The Trump Administration Targets China with Additional Sanctions

November 17, 2020

The Trump Administration continues to impose further economic sanctions aimed at China, which some media reports indicate is part of the outgoing administration's attempt to bind President-elect Biden's options regarding U.S.-China relations. Last week, we saw two notable updates.

On November 12, 2020, President Trump signed Executive Order 13959, targeting transactions by U.S. persons in certain securities of designated "Communist Chinese military companies" ("CCMC"). This was preceded earlier in the week with the sanctioning of four more Chinese officials for their role in implementing the new National Security Law for Hong Kong.

SANCTIONS AGAINST THE CHINESE MILITARY COMPANIES

Citing a threat to U.S. national security posed by China's military-industrial complex, President Trump issued Executive Order 13959 to prevent U.S. investors from financing the development and modernization of China's military. The restrictions in the Executive Order do not take effect until January 11, 2021, as discussed further below.

What New Restrictions Are Imposed Under the E.O. 13959?

- The Executive Order prohibits "any transaction in publicly traded securities, or any securities that are derivative of, or are designed to provide investment exposure to such securities, of any Communist Chinese military company" by any U.S. person.

- A "transaction" is defined narrowly as "the purchase for value of any publicly traded security." Thus, the Executive Order does not appear to bar a U.S. person from (a) continuing to hold already-owned CCMC securities, (b) selling CCMC securities to a non-U.S. person (at least until November 11, 2021, when the authorization to sell CCMC securities appears to expire) or (c) receiving a cash dividend or interest payment on a CCMC security.

- The Order defines "securities" by reference to U.S. federal securities laws and provisions of the Securities Exchange Act of 1934. The Order does not define "publicly traded," but the Order also does not appear limited to securities that are publicly traded in the United States. Thus, CCMC securities that are publicly traded outside the United States (*e.g.*, in securities markets in China or Hong Kong) are restricted by the Order.

- It is unclear what is meant in the Order by "securities that are derivative of" or "designed to provide investment exposure" to CCMC securities. For example, it is unclear whether U.S. persons may invest in exchange-traded funds or other vehicles that themselves have invested in CCMC securities. Future guidance may be necessary to address this question.

Who Must Comply with the New Restrictions Under E.O. 13959?

- The restrictions apply to "U.S. persons," which term is defined consistently with its use in U.S. sanctions programs—(i) any U.S. citizen or permanent resident; (ii) any entity organized under U.S. law, wherever doing business; or (iii) any person physically present in the United States, regardless of nationality.

- The Executive Order does not, by its terms, extend to entities organized outside the United States, including non-U.S. companies owned or controlled by U.S. persons (that are operated from abroad).

What Are Communist Chinese Military Companies?

- The Order defines CCMCs with respect to Section 1237 of Public Law 105-261, the National Defense Authorization Act for 1999. Earlier this year, pursuant to Section 1237, the U.S. Defense Department published two separate lists identifying 31 companies as CCMCs.[1]

- The Order also authorizes future designations by either (i) the U.S. Secretary of Defense, in consultation with the U.S. Treasury Secretary, or (ii) the U.S. Treasury Secretary.

When Do the Restrictions Apply?

- For the 31 companies already identified as CMCCs, the restrictions become effective on 9:30 am EST on January 11, 2021.

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1 Both lists currently may be accessed here: https://www.defense.gov/Newsroom/Releases/Release/Article/2328894/dod-releases-list-of-additional-companies-in-accordance-with-section-1237-of-fy/.

- Restrictions against companies designated in the future become effective 60 days after their designation.

Which Department or Agency Is Implementing E.O. 13959?

- Although not entirely clear yet, the Order tasks the U.S. Treasury Secretary (in consultation with the Secretary of State and, as appropriate, the Secretary of Defense) with submitting to Congress certain related reports, and the Office of Foreign Assets Control ("OFAC") within the Treasury Department has filed a notice of the Executive Order on its website.

- Accordingly, it appears that OFAC, which is tasked with implementing and enforcing U.S. sanctions, including financial restrictions, may implement Executive Order 13959. If that is the case, we think that, consistent with its historical practice in administering U.S. sanctions programs, OFAC may issue clarifying guidance prior to these restrictions becoming effective.

Can the Biden Administration Withdraw or Change the Order?

- Because this is an Executive Order, it would be within the incoming administration's authority to revise or revoke the Order after President-elect Biden is inaugurated on January 20.

- Many commentators believe President Biden will have other priorities and will not turn to revising restrictions on China. Additionally, during the campaign, Biden signaled a desire to be "tough on China." Thus, the restrictions in the Order appear unlikely to be revised immediately on change of administration.

ADDITIONAL SANCTIONS RELATED TO HONG KONG

Last week, the U.S. State Department designated another four senior Chinese and Hong Kong officials, accusing them of undermining Hong Kong's autonomy and freedoms (a charge that is, of course, denied by China and the relevant individuals). This action brings the total to 15 individuals who are now subject to U.S. sanctions for their roles with respect to China's relationship and dealings with Hong Kong (see our earlier Updates here and here).

As a reminder, the U.S. Treasury Department currently is preparing a report that will identify foreign financial institutions ("FFIs") that it determines have "knowingly conducted significant transactions" with 10 of the individuals designated earlier. Inclusion in that report would result in sanctions against the named FFIs (see our related Update here).

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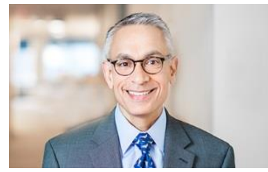

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