China's Security Proposal for Hong Kong: Implications for U.S. Economic Sanctions

June 1, 2020

At the start of last week, the U.S. President announced that the United States would take action in response to a new national security law for Hong Kong. The following day, U.S. Secretary of State Pompeo informed Congress that "Hong Kong does not continue to warrant treatment under United States laws in the same manner as U.S. laws were applied to Hong Kong before July 1997."

At the same time, in the U.S. Congress, Senators Pat Toomey (R-Pa.) and Chris Van Hollen (D-Md.) introduced the "Hong Kong Autonomy Act" to authorize sanctions against persons determined to have interfered in Hong Kong's recognized autonomy, as well as any non-U.S. financial institution determined to have conducted a "significant" transaction with such a person.

Do these events mark new trade restrictions or compliance obligations? No, last week's events noted above have not (yet) established any new sanctions or similar trade restrictions against China and did not impose any new compliance obligations.

A separate proclamation limiting Chinese graduate students' entry to the United States becomes effective at 12:00 pm eastern standard time on June 1, 2020.

So what is the impact of the U.S. Secretary of State's statement to Congress? Secretary Pompeo's statement to Congress, although made pursuant to the Hong Kong Policy Act of 1992 ("HKPA"), does not trigger any particular consequences.

Rather, the HKPA authorizes the U.S. President, by executive order, to withdraw Hong Kong's recognition under U.S. law as distinct from China "whenever the President determines that Hong Kong is not sufficiently autonomous to justify treatment under a particular law of the United States, or any provision thereof, different from that accorded" to China.

Accordingly, it appears that the U.S. President must take some further step to effect consequences under the HKPA, which could be implemented selectively (*i.e.*, with respect to one or several U.S. laws) or comprehensively (*i.e.*, U.S. law in general).

What sanctions would be authorized by the proposed Hong Kong Autonomy Act? The Hong Kong Autonomy Act ("HKAA"), as currently proposed, calls for the Secretary of State to identify in an annual report any "foreign person" determined to have materially contributed to the "failure of the Government of China to meet its obligations" to respect Hong Kong's autonomy. The report also must identify "any foreign financial institution that knowingly conducts a significant transactions [sic] with the foreign person."

The HKAA would authorize blocking sanctions against any foreign person upon identification and would require such sanctions upon the person's second appearance on a report.

Identified non-U.S. financial institutions would face an escalating "menu" of potential consequences. Within one year of inclusion in any report, an identified non-U.S. financial institution must be subject to at least 5 of 10 potential consequences, ranging from denial of credit from U.S. banks and denials of visas for corporate officers to denial of goods subject to U.S. export controls and blocking sanctions. As currently drafted, all 10 consequences must be imposed within 2 years of a bank's inclusion in a report.

Are there other relevant sanctions-related authorities? Yes, there are several other statutes or sanctions programs that may authorize designations in these circumstances, including the following.

Most directly, the Hong Kong Human Rights and Democracy Act of 2019 authorizes blocking sanctions (asset freezes) against persons determined to be responsible for (i) "the extrajudicial rendition, arbitrary detention, or torture of any person in Hong Kong" or (ii) "other gross violations of internationally recognized human rights in Hong Kong."

More generally, the Global Magnitsky Act and OFAC's related Global Magnitsky Sanctions Regulations authorize sanctions against any foreign person determined to be (i) "responsible for or complicit in" any "serious human rights abuse" or (ii) a leader or official of an entity whose members have engaged in a serious human rights abuse. Sanctions also are authorized against any foreign person determined to have materially assisted or supported (i) a serious human rights abuse or (ii) any foreign entity that has committed such an abuse.

More broadly, the U.S. President has authority under the International Emergency Economic Powers Act ("IEEPA") to restrict transactions involving a foreign country or national after declaring a "national emergency" with respect to an "unusual and extraordinary threat" to the "national security, foreign policy, or economy of the United States," "which has its source in whole or substantial part outside the United States." See 50 U.S.C. § 1701. Once the U.S. President has made the required declaration of emergency, the president has wide-ranging powers, including to restrict dealings involving, or freezing, the property of foreign nationals and countries if that property comes into the hands of a person subject to the jurisdiction of the United States. 50 U.S.C. § 1702.

Beyond the current tension over Hong Kong, other issues also raise trade compliance implications. These include, earlier in May, the United States' expansion of U.S. export controls to restrict the delivery of certain foreign-made goods to Huawei, citing national security concerns. More recently, the White House, announcing new restrictions to prohibit entry to the United States to Chinese graduate students determined to further a "military-civil fusion strategy" designed "to bolster the modernization and capability" of China's military, called on the Secretaries of State and Homeland Security to propose further measures "that would mitigate the risk posed by the PRC's acquisition of sensitive United States technologies and intellectual property."

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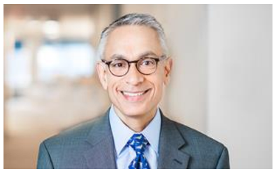

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