

Recent Developments on U.S. Ban on American Investment in Chinese Military Companies

February 17, 2021

This alert addresses recent developments relating to former President Trump's executive orders on Chinese Military Companies that affect both investors in covered securities and exporters.

OFAC's Frequent Asked Questions

On November 12, 2020, former President Trump issued an executive order ("EO"), pursuant to the National Defense Authorization Act for Fiscal Year 1999, as amended ("NDAA"), prohibiting U.S. persons from investing in publicly traded securities of any person designated by the Secretary of Defense or the Secretary of the Treasury as a "Communist Chinese military company" ("Chinese Military Company"). See our analysis of the Nov. 12 EO [here](#). Since then, the 2021 National Defense Authorization Act ("2021 NDAA") was enacted into law, the EO was amended, the list of Chinese Military Companies expanded, and frequently asked questions promulgated.

Between December 28, 2020 and January 27, 2021, the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC") issued 15 Frequently Asked Questions ("FAQs"), which interpreted the EO and clarified OFAC's enforcement interpretation of certain provisions of the EO. The FAQs are summarized below:

Expansion of the Definition of the "Chinese Military Company"

On January 1, 2021, the 2021 NDAA was enacted into law (available [here](#), the revisions discussed in this alert are in Sec. 1260 H. [pp. 578-79]). The 2021 NDAA significantly expands the definition of "Chinese Military Company" to include Chinese entities that are identified as "military-civil fusion contributors." As revised, the definition of Chinese Military Company includes any entity (natural persons are specifically excluded) that is:

- "directly or indirectly owned, controlled, or beneficially owned by, or in an official or unofficial capacity acting as an agent of or on behalf of, the People's Liberation Army or any other organization subordinate to the Central Military Commission of the Chinese Communist Party; or identified as a *military-civil fusion contributor* to the Chinese defense industrial base; and
- engaged in providing commercial services, manufacturing, producing, or exporting." (emphasis added)

In addition, the 2021 NDAA defines "military-civil fusion contributors" as entities within the following seven broadly defined industry categories:

- "Entities knowingly receiving assistance from the Government of China or the Chinese Communist Party through science and technology efforts initiated under the Chinese military industrial planning apparatus.
- Entities affiliated with the Chinese Ministry of Industry and Information Technology, including research partnerships and projects.
- Entities receiving assistance, operational direction or policy guidance from the State Administration for Science, Technology and Industry for National Defense.

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- Any entities or subsidiaries defined as a 'defense enterprise' by the State Council of the People's Republic of China.
- Entities residing in or affiliated with a military-civil fusion enterprise zone or receiving assistance from the Government of China through such enterprise zone.
- Entities awarded with receipt of military production licenses by the Government of China, such as a Weapons and Equipment Research and Production Unit Classified Qualification Permit, Weapons and Equipment Research and Production Certificate, Weapons and Equipment Quality Management System Certificate, or Equipment Manufacturing Unit Qualification.
- Entities that advertise on national, provincial, and non-governmental military equipment procurement platforms in the People's Republic of China."

In addition to the above seven categories, "military-civil fusion contributors" also include "[a]ny other entities the Secretary [of Defense] determines is appropriate".

Amendment of the EO

On January 13, 2021, former President Trump issued Executive Order 13974 ("amended EO") (available [here](#)), amending certain parts of the original EO. Sections 1(b) and (c) of the original EO provide U.S. persons 365 days from the entity's designation to divest covered securities. The amended EO provides that the divestment obligations with respect to a designated entity depend on the date the entity is designated as a Chinese Military Company, and clarifies that U.S. persons must divest any Chinese Military Company covered securities by November 11, 2021 (if the relevant entity was included in the original 31 entities designated in the EO) or 365 days after the date that the entity is designated as a Chinese Military Company.

The amended EO further clarifies that possession of any covered securities by a U.S. person is prohibited after the end of the applicable divestment period, and also revised the definition of "transactions" to include any "sale" of covered securities to clarify that sales of covered securities after the end of the divestment period would violate the amended EO. FAQ 873 noted in the table above also addresses this change.

The Current List of "Chinese Communist Military Companies"

The EO initially applied to 31 Chinese companies named in the Annex to the EO (available [here](#)) that had been previously listed by the Secretary of Defense. On January 8, 2021, OFAC published an updated version of its Non-SDN Communist Chinese Military Companies List ("NS CCMC List"). The updated NS CCMC List includes the initial list of 31 Chinese companies and 4 additional entities (available [here](#)) designated by DoD on December 3, 2020 and also includes additional identifying information relating to the listed entities, including A.K.A.s (also known as), issuer names (names that are exactly or closely match the names of identified entities) and equity tickers. On January 14, 2021, DoD designated 9 additional entities in the aviation, technology, and semiconductor industries as Chinese Military Companies (available [here](#)).

As of the date of this alert, 44 Chinese entities have been designated as Chinese Military Companies. In addition, the updated NS CCMC List also contains a list of subsidiaries of the 44 designated Chinese entities with names closely matching those designated entities. So, the total number of Chinese entities subject to the EO is more than 44.

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Under the amended EO, the transaction prohibition effective date for the initial 31 entities was January 11, 2021 and the divestment period will end on November 11, 2021. For entities subsequently designated as Chinese Military Companies, the transaction prohibition effective date begins at 9:30 a.m. eastern standard time on the date that is 60 days after the entity is designated and the relevant divestment period extends for 365 days after such designation.

The Impact on Exporters

The Chinese Military Companies list affects both investors of the covered securities and exporters. On December 23, 2020, the U.S. Department of Commerce Bureau of Industry and Security ("BIS") issued a list of designated military end users ("MEU List") under the Export Administration Regulations ("EAR") (see our prior alert available [here](#)). As due diligence guidance, BIS noted that exporters should closely scrutinize those Chinese Military Companies designated by DoD that are not currently in the MEU List. For compliance, the DoD-designated Chinese Military Companies raise a red flag requiring additional due diligence as to whether a license is required prior to the export, reexport or transfer of MEU Items to such DoD-designated entities. Therefore, in addition to the investors of the Chinese Military Company securities, exporters should also be mindful of the recent developments in Chinese Military Company designations discussed above.

Please contact one of the authors of this alert or your Miller Canfield attorney should you have any questions as to the applicability or restrictions of the amended EO, FAQs or the MEU List or enhanced EAR diligence requirements.