilities
  - Non-controlling investments ("covered investments") in high-risk sectors where foreign party will receive certain rights, access or involvement:
    - critical **technology**
    - critical **infrastructure**
    - sensitive personal **data**
- Mandatory filing requirements for:
  - Certain transactions involving "substantial" foreign government interest
  - Transactions involving critical technologies (including emerging and foundational technologies)
  - Failure to make a mandatory filing can result in a fine up to the value of the transaction
- Non-notified transaction reviews
- FIRRMA is over 5 years old – Treasury is currently working on changes

CONSEQUENCES OF NOT MAKING A CFIUS FILING

- CFIUS may require mitigation measures to address the national security concern
- CFIUS may impose financial penalties
- CFIUS may block the transaction, or require the foreign purchaser to divest from the US company
- CFIUS may initiate its own review to address national security concern, even after a transaction has closed

OUTBOUND INVESTMENT REVIEW (OUTBOUND CFIUS)

- Executive Order 14105 prohibiting Chinese (Macau and HK) in technology and data industries and requiring notification for lesser controlled investments
  - semiconductors and microelectronics
  - quantum information technologies
  - artificial intelligence (AI) sectors
- Treasury Department currently drafting regulations
- There will be no case by case review

RECENT CFIUS ACTIONS

- 2020 Actions:
  - Beijing Shiji Information Technology ordered to divest 2018 acquisition of StayNTouch: In March 2020, President Trump ordered Beijing Shiji Information Technology to divest its acquisition of StayNTouch, a U.S. hotel management software company. This decision was driven by concerns over the potential risks to U.S. national security, specifically regarding the sensitive data handled by StayNTouch's software.

RECENT CFIUS ACTIONS (CONT'D)

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- **2019 Actions:**
  - iCarbonX ordered to divest from PatientsLikeMe and HealthTell: iCarbonX, a Chinese genomics company, was ordered to divest its investments in PatientsLikeMe and HealthTell. CFIUS determined that these investments posed risks due to the sensitive health data managed by these companies.
  - Beijing Kunlun Tech agrees to divest 2018 acquisition of Grindr and restrict access to data: Beijing Kunlun Tech, which acquired Grindr, a popular dating app, in 2018, agreed to divest its ownership in 2019. This decision came after CFIUS raised concerns about the potential misuse of the app's sensitive personal data by the Chinese government.

iCarbonX

KUNLUN

RECENT CFIUS ACTIONS (CONT'D)

- 2019 Actions (Cont'd)
  - CFIUS investigating ByteDance acquisition of TikTok: In 2019, CFIUS began investigating ByteDance's acquisition of TikTok, citing concerns over data privacy and the potential for Chinese government access to U.S. user data. This scrutiny led to heightened regulatory actions and ongoing negotiations about the app's ownership and data management practices.

- 2018 Actions
  - Broadcom's attempted acquisition of Qualcomm: In one of the most high-profile cases, CFIUS intervened to block Broadcom's $117 billion bid to acquire Qualcomm. The decision was based on concerns that the merger would undermine U.S. leadership in 5G technology and potentially compromise national security.

RECENT CFIUS ACTIONS (CONT'D)

- 2018 Actions (Cont'd)
  - Ant Financial's attempted acquisition of MoneyGram: CFIUS rejected Ant Financial's bid to acquire MoneyGram, a U.S. money transfer company, citing concerns over the potential access to sensitive financial data of American citizens. This move highlighted the committee's focus on protecting personal data and financial infrastructure from foreign control, particularly by Chinese firms
- General Trends
  - CFIUS self-initiating cases and reviewing past transactions: CFIUS has increasingly taken a proactive stance by initiating reviews and investigations on its own, without waiting for notifications from the involved parties. This shift underscores a broader strategy to enhance scrutiny of foreign investments, especially in sectors involving sensitive personal data and critical technologies.

COVERED NOTICES BY COUNTRY, 2020-2022

- For the three-year period from 2020 through 2022, the highest number of notices were from Chinese investors, followed by Japanese and Singaporean investors.

Covered Transaction Notices by Acquirer Home Country or Economy, 2020-2022				
Country	**2020**	**2021**	**2022**	**Total**
China	17	44	36	97
Japan	19	26	15	60
Singapore	10	13	37	60
Canada	11	28	17	56
United Kingdom	14	13	18	45
France	11	13	14	38
Cayman Islands	5	18	10	33
South Korea	2	13	14	29
Israel	6	12	9	27
Germany	7	10	10	27

POTENTIAL LEGAL CHANGES THAT COULD IMPACT TRADE WITH CHINA

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- Protecting Americans From Foreign Adversary Controlled Applications Act (Tik Tok ban)
  - Prohibits distribution, maintenance and updates for “foreign adversary software applications”
  - For existing apps, requires divestiture within 270 days
  - Expressly names Bytedance and Tik Tok
  - Foreign Adversary countries are: China, Iran, North Korea, Russia
- EO 14117 and Protecting Americans’ Data From Foreign Adversaries Act Of 2024
  - Restricts data brokers from providing PII to foreign adversary countries
  - Justice Department developing regulations
- EO 14034: Implementing rules on securing information and communications technology and services supply chain

POTENTIAL LEGAL CHANGES THAT COULD IMPACT TRADE WITH CHINA (CONT.)

- Outbound foreign investment review
  - 2023 Consolidated Appropriations Act required Treasury and Commerce to report to Congress on the issue
  - Executive Order 14105
    - Directed Treasury Department to create outbound investment program
    - Prohibits some investments in sensitive tech in "countries of concern"
    - Notification requirements for less sensitive investments
    - China (inc. HK and Macau) is the only "country of concern"
  - H.R. 6349: expands EO 14105 to cover additional technologies and adds to countries of concern

EXAMPLE: S.3810 - TIME TO CHOOSE ACT OF 2024

- Bill Name: Time to Choose Act of 2024 (S.3810), introduced by Sen. Josh Hawley [R-MO] on Feb 27, 2024.
- Purpose: Prohibits US government contracts with consulting firms that also work for China, Russia, or other entities posing national security risks.
- Key Provisions:
  - Consulting firms must certify no contracts with "covered foreign entities" (e.g., Chinese Communist Party, People's Liberation Army).
  - Federal Acquisition Regulation (FAR) Amendments:
    - Require firms to certify they have no contracts with covered foreign entities before obtaining federal contracts.
    - Prohibit awarding contracts to firms that provide consulting services to such entities, based on self-certification..
- Penalties: False certifications can lead to contract termination, suspension, debarment, and penalties under the False Claims Act.
- Exemptions: Legal, audit, accounting, and compliance services excluded; state-sponsored entities not restricted.
- Current Status: Passed by Senate Committee on Homeland Security and Government Affairs on May 15, 2024, with bipartisan support (10-1 vote).

BEST ACTIONS TO LIMIT U.S. ENTITY RISKS REGARDING BUSINESS IN CHINA

- Watch retaliation actions to May 2024 301 duties
- Map stages of production/manufacturing/extraction in China
- Identify component and material suppliers of Chinese suppliers
- Obtain factor production reports and wage files
- Enhance commercial contract provisions
- Develop alternative supply chains
- Monitor UFLPA compliance
- Change “just in time” delivery schedules
- Have China exit plan

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QUESTIONS?

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THANK YOU