



## The New US Rules for Export Trade with Hong Kong

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Earlier this year, the U.S. Government initiated a series of actions to address the People's Republic of China's continuing efforts to undermine the autonomy of the Special Administrative Region of Hong Kong (Hong Kong). Those actions culminated on July 14, 2020 in two major developments impacting U.S. export trade with Hong Kong: (1) the issuing of Executive Order 13936 ("EO 13936," entitled "Executive Order on Hong Kong Normalization"), and (2) the signing into law of the Hong Kong Autonomy Act of 2020 (Pub. L. 116-149, the "HKAA"). The U.S. Departments of State, Commerce and the Treasury have since adopted new trade restrictions for Hong Kong, as directed under EO 13936 and the HKAA, raising new risks and compliance concerns for U.S. exporters.

EO 13936 and the HKAA are responses to China's most recent maneuvers to erode Hong Kong independence—guaranteed (albeit temporarily) under the 1984 Sino-British Joint Declaration treaty. In May of this year, China further advanced its Hong Kong agenda by enacting expansive new national security legislation. Among other things, the National Security Law increases the Chinese Government's role in Hong Kong's national security and enables criminal prosecution of the people of Hong Kong for broad categories of political activities deemed to threaten national security. The U.S. Government immediately condemned China's passage of the law, and on May 27, 2020, U.S. Secretary of State Mike Pompeo certified to the U.S. Congress that Hong Kong is no longer sufficiently autonomous from China to warrant differential treatment under U.S. laws.

The U.S. has now implemented measures to remove preferential status previously granted to Hong Kong, including through new export controls and sanctions adopted under EO 13936 and the HKAA. Those measure prohibit many types of export transactions involving Hong Kong and other dealings with sanctioned persons, in some cases, imposing new licensing requirements. They also raise important questions about U.S. companies' compliance obligations for transactions involving Hong Kong that are now subject to the same restrictions imposed on China. This client alert highlights the most significant developments in these areas.

### ***New Export Controls Affecting Hong Kong***

EO 13936 directs federal agencies to amend regulations, agreements, policies, and procedures to

eliminate or suspend different or preferential treatment afforded to Hong Kong that is not also afforded to China. Among EO 13936's mandates are new export controls under the ITAR (International Traffic in Arms Regulations) administered by the U.S. Department of State, Directorate of Defense Trade Controls (DDTC) and EAR (Export Administration Regulations) administered by the U.S. Department of Commerce, Bureau of Industry and Security (BIS). Both agencies have now amended their respective regulations and policies to strengthen controls on exports of sensitive items to Hong Kong, and to prevent their diversion to mainland China.

#### Exports of Defense Articles and Defense Services Under the ITAR

EO 13936 suspends Hong Kong's differential treatment from China under the Arms Export Control Act (22 U.S.C. 2751 *et seq.*). DDTC implemented EO13936 through a [policy notice](#) (published on its website) stating that the agency would now consider Hong Kong to be part of China for purposes of the arms embargo in section 126.1(d)(1) of the ITAR. Accordingly, sales, exports, reexports, and retransfers of defense articles and defense services are prohibited to Hong Kong without a license, and DDTC will apply a presumption of denial to license requests involving Hong Kong. This includes "where a Hong Kong person is named as an end-user, licensee (signatory) or sublicensee, or where Hong Kong appears as a marketing, transfer, re-transfer, re-export, sales, or distribution territory." It also includes deemed exports of ITAR technical data to Hong Kong persons in the U.S. and deemed re-exports to dual- and third-country nationals of Hong Kong outside the U.S.

There are two noteworthy implications of DDTC's new Hong Kong policy. First, DDTC has not revoked preexisting licenses involving Hong Kong. Second, any person who knows or has reason to know of an unauthorized, proposed, final, or actual sale, export, transfer, reexport, or retransfer of defense articles or defense services to Hong Kong must now "immediately" inform DDTC, under ITAR section 126.1(e)(2).

#### Exports of CCL and EAR99 Items Under the EAR

To address concerns about China acquiring sensitive items subject to the EAR, the Commerce Department's Bureau of Industry and Security (BIS) has suspended certain EAR preferences previously available for exports, reexports or transfers (in-country) involving Hong Kong. Hong Kong remains separately listed on the EAR's Commerce Country Chart and subject to CCL-based licensing requirements virtually identical to China. It also continues to be listed in the preferential Country Group B list for EAR license exceptions, which China is not. But, as directed under EO 13936, BIS has suspended Hong Kong's eligibility for those license exceptions.

As of July 31, 2020, an EAR license exception may not be used for exports or reexports to Hong Kong or transfers within Hong Kong if that license exception would not authorize the same transaction for China. The BIS action suspends 13 separate license exceptions otherwise available for exports and reexports to Hong Kong, restricts the use of license exceptions for transactions involving 9x515 or "600 series" items and Hong Kong, and suspends the use of License Exception APR (additional permissive reexport (EAR § 740.16(a)) for reexports from Hong Kong. Most significantly, this includes widely used License Exception GBS (EAR § 740.4), which is otherwise available for certain transaction involving Country Group B countries, and it applies broadly to "deemed" exports of controlled technology to Hong

Kong persons, whether in the U.S. or abroad. Export, reexports and transfers involving Hong Kong that were previously authorized under these EAR License Exceptions now require a specific license from BIS.

### ***New Economic Sanctions Against Hong Kong***

Signed into law concurrently with EO 13936, the HKAA adopts new economic sanctions targeting foreign persons responsible for eroding Hong Kong's independence and the foreign financial institutions that support them. Those sanctions stem from the law's parallel Congressional reporting requirements. Under the HKAA, the Secretaries of State and Treasury must jointly identify and report to Congress a list of foreign persons found to have materially contributed to China's failing to meet its obligations relating to Hong Kong's autonomy and a list of any foreign financial institutions that knowingly conduct a significant transaction with those foreign persons. Then, subject to possible Presidential waiver, the law requires imposition of certain economic sanctions against the listed parties.

The HKAA requires the President to impose sanctions against listed foreign persons (including natural persons and entities) within one year of their listing. These include both blocking sanctions—sanctions imposed against Specially Designated Nationals that prohibit transactions involving the blocked person's property or property interests—and exclusion from the United States. EO 13936 authorizes the Secretaries of State and Treasury to designate foreign persons for sanctions, describing various activities undermining Hong Kong's autonomy and restricting the freedom of expression or assembly of the citizens of Hong Kong. Pursuant to the EO, OFAC issued its first such designations on August 7, 2020, imposed blocking sanctions on 11 Hong Kong and Chinese government officials. Their property is now blocked and U.S. Persons are required to report the blocking of such property to OFAC.

Foreign financial institutions designated under the HKAA are subject to a menu of 10 possible sanctions, which are similar to those authorized against foreign financial institutions under the Iran and Russia sanctions programs. They include restrictions on transactions with U.S. financial institutions and access to the U.S. financial system, restrictions on exports of U.S. goods to the foreign financial institution, prohibitions on U.S. person investments in the foreign financial institution, and sanctions against their corporate officers. The HKAA requires the President to impose at least five of the available sanctions within one year of listing of the foreign financial institutions, and the remainder of the sanctions if the foreign financial institutions remains on the list after two years.

### **Key Takeaways**

EO 13936 and the HKAA are significant salvos in the U.S.'s ongoing efforts to counter China's expansion of political and economic power. For U.S. companies dealing with Hong Kong, they raise new concerns and risks for potential violations. This is especially true for companies dealing in controlled goods, technology, and software or employing foreign nationals of Hong Kong in the U.S.

As the Executive agencies continue to implement EO 13936 and the HKAA, and to clarify their enforcement policies and interpretations, many U.S. companies will implement procedures for additional scrutiny of Hong Kong transactions. This may include enhanced due diligence of parties to export transactions. In particular, while BIS has yet to clarify its position regarding whether the China military

end-use/end-user rule in EAR § 744.21 applies to Hong Kong, U.S. exporters will focus on “know your customer” procedures and obtain guidance or specific authorizations for transactions raising compliance questions. For additional background on U.S. measures to strengthen controls on exports to China, the Chinese military and entities supporting China military industries, see our recent client alerts [here](#).

## **Related People**

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## **Related Services**

- ITAR, Export Controls and Economic Sanctions