



China's Unreliable Entity List Provisions: Fighting Fire with Fire?

22 September 2020

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On September 19, 2020, China's Ministry of Commerce (MOFCOM) issued the *Provisions on the Unreliable Entity List* (the "UEL Provisions").¹ The UEL Provisions establish formal mechanisms for sanctioning specific foreign entities and individuals for conduct inconsistent with the Chinese government's core interests and policies, further complicating the management of regulatory, reputational, and political risks for companies operating in Asia.

Equipping Beijing with New Sanctions Tools

Chinese companies and individuals have increasingly been designated by foreign governments as subject to economic sanctions, export controls, procurement bans, operating restrictions, investment reviews, and other economic measures of foreign policy and security policy. In response, the Chinese government has adopted or reinvigorated analogous laws and procedures. The long-dormant national security review process under the National Development and Reform Commission—China's counterpart to the Committee on Foreign Investment in the United States (CFIUS)—has become more active. The "Catalogue of Technologies Prohibited or Restricted from Export" was amended in August 2020 to include a wide range of technologies, and the new Export Control Law has completed its second reading before the National People's Congress.

The UEL Provisions, in turn, equip Beijing with a general framework for economic sanctions. Chinese authorities publicly announced plans to establish a list of "unreliable" foreign entities in May 2019, and subsequently plans to sanction certain foreign companies and officials connected with U.S. government measures affecting China. The final UEL Provisions appeared together with an official English translation on a Saturday—one day before restrictions on the U.S. operations of Chinese-owned online applications WeChat and TikTok were slated to take effect. The timing underscores the Chinese government's readiness to respond in kind to foreign sanctions, export controls, and other measures targeting Chinese entities and individuals.

List-Based Sanctions Regime

The UEL Provisions establish a "list-based" sanctions regime through which specific foreign entities may be added to a published Unreliable Entity List (UEL). A "foreign entity" may include any foreign enterprise, other organization or individual.²

The UEL is the PRC's first general list-based sanctions framework. Similar list-based approaches appear within the economic sanctions and export controls regimes of many other jurisdictions, including the U.S., the E.U., and Australia. Whereas "comprehensive" sanctions programs apply to broad categories of companies and products from targeted countries or sectors, list-based sanctions enable governments to focus punitive measures on particular companies, organizations, and individuals engaged in conduct deemed objectionable. In the same vein, the threat that a specific

company or organization might be designated on a sanctions list as a result of its own commercial conduct may deter owners and managers from actions that might attract sanctions in the future.

No foreign entities have yet been formally included in the UEL.

Sanctionable Conduct and Extraterritorial Effect

Foreign entities may be designated in the UEL based on conduct in "international economic, trade and other relevant activities" either: (1) "endangering national sovereignty, security or development interests of China"; or (2) "suspending normal transactions with" or "applying discriminatory measures against" a Chinese "enterprise, other organization, individual" which "violates normal market transaction principles and causes serious damage to the legitimate rights or interests" of the Chinese party.³

Significantly, the UEL Provisions allow sanctions to be imposed in response to conduct occurring outside China—one of the few Chinese laws applying extraterritorially.

The decision to designate a foreign entity on the UEL should be based on: (1) "the degree of danger to national sovereignty, security or development interests of China"; (2) "the degree of damage to the legitimate rights and interests of enterprises, other organizations, or individuals of China"; (3) whether the foreign entity acted "in compliance with internationally accepted economic and trade rules"; and (4) any other relevant factors.⁴

The scope of sanctionable conduct is potentially broad. While many other jurisdictions allow economic sanctions in response to threats to national security or national sovereignty, conduct endangering China's "development interests" might encompass a wide range of competitive practices clashing with industrial policy or trade policy goals.

Authorizing sanctions against foreign companies for "suspending" business with Chinese parties or "discriminating" against Chinese parties may be intended to neutralize foreign governments' sanctions and export control measures against Chinese companies. For example, third-country companies may face liability under U.S. law in certain circumstances for using U.S.-origin technology, equipment, and inputs to supply certain Chinese companies or for dealing with sanctioned Chinese parties. Third-country suppliers seeking to avoid U.S. sanctions and export control risks often abstain from high-risk business with Chinese customers. Under the UEL Provisions, such third-country suppliers may now face Chinese sanctions for cutting off supply to Chinese customers. It is unclear how a defense of "foreign sovereign compulsion" by a U.S. supplier or a third-country supplier would fare under the UEL Provisions.

Potential Sanctions

The UEL Provisions authorize a broad spectrum of sanctions on designated foreign entities.⁵ Sanctions may include restrictions or prohibitions on the foreign entity's China-related import or export activities, on the foreign entity's investment activities in China, on the entry into China of the foreign entity's personnel or "means of transportation," or on the work permits and visa status of the foreign entity's personnel. Other penalties may include fines or "other necessary measures."

On its face, the text of the UEL Provisions would allow many measures applied through foreign sanctions and export control regimes: government procurement bans; bans on all transactions by Chinese persons with blacklisted entities; surgical restrictions on business operations; suffocating denials of visas and permits; or even freezing or seize of assets. Restrictions on designated foreign entities' investment activities might apply to new investments, or might extend to orders requiring divestment or restructuring of existing investments. The authorization of "fines" as a possible sanction, moreover, raises the possibility that actions contrary to Chinese government interests might result in administrative penalties.

The UEL Provisions provide no further guidance on the precise penalties for particular conduct. While the UEL Provisions do not explicitly provide that foreign-invested enterprises in China may be sanctioned for the offshore conduct of foreign parent companies or affiliates, the regulatory context suggests that such measures would be permitted under the UEL Provisions.

Enforcement Mechanism

The UEL Provisions contemplate the establishment of an inter-ministerial "Working Mechanism" consisting of relevant central government ministries and departments to conduct investigations and make decisions.⁶ An office of the Working Mechanism to support its activities will be established within the Ministry of Commerce (potentially within the Bureau of the Industrial Security and Import/Export Control).

Designations and Compliance Deadlines

The Working Mechanism has broad discretion to investigate potential grounds for sanctioning foreign entities by collecting evidence through various channels, and it may allow the foreign enterprise to present a defense.⁷ However, where the facts are "clear," the Working Mechanism may proceed with a UEL designation.⁸

Foreign entities are to be added to the UEL through a public announcement including "an alert about the risks of conducting transactions" with the designated foreign entity.⁹

Notably, the UEL expressly authorizes conditional designations setting a time limit for a foreign entity to "rectify" its conduct and thus avoid the implementation of sanctions.¹⁰

Permitting System

The UEL Provisions provide that Chinese entities may apply for permits to conduct otherwise-prohibited import or export transactions with foreign entities listed on the UEL, similar to the licensing procedures under the U.S. economic sanctions and export control schemes.¹¹

Implications

The UEL Provisions enable the Chinese government to use the threat or imposition of economic sanctions to deter and penalize conduct inimical to Chinese government interests and policies by foreign businesses, organizations, and entities. Amidst escalating trade tensions and pressures to "de-couple" China from other markets, multinational companies active in Asia may face clashing directives from the sanctions regimes of China, the U.S., and other jurisdictions.

[1] Bukekao Shiti Qingdan Guiding (《不可靠实体清单规定》) [Provisions on the Unreliable Entity List] (promulgated by the Ministry of Commerce on September 19, 2020 with immediate effect), <http://www.mofcom.gov.cn/article/b/fwzl/202009/20200903002593.shtml> (in Chinese), <http://english.mofcom.gov.cn/article/policyrelease/questions/202009/20200903002580.shtml> (the official English translation).

[2] UEL Provisions, Art. 2.

[3] UEL Provisions, Art. 2.

[4] UEL Provisions, Art. 7.

[5] UEL Provisions, Art. 10 provides that "the working mechanism may, based on actual circumstances, decide to take one or several of the following measures (hereinafter referred to as "the measures") with respect to the foreign entity which is included in the Unreliable Entity List, and make an announcement of the decision: (1) restricting or prohibiting the foreign entity from engaging in China-related import or export activities; (2) restricting or prohibiting the foreign entity from investing in China; (3) restricting or prohibiting the foreign entity's relevant personnel or means of transportation from entering into China; (4) restricting or revoking the relevant personnel's work permit, status of stay or residence in China; (5) imposing a fine of the corresponding amount according to the severity of the circumstances; (6) other necessary measures".

[6] UEL Provisions, Art. 4.

[7] UEL Provisions, Art. 5 and Art. 6.

[8] UEL Provisions, Art. 8 provides that "where the facts about the actions taken by the relevant foreign entity are clear, the working mechanism may, by taking into overall consideration the factors specified in Article 7 of these Provisions, directly make a decision on whether to include the relevant foreign entity in the Unreliable Entity List; if a decision is made to include in the Unreliable Entity List, an announcement shall be made".

[9] UEL Provisions, Art. 9.

[10] UEL Provisions, Art. 9 and Art. 11.

[11] UEL Provisions, Art. 12 provides that "where, under special circumstances, it is necessary indeed for an enterprise, other organization, or individual of China to conduct transactions with the foreign entity that is restricted or prohibited from engaging in China-related import or export activities, an application shall be submitted to the Office of the working mechanism, then the transactions with the foreign entity in question may be conducted upon approval".

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