

Rep. Ed Royce Introduces New Export Control Reform Legislation

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Last week, U.S. House of Representatives Foreign Affairs Committee Chairman Ed Royce (R-CA) introduced the Export Control Reform Act of 2018 (H.R. 5040), bipartisan legislation designed to modernize and establish permanent export controls on commercial, dual-use, and less sensitive military items. While the new legislation generally would codify many existing export controls, it potentially could have a significant impact on U.S. companies owned by foreign entities.

The U.S. Department of Commerce's Bureau of Industry and Security (BIS) administers the Export Administration Regulations (EAR), which control exports, reexports, and in-country transfers of commercial, dual-use, and certain military commodities, software, and related technology. The Export Administration Act of 1979, as amended, served as the principal statutory authority for the EAR. However, the Act lapsed in 2001, requiring the President to issue Executive Orders under the International Emergency Economic Powers Act since that time to ensure the continuing effect of the regulations.

The Export Control Reform Act of 2018 aims to establish permanent, codified export controls to ensure that U.S. industry maintains its technological advantage and that sensitive U.S. technology is not provided to countries or end-users of concern. The Chinese government's demand for access to U.S. companies' technology and source code as a cost of doing business in the country appears to be one of the drivers behind this new legislation. Below are key highlights:

- H.R. 5040 includes some definitions that do not precisely track, and in certain cases are more restrictive than, those currently in the EAR. For example, the definition of "United States person"

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Practice Areas

Export Controls and Economic Sanctions
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would include a corporation organized under the laws of the United States *if* natural U.S. persons own more than 50 percent of the outstanding capital stock or other beneficial interest in the entity. If left as is, this could have substantial ramifications because the definition, particularly when considered in conjunction with the definition of “foreign person” (*i.e.*, a person that is not a United States person), indicates that U.S. subsidiaries with foreign parent companies may not be treated as U.S. persons. Would a U.S. company transferring controlled technology to another U.S. company—but one owned by a foreign parent—now be engaging in a deemed export potentially requiring an export license?

- The legislation aims to provide Congress with significant oversight, including notification and veto power over any proposed rescission of a State Sponsor of Terrorism designation. Congress also would receive notification of all proposed amendments to the EAR as well as a detailed annual report analyzing the effectiveness of U.S. export controls.
- Currently, BIS, together with the U.S. Departments of Defense and State, can identify and place provisional controls (an “0Y521” classification) on new technology that provides a significant military or intelligence advantage to the United States. H.R. 5040 formally requires a regular, interagency process to identify emerging and other critical technologies that are not currently listed as controlled items.
- Although BIS provides significant guidance and engages in outreach to industry, the new legislation would codify requirements to assist U.S. businesses in export licensing and other processes and to publish and update “best practices” guidelines. It also would codify the requirement for the U.S. government to use its “best efforts” to render export licensing determinations within 30 days.
- In addition to export controls, the new legislation would provide a permanent statutory authority for antiboycott regulations currently administered by BIS as well as proliferation-related controls.
- The legislation also would codify civil and criminal penalties for export control violations as well as civil penalties for antiboycott violations. Violations may result in civil penalties of \$250,000 or twice the value of the transaction at issue, along with a general denial of export privileges and revocation of licenses. Criminal penalties for knowing violations may result in fines up to five times the value of the transaction or \$500,000, whichever is greater and/or imprisonment for up to five years. Willful violations are subject to even higher penalties, and the new legislation provides for debarment for certain criminal convictions. Additionally, H.R. 5040 calls for substantial potential sanctions (*e.g.*, a potential two plus year license debarment) for persons that knowingly illegally export certain missile technology-related items.

We will continue to track this legislation and its potential impact on U.S. and foreign companies. Please feel free to contact us if you have any questions or would like to discuss further.