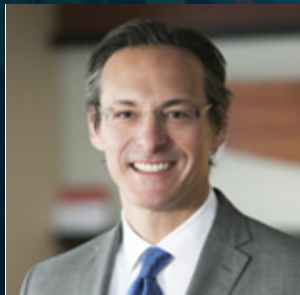


Morgan Lewis

Morgan Lewis Hedge Fund University™

THE SANCTIONS LANDSCAPE

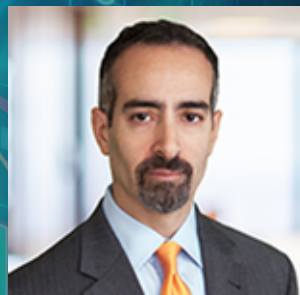
June 8, 2023



Timothy W. Levin
Partner
Philadelphia



Todd Liao
Partner
Shanghai/Boston

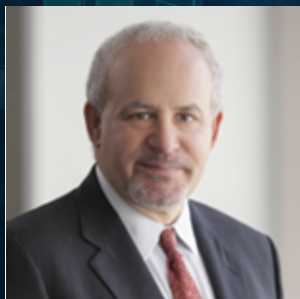


David Plotinsky
Partner
Washington, DC



Vasilisa Strizh
Partner
Boston

Presenters



Carl A. Valenstein
Partner
Boston



Katelyn M. Hilferty
Associate
Washington, DC



David Mendelsohn
Manager – Government Affairs
Washington, DC

Sanctions Considerations for Investment Funds

Morgan Lewis

Sanctions Considerations for Investment Funds

Office of Foreign Assets Control (OFAC)

- Comprehensive sanctions (Iran; Cuba; N. Korea; Syria; Crimea, Luhansk, and Donetsk regions of Ukraine)
 - Prohibit most or all activities based on the country
- Targeted sanctions
 - Prohibit activities primarily based on the person or entity
- Hybrid sanctions (Russia, Venezuela)
- Specially Designated Nationals (SDNs)
 - Individuals, groups, entities
 - Includes entities owned 50% or more by an SDN (or more than one SDN)

Sanctions Considerations for Investment Funds

- Screening the fund itself
 - Searching the term “Fund” on the SDN list today yields 54 “hits”
- More difficult when joining a legitimate fund, usually overseas, not subject to US sanctions, that may accept funds from SDNs
 - Are you now “in business” with an SDN?
 - Requires a detailed, and sometimes nuanced, analysis



Sanctions List Search

This Sanctions List Search application (“Sanctions List Search”) is designed to facilitate the use of the Specially Designated Nationals and Blocked Persons List (“SDN List”) and all other sanctions lists administered by OFAC, including the Foreign Sanctions Evaders List, the List of Persons Identified as Blocked Solely Pursuant to E.O. 13599, the Non-SDN Iran Sanctions Act List, the Part 561 list, the Sectoral Sanctions Identifications List and the Non-SDN Palestinian Legislative Council List. Given the number of lists that now reside in the Sanctions List Search tool, it is strongly recommended that users pay close attention to the program codes associated with each returned record. These program codes indicate how a true hit on a returned value should be treated. The Sanctions List Search tool uses approximate string matching to identify possible matches between word or character strings as entered into Sanctions List Search, and any name or name component as it appears on the SDN List and/or the various other sanctions lists. Sanctions List Search has a slider-bar that may be used to set a threshold (i.e., a confidence rating) for the closeness of any potential match returned as a result of a user’s search. Sanctions List Search will detect certain misspellings or other incorrectly entered text, and will return near, or proximate, matches, based on the confidence rating set by the user via the slider-bar. OFAC does not provide recommendations with regard to the appropriateness of any specific confidence rating. Sanctions List Search is one tool offered to assist users in utilizing the SDN List and/or the various other sanctions lists; use of Sanctions List Search is not a substitute for undertaking appropriate due diligence. The use of Sanctions List Search does not limit any criminal or civil liability for any act undertaken as a result of, or in reliance on, such use.

[Download the SDN List](#)

[Visit The OFAC Website](#)

[Download the Consolidated Non-SDN List](#)

[Program Code Key](#)

Lookup

Type:	All	Address:	
Name:	fund	City:	
ID #:		State/Province*:	
Program:	All 561List BALKANS BELARUS	Country:	All
Minimum Name Score:	100	List:	All

Lookup Results: 35 Found

Name	Address	Type	Program(s)	List	Score
FAR EAST AND BAIKAL REGION DEVELOPMENT FUND OJSC	d. 82 str. 2 ul. Sadovnicheskaya	Entity	UKRAINE-E013662	Non-SDN	100
OJSC THE FAR EAST AND BAIKAL REGION (DFVFI OPMFNT FUND)	d. 82 str. 2 ul. Sadovnicheskaya	Entity	UKRAINE-F013662	Non-SDN	100

Sanctions Considerations for Investment Funds

Rules of the Road:

- Passive investment is not immune to sanctions
- Diligence is required
- Know the fund and its participants
 - Assurance that no SDNs are among the investors
 - Restrictive language or exit rights
 - Understanding of who is responsible for doing the diligence, and what will be reported
 - OFAC example of a situation that creates higher risk and requires “heightened scrutiny”
 - “US hedge fund with an offshore related fund where beneficial owners are offshore investors”
- Avoid facilitation
 - Actions by US persons that “assist or support” prohibited activities
 - Includes (sometimes confused with) circumvention (also prohibited)—attempting to indirectly do that which may not be done directly by a US person
- Best practices
 - Contractual limits against use of US investors’ funds to support businesses with sanctioned countries or SDNs
 - If more than passive (e.g., any US investor governance participation), a US person must not participate in or take action to facilitate sanctioned activities

Selected Enforcement Actions

- **May 12, 2012:** Genesis Asset Managers (GAM) settled alleged single violation of the Iranian Transactions Regulations by remitting \$112,500 to OFAC
 - GAM's UK affiliate, acting as an agent of GAM US, purchased approx. \$3M in shares in the First Persian Equity Fund, a Cayman Islands company that invests exclusively in Iranian securities
- **June 30, 2022:** OFAC blocked Heritage Trust, a Delaware-based trust in which an OFAC-designated Russian oligarch had property interest in assets valued over \$1B
 - Funds of trust were invested in large public and private US companies and managed by a series of US investment firms and facilitators

Overview of Recent US Sanctions Against Russia Affecting Investment Funds

Morgan Lewis

Summary of US Actions Affecting Investment Funds

- **February 21, 2022: President Biden issues EO 14065**
 - In response to Russia recognizing the LNR/DNR
 - Extended 2014 Crimea region comprehensive sanctions to LNR/DNR
 - Mirrored the approach taken through the Crimean EO and sanctions regulations
- **February 22, 2022: Tranche #1**
 - Blocking sanctions on VEB.RF and Promsvyazbank
 - Sovereign debt prohibitions
 - Adds five “Members of the Russian Elite” to SDN List
- **February 23, 2022: Nord Stream 2 AG and its corporate officers sanctioned**
- **February 24, 2022: Tranche #2**
 - Blocking Sanctions on VTB, Otkritie, Sovcombank and Novikombank
 - CAPTA sanctions on Sberbank
 - Debt and equity restrictions on 13 Russian SOEs
 - Further sanctions on “Russian Elites”
 - Export restrictions
- **February 25, 2022: OFAC adds Russian leadership (Putin, Shoigu, Lavrov, and Gerasimov) to the SDN List**
- **February 26-28, 2022: Tranche #3**
 - Released in coordination with G-7 partners
 - Committed to remove certain Russian banks from SWIFT
 - Targeted Russian Central Bank, Ministry of Finance and Direct Investment Funds
 - Announced intent to form transatlantic task force to target sanctioned persons
- **March 3, 2022: Blocking sanctions on Russian elites and employees of online media sites**
- **March 8, 2022: President Biden issues EO 14066**
 - Prohibited imports into the US of Russian-origin crude oil, petroleum, petroleum products, LNG, coal, and coal products
 - Prohibited new investment in the energy sector of Russia by US persons
- **March 11, 2022: President Biden issues EO 14068**
 - Prohibited imports into the US of Russian-origin fish, seafood, and preparations; alcoholic beverages; non-industrial diamonds; and other products designated by OFAC
 - Prohibited exports from the US or by US persons of luxury goods and US dollar-denominated banknotes to Russia
 - Prohibited new investment in any sector of the Russian economy as determined by OFAC

Summary of US Actions – Cont'd

- **March 24, 2022: Tranche #4**
 - Targeted Russia's defense-industrial base, the Russia Duma and its members, and Sberbank CEO
- **March 31, 2022: OFAC issues determination under EO 14024; targets evasion networks and Russian technology companies**
 - Secondary sanctions may be imposed on persons operating in the aerospace, electronics, and marine sectors of the Russian economy
- **April 6, 2022: Tranche #5; President Biden issues EO 14071**
 - OFAC imposed full blocking sanctions on Sberbank and Alfa-Bank
 - OFAC sanctioned family members of Putin and Russian Security Council members
 - EO 14024 bans new investment in Russia and provision of certain services to persons in Russia by US persons
- **April 7, 2022: OFAC sanctions Alrosa and United Shipbuilding Corporation**
- **April 20, 2022: OFAC targets entities and individuals alleged to be involved in US sanctions evasion**
- **May 8, 2022: Tranche #6**
 - Targeted financial executives, Russian weapons manufacturer, and state-controlled television stations
- OFAC issued determination pursuant to EO 14071 prohibiting exports of accounting, trust and corporate formation, and management consulting services to Russia
- OFAC designated accounting, trust and corporate formation, and management consulting services sectors of Russian economy
- BIS expanded scope of items subject to Russian industry sector export controls
- **June 2, 2022: OFAC sanctions Kremlin elites and certain yachts and aircraft**
- **June 28, 2022: Tranche #7**
 - Implemented G-7 commitments
 - Targeted entities critical to Russia's defense industrial base, including Rostec
 - Designations taken in tandem with US Dept. of State
 - OFAC prohibited importation of Russian gold into the US
 - FinCEN issued joint alert with BIS related to export control evasion
- **August 2, 2022: OFAC sanctions additional Kremlin-connected elites**
- **September 15, 2022: OFAC issues additional determinations under EO 14024 targeting the quantum computing sector; targets additional Russian officials**
- **September 30, 2022: OFAC sanctions international suppliers for supporting Russia's defense sector**

Summary of US Actions – Cont'd

- **November 14, 2022: OFAC sanctions global Russian military supply chain, Kremlin-linked networks, and Kremlin-linked elites**
- **November 15, 2022: OFAC targets actors involved in production and transfer of Iranian drones to Russia for use in Ukraine**
- **November 22, 2022: OFAC issues determination under EO 14071**
 - Targeted services related to maritime transport of Russian origin crude oil
- **December 5, 2022: OFAC determines price cap on Russian origin crude oil**
- **December 15, 2022: OFAC targets entities in Russia's financial services sector**
 - Including Rosbank and certain VTB subsidiaries
- **December 22, 2022: State designates 10 Russian naval entities**
- **February 1, 2023: OFAC targets individuals and entities related to sanctions evasion network**
- **February 3, 2023: OFAC issues determinations under EO 14071 related to price cap for crude oil**
- **February 24, 2023: Tranche #8**
 - Actions taken in coordination with G-7
 - New determination targeting metals and mining sector
 - Additional financial services sector sanctions
 - Designations of entities that operate in Russian aerospace, technology, and electronics sectors
 - BIS expanded scope of industry sector restrictions and luxury goods sanctions
- **May 19, 2023: Tranche #9**
 - Actions taken in coordination with G-7
 - Designations targeting Russian evasion and procurement networks and Russian Foreign Intelligence Service
 - New determination targeting architecture, engineering, construction, manufacturing, and transportation sectors
 - BIS added 71 entities to the Entity List

United States: General Licenses – Broad Overview

- As with prior sanctions programs, the OFAC has issued a series of Directives, and simultaneously General Licenses; the Directives identify restricted activities while the General Licenses authorize specific actions (often for select periods) to enable a more orderly and effective implementation of those sanctions.
- The Russia General Licenses (GLs) allow
 - Short-term wind-down activities — i.e., time to divest debt or equity holdings of specific entities; certain after-market activities
 - Specific types of activities — i.e., the export to various Ukrainian regions of food, medicine and medical devices; personal remittances; NGO activity, etc.
- The GLs also allow for telecommunications and internet services to remain operational and mail services to continue.

Selected General Licenses Relevant to Investment Funds

- **General License No. 8G:** Authorizes until November 1, 2023 otherwise prohibited transactions “related to energy” that involve VEB Bank, Bank Otkritie, Sovcombank, Sberbank, VTB Bank, Alfa-Bank, Rosbank, Bank Zenit, Bank Saint-Petersburg, or their subsidiaries, or the Central Bank of Russian Federation. Among other things, “related to energy” means extraction, production, refinement, or purchase of petroleum, as well as the development, production, generation, transmission, or exchange of power.
- **General License No. 14:** Authorizes transactions prohibited by Directive 4 under EO 14024 involving the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, or the Ministry of Finance of the Russian Federation (Directive 4 entities), where the Directive 4 entity’s sole function is to act as an operator of a clearing and settlement system, provided that (i) there is no transfer of assets to or from any Directive 4 entity; and (ii) no Directive 4 entity is either a counterparty to or a beneficiary of the transaction.
- **General License No. 46:** Authorizes certain transactions related to the auction process announced by the EMEA Credit Derivatives Determination Committee to settle credit derivative transactions with a reference entity of “the Russian Federation” and prohibited under EO 14071.

Selected General Licenses

- **General License No. 63:** Authorizes transactions ordinarily incident and necessary to the divestment or transfer of debt or equity of Metalloinvest or its subsidiaries purchased prior to April 12, 2023, to a non-US entity through 12:01 a.m. EDT, July 11, 2023
 - Also authorizes all transactions ordinarily incident to facilitating, clearing, and settling trades of covered debt or equity placed prior to April 12, 2023, until July 11, 2023
 - Also authorizes transactions ordinarily incident to the wind-down of derivative contracts entered prior to April 12, 2023, that include a blocked Metalloinvest entity as a counterparty or are linked to covered debt or equity until July 11, 2023, provided that payments to a blocked person are made into a blocked account
- **General License No. 67:** Authorizes transactions ordinarily incident and necessary to the divestment or transfer of debt or equity of Polyus or its subsidiaries purchased prior to May 19, 2023, to a non-US entity through 12:01 a.m. EDT, August 17, 2023
 - Also authorizes all transactions ordinarily incident to facilitating, clearing, and settling trades of covered debt or equity placed prior to May 19, 2023, until August 17, 2023
 - Also authorizes transactions ordinarily incident to the wind-down of derivative contracts entered prior to May 19, 2023, that include a blocked Polyus entity as a counterparty or are linked to covered debt or equity until August 17, 2023, provided that payments to a blocked person are made into a blocked account
- **General License No. 69:** Authorizes transactions ordinarily incident and necessary to the processing of interest or principal payments on debt securities issued by International Investment Bank (IIB) prior to April 12, 2023 through 12:01 a.m. EDT, June 30, 2023, provided that such payments are not made to persons located in Russia and that any payments to a blocked person are made into a blocked account

OFAC FAQs Relevant to Investment Funds

- **Russia Harmful Foreign Activities Sanctions FAQ #1049**

- Defines what is meant by the term “new investment” as used in EOs 14066, 14068, and 14071 (i.e., the EO’s that prohibit new investment in Russia)
- New investment = the commitment of capital or other assets for the purpose of generating returns or appreciation made on or after the effective date of the relevant EO
- New investment does not include “maintenance” of an investment made prior to the applicable effective dates

- **Russia Harmful Foreign Activities Sanctions FAQ #1050**

- Defines types of transactions considered to be “maintenance” activities and therefore outside of the scope of the “new investment” prohibitions
- Generally, “maintenance” includes all transactions ordinarily incident to performing under an agreement in effect prior to the effective date of the respective EO prohibitions, provided that such transactions are consistent with previously established practices and support pre-existing projects or operations
- However, “maintenance” does not include expansion of pre-existing projects or operations beyond those in effect prior to the effective dates
- “Maintenance” also does not include commitments pursuant to exercise of rights under pre-existing agreement where such commitment is made on or after effective dates

Relevant OFAC FAQs – Cont'd

- **Russia Harmful Foreign Activities Sanctions FAQ #1053**

- Explains that transactions related to divestment in a pre-existing project or operation in Russia are permissible so long as no blocked person is involved

- **Russia Harmful Foreign Activities Sanctions FAQ #1054**

- Confirms that the EOs prohibit US persons from purchasing both new and existing debt and equity securities issued by an entity in Russia, but do not prohibit US persons from selling or divesting debt or equity securities issued by a Russian entity to a non-US person
- Explains that the purchase of shares in a US fund would not be considered a prohibited “new investment” unless the fund’s holding of debt or equity securities issued by entities in Russia represents a 50% or more share by value of the fund

Relevant OFAC FAQs – Cont'd

- **Russia Harmful Foreign Activities Sanctions FAQ #1055**

- Explains that the new investment prohibitions do not prevent US persons from lending funds to, or purchasing a debt or equity interest in, entities located outside of Russia, provided that such funds are not specifically intended for new projects or operations in Russia and the entity located outside of Russia derives less than 50% of its revenues from its investments in Russia

- **Russia Harmful Foreign Activities Sanctions FAQ #982**

- Confirms that US persons may not buy or sell debt or equity of blocked Russian financial institutions, and that a US fund may not buy, sell, or otherwise engage in transactions related to debt or equity of such blocked Russian financial institutions
- However, a US fund that contains blocked holdings generally is not itself considered a blocked entity unless the blocked holdings represent a 50% or more share by value of the fund

Russian Countersanctions Overview

Morgan Lewis

Russian Countersanctions



**Transaction
Restrictions**



**Payment
Restrictions**



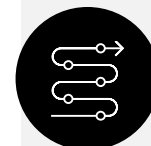
**Trade & Export
Restrictions**



**Blocking
Sanctions**



**Unfriendly
Country Persons**



**Directly or
Indirectly**



Exemptions



**Government
Approvals**



Consequences

Russian Countersanctions

Transaction Restrictions

- Transactions involving sanctioned persons
- Certain transactions involving unfriendly country persons, e.g., with Russian and non-Russian issuer securities and LLC equity interests incl. sale and purchase, options, pledges, and shareholder agreements
- Transactions involving unfriendly country persons with shares (equity interests) in many Russian companies incl. banks, energy companies, and subsoil and oilfield services companies
- Transactions involving unwanted or extremist individuals or organizations

Payment Restrictions

- Certain payments to unfriendly country persons incl. dividends, loans, guarantees, and IP license fees; RUR and blocked accounts
- Payments from unfriendly country persons for Russian natural gas
- Payments to sanctioned persons and unwanted or extremist individuals or organizations

Trade and Export (Re-Export) Restrictions

- Ukraine
- Certain goods incl. tech equipment
- Certain raw materials

Blocking Sanctions & Sanctioned Persons

- Directly listed individuals and companies
- Controlled companies incl. Russian

Russian Countersanctions

Transactions with Securities

- General rule: no transaction without the government commission (sub-commission) approval
- But specifics differ depending upon type of securities, parties and intermediaries involved, acquisition dates, and other factors
- Important: approval might be needed even if for an outside Russia transaction

Unfriendly Country Persons

- 60+ countries and territories incl. USA, UK, EU member states
- Individuals and companies registered, or with the main place of business or profit, in such countries
- Controlled companies incl. in some instances Russian

Directly or Indirectly

- In Russia or abroad
- Involving or for the benefit of

Exemptions Exist

- Laws and regulations including presidential decrees and government resolutions
- General licenses (aka extracts from the meeting minutes) issued by the government commission (sub-commission)
- Specific approvals issued by a sanctions authority
- Exemptions differ depending upon a particular countersanction

Russian Countersanctions

Government Approvals Key Gatekeepers

- President
- Government commission on foreign investments (special sub-commission)
- Central bank and certain other industry regulators

Consequences

- Transaction is null and void
- Risk of nationalization
- Liability incl. potentially criminal for individuals involved



Sanctions Compliance

- Agreement termination or failure to perform because of the US, EU, etc., sanctions: contradicts the public policy, not an excuse
- Sanctions compliance clauses: possible but must be drafted carefully



Jurisdictional Law

- In a dispute with a sanctioned person or on sanctions, a Russian arbitration (state commercial) court has exclusive jurisdiction
- A court can issue anti-suit injunction prohibiting non-Russian litigation or arbitration
- A court can award a fine against the non-compliant party in the full amount claimed by such party in non-Russian litigation or arbitration

Outbound Investments

Morgan Lewis

History of Outbound Investment Review

- Considered in Foreign Investment Risk Review Modernization Act of 2018, but ultimately not included
- National Critical Capabilities Defense Act of 2021 (NCCDA 2021)
 - Included in House of Representatives bill, America COMPETES Act
 - Not included in companion Senate legislation
 - Ultimately not included in final CHIPS Act that passed Congress and was signed by the President
- National Critical Capabilities Defense Act of 2022 (NCCDA 2022)
 - Part of conference committee discussions, but never formally introduced as a bill
- National Critical Capabilities Defense Act of 2023 (NCCDA 2023)
 - Re-introduced in May 2023

Policy Objectives, Status, and Potential Next Steps

Policy Objectives

- Technology transfer
- Support to PRC development of indigenous capabilities
- Supply chain for US critical capabilities

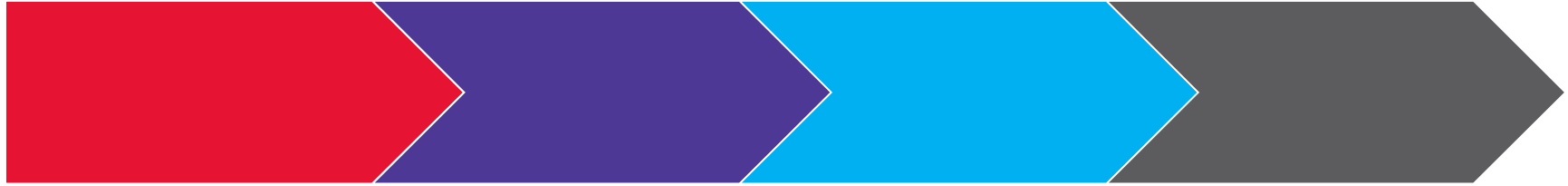
Status and Potential Next Steps

- **White House:** Implement outbound investment review through executive order
 - An executive order could preempt the need for congressional action, but Congress could still pass a bill if desired
 - Timing
- **Congress:** Include outbound investment in NDAA or another bill
- **International partners**

Potential Scope

- **Covered sectors**
 - Semiconductors
 - Artificial Intelligence
 - Quantum Computing
- **Considered but likely not covered**
 - Biotechnology and biomanufacturing
 - Battery technology and rare minerals
- **Investment accompanied by transfer of know-how and other expertise**
 - What about purely passive investment?
- **PRC military benefit**
- **Approval vs. Notification**
- **Mandatory vs. Voluntary**

Potential Process



**Department of
Treasury as
Chair**

**Roles for
Department of
Commerce and
other agencies**

**Possible
mitigation
option**

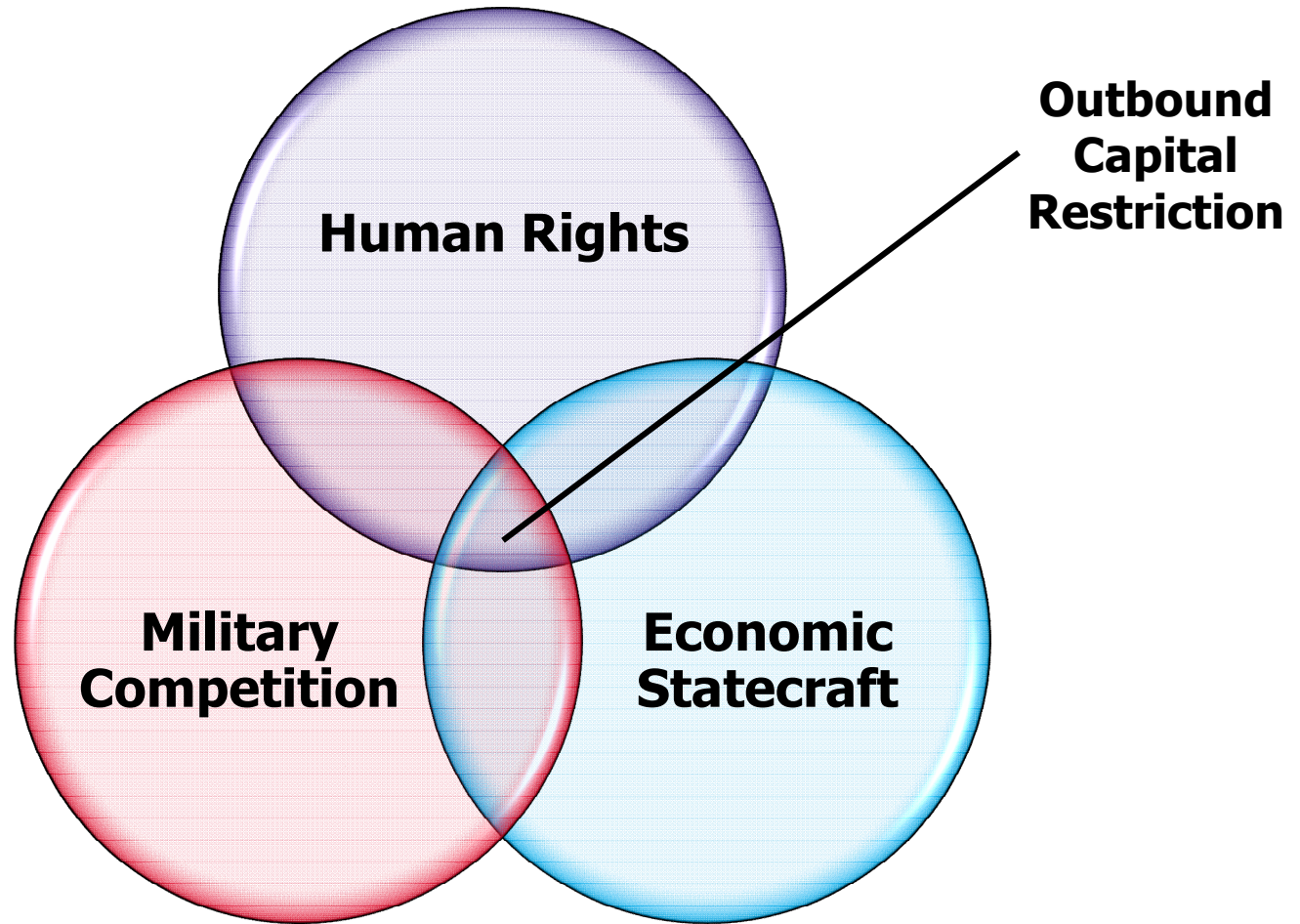
Enforcement

China Competition Policy in the 118th Congress

Morgan Lewis

China Competition Policy – 118th Congress

- Builds on efforts of the 117th Congress: USICA and House GOP China TF
- The Select Committee on Strategic Competition Between the United States and the Chinese Communist Party (“**Select Committee on China**” or “**Select Committee on the CCP**”)
- Remarkably Bipartisan... so far
- Three Lines of Effort:
 - Military Competition
 - Economic Statecraft
 - Ideological Competition/Human Rights
- No Legislative Jurisdiction
 - The Select Committee is meant to investigate and submit policy recommendations to the House of Representatives



118th Congress – Next Steps

- **Select Committee Economic Competition Policy Recommendations**
 - Will Financial Services be supportive?
 - Ways and Means?
- **Senate China Competition Legislation**
 - “Curtailing the flow of investment to the Chinese Government” is one of five policy pillars of the Senate Democrats’ efforts
- **Aligning with the Biden Administration and Executive Actions**

Sanctions Against Chinese Military Companies

Morgan Lewis

EO 13959 – Background

- National Defense Authorization Act (NDAA) of FY 1999, Section 1237, required the US Department of Defense (DOD) to:
 - Determine companies operating directly or indirectly in the United States that are “Communist Chinese military companies” (CCMCs)
 - Publish a list of CCMCs in the Federal Register
 - Make additions or deletions to the CCMC list published “on an ongoing basis”
- Authorized, but did not require, the President to impose sanctions under the International Emergency Economic Powers Act (IEEPA) on CCMCs
- June 2020 marked first time that the DOD identified CCMCs under Section 1237
 - List was then supplemented in August 2020

EO 13959 – Overview and Definitions

Overview

- ✓ EO issued by President Trump on November 12, 2020
- ✓ Declared a national emergency pursuant to authority under the IEEPA
- ✓ Named the same 31 entities on DOD's Section 1237 list
- ✓ Prompted by concerns over China's Military-Civil Fusion development strategy

Definitions

- **Communist Chinese military company** = persons already designated as such by the DOD and listed in the Annex to the EO; persons publicly designated by the DOD and/or Treasury
- **US Person** = any US citizen, permanent resident alien (green card holder), entity organized under US law or any US jurisdiction (including foreign branches), or person in the United States
 - Included private funds organized under US law
- **Transactions** = purchase for the value of any publicly traded security

EO 13959 – Prohibitions and Implementation

- Broadly prohibited any transaction in:
 1. publicly traded securities,
 2. any securities derivative of such securities, or
 3. securities designed to provide investment exposure to such securities of any “Communist Chinese military company” by any US person **beginning 9:30 a.m. EST on Jan. 11, 2021**
- Also prohibited such transactions in securities of any future-designated CCMCs 60 days after the designation
- Prohibited any transaction that evades or avoids, has the purpose of evading or avoiding, causes a violation of, or attempts to violate EO 13959
- Delegated authority to implement EO 13959 to Treasury (OFAC)

January 2021 Developments

- **On January 13, 2021**, EO 13559 was amended by **EO 13974**
 - Pursuant to the new amendments, CCMC securities could not be held by a US person after November 11, 2021, or 365 days after the CCMC determination, as applicable—essentially mandated divestment by US persons
 - Also expanded the definition of the term “transaction” to include the purchase for *sale* of any publicly traded security (previously just referred to purchase for “value”)
- **On January 14, 2021**, DOD designated additional Chinese companies as CCMCs targeted under **EO 13559**
- OFAC issued **General License 1**, which authorized transactions in the securities of the subsidiaries of designated CCMCs until 9:30 a.m. on **January 28, 2021**

New CCMC EO 14032 – June 3, 2021

- President Biden revised and superseded EO 13959
 - Replaced EO 13959’s criteria for designation
 - Eliminated DoD’s ability to designate companies under the sanctions
 - Included an annex with 59 listed companies subject to the EO’s prohibitions after a 60-day wind-down period
 - Eliminated the requirement to divest within one year, but authorization to divest holdings expires after one year such that US persons can either divest or hold onto securities indefinitely
- OFAC issued eight new FAQs regarding the EO and amended seven existing FAQs related to EO 13959
- OFAC also replaced the CCMC list with a new list entitled the “Non-SDN Chinese Military-Industrial Complex Companies List” (NS-CMIC List)

Relevant OFAC FAQs

- **Chinese Military Companies Sanctions FAQ #857**

- Explains that the prohibitions in EO 13959, as amended, only apply to subsidiaries of CMICs publicly listed on the NS-CMIC List by OFAC (i.e., **OFAC's 50% rule does not apply**)

- **Chinese Military Companies Sanctions FAQ #859**

- Defines “publicly traded securities” to mean any “security,” as defined by the Securities Exchange Act, denominated in any currency that trades on a securities exchange or through the method of trading that is commonly referred to as “over-the-counter,” in any jurisdiction

- **Chinese Military Companies Sanctions FAQ #860**

- Provides examples of financial instruments covered by the provision stating that the prohibitions apply to any publicly traded securities that are derivative of such securities or are designed to provide investment exposure to such publicly traded securities
- Includes derivatives (e.g., futures, options, swaps), warrants, American depository receipts (ADRs), global depository receipts (GDRs), exchange-traded funds (ETFs), index funds, and mutual funds

- **Chinese Military Companies Sanctions FAQ #861**

- Confirms that EO 13959, as amended, prohibits US persons from investing in US or foreign funds, such as ETFs or other mutual funds, that hold publicly traded securities of CMICs

Relevant OFAC FAQs – Cont'd

- **Chinese Military Companies Sanctions FAQ #863**

- Explains that activity by US persons related to the following services are considered permissible: clearing, execution, settlement, custody, transfer agency, back-end services, and other such support services.

- **Chinese Military Companies Sanctions FAQ #865**

- Provides that market intermediaries, including market makers, and other participants may engage in ancillary or intermediary activities that are necessary to effect divestiture during the relevant wind-down periods or that are not otherwise prohibited under EO 13959.

- **Chinese Military Companies Sanctions FAQ #871**

- Confirms that transactions and activities by securities exchanges operated by US persons involving the purchase or sale of publicly traded securities of any entity listed on the NS-CMIC List are not prohibited.

- **Chinese Military Companies Sanctions FAQ #900**

- Explains how OFAC will use its new authority to sanction persons who operate in the surveillance technology sector of the PRC economy under the amended EO.
- Explains that OFAC intends to target persons whose operations include or support, or have included or supported, (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.

Relevant OFAC FAQs – Cont'd

- **Chinese Military Companies Sanctions FAQ #901**

- Explains that for purposes of assessing whether certain purchases or sales are permissible under EO 13959, as amended, US persons may rely upon the information available to them in the ordinary course of business.

- **Chinese Military Companies Sanctions FAQ #902**

- Clarifies that US persons are not prohibited from providing investment advisory, investment management, or similar services to a non-US person, including a foreign entity or foreign fund, in connection with the non-US person's purchase or sale of a covered security, provided that the underlying purchase or sale would not otherwise violate EO 13959, as amended (e.g., neither the purchase nor sale of the covered security is for the ultimate benefit of a US person).

- **Chinese Military Companies Sanctions FAQ #903**

- States that US persons employed by non-US entities are not prohibited from being involved in, or otherwise facilitating, purchases or sales related to a covered security on behalf of their non-US employer, provided that such activity is in the ordinary course of their employment and the underlying purchase or sale would not otherwise violate EO 13959, as amended.

- **Chinese Military Companies Sanctions FAQ #904**

- Explains that US market makers, and non-US market makers who employ US persons, are permitted to engage in activities that are necessary to effect divestiture during the 365-day periods in which divestment transactions are permitted, including the conversion of ADRs of a CMIC into underlying securities of the CMIC on the foreign exchange where the underlying securities are listed.

Relevant OFAC FAQs – Cont'd

- **Chinese Military Companies Sanctions FAQ #905**

- Confirms that EO 13959 does not prohibit US persons from engaging in all activities with companies listed on the NS-CMIC list; only with respect to purchases or sales of publicly traded securities.

- **Chinese Military Companies Sanctions FAQ #1046**

- Confirms that US persons are not required to divest their holdings of CMIC securities during the relevant 365-day divestment period and may continue to hold such securities.

- **Chinese Military Companies Sanctions FAQ #1047**

- Explains that US persons who hold securities of CMICs may continue to receive cash dividends and stock splits related to such covered securities, and US financial institutions may continue to process such transactions. However, purchases of CMIC securities effected through dividend reinvestments constitute purchases that are prohibited pursuant to EO 13959, as amended.
- US persons may, however, continue to facilitate the distribution of dividend reinvestments for non-US persons after the relevant divestment period.

- **Chinese Military Companies Sanctions FAQ #1048**

- Confirms that EO 13959 does not require US financial institutions to block transactions. However, transactions that would be prohibited under EO 13959 must be rejected and reported to OFAC within 10 business days.

Chinese Countersanctions

Morgan Lewis

Setting the Stage

The US government (the Executive and Congressional branches) has taken an assertive stance with respect to the People's Republic of China ("PRC" or "China"):



Executive orders designed to manage China's engagement in the US



Regulations that limit China's access to US products, technology, and markets



Policies designed to draw inferences regarding China's actions — e.g., designations regarding "foreign adversaries"



Outreach to allies and partners to share intelligence and other information regarding the Chinese government's actions as well as the actions of various Chinese companies



Changes in laws and regulations by allies and partners that impact China's ongoing global engagements

Setting the Stage

- These actions have elicited reactions from the Chinese government
- Not inconsistent with other governments' reactions when the US applies restrictions to global or domestic activities
- Policy and regulatory changes in China
- Shifts in approach to the new Administration
- Preparation of a list of negotiating points to discuss with the Biden Administration

China's Blocking Statutes

Morgan Lewis

Blocking Statute of January 9, 2021 – An Overview

Rules on Counteracting Unjustified Extra-territorial Application of Foreign Legislation and Other Measures

- Issued by China's Ministry of Commerce (MOFCOM) on January 9, 2021
- Took immediate effect—but no public cases
- Vague and general in nature
 - Aimed at blocking effect of extraterritorial laws impacting Chinese trade with entities in third-party jurisdictions

How Does the Blocking Statute of January 9, 2021 Work?

- Working mechanism
- Prohibition order
- Reporting obligation
- Confidentiality of reports
- Unclear scope of coverage – subsidiaries of MNCs in China, overseas Chinese subsidiaries, JVs in China?
- Compensatory damages via court proceedings

Blocking Statute of June 10, 2021 – An Overview

PRC Law to Counter Foreign Sanctions

- Issued by Standing Committee of the National People's Congress on June 10, 2021
- Took immediate effect
- Vague and general in nature
- Broad reach

How Does the Blocking Statute of June 10, 2021 Work?

- **Competent departments of the State Council (State Council)**
 - May decide to include in a countermeasure list the individuals and organizations directly or indirectly involved in the development, decision-making, and implementation of the discriminatory restrictive measures against China or PRC nationals/organizations.
 - May decide to adopt countermeasures.
 - The decisions made by the State Council are final, but may be suspended, modified, or removed by the State Council if the relevant circumstances change.
- **Coordination and information sharing of the relevant work among gov't dep'ts**
- **Obligation to Abide by the Countermeasures**
 - Organizations and individuals within the territory of the PRC shall implement the countermeasures adopted by the State Council.
 - Prohibition against organizations and individuals within the territory of the PRC from complying with or implementing discriminatory measures taken by foreign countries against Chinese citizens and organizations.

What Foreign Sanctions May Be Blocked?

- Violate international law or the basic principles of international relations;
- Contain or suppress China under various pretexts or pursuant to its own laws;
- Directly or indirectly involve the development, decision-making, and implementation of discriminatory restrictive measures against China or PRC nationals/organizations;
- Meddle in China's internal affairs; and
- Conduct, assist in, or support acts that compromise China's sovereignty, security, or development interests, and necessary countermeasures need to be adopted.

Who May Be Included on the Anti-Sanctions List or Subject to the Countermeasures?

- **Foreign Persons**

- MNC?
- Management of MNC?
- Spouses or immediate family of individuals?
- Actual controller of MNC? Affiliated companies?

- **Chinese Persons**

What are Exemptions and Penalties for Violation?

- **Exemptions**

- None
 - No judicial appeal
 - Countermeasures may be suspended, modified, or removed by the State Council

- **Penalties for Violation**

- Failure to abide by the countermeasures would be punished by the State Council, including being restricted or prohibited from carrying out relevant activities.
- PRC individuals or organizations may sue the organizations or individuals implementing or assisting in the implementation of the foreign discriminatory restrictive measures and claim for the compensation.

Practically, What Does this Mean for MNCs?

- What corollary consequences might there be for MNCs following foreign sanctions?
 - Anti-Sanctions List and other Countermeasures
 - Social Credit System
 - Unreliable Entities List
- How is China likely to enforce the blocking statutes?
- What industries are likely to be impacted?
- Should companies look at lobbying their governments?

What Can MNCs Do to Mitigate the Risks?

- Consider conflict of laws between US and China and assess compliance risks under both sets of laws
- Look for possible reaction from foreign governments, especially Biden administration
- Watch for detailed implementing regulations
- Watch for issuance of Prohibition Orders from MOFCOM
- Consider impact on China-based subsidiaries and personnel
- Consider reporting obligations and risk of penalties and private lawsuits
- Review compliance clauses in existing contracts
- Consider amending termination rights

Other Potential Indirect Forms of Countersanctions

Recent government dawn raids focusing on international due diligence and consulting firms:

- **Mintz Group**. March 20, 2023: Chinese authorities raided the Beijing office of Mintz Group, a due diligence consulting firm, based on its alleged involvement in Xinjiang forced labor supply chain due diligence. Five local employees were arrested. On March 24, 2023, Mintz Group closed its Beijing office.
- **Bain & Company**. April 2023: Shanghai police raided the Shanghai office of Bain & Company and questioned its employees. According to *Financial Times'* report, the police also took away computers and phones.

Other Potential Indirect Forms of Countersanctions

New Anti-Espionage Law and Investigations:

- The New Anti-Espionage Law, which will take effect on July 1, 2023, expands the scope of espionage activities, establishes broad criteria for determining espionage behavior, grants extensive investigative power to national security agencies, and clarifies the legal liability for espionage activities.
- Chinese authorities have raided the offices of consulting firm Capvision as Beijing ramps up its anti-espionage campaign in the consulting sector. On May 8, 2023, Chinese broadcasters reported that multiple Capvision offices, including in Shanghai, Beijing, Suzhou, and Shenzhen, were raided after authorities found it “ignored potential national security risks” and failed to “carry out its responsibilities and obligations to prevent espionage.” The report did not indicate exactly when the raids occurred.

Other Potential Indirect Forms of Countersanctions

Cybersecurity review against Micron and banning of its products



291098.shtml

Times

SOURCE / ECONOMY

Micron fails cybersecurity review in China, meaning its products could be banned

Case deemed 'individual,' won't affect China's opening-up policy

By GT staff reporters
Published: May 21, 2023 10:53 PM

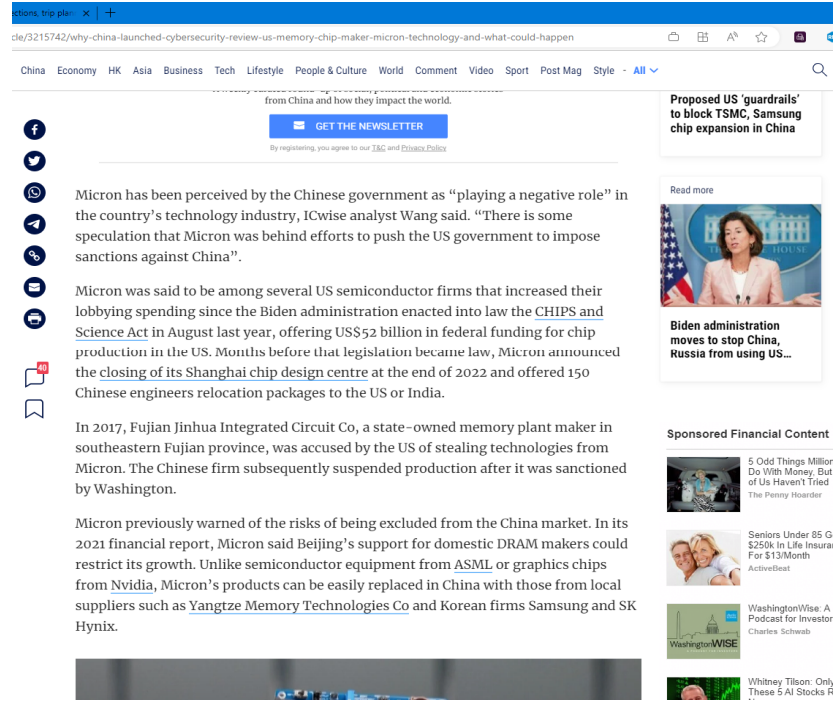


Cyber security. Photo: iC

China on Sunday made public the results of its cybersecurity review of US semiconductor maker Micron Technology, saying that the company didn't pass the review because it has severe cybersecurity problems that could pose significant security risks to China's critical information infrastructure supply

58°F Cloud

Morgan Lewis



de/3215742/why-china-launched-cybersecurity-review-us-memory-chip-maker-micron-technology-and-what-could-happen

China Economy HK Asia Business Tech Lifestyle People & Culture World Comment Video Sport Post Mag Style · All

GET THE NEWSLETTER

By registering, you agree to our [T&C](#) and [Privacy Policy](#)

Micron has been perceived by the Chinese government as "playing a negative role" in the country's technology industry, ICwise analyst Wang said. "There is some speculation that Micron was behind efforts to push the US government to impose sanctions against China".

Micron was said to be among several US semiconductor firms that increased their lobbying spending since the Biden administration enacted into law the CHIPS and Science Act in August last year, offering US\$52 billion in federal funding for chip production in the US. Months before that legislation became law, Micron announced the closing of its Shanghai chip design centre at the end of 2022 and offered 150 Chinese engineers relocation packages to the US or India.

In 2017, Fujian Jinhua Integrated Circuit Co, a state-owned memory plant maker in southeastern Fujian province, was accused by the US of stealing technologies from Micron. The Chinese firm subsequently suspended production after it was sanctioned by Washington.

Micron previously warned of the risks of being excluded from the China market. In its 2021 financial report, Micron said Beijing's support for domestic DRAM makers could restrict its growth. Unlike semiconductor equipment from ASML or graphics chips from Nvidia, Micron's products can be easily replaced in China with those from local suppliers such as Yangtze Memory Technologies Co and Korean firms Samsung and SK Hynix.

Proposed US 'guardrails' to block TSMC, Samsung chip expansion in China

Read more

Biden administration moves to stop China, Russia from using US...

Sponsored Financial Content

5 Odd Things Millor Do With Money, But of Us Haven't Tried The Penny Hoarder

Seniors Under 85 G \$25k in Life Insura For \$13/Month ActiveBest

WashingtonWise: A Podcast for Investor Charles Schwab

Whitney Tilson: Only These 5 AI Stocks R

Timothy W. Levin



Timothy W. Levin
Philadelphia
+1.215.963.5037
timothy.levin@morganlewis.com

Tim, leader of the firm's investment management practice, counsels investment advisers and other financial services firms on the design, development, and management of pooled investment vehicles and investment advisory programs. He also advises fund managers in connection with organization, registration, and ongoing regulatory compliance. Additionally, he represents managers and sponsors of unregistered pooled investment vehicles.

[Read Tim's extended profile >>](#)

Todd Liao



Todd Liao

Shanghai

+86.21.8022.8799

todd.liao@morganlewis.com

Todd works with clients on a wide range of financial transactions and legal issues involving China. He frequently works with multinational corporations on cross-border mergers and acquisitions, foreign direct investment and investment financing, disposal of Sino-foreign joint ventures and assets, and the structuring of complex commercial transactions. Todd also handles intellectual property (IP) work, specifically assisting clients with managing their trademark portfolios. He is admitted in New York only.

[Read Todd's extended profile >>](#)

David Plotinsky



David Plotinsky

Washington, DC

+1.202.739.5742

david.plotinsky@morganlewis.com

David, the former acting chief of the US Department of Justice's Foreign Investment Review Section, represents clients such as venture capital, private equity, and infrastructure firms. In particular, he steers clients through government national security review processes for foreign investment, including by the Committee on Foreign Investment in the United States (CFIUS) and Team Telecom. In addition, David focuses on trade, information communications technology and services, and critical and emerging technology. He maintains a security clearance and advises clients on their most sensitive matters.

[Read David's extended profile >>](#)

Vasilisa “Vasya” Strizh



Vasilisa Strizh

Boston

+1.617.341.7987

vasilisa.strizh@morganlewis.com

Vasya represents strategic and financial investors on complex corporate projects, including acquisitions, divestitures and joint ventures, public and private equity offerings, and structured settlements, both in the United States and globally. She provides strategic advice on exit strategies for companies and funds seeking to restructure or liquidate their holdings. Vasilisa has served as the lead lawyer on cross-border deals for more than 20 years, successfully bridging cultural gaps in global investments. She brings deep knowledge of the unique international business environment and government expectations from the investor perspective.

[Read Vasilisa’s extended profile >>](#)

Carl A. Valenstein



Carl A. Valenstein

Boston

+1.617.341.7501

carl.valenstein@morganlewis.com

Carl focuses his practice on domestic and international corporate and securities matters, mergers and acquisitions, project development, and transactional finance. He counsels extensively in the life science, telecom/electronics, and maritime industries, and has worked broadly in Latin America, the Caribbean, Europe, Africa, Asia, and the Middle East. He previously served as co-chair of the International Section of the Boston Bar Association and co-chairs the firm's environmental, social, and governance (ESG) and sustainable business and Cuba initiatives. Carl is the leader of the Boston office corporate and business transactions practice.

[Read Carl's extended profile >>](#)

Katelyn M. “Katie” Hilferty



Katelyn M. Hilferty

Washington, DC

+1.202.739.5674

katelyn.hilferty@morganlewis.com

Katie helps clients navigate US cross-border and trade compliance requirements, including export controls under the International Traffic in Arms Regulations (ITAR) and Export Administration Regulations (EAR), economic sanctions administered by the US Department of Treasury’s Office of Foreign Assets Control (OFAC), import and customs laws and regulations enforced by US Customs and Border Protection (CBP), anti-money laundering (AML)/Bank Secrecy Act (BSA) compliance matters, Bureau of Economic Analysis (BEA) international survey reporting, and national security issues before the Committee on Foreign Investment in the United States (CFIUS).

[Read Katie’s extended profile >>](#)

David Mendelsohn



David Mendelsohn

Washington, DC

+1.202.739.5431

david.mendelsohn@morganlewis.com

David leverages 15 years of government relations experience to advise Morgan Lewis attorneys and clients on legislative and regulatory policy matters and implement comprehensive government relations strategies. David works with clients and Morgan Lewis subject matter experts on a wide range of legislative issues, including: national security, trade, digital assets, transportation, energy, and health care.

David is an active member of Morgan Lewis' responsible labor working group, US-China working group, Ukraine Conflict task force, digital assets working group, and automotive and EV industry groups.

THANK YOU

© 2023 Morgan Lewis

Morgan, Lewis & Bockius LLP, a Pennsylvania limited liability partnership

Morgan Lewis Stamford LLC is a Singapore law corporation affiliated with Morgan, Lewis & Bockius LLP.

Morgan, Lewis & Bockius UK LLP is a limited liability partnership registered in England and Wales under number OC378797 and is a law firm authorised and regulated by the Solicitors Regulation Authority. The SRA authorisation number is 615176.

Our Beijing and Shanghai offices operate as representative offices of Morgan, Lewis & Bockius LLP.

In Hong Kong, Morgan, Lewis & Bockius is a separate Hong Kong general partnership registered with The Law Society of Hong Kong.

This material is provided for your convenience and does not constitute legal advice or create an attorney-client relationship. Prior results do not guarantee similar outcomes. Attorney Advertising.