

CLIENT ALERT

President Biden Revises the Trump Administration's Prohibition on Investments in Chinese Military-Industrial Complex Companies

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Placing the investment restrictions for listed Chinese companies on firmer legal footing, President Biden, on June 3, 2021, issued [Executive Order 14032](#) ("E.O. 14032"), which amends the scope of [E.O. 13959](#) (issued by President Trump on November 12, 2020). E.O. 14032 prohibits certain dealings by U.S. persons in publicly traded securities, or any securities that are derivative of, or are designed to provide investment exposure to such securities, of any Chinese Military-Industrial Complex Companies ("CMICs"). Additionally, the Office of Foreign Assets Control ("OFAC") provided additional guidance in the form of [Frequently Asked Questions](#) ("FAQs") clarifying the scope of E.O. 14032.

E.O. 14032 clarifies and slightly modifies the scope of the prohibitions under E.O. 13959, changes the designation criteria for targeting CMICs under E.O. 14032, and shifts the primary responsibility for designating such companies from the Defense Department to the Treasury Department. Additionally, E.O. 14032 replaces the Non-SDN Communist Chinese Military Companies Sanctions List with a new [Non-SDN Chinese Military Industrial Complex Companies List](#) ("NS-CMIC List"). OFAC has clarified that the restrictions only apply to the securities of companies that exactly match an entry on the NS-CMIC List, which impacts the applicable deadlines for compliance (as discussed below).

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I. Revised Prohibitions on Investments in Chinese Securities

E.O. 14032 fully replaces the prohibitions in E.O. 13959 and revokes [E.O. 13974](#), which was issued by the Trump administration to make minor clarifications to some of the language in E.O. 13959. Like E.O. 13959, E.O. 14032 contains language that prohibits the purchase or sale by U.S. persons of any publicly traded securities, or any publicly traded securities that are derivative of such securities or are designed to provide investment exposure to such securities, of any person listed in the Annex to E.O. 14032. However, the new prohibitions take effect on August 2, 2021. As a result, there are no current prohibitions on these securities, and none will be in effect until August 2. Furthermore, U.S. persons are permitted to buy and sell such securities between August 2, 2021 and June 3, 2022, so long as the purchases and sales are made solely for the purpose of divesting, in whole or in part, from such securities, meaning U.S. persons can divest as well as close short positions until June 3, 2022.

OFAC has adopted its original guidance that U.S. persons may facilitate purchases and sales of covered securities, and has gone even further to say that a U.S. investment adviser to an off-shore fund can authorize purchases and sales by that offshore fund. Specifically, OFAC’s guidance in FAQ 902 confirms that U.S. persons are not prohibited from providing investment advisory, investment management, or similar services to a non-U.S. person, including a foreign entity or foreign fund, in connection with the non-U.S. person’s purchase or sale of a covered security. Additionally, new guidance in FAQ 903 makes clear that U.S. persons employed by non-U.S. entities are not prohibited from being involved in, or otherwise facilitating, purchases or sales related to a covered security on behalf of their non-U.S. employer, provided that such activity is in the ordinary course of their employment and the underlying purchase or sale would not otherwise violate the sanctions.

II. Shift in Designation Authority and Criteria

E.O. 14032 also shifts the designation authority from the Department of Defense to the Department of the Treasury and away from entities that would be considered Communist Chinese Military Company (“CCMC”) pursuant to Section 1237 of Public Law 105-261, as amended. Under E.O. 13959, the designation authority was based on the definition of CCMC in Section 1237 of Public Law 105-261, as amended, meaning entities owned or controlled by, or affiliated with, the People’s Liberation Army, any ministry of the People’s Republic of China, or an entity affiliated with the defense industrial base of China. In contrast, E.O. 14032 authorizes the Secretary of the Treasury to designate entities determined to operate or have operated in the defense and related materials sector or the surveillance technology sector of the Chinese economy. FAQ 900 states that OFAC will use its discretion to target persons whose operations include or support “(1) surveillance of persons by Chinese technology companies that occurs outside of the PRC; or (2) the development, marketing, sale, or export of Chinese surveillance technology that is, was, or can be used for surveillance of religious or ethnic minorities or to otherwise facilitate repression or serious human rights abuse.”

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III. List of Chinese Companies Remains Static, but Could Grow in the Future

E.O. 14032 includes an updated list of Chinese companies included in the NS-CMIC List, which currently includes 59 entities. Notably, Xiaomi Corporation and Luokung Technology Corporation, two entities that successfully challenged their original designation as a CCMC in federal court and for which OFAC had suspended the restrictions, were not included in the Annex to E.O. 14032 or the new NS-CMIC List. Significantly, OFAC clarified in FAQ 857 that the restrictions imposed by E.O. 14032 only apply to the securities of companies that exactly match an entry on the NS-CMIC List, and confirms that the prohibitions do not apply to subsidiaries of CMICs unless such subsidiary itself is publicly listed on the NS-CMIC List.

For companies added to the NS-CMIC List in the future, the prohibitions will take effect 60 days after the date the person is listed with transactions for the sole purpose of effecting a divestment from the securities of that person permitted for one year after the date the person is listed. The shift in designation authority and the new focus on entities operating in the defense and related materiel sector or the surveillance technology sector of the Chinese economy may pave the way for the designation of entities that would not have been captured by the definition of Communist Chinese Military Company in E.O. 13959. Additionally, OFAC's stated focus on the use of surveillance technology, specifically for the purpose of facilitating repression and serious human rights abuse, indicates that we may see additions to the NS-CMIC List related to the suppression of protests in Hong Kong and the human rights abuses being committed against the Uyghur population in Xinjiang. Additionally, the successful challenges by Xiaomi Corporation and Luokong Technology Corporation may lead to additional challenges by entities listed on the NS-CMIC List and cause additional changes to the list prior to August 2, 2021.

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