



LTI Newsletter

Bringing you the Latest Developments in U.S. and Chinese Strategic Trade Compliance Policy

Summer 2009

An Executive Note

Dear Friends and Partners,

This week, we attended an event in Beijing featuring U.S. Secretary of Commerce Gary Locke as the honored speaker. Secretary Locke was accompanied on his first official mission to China by many high-ranking U.S. Government officials, including Energy Secretary Steven Chu and White House Cabinet Secretary Chris Lu. This delegation, as the Secretary pointed out, communicated a very strong message about the importance the United States places on the U.S.-China bilateral relationship and the need for increased cooperation in areas such as clean energy, which was the focus of this trip. Secretary Locke emphasized the great business opportunities available in the areas related to green energy development and stressed that the United States and China must cooperate in this area because the environment does not recognize international boundaries. He also stated that the Department of Commerce will be restructuring its services to better serve U.S. companies, especially the small to medium size businesses. Secretary Locke stated that in moving forward on cooperative efforts related to environmental issues, energy issues, as well as any other area of mutual interest, it is critical that our goals cannot promote American interests at the cost of Chinese interests, nor can they promote Chinese interests at the cost of American interests. We need to find solutions that benefit both sides and the world community as a whole.

We were very impressed by the positive direction that this delegation's visit and the Secretary's speech intoned. There is much hard work ahead, but it seems that this visit is building an excellent foundation from which progress can be made in increasing U.S.-China cooperation. Soon we will have a better sense of the progress, as there are two major events on the horizon with the S&ED in July and the JCCT in September.

- John and Nina

Recent Trade Developments

On the China Side ...

China's State Council Announces Support for Exporters

On 27 May 2009, China's State Council announced policies to boost external demand. Using funds from the central budget, the Chinese government will provide USD 84 billion in export credit insurance, tax incentives to labor-intensive and high-tech industries, and greater financial guarantees to small businesses engaged in exports. The government will also take measures to keep the RMB stable in order to help exporters mitigate exchange risk. The State Council announced a dual-pronged approach of stabilizing exports and promoting domestic demand in order to weather the global financial crisis.

Chinese Government Asks Japan to Loosen High-Tech Export Controls

At a 6 June 2009 press conference in Beijing, the day before high-level economic talks with Japan, China's Minister of Commerce Chen Deming suggested that Japan ease restrictions on the export of high-tech equipment to China. Japanese media representatives suggested that China send a buying mission to Japan, as it has done to Europe. Chen indicated that a buying mission could be arranged, but that the goal was mutual investment rather than one-way investment. Chen stressed that the trade imbalance would be greatly eased if Japanese enterprises were allowed to sell more high-tech items to China.

The second China-Japan High-Level Economic Dialogue took place the next day on 7 June 2009 in Tokyo. The talks were co-chaired by Chinese Vice Premier Wang Qishan and Japanese Foreign Minister Hirofumi Nakasone. The four main topics discussed included improvement of the global financial situation, increasing cooperation in trade and investment, and increasing cooperation regarding the environment and energy.

MOFCOM Establishes New General License for Dual-Use Exports

On 1 July 2009, a new Chinese Ministry of Commerce (MOFCOM) "General License" for dual-use exports became available. Those that receive a General License will be able to conduct multiple exports of dual-use items and technologies from the PRC to multiple end-users without needing a license for each individual transaction. Prerequisites for receiving a General License are as follows: 1) the applicant must have a history of exporting dual-use items and technologies from China for at least two years, 2) the applicant must be in good legal standing, and 3) the applicant must be able to demonstrate knowledge of China's export control regulations. The General License bears much resemblance to BIS's Special Comprehensive License (SCL) in that both require companies to implement internal mechanisms to ensure compliance and both have similar reporting, recordkeeping, inspection, and review requirements. The following chart presents a comparison of the MOFCOM General License to the BIS SCL.

Terms	MOFCOM General License	BIS Special Comprehensive License
Eligible Items	Dual-use items and technologies	All items subject to EAR*
Term of Validity	Three years	Four years with one-time, four-year extension available
Compliance	Companies are required to implement "Internal Control Mechanisms" for dual-purpose items and technologies	Companies are required to implement an Internal Control Program (ICP)
Licensing History	Companies must have been engaged in the export of dual-purpose items and technologies for two years or more prior to application	Companies must show a history of receiving continuous licenses for large volume exports
Regulatory Knowledge	Parties must demonstrate knowledge of PRC policies and regulations on the control of exports of dual-purpose items and technologies	Parties must show evidence of knowledge of all provisions of the EAR
End-User Assurances	During application process, companies commit that they will get written	During application process, companies must demonstrate end-user reliability and

	guarantees from each end-user before executing each contract	submit statements of compliance signed by proposed consignees
Reporting / Recordkeeping	Requirement to submit reports to MOFCOM every six months detailing all transactions conducted under General License	Recordkeeping requirement on each sale or reexport under SCL; Records must be kept available for BIS inspection upon request
Inspection / Review	MOFCOM reserves the right to conduct company site visits and inspections of internal control mechanisms	BIS maintains right to conduct announced and unannounced system reviews

* except those specified in §752.3.

Ministry of Science and Technology (MOST) to Support Indigenous Innovation in High-Tech Enterprises

The promotion of indigenous innovation became a primary agenda of the Chinese Government under the Eleventh Five-Year-Plan. China's Ministry of Science and Technology (MOST) is formulating a set of standards intended to support the development of high-tech enterprises engaging in indigenous innovation. MOST also intends to stimulate innovation in China by providing insurance, loans, and additional financial support to indigenous companies that take risks to pursue innovative scientific projects.

On the U.S. Side ...

US Treasury Secretary Timothy Geithner Visits Beijing

From 31 May to 2 June 2009, U.S. Treasury Secretary Timothy Geithner visited Beijing to discuss U.S.-China economic cooperation. During the visit Geithner met with Chinese President Hu Jintao and gave a speech at Peking University. One topic addressed during his visit was the loosening of U.S. high-tech export controls to China. In light of a recent report by the American Chamber of Commerce in Beijing, which stated that U.S. companies lose USD 1 billion annually because of overly restrictive export controls, the point was raised that loosening these controls would be mutually beneficial to the Chinese and U.S. economies. Other topics raised during Geithner's visit were the importance of the U.S.-China Strategic and Economic Dialogue (S&ED), which will continue under the Obama Administration, and the security of Chinese assets in U.S. hands.

Tennessee Professor Sentenced to Four Years in Prison for Violating U.S. Arms Export Control Act

On 1 July 2009, seventy-two-year-old professor Dr. John Reece Roth of Knoxville, Tennessee received a sentence of four years in prison after being convicted of violating the U.S. Arms Export Control Act. In 2005 and 2006, Roth was conducting research for the U.S. Air Force on specialized plasma technology for the wings of unmanned aerial vehicles (UAVs) when he illegally transferred technical data to the PRC. He also granted unauthorized access to his research to Chinese and Iranian graduate students, which constitutes a violation of U.S. "deemed export" regulations, even though the transfer occurred within the United States.

USG Puts Forth Bill to Adjust Jurisdiction of Commercial Satellites

Bill H.R. 2410, currently before the U.S. House of Representatives Committee on Foreign Affairs, includes a section (826) seeking to empower the President to reevaluate the designation of commercial satellites as munitions as opposed to dual-use items. This reevaluation could result in the switching of their jurisdiction from the International Trafficking in Arms Regulations (ITAR), under the Department of State, to the Export Administration Regulations (EAR), under the Department of Commerce, except when the end-user is located in the People's Republic of China. Congress removed this Executive power regarding satellites from the President in 1999. The bill also seeks to increase the penalties for violating the ITAR.

BIS Conducts Review of Foreign Export Control Practices (FECF)

The U.S. Department of Commerce Bureau of Industry and Security (BIS) is conducting a review of the dual-use export control practices of France, Germany, Italy, Sweden, United Kingdom, and Japan. With the goal of increasing the efficiency and effectiveness of the U.S. export control system and identifying areas for greater multilateral export control synchronization, BIS will be looking at the following aspects of foreign export control practices: 1) license authorizations, 2) license conditions, 3) re-export controls, 4) unilateral export controls, 5) efficiency and processing times, and 6) comparison of the above countries' export control practices with those of the People's Republic of China. BIS is currently in the data collection phase of this review. If you are interested in submitting comments on this topic, please contact LTI.

Chinese Information Security and Encryption Regulations

Update on CCC Mark for 13 Categories of Information Security (IS) Items

On 15 July 2009, the China Office of State Commercial Cryptography Administration (OSCCA) published the cipher testing criteria and guidelines for government procurement of six of the thirteen categories of encryption items that fall under the new regulations. The six categories of information security products are firewalls, secure database systems, secure operating systems, secure routers, secure separation and information exchange products, and smart card chip operating systems. These criteria are available to view in Chinese on the OSCCA website. OSCCA will announce the testing criteria and guidelines for the remaining seven categories in the near future, and LTI will keep you posted as further information arises.

Update on Implementation of New Encryption H.S. Codes

In other encryption related news, Chinese Customs and OSCCA did not release the procedures for importing the twelve specified encryption products under the new H.S. Codes in April of this year as expected. Neither Chinese Customs nor OSCCA provided information on a new release date and gave no reason for the delay. OSCCA and other Chinese officials have stated, however, that the core function test still applies when determining whether an item is covered under the encryption H.S. Codes. This means the H.S. Codes apply to "specialized hardware and software for which encryption and decoding operations are core functions." If a product qualifies under this core function test, the company will have to obtain an import license from OSCCA to import the product. If it does not qualify, then the product would not be classified under one of these H.S. Codes and not require an import license from OSCCA per those H.S. Code requirements. Information on obtaining an import license is located on the OSCCA website and is relatively simple. We would advise caution, though, in self-classifying products under this code unless you are sure they meet the core function test, because future procedures for obtaining the import license may be much greater. At this point, we advise checking with OSCCA if in doubt as to whether your product is covered under these H.S. Codes.

Chinese Government Delays Mandatory Computer Filtering Software Amidst Public Discontent

On 19 May 2009, the Chinese Ministry of Industry and Information (MIIT) issued a notice on their official website that PC makers must pre-install an Internet filtering software program or offer it on a CD-ROM included with all PCs sold in China after 1 July 2009. The software, called Green Dam Youth Escort, blocks sites with pornographic and violent content. The software was designed and licensed by a Chinese company called "Jin Hui." The initial MIIT notice did not clearly express whether or not the new rule would be compulsory for all PC makers selling computers in China, nor did it include any details about how the rule would be enforced, but it generated great controversy.

Immediately upon circulation of the MIIT notice, consumers and trade associations in China and outside China began publicly and privately criticizing the new requirement, raising concerns about protection of user information, compliance with WTO regulations, and the scope of website content that would be blocked by the filter. Some companies raised their concerns to MIIT that the requirement would negatively impact the industry as such changes were too difficult, especially given the short time frame.

On 30 June 2009, MIIT announced on its official website and through Xinhua, the official Chinese State News Agency, that MIIT will delay the mandatory implementation of the Green Dam pre-installation. This is being seen as a major rollback of the policy by the Chinese government in the face of increasing pressure from foreign and domestic constituents. However, MIIT plans to continue its original direction by implementing requirements step-by-step. MIIT will continue to provide free Internet downloads and installation of the filtering software in middle and primary schools, Internet bars, and computers in other public places, and it will continue to encourage computer companies that have already installed the software to actively expand their presence in the market. In terms of the pre-installation on other computers, MIIT will solicit opinions from various parties in order to revise the proposal and improve the implementation strategies.

China-EU Trade Relations

China-EU Trade Statistics

According to MOFCOM, the EU is China's largest trading partner and the number one source of technology imports into China. China is the second largest trading partner for the EU and the fastest growing export market. China-EU trade exceeded USD 425 billion in 2008 and from January to May 2009, reached USD 129.26 billion. In the past year, China has made a concerted effort to cultivate trade and investment with European countries.

China Continues Seeking Investment Opportunities in Europe

In the spring of 2009, MOFCOM led the China Trade and Investment Promotion Delegation on investment seeking missions to Germany, Switzerland, Spain, Britain, France, and the United States, signing nearly USD 20 billion in deals. From 15-22 June, the MOFCOM delegation sought trade and investment opportunities in Russia, Slovakia, and Croatia, signing USD 3 billion in deals in Russia alone. From 4-9 July, the delegation visited Italy, Sweden, Finland, and Portugal. The China Trade and Investment Promotion Delegation consisted of high-level officials from several government ministries and approximately three hundred Chinese entrepreneurs. The delegation targeted deals that involve two-way investment and technical cooperation. These types of visits often take place as a follow-up to official state visits by Hu Jintao.

China-EU High-Level Economic Dialogues Take Place in Brussels, London, and Prague

China and the EU held their second round of high-level economic talks from 7-8 May 2009 in Brussels. Chinese Vice Premier Wang Qishen called for greater mutual market access between the EU and China, saying that China planned to remove barriers for European companies to invest in China while promoting procurement and imports from Europe.

From 10-12 May 2009, Premier Wang made an official visit to London for the second China-UK Economic and Financial Dialogue. Co-hosted by Wang and British Chancellor of the Exchequer Alistair Darling, major topics included increasing trade and investment, promoting financial stability, promoting capital markets, energy collaboration, sustainable development, and green growth.

On 20 May 2009, the 11th China-EU Summit took place in Prague. The meetings were presided over by Chinese Premier Wen Jiabao, Czech President Vaclav Klaus, and European Commission President Jose Barroso. The participants of the summit reached agreements on establishment of a center for clean energy, a science and technology partnership, and cooperation regarding SMEs. The two sides failed to sign a memo of understanding on high-tech trade. The Chinese side would like to see the EU lift its arms embargo and loosen restrictions on the export of high-tech products to China.

Coming Soon

First Indian Company to Receive VEU Status by End of July

On 2 July 2009, the U.S. Department of Commerce Bureau of Industry and Security (BIS) announced that General Electric India in New Delhi would be the first Indian company to receive VEU status. The announcement will appear in the Federal Register by the end of July, at which time U.S. companies will be able to export certain high-tech, dual-use items to General Electric India without applying for individual export licenses. The VEU program was pioneered in China in 2007 as a way to enhance trade with overseas companies that had demonstrated long-term commitment to compliance; six Chinese companies currently hold VEU status.

China-US Strategic and Economic Dialogue (S&ED) to Take Place at End of July

The first meeting of the China-US Strategic and Economic Dialogue (S&ED) under the Obama Administration will take place in Washington, DC during the last week of July. U.S. President Barack Obama has appointed Secretary of the Treasury Timothy Geithner and Secretary of State Hillary Clinton to serve as Special Representatives to the two-day meeting. The S&ED was established by U.S. President George W. Bush and Chinese President Hu Jintao in September 2006. It will continue under the Obama Administration as annual, cabinet-level meetings.

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MOFCOM Export License and End-User Statement Manuals

By this fall, LTI will be publishing two new instructional manuals for purchase. These manuals will cover the MOFCOM export licensing process and the MOFCOM end-user statement process. The MOFCOM Export License Manual provides details about the Chinese export control system to include an overview of and links to Chinese laws and regulations, but more importantly, the manual walks the user through the registration, classification, and export licensing process at MOFCOM. The MOFCOM End-User Statement (EUS) Manual supplies companies with step-by-step guidance for obtaining an End-User Statement from the Ministry of Commerce for the import of sensitive and controlled items into China. The EUS manual will be offered in both English and Chinese. This is the first time the Chinese export control licensing and end-user statement processes have been summarized in such step-by-step detail, and it is also the first time that such information is available in English. Both of these manuals will be available for purchase soon on our website; if you are interested in these manuals, please contact us.

KENTUCKY CORNER

The Kentucky China Trade Center (KCTC) has expanded its reach this summer with the addition of three new employees. Sophia Chiao, Public Relations Specialist, started on 1 June 2009 and has been busy introducing the KCTC to several new media outlets. With prior experience at China Central Television (CCTV) and three years promoting the country of Tunisia in China, Sophia is up to the challenge of advancing Kentucky as a destination for investment, tourism, and education. In addition, Kentucky native Benjamin Woodman, currently enrolled in Princeton's Woodrow Wilson School of Public & International Affairs, has been working with Hu Di, from the Beijing University of Science and Technology, on a plan to recruit more Chinese students to Kentucky Universities. In spite of the weak global economy and H1N1 influenza pandemic, the KCTC is continuing to find Kentucky-China trade and investment opportunities.

In mid-July 2009, KCTC Director David Snodgrass and Sophia Chiao are leading a delegation of equine specialists to Kentucky to introduce them to the 2010 Alltech FEI World Equestrian Games. The Games are

the largest sporting event to occur in the United States since the 2002 Olympic Games. The goal of the visit is to facilitate more participation from Chinese athletes in equestrian sports and attract a greater Chinese fan base. The delegation is comprised of Mr. Yue Gaofeng, Standing Secretary General of the China National Horse Industry Association under the Chinese Ministry of Agriculture; Ms. Wang Qin, Ph.D., from the College of Animal Science and Technology in China's Agriculture University; Mr. Zhang Yida, Chairman of the Beijing Xin Hong Ji Sheng Cheng Real Estate Group Co., Ltd, who will be establishing an arena and clubhouse for horse shows in Beijing; and Mr. Zhao Xigang, Chairman of the Shanlihe Horse Farm in Zhejiang, China. Check the KCTC website, www.kentuckychinatrade.com, for outcomes of the delegation's visit to Kentucky.