KPMG

China Tax Alert

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China to enforce key export controls on select aerospace items and special organic materials

Summary：

On May 30th, 2024, the Ministry of Commerce of China and three other Chinese ministries jointly issued a Notice (No.21, 2024), announcing the decision to implement export control on the following four categories of items and technologies involving aerospace and special organic materials, starting from July 1st, 2024:

I. Equipment, software, and technology related to the manufacture of aerospace structures and engines;

II. Equipment, software, and technology related to gas turbine engines/gas turbines manufacturing;

III. The equipment, software, and technology related to the spacesuit window;

IV. Ultra-high molecular weight polyethylene fiber items.

The newly controlled items are primarily associated with technology-intensive industries, and the corresponding compliance requirements for technology export control are of utmost importance. In light of the rapidly evolving international export control landscape and China's proactive counter-sanction measures, time is of the essence. Enterprises involved in businesses related to these items must act swiftly to establish a comprehensive internal export control compliance program. This is crucial to effectively manage the associated compliance risks and ensure prompt adherence to the new regulations.

Background

On May 30th, 2024, the Ministry of Commerce of China, the General Administration of Customs, and the Equipment Development Department of the Central Military Commission jointly issued a Notice. They announced that starting from July 1st, 2024, four categories of items will be subject to export control measures and shall not be exported without authorization from Chinese authorities:

1. Equipment, software, and technology related to manufacturing aerospace structures and engines.

   I. Tooling, molds, fixtures, and other process equipment, specially designed for superplastic forming/diffusion bonding of titanium, aluminum, and their alloys for the manufacture of any of the following items (refer to HS Code: 8203200010, 8204110010, 8204120010, 820540010, 8205900010, 8206000010, 8480419010, 7326901910):

      1) Aircraft structures or spacecraft structures;

      2) Aircraft engines or space engines;

      3) Components specially designed for aircraft structures or spacecraft structures;

      4) Components specially designed for aircraft engines or space engines.

II. Software specially designed or modified for research & development, production, or use of the items listed in 1.1 above.

III. Technologies and their carriers used for research and development, production, or use of the items listed in 1.1 above, including design drawings, process specifications, process parameters, processing procedures, simulation data, etc.

2. Equipment, software, and technology related to gas turbine engines/gas turbine manufacturing.

I. Directional crystal or single crystal casting equipment for manufacturing superalloys required for turbine configuration components such as gas turbine engines/gas turbine blades, guides, etc. (refer to HS Code: 8454301101, 8454309010).

II. Precision casting intermediate products (including ceramic cores, wax pattern modules, and mold shells), specially designed for manufacturing turbine configuration components such as gas turbine engine/gas turbine blades, guides, casings, etc; as well as process equipment such as tools, molds, and fixtures specially designed for manufacturing the above-mentioned intermediate products (refer to HS Code: 6903100010, 6903200010, 6903900010, 69091100, 690912010, 690919010, 8480490010, 8205900020, 8428909030, 8480600010, 7326901920, 7616991020, 903180081).

III. Process equipment such as tools, molds, clamps, etc., specially designed for solid-state connection of disks of materials such as superalloys, titanium alloys, or intermetallic compounds used in gas turbine engines/gas turbines (refer to HS Code: 8205900030, 6804219010, 6804229010, 8207201010, 8207209010, 820730030, 8480419020, 8466200010, 7326901930, 9031809082).

IV. Software specially designed or improved for research and development, production, or use of the items listed in 2.1, 2.2, and 2.3 above.

V. Technologies and their carriers used for research and development, production, or use of the items listed in 2.1, 2.2, and 2.3 above, including design drawings, process specifications, process parameters, processing procedures, simulation data, etc.

3. Equipment, software, and technology related to spacesuit windows.

I. Moulds specially designed for manufacturing spacesuit windows (refer to HS Code: 8480719020).

II. Software specially designed or modified for research and development, production or use of the items listed in 3.1 above.

III. Technologies and their carriers used for research and development, production or use of the items listed in 3.1 above, including design drawings, process specifications, process parameters, processing procedures, simulation data, etc.

4. Ultra-high molecular weight polyethylene fiber items.

I. Ultra-high molecular weight polyethylene fibers with breaking strength ≥40cN/dtex, initial modulus ≥1600cN/dtex, and untwisted (refer to HS Code: 5402491010, 5501900010, 5503909010).

II. Soft weftless fabric laminates made of ultra-high molecular weight polyethylene fibers (without compression) with areal density ≤5.3kg/m2, anti-1.1g standard simulated fragment (17 grains simulated fragment FSP)V50≥700m/s (tested per GJB4300A-2012 Appendix B, Ballistic Limit V50 Test Method) (refer to HS Code: 580640910).

III. Technologies and carriers to produce the items listed in 4.1 and 4.2 above, including design drawings, process specifications, process parameters, processing procedures, simulation data, etc.

Based on the items' features and uses, the newly included items in the scope of control mainly belong to the technology-intensive advanced manufacturing sectors. They have strong dual-use characteristics, including finished products, intermediate products, raw materials, equipment, molds, and technical data in design, production and manufacturing. According to the analysis of the published export statistics of the General Administration of Customs from May 2023 to April 2024, the major export destinations of the controlled items mentioned above include the United States, Germany, South Korea, Mexico, and Russia.

Compared to the previous notices for controlled items released by the Chinese authority, Notice (No. 21 of 2024) provides a more detailed description of the technologies and data related to physical items. It specifies that the relevant data are managed together as controlled items. According to the Export Control Law, the scope of export control items includes “relevant technical information and data”. This definition is broad and may be difficult to apply directly in practice. Since the industries involved are technology-intensive, a clear definition of technologies and data in government notice or the list of dual-use items would benefit enterprises and law enforcement agencies in determining controlled items in actual operations.

Since the Export Control Law was enacted in 2020, the Ministry of Commerce and other relevant departments have issued several notices to modify the list of dual-use items. The issuing authorities should typically include the Ministry of Commerce and the General Administration of Customs. Other departments may also be involved based on the nature of the items being adjusted. This might include the Bureau of Science, Technology, and Industry for National Defense and the Equipment Development Department of the Central Military Commission. When the adjusted items have significant military applications, the Equipment Development Department of the Central Military Commission and the Bureau of Science, Technology, and Industry for National Defense are simultaneously involved. According to China's export control laws and regulations, relevant agencies of the Central Military Commission will participate in adjusting export control policies and reviewing and approving significant license applications for such items.

KPMG observations

The controlled items listed in the notice are all provided with HS Codes for reference, which helps export enterprises identify the controlled items. However, as described in the notice, these HS Codes are for reference only and cannot be solely based on confirming the control status of the items. In order to finally confirm the controlled conditions of the items, it is necessary to compare and analyze the information such as various performance parameters, characteristics, uses and materials of the items with the descriptions in the control list. During this process, if the enterprise cannot confirm whether the items are controlled or not, or encounters any problems in applying for a license, it should seek the assistance of a professional firm promptly, or contact the relevant government agencies.

Due to the technology-intensive industry attribute, the scope of controlled items includes a considerable part of technology and data, which are non-physical items. The export control of technology and data differs from that of physical items, raising the "deemed export" issue. For physical items, the license is verified by the Customs at the export clearance stage after obtaining the license. Non-physical items, such as technical information, are not subject to Customs clearance when exported or transferred overseas. In addition, under the Export Control Law, the supply of controlled items from Chinese citizens, legal persons, and organizations to foreign organizations and individuals is subject to export control, even if the process takes place entirely in China, i.e., the "deemed export" principle. Prior to technology export or technology transfer, relevant enterprises shall sort out all the technical information and data within the enterprise in advance, identify the controlled items, and implement corresponding management to prevent the unauthorized transfer of controlled technologies.

The notice also pointed out that products specially used for military purposes related to the categories mentioned above of controlled items need to be controlled following the Regulations of the PRC on Administration of Military Products Exports. Some dual-use items are very similar to military products in characteristics and parameters, but differ in export control management requirements. Suppose certain dual-use items have clear military and police purposes at the time of design or production. In that case, it is highly probable that they will be included in the scope of military product export control. In this regard, apart from classifying items according to the export control list of dual-use items and technologies, export enterprises should pay special attention to whether the products to be exported may fall within the scope of military product export control.

Based on the statistical analysis of the public data of China Customs, the major export destinations of the above-mentioned controlled items are the United States, South Korea, other Western countries, and Russia. Given recent international export control dynamics and China's countermeasures and sanctions against some US military-industrial enterprises, enterprises exporting such aerospace and special organic material items with potential military use should exercise particular caution. In addition to confirming the controlling status of the items, they should also conduct comprehensive due diligence on the relevant transactions to eliminate compliance risks related to the end-user and end-use.

From the corporate compliance perspective, enterprises that may be involved in the export control of dual-use items or restricted technologies should establish a sound internal compliance mechanism under the relevant government guidelines. China is adjusting the scope of controlled items from time to time and continuously improving its export control regulations and relevant enterprise facilitation measures. In August 2023, the Ministry of Commerce issued a notice to promote the pilot work of general licensing of dual-use items in Tianjin, Hebei, Shanghai, Jiangsu, Fujian, Shandong, Guangdong, and Hainan provinces. Establishing an internal compliance mechanism for export control by enterprises can not only help enterprises control the relevant compliance risks to the maximum, but also bring more convenience to enterprises in procedures such as applying for general export licenses.

If you have any questions about the above, please contact the relevant KPMG tax experts for further discussion.

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