

Comments on Export Controls and Intellectual Property Protection

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US Export Controls and IP Protection – China

Overview

US export control and intellectual property protection measures focused on China reflect a broad transition in bilateral relations.

Partner > Competitor/Adversary

From the 1990s US foreign policy and business establishments had taken a positive approach toward developing relations with China.

- China as a “responsible stakeholder;”
- Liberalized trade relations > progress toward political liberalization and strategic partnerships.

This mindset persisted despite aggressive Chinese actions on foreign investments, IP exploitation, intensified cyber espionage and growing regional tensions.

- Inevitable disillusionment thus more abrupt – and harsh.

Hard line toward China predates Trump administration, but has accelerated in context of strategic confrontation, trade disputes, and cyber espionage.

- Danger of over-reaction – from complacency to paranoia.
- An ongoing debate; priority on security vs. stifling of trade, investment, innovation.

US Export Controls and IP Protection – China

US Export Control Structure

Arms Export Control Act (AECA) – defense items and technologies on Munitions Control List; implemented through International Traffic in Arms Regulations (ITAR) administered by Department of State, Directorate of Defense Trade Controls (DDTC).

Export Administration Regulations (EAR) – defense-applicable commercial (dual-use) items and technologies under Commerce Control List; administered by Department of Commerce Bureau of Industry and Security (BIS).

Trade and economic regulations (sanctions programs) administered by the Department of Treasury Office of Foreign Assets Control (OFAC).

As applied to China

The US maintains a comprehensive embargo on defense exports China (items included in US Munitions List (USML) under ITAR – end products as well as components and technologies.

Under the “China Military Rule” the US government prohibits export of civil/dual-use items to China if there is reason to believe that they are intended for military end-use.

- Further Commerce restrictions on high-tech exports are pending
- Chinese entities often carry on both military and commercial activities; exporter responsible for assessing the legitimacy of end-use application and seeking government guidance.

US Export Controls and IP Protection – China

Transactions with Restricted Parties

US government lists of persons and entities restricted from trading with US persons and/or US-origin items (identified national security threats, supporters of terrorist activities, or criminal organizations).

- Debarred Parties List (convicted of AECA violations);
- Denied Persons List (barred from export activities under EAR);
- Entity List (cannot receive EAR-restricted items -- unless exception granted through a license review);
- Unverified List (foreign parties of unverified legitimacy; Commerce/BIS licenses required for all exports);
- Nonproliferation Sanctions List (foreign parties subject to sanctions under legislation or executive order);
- List of Specially Designated Nationals and Blocked Persons (OFAC list of persons and entities owned or controlled by sanctions-targeted countries; barred from transactions with US nationals).

These lists include a growing number of Chinese organizations.

- Trump Administration 05/15/19 Executive Order “Securing the Information and Communications Services Supply Chain” – prohibits transactions with entities “controlled by or subject to...a foreign adversary.”
- Huawei added to Entity List the following day.
- Several tech firms placed on Entity List this summer; more firms related to human rights abuses in October.

US Export Controls and IP Protection – China

Committee on Foreign Investments in the United States (CFIUS)

CFIUS established in 1975 to supervise foreign direct investments in the US.

- Multi-agency, chaired by Treasury Dept (with State, DoD, Commerce, White House)

CFIUS jurisdiction has since expanded to review of any national security concerns related to foreign investment in US companies.

- Blocked acquisition of a semi-conductor maker by a Chinese state-backed private equity firm; concern with IP transfer and national security need to protect the semi-conductor supply chain.

Foreign Investment Risk Review Modernization Act (FIRRMA) of 2018 greatly expanded CFIUS authority over investment in tech industries of interest to China.

- Chinese investment in US has almost collapsed as investors have turned to Europe.

IP protection measures are not limited to business investments.

- Several Chinese universities are now on the Commerce Dept's Unverified List.
- IP protection also seen in actions to limit visa stays for Chinese researchers and access to research grants from Chinese sources.
- Prosecutions of Chinese nationals working at US companies for economic espionage.

Export Controls – Japan and South Korea

National Security or Politics?

Actions by the Japanese and ROK governments to remove each other from their White Lists of preferred trade partners are justified as national security concerns, but in reality reflect the re-emergence of long-standing political tensions.

- The persistence of “history” issues in Japan-Korea engagement;
- Political leadership in both countries appear more focused on nationalist sentiment than broader consequences of deteriorating relations.

Damage to mutual interests – and regional security – from measure/counter-measure escalation only benefits adversaries.

- What will legalistic posturing in WTO accomplish?

Separate political grievances from what should be technical issues in application of export control measures:

- Establish working-level dialogue; adopt measures that would provide each side a way to agree their concerns have been addressed, for example:
- ROK – adjust export control processes to confirm compliance with UN sanctions on N Korea;
- Japan – restore ROK to White List, allowing ROK to reciprocate.

Japan in the International Defense Market

Basic Issues

GOJ policy states support for a strong defense industrial/technology base, but...

GOJ cannot meet this goal through continued subsidy of indigenous programs with little/no export potential.

- Captive market for JMoD procurement diminishing with increasing reliance on imports.
- Small profit margins from defense production; no incentive for industry to undertake R&D investments or market initiatives.

Only way forward is to engage international defense community. Continued isolation > an industrial/tech base left behind and left out.

Indigenous projects, licensed production may be necessary but are not sufficient.

Future for defense industry through international partnerships – multinational programs, two-way resource investments.

GOJ cannot not just control industry; must enable it.

- Incentives vs. subsidies.
- Effective institutional framework – export control and industrial security processes, more open approach to investments and multilateral programs.

Japan in the International Defense Market

Export Policy: Depends on Implementation

Three Principles (3Ps) Policy for Defense Exports (2014) is often misunderstood.

- A revision of earlier policy, not a “relaxation” of arms export restrictions.
- “No” has shifted to highly conditional “Maybe” – door unlocked, but not really open.
- On paper current 3Ps policy is similar to other countries; real differences lie in application – non-transparent process, uncertain precedents, lack of clear guidance.

Little to show for export actions over past five years:

- Some government-initiated transfers of surplus defense equipment to SE Asia.
- Other efforts to market end products (like maritime patrol aircraft) have failed over high costs and lack of awareness/credibility on the international market.
- Most ambitious attempt at defense export – Australia’s future submarine program – lost due to ineffective gov’t-industry coordination, inexperience in defense business.

Industry criticizes government for not supporting export activity; government criticizes industry for not pursuing potential opportunities in international markets.

Both are right; reflects years of “hot house” defense acquisition/industry culture.

Japan in the International Defense Market

What measures can Japan take to support defense export activity?

GOJ remains passive; may approve licenses, but does not support exports.

- Reluctant to accept defense exports as an instrument of national security/foreign policy; no reference to positive support for exports in guidance on revised 3Ps policy.
- No “marketing licenses” as understood elsewhere; industry advised to consult with GOJ officials before pursuing any initiative, but there is no standard mechanism to handle such inquiries.
- Transparent, timely action on licenses will build industry, and foreign partner confidence.
- Credible Information/industrial security processes to support greater participation in international programs –still a work in progress.

Building presence in the international market – an incremental, bottom-up process.

- Innovative (including dual-use) products will gain attention of defense agencies and industry;
- Use of Japan-produced components for third country defense equipment (some initial examples, but further success depends on implementing measures noted above).
- Defense industry partnerships mean more than exports; companies must invest overseas; GoJ must support them – and allow foreign investment in Japan.
- Companies must invest in business development; learn from inevitable failures on path to success.

Japan in the International Defense Market

How to safeguard exports of defense equipment?

Promotion of regional stability and global peace are necessary – but not sufficient – objectives for defense export policy.

- All legitimate participants in the international defense market must balance trade-offs among interests in national security and foreign policy goals with support/protection of their defense industrial/technology base.

Two outstanding issues in safeguarding defense exports from misuse: third party transfers and end-user guarantees.

- Not as difficult to manage in potential exports of Japanese products to a specific customer.
- Far more challenging in transfers of Japanese systems and components in support of international defense programs:
 - Supply of license-produced components to US prime for international user support (F-35 global supply chain, F100 engines parts, Patriot missile components);
 - Multinational defense programs (one or more partners, other export customers).
- It is not feasible to trace the flow of every component to every eventual end-user; must rely on clearly stated third party transfer provisions in licenses, and credible end-user guarantees on part of recipients.