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November 18, 2020

## **President Trump Issues an Executive Order Prohibiting U.S. Persons from Investing in Listed “Communist Chinese Military Companies”**

On November 12, 2020, President Trump issued an Executive Order entitled, “Addressing the Threat from Securities Investments that Finance Communist Chinese Military Companies” (the “Order”).<sup>1</sup> After a 60-day grace period ending on January 11, 2021, the Order will prohibit U.S. persons<sup>2</sup> from engaging in transactions in publicly traded securities (or any securities that are derivative or otherwise designed to provide investment exposure to such securities) of any identified “Communist Chinese military company” (“CCMC”). U.S. persons will have until November 11, 2021, to divest from any publicly traded securities of currently identified CCMCs held at the end of the grace period (*i.e.*, held as of January 11, 2021). The Order also appears to prevent CCMC’s from engaging in public offerings in the United States, as well as public offerings outside the United States that involve U.S. underwriters. A list of the currently identified CCMC companies, which include major Chinese telecommunications, energy, and construction companies, among others, is provided at the end of this memorandum.

In the Order, President Trump cited the national security threat posed by the People’s Republic of China’s (the “PRC”) national strategy of Military-Civil Fusion, and, specifically, the threat posed by Chinese companies that sell securities to U.S. investors and then invest this capital to finance the development and modernization of the Chinese military. The Order relies on the President’s powers under the International Emergency Economic Powers Act (“IEEPA”).

The Order and the sanctions imposed therein will be administered and enforced by the U.S. Department of the Treasury’s Office of Foreign Assets Control (“OFAC”). The Order’s prohibitions do not, however, take the form of typical OFAC sanctions (*i.e.*, they are more limited than OFAC’s typical “blocking” sanctions), and the precise scope of the new sanctions is unclear. The new sanctions are analogous in some ways to OFAC’s sectoral sanctions prohibiting certain U.S. nexus transactions in certain Russian companies’ debt and equity or the sanctions targeting certain Venezuelan government debt and equity. Following the imposition of those sanctions, OFAC quickly issued guidance addressing the scope of those sanctions, as well as several general licenses mitigating the sanctions’ immediate impact. Here, OFAC has not yet issued any guidance, but we expect such guidance to be forthcoming.

In the interim, U.S. persons planning to acquire publicly traded CCMC securities or to facilitate trading in such securities should use the 60-day grace period to assess the implications of the Order on their plans, and U.S. persons who hold such securities should consider the likely impact on the marketability of such securities going forward.

### **Current and Future Identification as a CCMC**

Under the Order, a CCMC means any person that is: (1) currently listed on the U.S. Department of Defense (“DoD”) list of CCMCs operating directly or indirectly within the United States (as defined by the National Defense Authorization Act for Fiscal Year 1999, as amended (the “Act”)) and listed in the Annex of the Order<sup>3</sup>; (2) identified at a future date by the Secretary of Defense or Secretary of the Treasury as a CCMC under the Act; or (3) any person publicly listed by the Secretary of the Treasury as a subsidiary of a CCMC.

DoD has been required to maintain classified and unclassified versions of a list of CCMCs and share such list with Congress and relevant U.S. government agencies annually since 1999, pursuant to the Act. Earlier this year, DoD issued the first public version of the CCMC list. Specifically, on June 24, 2020, DoD sent a public letter to Senator Tom Cotton that included an attachment listing 20 companies headquartered in the PRC that DoD determined to be CCMCs operating directly or indirectly in the United States.<sup>4</sup> On August 28, 2020, DoD published a list of another 11 companies that DoD had determined to be CCMCs. To date, DoD has publicly identified a total of 31 Chinese companies as CCMCs for purposes of the Act (and therefore, by reference, also for purposes of the Order).

The Act defines the criteria for identification as a CCMC as:

- “[A]ny person identified in the Defense Intelligence Agency publication numbered VP-1920-271-90, dated September 1990, or PC-1921-57-95, dated October 1995, and any update of those publications for the purposes of [the Act];” and
- [A]ny other person that: (i) is owned or controlled by, or affiliated with, the People’s Liberation Army or a ministry of the government of the People’s Republic of China or that is owned or controlled by an entity affiliated with the defense industrial base of the People’s Republic of China; and (ii) is engaged in providing commercial services, manufacturing, producing, or exporting.”<sup>5</sup>

For purposes of the Act, the term “People’s Liberation Army” means the land, naval, and air military services, the police, and the intelligence services of the PRC, and any member of any such service or police force.

Changes to the CCMC list are to be made in consultation with the Attorney General, the Director of National Intelligence, and the Director of the Federal Bureau of Investigation.

### **Effects of the Order**

The Order, after a 60-day grace period ending on January 11, 2021, broadly prohibits U.S. persons from engaging in any transaction in publicly traded securities, or any securities that are derivative of, or are designed to provide investment exposure to such securities, of currently listed CCMCs (*i.e.*, the 31 PRC

companies currently identified on the CCMC lists maintained by DoD). “Transaction” is defined for purposes of the Order to mean “the purchase for value of any publicly traded security.” To the extent that a U.S. person holds publicly traded securities of a currently listed CCMC as of January 11, 2021, the Order allows a wind-down period permitting the divestment of any such securities by the U.S. person until November 11, 2021.

With respect to any entity that may be identified and listed as a CCMC after the date of the Order, the Order prohibits U.S. persons, wherever located, from transacting in that newly-listed entity’s publicly traded securities (or any securities that are derivative or otherwise designed to provide investment exposure to such securities) after 60 days from the date of the entity’s listing as a CCMC. U.S. persons in possession of securities of such newly-listed CCMCs will have 365 days from the date of that entity’s listing to divest the securities of the CCMC that they hold. The Order also prohibits any transaction by a U.S. person or within the United States that evades or avoids, has the purpose of evading or avoiding, causes a violation or, or attempts to violate the prohibitions of the Order. The Order also prohibits any conspiracy (not limited to U.S. persons or within the United States) to violate the prohibitions of the Order.

The Order defines the term “U.S. person” to include “any [U.S.] citizen, permanent resident alien, entity organized under the laws of the United States. . .or any person [located] in the United States.” For purposes of the Order, the terms “security” and “securities” have the same very broad definition as the term “security” under the U.S. Securities Exchange Act, which encompasses ADRs and reads as follows:

any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a ‘security’, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.<sup>6</sup>

But the Order also states that any “note, draft, bill of exchange, or banker’s acceptance which has a maturity at the time of issuance of not exceeding 9 months, exclusive of days of grace, or any renewal thereof. . .shall be a security for purposes of the [Order].”

### **Implications**

The Order is the latest action taken by the Trump Administration that seeks to reduce Chinese companies’ access to the U.S. economy—in this case, the access of listed CCMCs to U.S. capital markets and U.S.

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investors. Although the current list of CCMCs includes several Chinese companies that have been the target of prior U.S. sanctions or export prohibitions (*e.g.*, Huawei, Hikvision, and China Aerospace Science and Industry Corporation), other currently listed CCMCs have not previously been targeted by the Trump Administration. Since the prohibition on U.S. persons acquiring the publicly traded securities of CCMCs applies on a global basis, the prohibition is not limited to securities of Chinese companies that are listed in, or otherwise trade publicly, in the United States.

We expect that OFAC will promulgate implementing regulations and issue guidance with respect to the implementation of the Order in the coming weeks. Some topics that may be covered by the forthcoming guidance include:

- *Permissibility of holding securities after the wind-down period.* While the Order does not explicitly prohibit U.S. persons from *continuing to hold* CCMC securities after the end of the wind down period, OFAC may issue guidance as to whether U.S. persons may continue to engage in ancillary transactions related to such securities (*e.g.*, receipt of dividends).
- *Potential applicability of OFAC's 50 Percent Rule.* Although the Order itself suggests that its prohibitions will only apply to CCMC subsidiaries identified by DOD or the Treasury Department as CCMCs or *publicly listed* by the Treasury Department as subsidiary of a listed CCMC, OFAC could nonetheless issue guidance applying its 50 percent rule (providing that entities owned 50 percent or more, in the aggregate, by OFAC-sanctioned persons must themselves be treated as OFAC-sanctioned persons, whether or not such entities have been explicitly sanctioned by OFAC) in the context of the Order. A number of the currently listed CCMCs have subsidiaries with publicly traded securities.
- *Guidance regarding permitted activity.* Violations of the Order will be subject to the civil and criminal penalties available under IEEPA. However, OFAC may issue guidance or general licenses that limit the scope of prohibited conduct under the Order.

We will continue to monitor actions taken by the U.S. government related to the Order and provide further updates as appropriate.

**CCMCs Identified as of November 12, 2020<sup>7</sup>**

Aero Engine Corporation of China  
Aviation Industry Corporation of China (AVIC)  
China Academy of Launch Vehicle Technology (CALT)  
China Aerospace Science and Industry Corporation (CASIC)  
China Aerospace Science and Technology Corporation (CASC)  
China Communications Construction Company (CCCC)  
China Electronics Corporation (CEC)  
China Electronics Technology Group Corporation (CETC)  
China General Nuclear Power Corp.  
China Mobile Communications Group  
China National Chemical Corporation (ChemChina)  
China National Chemical Engineering Group Co., Ltd. (CNCEC)  
China National Nuclear Corp.  
China North Industries Group Corporation (Norinco Group)  
China Nuclear Engineering & Construction Corporation (CNECC)  
China Railway Construction Corporation (CRCC)  
China Shipbuilding Industry Corporation (CSIC)  
China South Industries Group Corporation (CSGC)  
China Spacesat  
China State Construction Group Co., Ltd.  
China State Shipbuilding Corporation (CSSC)  
China Telecommunications Corp.  
China Three Gorges Corporation Limited  
China United Network Communications Group Co Ltd  
CRRC Corp.  
Dawning Information Industry Co (Sugon)  
Hangzhou Hikvision Digital Technology Co., Ltd. (Hikvision)  
Huawei  
Inspur Group  
Panda Electronics Group  
Sinochem Group Co Ltd

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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- <sup>1</sup> The White House, “Executive Order on Addressing the Threat from Securities Investments that Finance Communist Chinese Military Companies,” (Nov. 12, 2020), available [here](#).
- <sup>2</sup> “U.S. Persons” means, for purposes of the Order, U.S. citizens, permanent residents, entities organized under U.S. laws, or any person located within the United States.
- <sup>3</sup> See U.S. Dep’t of Defense, Press Release, “DOD Releases List of Additional Companies in Accordance with Section 1237 of FY99 NDAA,” (Aug. 28, 2020), available [here](#); Annex to the Order, available [here](#).
- <sup>4</sup> Office of Senator Tom Cotton, Press Release, “Cotton, Gallagher React to DoD List of Chinese Military Companies,” (Jun. 24, 2020), available [here](#).
- <sup>5</sup> Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub. L. No. 105-261 § 1237 (1999), available [here](#).
- <sup>6</sup> Securities Exchange Act of 1934, Pub. L. 73-291 § 3(a)(10), as codified as amended at 15 U.S.C. 78c(a)(10).
- <sup>7</sup> Annex to the Order, available [here](#).