

THE DAWN OF CAPITAL MARKETS SANCTIONS

The U.S. Government Embraces a Potent
New Lever of Financial Statecraft



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NEW LEVER OF FINANCIAL STATECRAFT

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EXECUTIVE SUMMARY

[The Dawn of Capital Markets Sanctions](#)

Among the many new forms of economic and financial statecraft directed at China by the U.S. government over the past several years, the effort to restrict and discipline Chinese corporate access to U.S. capital, and even implement the first-ever capital markets sanctions, stands out as the most innovative, novel and likely most consequential.

This potent new front was opened over the course of a series of actions that mostly took place during the latter half of the Trump Administration, culminating with the issuance of Executive Order (E.O.) 13959 on November 12, 2020, and with the affirmation and strengthening of these policies in E.O. 14032 that was issued by the Biden Administration on June 3, 2021.

Although we are still in the early days of the U.S. security community's leveraging of the U.S. capital markets as a source of national power and influence – while also protecting them (and U.S. shareholders) from exploitation, non-transparency and serving to fund various authoritarian pursuits – the bipartisan actions of the past two years have established new precedents of historic importance. The significance of these actions bears understanding, including what makes them unique compared to other, established forms of economic and financial statecraft.

As a baseline, it is worth remembering that, although the U.S. capital markets hold approximately half of the world's investible capital and well over half of its liquidity, they have almost never been seen either as an instrument of American power projection and defense that could be leveraged to protect U.S. strategic interests or as an asset that bears protecting from corporate actors with malevolent agendas. This has not been the case with regard to trade, export controls, foreign investment or even banking, each of which represent aspects of the U.S. economy and financial system that have been deemed reasonable and worthy of protection and/or leveraging when the stakes are sufficiently high with regard to national security or human rights policy.

Even in situations where sanctions of various types have been seen as the non-military options of last resort in crisis scenarios, the U.S. capital markets have been kept sacrosanct and off-limits for the past two decades or more from the point of view of imposing restrictions guided by these overarching issues of national importance. This has stubbornly persisted despite the dominant position held by the United States in this specific domain globally.

Barring any reversal or dilution, the actions of the past two years have broken this impasse, with significant consequences for both U.S. adversaries and competitors, especially China, and market players of various types, from retail investors to Wall Street mavens.

[Executive Orders 13959 and 14032](#)

The Trump Administration's original order, E.O. 13959, prohibited U.S. investors from holding the securities of companies identified as "Communist Chinese Military Companies" (CCMCs) by the U.S. Department of Defense. The requirement to identify and publicly list CCMCs emanated from a provision written into Section 1237 of the 1999 National Defense Authorization Act. Absent E.O. 13959, however, this list of companies had no practical penalty, serving a primarily educational function or simply as a means "to name and shame" the targeted companies. The issuance of E.O. 13959 changed this in dramatic fashion, imposing the first-ever capital markets sanctions targeting Chinese companies.

While observers waited to see if the Biden Administration would reverse course on this policy mechanism due to the potential perception of the E.O. as an "ill-considered, last-minute" action by an outgoing president, President Biden did the opposite by issuing E.O. 14032, titled "Addressing the Threat from Securities Investments that Finance Certain Companies of the People's Republic of China." In this order, the White House expanded the scope of sanctionable companies (e.g., to include surveillance technology sector enterprises in order to address human rights abuses) and institutionalized, on a bipartisan basis, capital markets sanctions as a permanent and powerful new policy tool in the hands of American leadership). The Biden Administration declared on June 3 that,

"...the [Biden] Administration will not hesitate to prevent U.S. capital from flowing into the PRC's defense and related materiel sector, including companies that support the PRC's military, intelligence, and other security research and development programs; or into Chinese companies that develop or use Chinese surveillance technology to facilitate repression or serious human rights abuse."¹

Although there are significant unanswered questions about the extent and intensity with which the Biden Administration intends to follow through on this policy, the initial set of actions and statements that were announced appeared to show solidarity with the compelling logic and worthiness of what they inherited. Indeed, the fact sheet that accompanied the E.O. noted that

¹ <https://www.whitehouse.gov/briefing-room/statements-releases/2021/06/03/fact-sheet-executive-order-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china/>

E.O. 14032 is intended to “solidify and strengthen” E.O. 13959 and “prohibit U.S. investments in the military-industrial complex of the People’s Republic of China.”²

Key Questions on Implementation

Nevertheless, among the key questions that will persist for some time is whether the U.S. Department of the Treasury, which has been newly put in charge of implementing these capital markets sanctions, will be proactive about adding to the list of implicated companies that it now controls almost entirely. This new list is described as the Non-SDN Chinese Military-Industrial Complex Companies (NS-CMIC) list, which will be maintained by the Treasury Department's Office of Foreign Assets Control (OFAC). Observers are also watching for any dilution or walking-back of key provisions – and intentions – of E.O. 14032 and its predecessor (e.g., through such means as publishing “Frequently Asked Questions” used to clarify and adjust the fine points of policy announcements such as these).

While President Trump’s original E.O. 13959 gave primary authority to the Pentagon over the selection of companies that were to be targeted with capital markets sanctions, E.O. 14032 gives near total discretion to the Secretary of the Treasury as to which Chinese companies go on the NS-CMIC list and which do not. A number of Congressional members have already expressed skepticism with regard to Treasury's objectivity in this connection.

Despite this rather serious implementation question, the E.O. targets with capital markets sanctions any company determined by the U.S. Treasury Department “to operate or have operated in the defense and related materiel sector or the surveillance technology sector of the economy of the PRC.” If properly and comprehensively executed, this would broaden considerably the application of the sanctions imposed by E.O. 13959.

Going forward, there are a number of important milestones and barometers that can, and likely will, be used to measure the degree to which the Biden Administration intends to expand on its initial list and implement the underlying sanctions. Perhaps most important will be how the Treasury Department’s list of companies compares to the public lists that are already mandated of the Pentagon, including the new Section 1260H list that was mandated in the most recent NDAA for 2021 that also calls for a public list of Chinese military companies (expanded to include those involved in official Chinese military-civil fusion programs).

² <https://www.whitehouse.gov/briefing-room/statements-releases/2021/06/03/fact-sheet-executive-order-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china/>

The overlap between the methodology that underpins these separate lists and that which is supposed to earn Chinese companies a place on the Treasury Department's NS-CMIC list, based on the targeting criteria put in place by E.O. 14032, invites an obvious comparison between the actions coming out of the U.S. government from different agencies. Any company that ends up on the Pentagon's Section 1260H list, but not on the Treasury Department's NS-CMIC list, will raise concern, confusion and likely opposition and activism from Capitol Hill, NGOs and other constituencies. The same is likely true even of companies determined by expert non-governmental researchers, from NGOs to the media, that can be documented to have ties that make them worthy of inclusion on the Treasury list.

Separate from the capital markets sanctions now imposed by two successive administrations, the "Innovation and Competition Act of 2021" (the comprehensive, bipartisan legislation putting forth a strategy for countering China that was passed by the Senate on June 8), includes reporting language in Section 3407 that will likewise put a spotlight on the Treasury Department's NS-CMIC list. This section requires that a detailed and well-researched report be issued within 180 days on the presence of Chinese corporate "bad actors" in the U.S. capital markets and their identities. The specific requirements for this report are sufficiently detailed and comprehensive that, when published, it is likely to have direct relevance and significance to those at the Treasury Department maintaining the NS-CMIC list.³

[The Means of Access for Chinese Companies to U.S. Capital](#)

The scrutiny from the public and the government of the identities and business operations of Chinese companies accessing the U.S. capital markets has intensified alongside the increase in the number and type of such companies entering the markets. Chinese companies have become more accessible to U.S. investors via their inclusion by major index providers in ubiquitous international and emerging markets indices and their derivative index funds as well as through direct listings on U.S. exchanges.

U.S. policymakers have targeted both of these points of access during the past year, objecting to the track records of many of these companies on issues of national security and human rights, but also taking issue with the "investor protection" problems associated with opaque Chinese companies entering the portfolios of American retail investors without being subject to the same transparency and disclosure requirements that are expected of their U.S. corporate counterparts. Indeed, a number of high-profile cases in recent years of Chinese companies defrauding investors

³ <https://www.congress.gov/bill/117th-congress/senate-bill/1260/text?q=%7B%22search%22%3A%5B%221260%22%5D%7D&r=3&s=3>

has motivated policymakers to take action on this issue from this “investor protection” perspective.

On the matter of Chinese companies directly listing on U.S. exchanges, the Congress unanimously passed the Holding Foreign Companies Accountable Act (HFCAA) in December 2020, which was an effort to unwind the exemptions that Chinese companies have enjoyed for most of the past two decades from the same official auditing requirements that govern U.S. companies, i.e., those administered by the Public Companies Accounting Oversight Board (PCAOB), which requires access to independent audits for companies listed on U.S. exchanges. The HFCAA requires the delisting of any Chinese company that fails to come into compliance with these rules within three years. As the PCAOB exemptions in place for Chinese companies are there at Beijing’s insistence, due to the accounting records of Chinese companies being considered “state secrets,” the provisions of the HFCAA have set in motion a rather serious, necessary and belated showdown with the Chinese Communist Party (CCP) on fundamental “disclosure” issues.

[The Interweaving of CCP Strategic Objectives and the Operations of Chinese Companies Adds to the Impetus for Action](#)

Recently, it was reported in May 2021, that the China Securities Regulatory Commission (CSRC) was considering requiring companies pursuing IPOs outside of mainland China to get their listing documents approved by the government before doing so in order to ensure that their disclosures did not release sensitive data that might be of national security interest.

In the U.S., this move has merely served to reinforce the concerns described above, which are rooted in the reality that the behavior of Chinese companies is, in most, if not all, circumstances, monitored and controlled by the state. Indeed, the fact that Beijing perceives the financials and operations of even their ostensibly privately held, publicly traded companies (let alone their publicly traded state-owned enterprises) to be “state secrets,” has been an open admission for years, underpinning their argument for why they should not have to be subject to the same disclosure requirements as their international competitors.

Laws enacted in Beijing during the tenure of President Xi Jinping, such as the National Intelligence Law and Cybersecurity Law, each passed in 2017, have further entrenched the ability of the CCP to weaponize its companies for strategic purposes, including espionage, adding to the U.S. government’s and the markets’ perception of the often asymmetric risk that is baked into these companies.

This has created not just national security problems for U.S. policymakers, but serious questions about the rationale behind China's approach – and that of their companies – to disclosure and transparency and the degree to which it is all intertwined with Beijing's perception of national security and the advancement of the CCP's strategic objectives.

[Leveraging and Protecting the U.S. Capital Markets Emerges as a Key Component of Economic and Financial Statecraft](#)

Ultimately, however, as important as the particulars of implementation of these policies are, what has transpired already in the U.S. government with regard to capital markets sanctions is extraordinary. A set of unprecedented measures have been imposed, reinforced and strengthened by two administrations – one Republican and one Democrat – all taking place in a hyper-partisan political environment. Even the HFCAA of 2020 was remarkably bipartisan (indeed unanimous) and retains its high level of support.

These developments demonstrate a new awareness and appreciation by the U.S. security community and the American body politic of the immense geopolitical leverage that exists by virtue of the U.S. capital markets and a willingness to make use of that leverage – all for the first time. It demonstrates that Wall Street has failed, also for the first time, to prevent U.S. policymakers from moving into their protected “air space” to exercise this aspect of American power for national security, human rights and investor protection purposes. Perhaps most importantly, it represents a new focus by the U.S. security community, particularly the National Security Council, on an area where the economic and financial ambitions of the CCP are especially vulnerable (e.g., a rigid requirement for large-scale, dollar-denominated financing out of the U.S. capital markets annually).

While China's own capital markets are growing and those of other exchanges around the world have yet to follow suit in terms of demonstrating a similar willingness to impose sanctions of this new type, the dominance of United States in this domain means that Washington retains the capacity to lead in a manner that carries a real cost for Chinese companies that are engaging in behavior that raises national security, human rights and investor protection concerns. This is not cheery news to the CCP, which can be expected to push back vigorously, as it did within days of the Biden Administration's June 3 announcement of E.O. 14032.

BACKGROUND

The lack of scrutiny of, or reaction to, the growing number of Chinese companies accessing the U.S. capital markets over the past two decades has resulted in a situation where scores of millions of American retail investors are, usually unwittingly, holding the securities of Chinese companies that are engaged in business operations that conflict with the national security and human rights concerns of the United States and its allies and partners around the world. Regardless of their track records in these policy areas, these companies are, in almost all cases, also not meeting the transparency and disclosure requirements legally required of other companies present in the U.S. capital markets.

The companies getting caught in this net include Chinese entities that are: sanctioned or officially designated; linked to the PLA; complicit in human rights abuses; involved in building and militarizing Beijing's illegal islands in the South China Sea; participating in the construction of Beijing's surveillance state (at home and abroad); contributing to China's military-civil fusion programs; manufacturing advanced weapons systems; engaged in weapons proliferation, espionage and/or cyber-attacks; and complicit in environmental degradation among other issues of concern.

Most of the time, these companies enter the investment portfolios of average investors through index funds, particularly exchange-traded funds (ETFs), that are benchmarked against indices. The providers of these indices perform little to no non-financial diligence or screening (especially on matters of national security and human rights) before incorporating these companies as constituents in their investment products via their listings on domestic Shenzhen and Shanghai exchanges (so-called "A Shares").

Certain Chinese companies, however, enter the U.S. capital markets directly via listings on U.S. exchanges. They have done so by taking advantage of preferential treatment being administered by the Securities and Exchange Commission (SEC) that stem from regulations enacted in the early 2000s that exempted Chinese enterprises from certain legally-binding compliance requirements. As a result, rules related to fiduciary responsibility, good corporate governance, complete disclosure and transparency, the rule of law and other safeguards have often been circumvented by Chinese companies – with the permission of U.S. regulators – thereby intensifying the financial risks posed to American investors.

The situation grew worse in the wake of the Enron fraud in the early 2000s, when American firms were forced to comply with the Sarbanes-Oxley legislation, while Chinese firms were – and remain – exempt from the same requirements since May 2013. Beijing's demand for dollar-

denominated capital to finance its Belt and Road and other costly initiatives has increased markedly since then, as has the scope and type of companies coming to the U.S. markets. Of course, over this same period, the behavior of the CCP, led by China's president, Xi Jinping, has also become more aggressive and ambitious in terms of reinforcing the principles of authoritarianism at home, including by centralizing control over the entire business sector through such measures as inserting CCP cells within the organizational structures of Chinese companies, and projecting its model of governance abroad.

Indexes, ETFs, and A-Shares

With the rather rapid inclusion of the China "A-shares" into major stock market indices, the establishment of the Japan-China ETF Connectivity scheme, and the launch of the Shanghai-London Stock Connect program, international investor exposure to public Chinese companies has multiplied several-fold over the past two years.

Exchange-traded funds (ETFs) are passively managed, tracking specific stock market indices that measure the performance of a fixed set of securities. Each index provider maintains its own criteria to screen securities for inclusion in its global market indices, which are all weighted by market capitalization and meet certain liquidity requirements.

Many index providers curate ESG specialty indexes that are in compliance with industry-standard, non-financial environmental, social, and corporate governance (ESG) factors that socially conscious investors are increasingly applying as part of their analysis process to screen potential investments. The scope constraints of ESG, well-intentioned as they may be, however, have thus far not taken into account the types of national security- and human rights-related risk factors present in companies that are under the influence of states, like China and Russia.

When, in an ominous development for the national security community, leading index providers MSCI, FTSE Russell, and S&P Dow Jones made the decision to include hundreds of mainland Chinese "A-shares" in their international and global indexes in 2018 and 2019, Chinese companies in mainland stock exchanges became integrated into the investment holdings of U.S. individual and institutional investors. In May 2018, MSCI released a list of 234 Chinese A-shares to be included in its MSCI Emerging Markets (EM) Index, which has \$1.8 trillion in active and passive assets benchmarked against it, beginning in June.⁴ One year later, FTSE Russell followed suit with its decision to incorporate 1,051 A-share companies into its FTSE Emerging Index, which is

⁴ <https://www.msci.com/documents/1296102/1362201/MSCI-MIS-EM-May-2018.pdf/b1b05adf-4bf3-9acc-404c-9865da3e9997>

tracked by \$140 billion globally.⁵ In both cases, the number and weighting of Chinese companies in these indices has since grown considerably.

The various economic, geographical, and growth criteria that leading index providers evaluate when building an index, including new constituents or increasing constituent weighting, do not include consideration for the material risks in relation to national security, sanctions regimes, human rights violations or non-compliance with U.S. federal securities laws. MSCI's methodology for index inclusion, for example, features minimum size, market-cap, liquidity, and length of trading requirements. FTSE's methodology is primarily concerned with availability of timely data, demonstration of international interest, and liquidity requirements.⁶

Direct Overseas Listings and the Use of Offshore Shell Companies

Chinese companies can choose to raise funds through direct overseas listings, where they obtain primary listing status on overseas stock exchanges or through backdoor listings using shell companies. Overseas listings can increase a Chinese company's international visibility and promote the company's products and services to an international market. To list through backdoor options, Chinese firms can purchase already-listed shell companies or create shells, which they have often done by registering a new holding company overseas in locales such as Bermuda, the British Virgin Islands, the Cayman Islands, or the Dutch Caribbean.

As of June 2020, the Cayman Islands hosts over 50 percent of Chinese companies traded on American exchanges, compared to just 4.8 percent in Delaware. Among the many loopholes that have enabled Chinese entities to exploit the U.S. capital markets at the expense of shareholders is the Variable Interest Equity (VIE) corporate structure that has been used by Chinese firms to list abroad.

VIEs have been employed by Chinese firms as a way to circumvent strict foreign ownership limitations imposed by Beijing. To operate as a VIE company, a Chinese entity will enter into a contractual agreement with an offshore entity (i.e., a Cayman subsidiary) to form an economic partnership or agreement that essentially infuses that subsidiary with the overall economic value of the business of the parent entity. This means shares in the subsidiary essentially mirror the value of holding shares in the parent.

This structure allows for the parent operating company to derive funding from securities issued by its offshore subsidiary and for foreign shareholders to own a stake in the success of the Chinese

⁵ <https://www.ftserussell.com/blogs/china-shares-inclusion-seven-key-points>

⁶ <https://institutional.vanguard.com/VGApp/iip/institutional/csa/investments/benchmarks/home>

parent company, but in a manner that does not technically grant shareholders any actual ownership in the China-domiciled parent. While a VIE does not necessarily need to be incorporated in the Cayman Islands, many companies choose to do so because of the benefits provided by Cayman Companies Law. This structure, while commonly used and accepted by Wall Street, also poses potentially serious risks for investors.

The VIE structure and the permissive legal environments of offshore countries of registration, such as the Cayman Islands, has been a key enabler of Chinese companies looking for a way to raise funds from U.S. investors without subjecting themselves to the same levels of transparency, disclosure, regulatory and legal requirements as the vast majority of U.S. companies.

As described further below, one of the ways lax regulation and judiciary process in these locales has harmed U.S. investors has been in the way that delistings have occurred, where publicly traded Chinese controlled companies have chosen to privatize by forcing out their U.S. shareholders at significant undervaluation. The result has been, even in departing U.S. markets, partially in response to the pressures described above, Chinese companies have been permitted by these jurisdictions to harm U.S. investors one last time.

Using these, among other strategies, Chinese companies, including those that have raised national security, human rights and investor protection issues, have entered the investment portfolios of U.S. investors and derived significant intangible as well as tangible benefits (i.e., prestige and legitimacy) from direct listings on prominent U.S. exchanges, such as the New York Stock Exchange (NYSE).

U.S. CAPITAL MARKETS LEVERAGE

A *Wall Street Journal* article from September 2020 cited eight U.S.-listed Chinese companies that had launched additional listings in Hong Kong or Shanghai during the course of that year, citing the risk of being delisted or cut off from U.S. capital markets in their prospectuses.⁷ Last year reportedly saw a record number of secondary listings floated in Hong Kong and Shanghai. For some, this news and the underlying trend was a demonstration of new U.S. pressure having the desired effect (in certain circumstances) of limiting U.S. shareholder exposure to companies unwilling to abide by federal securities laws, appropriate regulatory standards, proper governance, or eschew nefarious activities.

Others, however, have argued that the delisting and exclusion of Chinese companies from the U.S. capital markets will only result in an exodus of publicly traded Chinese companies and IPOs to domestic Chinese markets, resulting in a significant capital outflow and losses for U.S. banks and investors (and, it is contended, harm the broader economy and competitiveness of the U.S. capital markets in the process). The premise of this argument is that China does not especially need U.S. capital or large-scale dollar financing annually and will find the money elsewhere. It is argued that the United States would be “shooting itself in the foot” if it follows through in delisting Chinese companies which are non-compliant or determined to be threats to national security and human rights.

Proponents of this view, however, neglect to address:

- 1) the merits of the U.S. regulatory and security policy concerns that underpin these select companies being expelled;
- 2) the ethics of permitting the U.S. capital markets – the largest, deepest and most liquid in the world – to be tapped by companies that are non-compliant with basic shareholder protection standards and/or that are engaged in business activity that raises serious national security and human rights concerns; and
- 3) the reality that, at best, Chinese companies departing the U.S. capital markets are doing so primarily in response to political pressures, not because they see it as in their financial interests. In other words, while it may be possible to point to “silver linings” for Beijing associated with this trend, the forced retreat of Chinese companies from the U.S. markets is more of a nightmare than a benefit for CCP leadership, particularly if a return trip to

⁷ <https://www.wsj.com/articles/chinese-companies-head-home-to-raise-money-as-beijings-relations-with-u-s-fray-11601199002>

U.S. markets via inclusion in index funds are also cut off (as they are in E.O. 13959 and E.O. 14032).

This perspective also neglects to consider the unique attributes of the U.S. capital markets that make them indispensable for a country with urgent dollar financing requirements of the scale needed by China. The U.S. capital markets are approximately the size of the rest of the world's combined and represent an even larger proportion of the world's investible capital and liquidity. American markets are also perceived as having among the best analysts, research capabilities, and fair regulatory environments available.

While individual companies can avail themselves of alternatives, a country with China's aspirations for growth lacks any near-term substitute for the U.S. capital markets. The value of Chinese technology companies' public offerings, for example, would be too large to be managed by other global markets over time. These factors, along with the prestige garnered in listing on a U.S. exchange, cement the status of U.S. capital markets as the world's "gold standard," as emphasized by a *Wall Street Journal* article published in August.⁸ This reality is demonstrated by the 30 Chinese companies that have gone public on U.S. exchanges in 2020 alone.⁹

China's demand for liquidity denominated in U.S. dollars represents a critical source of funding for the Chinese government's activities at home and abroad. According to Natalie Blythe, head of global trade and receivables finance at HSBC, the unprecedented funding requirements of President Xi's Belt and Road Initiative "require tapping into every single source of public and private funding available" to maintain sufficiently deep currency reserves supplemented by public and private sources of funding.¹⁰

The reaction of China's largest telecommunications companies, China Mobile, China Unicom, and China Telecom, to being delisted by the New York Stock Exchange (NYSE) following the issuance of E.O. 13959 is likely indicative of how other Chinese companies feel concerning the importance of these listings, both from a financial and reputational perspective. The NYSE announced on December 31, 2020 that it would delist the three major Chinese telecom carriers – China Mobile (CHL), China Telecom (CHA), and China Unicom (CHU) in accordance with E.O. 13959's divestment mandate and additional directives from the U.S. Treasury Department's Office of Foreign Assets Control (OFAC) – with plans to suspend trading on January 7 or January

⁸ https://www.wsj.com/articles/the-gold-standard-why-chinese-startups-still-flock-to-the-u-s-for-ipo-11597313278?mod=article_inline

⁹ <https://www.cnbc.com/2020/12/18/china-based-companies-raise-the-most-money-via-us-ipo-since-2014.html>

¹⁰ https://www.wsj.com/articles/the-gold-standard-why-chinese-startups-still-flock-to-the-u-s-for-ipo-11597313278?mod=article_inline

11.¹¹ Each of the companies sent letters to the Board of the NYSE within hours of President Biden's inauguration, in hopes and anticipation that the new administration would adopt a more lenient posture.¹² The final appeal of these companies to remain on a U.S. exchange was rejected on May 7, 2021 and the NYSE proceeded with delisting plans.¹³

¹¹ <https://www.reuters.com/article/us-usa-china-nyse-delisting/nyse-starts-process-of-delisting-three-chinese-telco-companies-idUSKBN29621Q>; <https://www.bloomberg.com/news/articles/2021-01-06/treasury-names-three-chinese-telecoms-that-exchanges-must-delist>

¹² <https://asia.nikkei.com/Business/Markets/Chinese-telcos-test-Biden-on-Day-One-with-NYSE-listing-plea>

¹³ <https://www.wsj.com/articles/nyse-to-delist-chinese-telecoms-carriers-after-rejecting-appeals-11620394719>

A HISTORIC FIRST: EXECUTIVE ORDER 13959

On November 12, 2020, President Trump invoked his authorities under the International Emergency Economic Powers Act (IEEPA) and the National Emergencies Act to issue E.O. 13959 to issue E.O. 13959, embodying the first-ever capital markets sanctions deployed against China. The E.O. prohibited U.S. investors from investing in Chinese companies that have been determined by the Defense Department to be “Chinese Communist Military Companies” (CCMCs) per requirements implemented by Section 1237 of the National Defense Authorization Act (NDAA) of FY 1999. The E.O. imposed a number of policies that sought to limit the degree to which companies affiliated with the Chinese military could benefit from U.S. capital, including the following important provisions:

- ❖ all U.S. investors worldwide were prohibited from holding the securities of CCMCs effective November 11, 2021;
- ❖ subsidiaries that are 50% or more owned by CCMCs were to be automatically placed on a list managed by the Office of Foreign Assets Control (OFAC) of the Treasury Department that would serve as the official list of restricted holdings;
- ❖ subsidiaries of these CCMCs, irrespective of the percentage ownership, were to be added directly to by the Pentagon to the Section 1237 list (and then mirrored by the OFAC list that imposes the capital markets sanctions); and
- ❖ the E.O. required index funds (especially exchange-traded funds) to face the same prohibitions and be restricted in their ability to hold these companies (i.e., the CCMCs and their subsidiaries) in passive investment products.

Prior to E.O. 13959, there was no real penalty to being designated as a CCMC by the Pentagon. This E.O. gave real teeth to that list and began a dialogue about what other lists of known – or at least U.S. government-identified – corporate entities believed to be high risk for reasons of national security or human rights might also warrant such treatment. For example, officials began to ask if companies from the Entity List, a list of companies subject to special export controls that is managed by the Bureau of Industry and Security (BIS) by the U.S. Commerce Department, should be subject to capital markets sanctions, including those included on the list for human rights violations.

Publicly Traded Chinese Military Companies Implicated by E.O. 13959

Ultimately, after five tranches of companies were added by the Pentagon to the list of CCMCs, there were 44 companies on the list, 11 of which were directly publicly traded.¹⁴ Stemming from these 44 companies, approximately 133 publicly traded subsidiaries were implicated. As of the end of the Trump Administration, however, the Treasury Department had only affirmed a small subset of these companies as being subject to capital markets sanctions (despite the implicated companies having been separately identified and listed by a public State Department “Fact Sheet” addressing this issue¹⁵), leaving the fine points of these designations and the E.O.’s interpretation to President Biden.

RWR conducted its own research and published a list – initially on June 30, 2020,¹⁶ and then updated on June 3, 2021¹⁷ -- that documented those publicly traded Chinese companies implicated by E.O. 13959 and Section 1237 of the NDAA of 1999. This list included the publicly traded subsidiaries and affiliates of these companies. The names on this list were accessible to U.S. individual and institutional investors as A-shares, H shares, or Red Chips, and, in some cases, were included in popular indexes like the MSCI Emerging Markets (EM) Index and the FTSE All-World Index, which have been used as benchmarks for exchange-traded funds (ETFs) with international exposure. Most of these companies remain accessible to U.S. investors and included in prominent investment products.

¹⁴ There were originally 46 companies, but Xiaomi Corp. and Luokung Technology both filed lawsuits and were granted preliminary relief against the financial restrictions in early 2021. The companies were removed from the Defense Department list of CCMCs and were not included in the new list of Chinese military-industrial companies (CMICs) created by President Biden and housed under the Treasury Department under E.O. 14032.

¹⁵ <https://2017-2021.state.gov/communist-chinese-military-companies-listed-under-e-o-13959-have-more-than-1100-subsidiaries/index.html>

¹⁶ <https://www.rwradvisory.com/rwr-releases-report-on-the-u-s-capital-markets-exposure-of-chinese-pla-affiliated-companies-listed-and-released-by-the-pentagon/>

¹⁷ <https://www.rwradvisory.com/updated-list-of-publicly-traded-chinese-entities-implicated-by-the-original-executive-order-13959-targeting-pla-affiliated-companies/>

THE LATEST: EXECUTIVE ORDER 14032

What Was Clarified by President Biden's Executive Order 14032?

- ❖ The text of the Fact Sheet published by the White House describing President Biden's E.O. 14032 amending E.O. 13959 was tough and pointed, not just concerning the threat, but also about the soundness of the underlying concept of capital markets sanctions, noting, for example, that, "This E.O. prevents U.S. investment from supporting the Chinese defense sector...It signals that the Administration will not hesitate to prevent U.S. capital from flowing into the PRC's defense and related materiel sector..."
- ❖ In solidifying and strengthening E.O. 13959, the White House preserved the fundamental principles of the original Order, streamlined the process for targeting companies and broadened the number of companies that were listed as officially implicated by these sanctions. They did so by creating a new list that would be entirely managed by the Treasury Department that would constitute the list of companies subject to the capital markets sanctions. This list is described as the Non-SDN Chinese Military-Industrial Complex Companies List (i.e., the NS-CMIC list), administered by the Treasury Department's Office of Foreign Assets Control (OFAC).
- ❖ One of the strengthening aspects of E.O. 14032 is the definition of companies targeted by capital markets sanctions, which included entities determined "to operate or have operated in the defense and related materiel sector or the surveillance technology sector of the economy of the PRC," or those determined "to own or control, or to be owned or controlled by, directly or indirectly," such entities. This expanded the companies implicated by these capital markets sanctions – if the definition actually leads to the appropriate listings – beyond the definition that was used by E.O. 13959, which was linked only to CCMC designations. The parameters of E.O. 14032 even go beyond even what is mandated under Section 1260H of the 2021 NDAA, which expanded the criteria of Section 1237 of the 1999 NDAA, to include Chinese companies involved in China's official military-civil fusion programs.
- ❖ Section 1260H of the NDAA for FY 2021 provided an updated definition of a qualifying Chinese military company as an entity, "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.”¹⁸

- ❖ The adoption of the expansive list of companies in the annex of the amended Executive Order sets a precedent of including subsidiaries and affiliates of designated companies. The list adopted was almost identical to a list that was included in the “Fact Sheet” published by the State Department under the Trump Administration, which (as described above) was published seemingly to document which of the CCMCs were publicly traded and their respective publicly traded subsidiaries.¹⁹ This established a presence of including the publicly traded subsidiaries of companies caught in the net of the E.O.’s methodology, even when they, independently, may not have such ties.
- ❖ If applied consistently in the future, this would mean that the U.S. government does not intend merely to name the privately held (or state-owned) parent companies (that are immune to capital markets sanctions), while leaving their publicly traded subsidiaries unaffected – which is a strategy that has been employed in the past by sanction policy practitioners as a means of symbolically rebuking a company, but doing so in a manner that leaves its subsidiaries or affiliates alone, so as not to inflict an actual cost (and to avoid the diplomatic and sometimes economic fallout of that cost).
- ❖ In other words, avoiding sanctioning the parts of a company’s family tree that are actually vulnerable has been used as a means of signal sending, rather than actually seeking to penalize an offending company and its assets (including its subsidiaries). Some of the companies implicated in the annex to E.O. 14032, for now, demonstrate an effort to ensure that the publicly traded subsidiaries of targeted parent companies properly bear the responsibility and risk of their controlling shareholder.
- ❖ Finally, E.O. 14032 also affirmed the relevance of the original capital markets sanctions to index funds, a critically important detail that, as described above, implicates a primary point of access – and fundraising – by Chinese companies to the U.S. capital markets.

What Questions Remain?

- ❖ The placement of the Treasury Department as the central player in the management of the new list is potentially troubling and means that there is no automatic process for

¹⁸ <https://www.congress.gov/116/bills/hr6395/BILLS-116hr6395enr.pdf>

¹⁹ <https://2017-2021.state.gov/communist-chinese-military-companies-listed-under-e-o-13959-have-more-than-1100-subsidiaries/index.html>

sanctioning Chinese companies as a result of another agency or department (particularly, the Department of Defense) seeing fit to include them in a list (such as the Section 1260H list). Although this introduces the possibility of a significant disparity between lists that have similar methodologies, the public nature of the Section 1260H list will, at minimum, necessitate an explanation for such differences. Indeed, an explanation will be required in these instances to ensure a clear message to the markets and to satisfy the implementation concerns of other stakeholders, including those on Capitol Hill, who are advocates for an unswerving, tough line on these funding issues.

- ❖ There are several companies that were listed as CCMCs by Section 1237 that did not make it onto the annex of the amended Executive Order: CRRC, Dawning (Sugon), CNCEC, CSCEC and AMEC. Answers to questions about the rationale behind these kinds of disparities will be early tests of how convincingly the Treasury Department will be able to explain the differences between its list and those of other agencies purporting to be documenting the same types of entities.
- ❖ There are efforts underway on Capitol Hill to legislate on capital markets sanctions, as legislators are seeking to codify some of the measures already implemented by Executive Order. These efforts could gain momentum, should the Biden Administration not enforce the E.O. 14032 as aggressively as expected by the Congress. Whether or not the White House retains control of the process or if it is codified into law, making it more of a rigid requirement and risk factor for the markets, will depend on a number of the factors described above.

[What Are the Present Differences between the Lists?](#)

The first list of companies implicated by Section 1260H was released just hours following the announcement of E.O. 14032 on June 3. Although the new E.O. detached the capital markets sanctions from the listing processes of the Pentagon, rendering the Section 1237 list and the new Section 1260H list technically irrelevant from the point of view of automatic sanctions, these lists remain important for the reasons cited above. There is significant overlap between the methodology for inclusion on these lists and that which was adopted by the Biden Administration in E.O. 14032 for the new OFAC-administered list of NS-CMIC companies.

There are five publicly traded companies from the Pentagon's Section 1237 list of CCMCs that were not included in the more recently issued 1260H list²⁰ and also not included in the Treasury Department's NS-CMIC list issued on June 3, 2021.²¹ These companies are:

- ❖ China State Construction Engineering Corporation (CSCEC) (601668.SS)
- ❖ Dawning Information Industry Co., Ltd. (Sugon) (603019.SS)²²
- ❖ China National Chemical Engineering Group Co., Ltd. (CNCEC) (601117.SS)
- ❖ CRRC Corporation Ltd. (601766.SS) (01766.HK)
- ❖ Advanced Micro-Fabrication Equipment Inc. (AMEC) (688012.SS)

There are 18 companies on the NS-CMIC list that are not on DoD's 1260H list.

- ❖ Aero Engine Corporation of China (AECC) (not public)
- ❖ Aerospace Communications Holdings Co., Ltd. (Aerocom) (600677.SS)
- ❖ Aerosun Corp. (600501.SS)
- ❖ Anhui Great Wall Military Industry Co., Ltd. (601606.SS)
- ❖ Changsha Jingjia Microelectronics Co., Ltd. (300474.SZ)
- ❖ China Academy of Launch Vehicle Technology (CALT) (not public)
- ❖ China Aerospace Science and Technology Corporation (CASC) (not public)
- ❖ China Aerospace Times Electronics Co., Ltd. (CATEC) (600879.SS)
- ❖ China Avionics Systems Co., Ltd. (600372.SS)
- ❖ China Nuclear Engineering & Construction Corp. Ltd. (CNECC), formerly China National Nuclear Corp. (601611.SS)
- ❖ China Satellite Communications Co., Ltd. (China Satcom) (601698.SS)
- ❖ China Shipbuilding Industry Corp. (CSIC) (601989.SS)
- ❖ China Shipbuilding Industry Group Power Co., Ltd. (600482.SS)

²⁰ <https://media.defense.gov/2021/Jun/03/2002734519/-1/-1/0/ENTITIES-IDENTIFIED-AS-CHINESE-MILITARY-COMPANIES-OPERATING-IN-THE-US.PDF>

²¹ <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/executive-order-on-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china/>

²² Sugon is also included on the BIS Entity List administered by the Commerce Department. It was added in 2019 for military end-use concerns related to supercomputer development. <https://www.federalregister.gov/documents/2019/06/24/2019-13245/addition-of-entities-to-the-entity-list-and-revision-of-an-entry-on-the-entity-list>

- ❖ CSSC Offshore and Marine Engineering (Group) Co., Ltd. (COMEC) (600685.SS) (00317.HK)
- ❖ Guizhou Space Appliance Co., Ltd. (002025.SZ)
- ❖ Nanjing Panda Electronics Co., Ltd. (600775.SS) (00553.HK)
- ❖ North Navigation Control Technology Co., Ltd. (600435.SS)
- ❖ Shaanxi Zhongtian Rocket Technology Co., Ltd. (003009.SZ)

There are 26 companies on the 1260H list that are new and were not on the original 1237 list.

- ❖ Aerospace CH UAV Co., Ltd (002389.SZ)
- ❖ AVIC Aviation High-Technology Company Limited (600862.SS)
- ❖ AVIC Heavy Machinery Co., Ltd. (600765.SS)
- ❖ AVIC Jonhon Optronics Technology Co., Ltd. (002179.SZ)
- ❖ AVIC Shenyang Aircraft Co., Ltd. (600760.SS)
- ❖ AVIC Xi'an Aircraft Industry Group Co., Ltd. (000768.SZ)
- ❖ China Communications Construction Group (Limited) (CCCCG) (not public)
- ❖ China Marine Information Electronics CO., Ltd. (600764.SS)
- ❖ China Mobile Ltd. (00941.HK)
- ❖ China Telecom Corporation Ltd. (00728.HK)
- ❖ China Unicom (Hong Kong) Limited (00762.HK)
- ❖ CNOOC Ltd. (0883.HK) (NYSE: CEO)
- ❖ Costar Group Co., Ltd. (not public)
- ❖ Fujian Torch Electron Technology Co., Ltd. (603678.SS)
- ❖ Huawei Investment & Holding Co., Ltd. (not public)
- ❖ Inner Mongolia First Machinery Group Co., Ltd. (600967.SS)
- ❖ AVIC Jiangxi Hongdu Aviation Industry Co., Ltd. (600316.SS)
- ❖ Semiconductor Manufacturing International (Beijing) Corporation (not public)
- ❖ Semiconductor Manufacturing International (Shenzhen) Corporation (not public)
- ❖ Semiconductor Manufacturing International (Tianjin) Corporation (not public)
- ❖ Semiconductor Manufacturing South China Corporation (not public)
- ❖ SMIC Holdings Limited (not public)

- ❖ SMIC Hong Kong International Company Limited (not public)
- ❖ SMIC Northern Integrated Circuit Manufacturing (Beijing) Co., Ltd. (not public)
- ❖ SMIC Semiconductor Manufacturing (Shanghai) Co., Ltd. (not public)
- ❖ Zhonghang Electronic Measuring Instruments Company Limited (300114-SZ)

There are eight companies on the 1260H list, all subsidiaries of SMIC, that were not on the NS-CMIC list, although none are publicly traded.

- ❖ Semiconductor Manufacturing International (Beijing) Corporation (not public)
- ❖ Semiconductor Manufacturing International (Shenzhen) Corporation (not public)
- ❖ Semiconductor Manufacturing International (Tianjin) Corporation (not public)
- ❖ Semiconductor Manufacturing South China Corporation (not public)
- ❖ SMIC Holdings Limited (not public)
- ❖ SMIC Hong Kong International Company Limited (not public)
- ❖ SMIC Northern Integrated Circuit Manufacturing (Beijing) Co., Ltd. (not public)
- ❖ SMIC Semiconductor Manufacturing (Shanghai) Co., Ltd. (not public)

CASE STUDIES: PROFILES OF PUBLICLY TRADED CHINESE COMPANIES

As noted above, among the many publicly traded Chinese companies present in the U.S. capital markets are entities that have already raised national security and human rights concerns – including companies that have previously been sanctioned, or are currently subject to economic and trade sanctions by the U.S. government. Below are profiles of some of the more prominent companies.

Aviation Industry Corporation of China (AVIC)

- ❖ AVIC and its network of subsidiary units develop and produce a range of aircraft (e.g., fighters, trainers, and helicopters), unmanned aircraft systems (UAS), and airborne weapons for the People’s Liberation Army Air Force, People’s Liberation Army Naval Air Force, and People’s Liberation Army Rocket Force.
- ❖ AVIC and its subsidiaries have been sanctioned by the U.S. government several times for proliferation activities in violation of the Iran, North Korea, and Syria Nonproliferation Act. The company allegedly helped Iran to develop a new ground-based anti-ship cruise missile and has separately transferred weapons systems and equipment to sanctioned countries such as Sudan, Iraq, and North Korea.²³
- ❖ AVIC was included in the first list of Communist Chinese Military Companies (CCMCs) released by the U.S. Department of Defense in June 2020, as well as the new list of Chinese Military Companies (CMCs) released by the Defense Department in June 2021 – with the addition of six publicly-traded subsidiaries.²⁴ AVIC was also added to the Biden Administration’s list of NS-CMIC companies that are subject to capital markets restrictions, following the issuance of E.O. 14032 in June 2021.²⁵ It should be noted that

²³ https://www.everycrsreport.com/files/20040416_RL31555_967a00924579d573593255b157b852094eff97c0.pdf;
https://www.hrw.org/legacy/reports98/sudan/Sudarm988-05.htm#P577_102736;

<http://www.janes.com/article/80108/sudan-s-new-ftc-2000-jets-arrive>

²⁴ https://media.defense.gov/2020/Aug/28/2002486659/-1/-1/LINK_2_1237_TRANCHE_1_QUALIFYING_ENTITIES.PDF;

<https://media.defense.gov/2021/Jun/03/2002734519/-1/-1/0/ENTITIES-IDENTIFIED-AS-CHINESE-MILITARY-COMPANIES-OPERATING-IN-THE-US.PDF>

<https://media.defense.gov/2021/Jun/03/2002734519/-1/-1/0/ENTITIES-IDENTIFIED-AS-CHINESE-MILITARY-COMPANIES-OPERATING-IN-THE-US.PDF>

²⁵ <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/executive-order-on-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china>

AVIC has at least 26 publicly traded subsidiaries, although not all have military operations.

China Shipbuilding Group Co., Ltd.

- ❖ China State Shipbuilding Corporation (CSIC) merged with China State Shipbuilding Corporation (CSSC) in November 2019 to become the world's largest shipbuilder by sales, now known as China Shipbuilding Group Co., Ltd. Both CSIC and CSSC appear to have retained management of their pre-merger assets, which were divided by region, and both remain publicly traded.
- ❖ Naval equipment produced by China Shipbuilding Group includes guided missile destroyers, frigates, conventional submarines, nuclear-powered ballistic missile submarines, unmanned aerial vehicle (UAV) systems, and, most notably, aircraft carriers. China's first carrier, the Type 001 aka Liaoning, was purchased from Ukraine and refitted at the Liaoning Province shipyard of CSIC's subsidiary, Dalian Shipbuilding Industry Corporation, before entering PLAN service in September 2012.²⁶ China's first domestically designed and built aircraft carrier, the Type 001A, was also manufactured at Dalian's Liaoning shipyard and began sea trials in May 2018.²⁷ CSIC is presently working on China's third carrier and first nuclear-powered carrier with a speculative completion date of 2025, when China plans to launch its fully integrated and networked blue-water navy.²⁸
- ❖ CSIC and CSSC were both included in the first list of CCMCs released by the U.S. Department of Defense in June 2020.²⁹ CSSC was also included in the new list of CMCs released by the Defense Department in June 2021, with the addition of CSIC subsidiary China Marine Information Electronics (CMIE), although CSIC itself was removed.³⁰ All three companies, plus CSIC subsidiary China Shipbuilding Industry Group Power, were added to the Biden Administration's list of NS-CMICs that are subject to capital markets

²⁶ <https://www.reuters.com/article/us-china-military-carrier/china-announces-formal-handover-of-first-aircraft-carrier-idUSBRE88O04Z20120925>

²⁷ <http://www.chinadaily.com.cn/a/201805/14/WS5af8864ca3103f6866ee80c3.html>

²⁸ <https://www.reuters.com/article/us-china-defence-uke/china-has-plan-to-build-nuclear-powered-aircraft-carrier-idUSKCN1GC159>

²⁹ <https://media.defense.gov/2021/Jun/03/2002734519/-1/-1/0/ENTITIES-IDENTIFIED-AS-CHINESE-MILITARY-COMPANIES-OPERATING-IN-THE-US.PDF>

³⁰ https://media.defense.gov/2020/Aug/28/2002486659/-1/-1/1/LINK_2_1237_TRANCHE_1_QUALIFYING_ENTITIES.PDF

restrictions, following the issuance of E.O. 14032 in June 2021.³¹ CSIC and CSSC have at least eight listed companies between them, all of which are involved in the shipbuilding industry.³²

Hangzhou Hikvision Digital Technology Co., Ltd.

- ❖ Hikvision has its origins in a Chinese government research institute and manufactures security and video surveillance products that have been instrumental in the Chinese government's efforts to put in place a surveillance state in the Xinjiang Uyghur Autonomous Region (XUAR). Hikvision provided systems to secure the Qinghai-Tibet railway before the same technology was deployed in Xinjiang for security and surveillance purposes, including to equip the detention camps that reportedly hold over a million ethnic Uyghurs.
- ❖ Hikvision's controlling shareholder is the state-owned China Electronics Technology Group Corporation (CETC). The U.S. Department of Commerce Bureau of Industry and Security (BIS) added 17 of CETC's subsidiaries to its Entity List in August 2018 for "activities contrary to the national security or foreign policy interests of the United States." More specifically, these subsidiaries of CETC are believed to be "involved in the illicit procurement of commodities and technologies for unauthorized military end-use in China."³³
- ❖ On October 9, 2019, the Bureau of Industry and Security (BIS) also added 28 Chinese entities to the Entity List, including Hikvision, for "acting contrary to the national security or foreign policy interests of the United States." Specifically, Hikvision and the other 27 entities have been determined by the U.S. government to be involved in human rights violations and abuses in Xinjiang.³⁴
- ❖ The U.S. General Services Administration released an interim rule amending the Federal Acquisition Regulation (FAR) pursuant to the FY19 National Defense Authorization Act (NDAA) in August 2019, prohibiting federal agencies from procuring telecommunications and video surveillance services or equipment from Hikvision.

³¹ <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/executive-order-on-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china>

³² <https://www.globaltimes.cn/content/1156452.shtml>

³³ <https://www.federalregister.gov/documents/2018/08/01/2018-16474/addition-of-certain-entities-and-modification-of-entry-on-the-entity-list>

³⁴ <https://www.federalregister.gov/documents/2019/10/09/2019-22210/addition-of-certain-entities-to-the-entity-list>

- ❖ Hikvision has been included in the first list of CCMCs released by the U.S. Department of Defense in June 2020, the new list of CMCs released by the Defense Department in June 2021, and the Biden Administration’s list of NS-CMICs issued in June 2021.³⁵ Under President Biden’s recently issued E.O. 14032, Hikvision was also named a provider of Chinese surveillance technology used to “facilitate repression or serious human rights abuses” presenting threats to the “national security, foreign policy, and economy of the United States.”³⁶

³⁵ <https://media.defense.gov/2021/Jun/03/2002734519/-1/-1/0/ENTITIES-IDENTIFIED-AS-CHINESE-MILITARY-COMPANIES-OPERATING-IN-THE-US.PDF>; https://media.defense.gov/2020/Aug/28/2002486659/-1/-1/1/LINK_2_1237_TRANCHE_1_QUALIFYING_ENTITIES.PDF; <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/executive-order-on-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china>

³⁶ <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/executive-order-on-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china>

CHINA PUSHES BACK AGAINST U.S. CAPITAL MARKETS PRESSURE

As U.S. pressure on China – including via capital markets sanctions – has grown, Beijing has been increasingly looking for, and implementing, retaliatory countermeasures. Although these responses have been varied and unconventional, they may be establishing a new norm of pushback from Beijing. Most recently, the CCP stamped through its “rubber stamp” legislature a new law that would protect its companies from foreign sanctions.

In January 2021, Beijing announced that it would allow Chinese courts to punish companies that comply with foreign laws that damage national interests, and there are already a variety of examples of Chinese sanctions issued against offending foreign officials and companies for policies and statements perceived by Beijing as harmful to its interests and international reputation.³⁷

The circumstances described below are just a few examples of a jockeying for influence and leverage that is playing out in ever-more dramatic fashion in the domain of economic and financial statecraft between the U.S. and China. Just as the U.S. is now willing to use selectively its unique leverage in the capital markets to push back against predations of the CCP on the global stage, Beijing is similarly determined to show foreign powers, businesses and investors that they will pay a price for choosing to align themselves with U.S. positions that the CCP considers threatening to their core strategic interests.

[New Chinese Legislation Protecting Its Companies from Foreign Sanctions](#)

On June 10, 2021, China passed a new bill that is intended to counter the sanctions emerging from Washington, DC, in this case most directly in response to the “Innovation and Competition Act of 2021” that is still moving through the U.S. Congress at this writing. According to a *Reuters* interpretation, the new law – effective immediately -- puts at risk of sanctions any “individual or entity “involved in the making, or implementation of, discriminatory measures against Chinese citizens, or interfering with China's internal affairs could be put onto a blacklist.”³⁸ The legislation also reportedly puts at risk the relatives of these individuals as well as the organizations where they work.

³⁷ <https://www.msn.com/en-in/news/world/china-mulls-new-law-to-fight-foreign-sanctions-amid-rising-us-pressure/ar-AAKNlxs?li=AAggbRN&%253Bocid=iehp>

³⁸ <https://www.reuters.com/world/china/an-eye-an-eye-chinas-new-anti-foreign-sanctions-law-2021-06-11/>

Targeting Foreign Businesspersons and Companies

On a number of occasions this year, Beijing has targeted and penalized businesspersons and foreign companies that have acknowledged the risk associated with having supply chains run through Xinjiang, where Beijing is reportedly using forced labor and committing genocide against the minority Uyghur population.

After H&M announced, it would stop buying cotton from the region,³⁹ for example, the company was met with swift and widespread repercussions in China, both from consumers (incited on social media by the government) and government officials alike. Xu Guixiang, a government publicity official in Xinjiang, said in a press briefing in March 2021 that foreign companies operating in China should avoid becoming involved in politics or risk losing access to the Chinese market. H&M stores in China were subsequently removed from Apple and Baidu map services.⁴⁰

Targeting Foreign Government Officials

China has also targeted foreign officials deemed responsible for the U.S. government policy behind the creative measures of the past several years. For example, on January 20, 2021, Beijing targeted former senior Trump Administration officials: Mike Pompeo; Peter Navarro, Robert O'Brien, David Stilwell, Matt Pottinger, Alex Azar, Keith Krach, John Bolton, Steve Bannon and Kelly Craft with targeted sanctions. These individuals were described as:

“...anti-China politicians in the United States, out of their selfish political interests and prejudice and hatred against China and showing no regard for the interests of the Chinese and American people, have planned, promoted and executed a series of crazy moves which have gravely interfered in China's internal affairs, undermined China's interests, offended the Chinese people, and seriously disrupted China-U.S. relations.”

Selectively Instructing Chinese Companies to Return to China's Capital Markets

On the financial front, Beijing has instructed successful Chinese companies to leave U.S. exchanges and return home to help develop China's capital markets. As regulatory pressure increases and bilateral relations grow more tense, Beijing has begun implementing policies to ease the return of Chinese companies to its domestic markets.

³⁹ <https://www.nytimes.com/2021/04/06/business/xinjiang-china-cotton-brands.html>

⁴⁰ <https://www.reuters.com/world/china/china-says-us-uk-eu-canada-seek-destabilise-china-2021-03-29/>

These policies serve several purposes for Beijing, not just retaliation. By bolstering the liquidity, value, and legitimacy of mainland markets, Beijing simultaneously makes good on some of its promises to “open up” its financial markets, becomes a more reputable global financial center, and attracts foreign capital, all while assuming a position of greater control over leading Chinese companies that have triggered substantial anxiety among CCP leadership due to their embrace by foreign markets (e.g., the Ant Group, etc.)

Although the realization of the country’s financial goals should involve wholeheartedly embracing the success of some of its companies on foreign exchanges, this “upside” has come into conflict with the preservation and centralization of power and control (particularly under the watchful, rather paranoid gaze of Xi Jinping). This was in clear evidence during the recent collapse of what would have been an IPO of historic proportions by Ant Group in November 2020 and a capricious \$3 billion fine recently imposed on Alibaba.

Some of Beijing’s efforts to retain control over its publicly traded companies include the examples listed below.

- ❖ In 2015, China’s premier Li Keqiang announced to the State Council that there would be relaxations on listing regulations for domestic startups, particularly those using the Variable Interest Equity (VIE) structure for operations abroad.
- ❖ In 2018, the China Securities Regulatory Commission (CSRC) announced that it would begin allowing the domestic flotation of overseas-listed Chinese companies, enabling a slew of U.S-listed Chinese companies to list also on the Chinese markets.⁴¹ This is closely linked to the move by the CSRC to fast-track IPOs in fields essential to the Chinese economy (one of the major detractors to listing on domestic exchanges had been the lengthy IPO approval period), particularly in emerging fields such as high end manufacturing, AI, biotechnology, and other tech companies.⁴²
- ❖ In May 2020, the CSRC made an additional adjustment to the listing requirements for red-chip companies, companies registered abroad but operating in mainland China and largely controlled by Chinese state entities, that wish to list on domestic markets. Previously, red-chip entities required a capitalization of at least 200 billion yuan to list in mainland China. This reform lowered the market capitalization to 20 billion yuan.⁴³

⁴¹ <https://www.cnbc.com/2018/06/06/china-allows-domestic-fundraising-for-overseas-listed-firms.html>

⁴² <https://assets.kpmg/content/dam/kpmg/cn/pdf/en/2018/06/2018-mid-year-ipo-review-china-hk.pdf>
https://news.cgtn.com/news/3d6b444e78456a4d/share_p.html

⁴³ http://english.www.gov.cn/statecouncil/ministries/202005/01/content_WS5eac25d4c6d0b3f0e9496db5.html

Calling Chinese companies home with streamlined re-listing and IPO requirements has had the effect of encouraging some Chinese companies listed in the United States to pursue privatization under the legal jurisdiction of the Cayman Islands, where most are domiciled. As noted above, in many cases, this delisting process has resulted in the “squeezing out” of minority shareholders at management-set valuations on terms that are detrimental to American minority shareholders: a harmful “exit strategy” being employed regularly.

Over 95 percent of Chinese firms listed in the United States, but incorporated in the Cayman Islands, issue securities through a Cayman entity. In recent years, companies like Sohu.com and China Biologic Products, which were legally domiciled in Delaware, have spent millions of dollars hiring American law firms to change their business registrations to the Cayman Islands, presumably to take advantage of its lax corporate governance regime.

[Using Offshore Registrations to Delist from U.S. Exchanges at Unfair Valuations](#)

Many of these U.S.-listed Chinese companies, after gaining access to U.S. capital, are now delisting and trying to purchase back shares at significant discount to fair value. Some have then relisted – after a brief hiatus – on the Hong Kong or a Chinese mainland exchange at a much higher valuation. This maneuver relies on a combination of opaque ownership structures, offshore domiciling and expensive legal teams to achieve a profit at the expense of American minority shareholders. Offshore regulations governing take-private transactions have allowed Chinese management teams and aligned private equity firms to “squeeze out” minority shareholders, offering them little recourse to protest undervalued share prices.

Ultimately, the lack of transparency, disclosure and fairness afflicting investors in Chinese companies, together with increased regulatory pressure in the United States, has created an ironic – and unacceptable – situation where some companies targeted by policymakers and the media for being “bad actors” in the areas of national security and human rights (as described above), are taking advantage of their departure from U.S. exchanges to harm U.S. investors one last time on their way out the door.

Without access to independent government audits, investors and regulators are, in many cases, unable to assess whether the company valuation has been deliberately manipulated during the take-private deal, leaving U.S.-based minority shareholders who experience material losses during this exit strategy, to rely on appraisal litigation in pursuit of fair value. The rulings in these lawsuits, however, have not been fair or favorable to the investors, with the Cayman judiciary highly deferential to the Chinese management and owners, while exhibiting undue skepticism towards investors. As such, these lawsuits have not served as a deterrent for Chinese

entities concerning these unfair practices. As a result, U.S.-listed Chinese entities now have a proven playbook of accounting and legal maneuvers available to them that can deliver a highly profitable retreat from justifiable U.S. political pressure.

Although the percentage of Chinese companies present in the U.S. capital markets that have carried out delistings and relistings in the manner described above is still relatively small, there are many more that could follow this fraudulent path that have collectively tapped U.S. retail investors for hundreds of billions of dollars. Accordingly, the potential for the problems associated with delisting – including the resulting lawsuits – to become more important is significant. This is especially the case given the growing bipartisan scrutiny of how seemingly benign Chinese commercial entities pose serious strategic concerns for the U.S. security and human rights communities, while also raising material investor protection issues.

In other words, there may be a number of companies that have the capacity, as well as an ever-increasing motive, to follow the same route described above to defraud millions of American shareholders and reap huge profits in the process. While the increased U.S. oversight and pressure facing Chinese companies listed on U.S. exchanges is necessary to uphold fiduciary responsibility, proper diligence and authentic investor protection, additional attention is required to ensure that the exit strategy most often used by these same companies is not permitting a profitable departure at the expense of the very shareholders that they have already exploited.

The regulations governing privatization deals differ significantly for companies incorporated in the United States – particularly Delaware, the most common U.S. state for incorporation – and the Cayman Islands, where most U.S.-listed Chinese companies are domiciled. Efficient and established court systems and regulatory bodies ensure that shareholders of Delaware-incorporated companies are protected from fraud through stringent disclosure requirements and from “squeeze out” privatization deals by supervised and regulated processes for privatization and guaranteed legal recourse. For these and other reasons, Delaware has – unsurprisingly – not been China’s top choice for business registrations.

Delaware corporate law aims to incentivize incorporation by offering consistent enforcement of regulations as well as investor protection and recourse for harmful practices such as self-dealing, which is prevented by stringent regulations around vertical integration and oversight of related party transactions. Cayman Companies Law, by contrast, offers little protection against such harmful practices. This lax regulatory regime even facilitates the forced squeeze-out of minority shareholders at a significant discount to fair value, allowing Chinese controlling shareholders to reap huge economic windfalls at the expense of U.S. investors.

This kind of opacity is ideal for Chinese companies that rely on listing and capital raising through their Cayman affiliates as a central feature of their corporate strategy. Whereas this type of structure would be regulated under Delaware law to prevent self-dealing transactions, in the Cayman Islands, shareholder protections are considerably less robust.

OUTLOOK FOR APPLYING CAPITAL MARKETS SANCTIONS AGAINST CORPORATE HUMAN RIGHTS ABUSERS

[Applying Capital Markets Sanctions to China's Human Rights Abusers](#)

On the human rights front, it is important to note that, while “NS-CMICs” presently face capital markets sanctions via E.O. 14032, the securities of Chinese companies involved in enabling what has been designated as genocide by the current Administration, forced labor practices, repression of the Tibetans and other egregious human rights offenses face no similar limitations. The exception could be the category of business activity that is “surveillance technology” that was added in E.O. 14032, but their inclusion currently resides under an umbrella of national security concern, as did their predecessor list of CCMCs that was targeted by E.O. 13959.

This situation could be addressed by building on existing policy precedent with regard to prohibitions currently in place targeting Chinese military companies. There is already interest in this concept on Capitol Hill. Doing so would first require the creation of a new official list, perhaps termed the “Chinese Corporate Human Rights Abusers List,” which could initially draw from the inclusion of companies that meet this criteria that have already been added to the Commerce Department’s “Entity List” and the Pentagon’s Section 1237 and 1260H lists. A company’s appearance on this new, official list – regardless of which agency manages it – could automatically trigger the imposition of capital markets sanctions, potentially mirroring those detailed in E.O. 13959 and E.O. 14032. Alternatively, the methodology of E.O. 14032 could be amended and expanded further.

U.S. sanctions regimes to date have not included any restrictions on offending companies listing or trading in U.S. capital markets or being held in portfolio via index funds for reasons of human rights abuses. Indeed, the “naming and shaming” of these companies, or even targeting them with trade sanctions or export controls, which has been the approach to date, has been of little consequence to fund managers on Wall Street and elsewhere. Such sanctions, export controls and designations have not prohibited – or, in many cases, even reduced – the inclusion of these companies in major indexes and index-managed funds. As the human rights abuses taking place in China – enabled by Chinese companies – comes increasingly to light, however, there are an array of potential entities that might well become implicated.

The Expansion of Corporate Human Rights Abusers to Companies Exploiting Laborers at Belt and Road Projects

A report published at the end of April 2021 brought to the fore that China has not only been brazen about committing, allowing, and enabling human rights abuses against ethnic minorities, but also against Chinese laborers working on development projects around the world (implicating major Chinese companies, including state-owned enterprises).⁴⁴ Several recent articles^{45, 46} have highlighted the backlash to Belt and Road Initiative (BRI) projects for a variety of reasons, but a *Washington Post* piece, and the NGO report it references, was the first to allege that Chinese government actors, likely in coordination with Chinese companies, have been forcing Chinese nationals to work on BRI projects under conditions that some NGOs have labeled as egregious enough to be considered violations of these workers' human rights. The companies implicated risk being added to the list of entities targeted not just for export controls and sanctions, but capital markets sanctions following the new model put in place by E.O. 13959 and consolidated in E.O. 14032.

Publicly Traded Chinese Companies Already on the "Entity List" for Human Rights Abuses, but Not Targeted with Capital Markets Sanctions

Since the fall of 2019, the Commerce Department has already added several dozen Chinese companies to the Entity List for "acting contrary to the foreign policy interests of the United States" and, more specifically, having been implicated in human rights violations and the implementation of mass arbitrary detention, high-technology and biometric surveillance, and forced labor against Uyghurs in Xinjiang.

- ❖ On July 22, 2020, the Commerce Department added eleven Chinese companies to the Entity List "in connection with the practice of forced labor involving Uyghurs and other Muslim minority groups" and "conducting genetic analyses used to further the repression of Uyghurs and other Muslim minorities" in the XUAR.⁴⁷

⁴⁴ https://www.washingtonpost.com/world/asia_pacific/china-labor-belt-road-covid/2021/04/30/f110e8de-9cd4-11eb-b2f5-7d2f0182750d_story.html

⁴⁵ <https://www.foreignaffairs.com/articles/china/2021-04-20/how-not-win-allies-and-influence-geopolitics>

⁴⁶ <https://www.scmp.com/news/china/diplomacy/article/3130866/pakistan-bombing-puts-spotlight-security-chinas-flagship-belt>

⁴⁷ <https://www.commerce.gov/news/press-releases/2020/07/commerce-department-adds-eleven-chinese-entities-implicated-human>

- ❖ On June 5, 2020, the Commerce Department added nine Chinese companies to the Entity List for having been “implicated in human rights violations and abuses,” mass arbitrary detention, and high-tech surveillance in the XUAR.⁴⁸
- ❖ On May 22, 2020, the Commerce Department added eight Chinese companies and institutions to the Entity List for being “complicit in human rights violations and abuses,” mass arbitrary detention, and high-tech surveillance in the XUAR.⁴⁹
- ❖ On October 9, 2019, the Commerce Department added 28 entities, including eight Chinese companies to the Entity List for having been “implicated in human rights violations and abuses,” mass arbitrary detention, and high-tech surveillance in the XUAR.⁵⁰

Of these recent 47 additions to the Entity List, 16 are publicly traded on the Shanghai (SS), Shenzhen (SZ), and Hong Kong (HK) Stock Exchanges, either directly or through or their parent entities. Listed by most recent date of Entity List addition, these are:

Hefei Meiling Co., Ltd. (000521.SZ)

- ❖ Meiling is a major home appliance manufacturer based in Hefei Economic and Technological Development Zone that produces refrigerators, freezers, air conditioners, and other home appliances, supplying overseas companies such as Electrolux. As of 2018, the company employed over 1,500 Uyghur workers that had been transferred from Xinjiang to Anhui province.⁵¹ Hefei Meiling changed its name to Changhong Meiling Co., Ltd. in June 2018, but this change is not reflected in BIS documents.

KTK Group Co., Ltd. (603680.SS)

Subsidiary of CRRC Co., Ltd. (601766.SS) (01766.HK)

- ❖ KTK Group manufactures railway transportation supporting products including vehicle interiors, control systems, and rolling stock accessories for international customers including Alstom, Bombardier, and Siemens. It employs about a thousand workers that

⁴⁸ <https://www.federalregister.gov/documents/2020/06/05/2020-10868/addition-of-certain-entities-to-the-entity-list-revision-of-existing-entries-on-the-entity-list>

⁴⁹ <https://www.commerce.gov/news/press-releases/2020/05/commerce-department-add-nine-chinese-entities-related-human-rights>

⁵⁰ <https://www.federalregister.gov/documents/2019/10/09/2019-22210/addition-of-certain-entities-to-the-entity-list>

⁵¹ <http://archive.ph/wip/AAvQv>

have been transferred from Xinjiang to its factories in Jiangsu.⁵² Formerly known as Jiangsu Jianhu Rail Transit Equipment Co., Ltd.⁵³

Nanjing Synergy Textiles Co., Ltd.

Subsidiary of Victory City International Holdings Ltd. (00539.HK)

- ❖ Nanjing Synergy Textiles produces and supplies cotton knitting yarns for yarn and fabric processing, using a number of workers from Xinjiang – including ethnic Kazakhs – that have been transferred to the company’s Jiangsu factories.⁵⁴

Nanchang O-Film Tech Co., Ltd.

Subsidiary of OFilm Group Co., Ltd (002456.SZ)

- ❖ O-Film Tech produces optoelectronics for end-use consumer goods such as electronics and smart vehicles. It employs over a thousand Uyghur workers transferred out of Xinjiang to its Jiangxu factories.⁵⁵ Uyghur and Kazakh workers are reportedly subject to coercive labor practices and make touch screens and fingerprint recognition scanners for international tech companies like Apple, Samsung, Lenovo, and Huawei.⁵⁶

Jiangsu Tanyuan Technology Co. Ltd. (603133.SS)

- ❖ Tanyuan Technology is a primary supplier of graphite heat dissipation materials used in touch screens for consumer electronics and vehicles, using at least 250 Uyghur workers transferred from Xinjiang to Jiangsu.⁵⁷

Xinjiang Silk Road BGI Co., Ltd.

Subsidiary of BGI Genomics Co., Ltd. (300676.SZ)

- ❖ According to BGI Genomics, which provides DNA sequencing and biomedical services, Xinjiang Silk Road BGI has not been active since its establishment in November 2016.⁵⁸

⁵² <http://www.xjnlk.gov.cn/info/1161/19344.htm>; <https://www.harderrlp.com/wp-content/uploads/2020/04/Dkt-1-Complaint.pdf>

⁵³ <http://www.wjjh.com/>

⁵⁴ <http://archive.ph/recum>

⁵⁵ <http://archive.ph/qEvOK>

⁵⁶ <https://abcnews.go.com/Business/wireStory/gadgets-tech-giants-made-coerced-uyghur-labor-69450269>

⁵⁷ <http://archive.ph/hRVKq>

⁵⁸ <https://www.bgi.com/us/company/news/statement-regarding-bgis-subidiaries-being-added-to-uss-entity-list/>

Beijing Liuhe BGI Co., Ltd.*Subsidiary of BGI Genomics Co., Ltd. (300676.SZ)*

- ❖ Beijing Liuhe BGI provides commercial DNA sequencing services for disease-related scientific research, and has been involved in studies of Uyghur genetic information.⁵⁹

Aksu Huafu Textiles Co., Ltd.*Subsidiary of Huafu Fashion Co., Ltd. (002042.SZ)*

- ❖ Aksu Huafu Textiles produces mélange yarn out of Aksu Textile Industrial City. Huafu Fashion is the world's largest supplier of mélange yarn. The company operates a vocational training program in cooperation with the government that feeds workers to its factories and mills, and has been identified as a forced labor pipeline.⁶⁰

FiberHome Telecommunication Technologies Co., Ltd. (600498.SS)

- ❖ Fiberhome operates a strategic base in Xinjiang and has a strategic cooperation agreement with the Xinjiang Production and Construction Corps (XPCC) to build smart cities equipped with surveillance technology. XPCC is a ubiquitous paramilitary organization that has also been added to the Entity List for its involvement building detention centers and facilitating forced labor programs in the XUAR.⁶¹

Nanjing FiberHome Starrysky Communication Development Co., Ltd.*Subsidiary of FiberHome (600498.SS)*

- ❖ Starrysky produces network security and big data software, including a smart policing mobile application used by Chinese border authorities to extract personal data from the smartphones of travelers entering Xinjiang and scan for religious content.⁶²

Dongfang Netpower Technology Co., Ltd. aka NetPosa (300367.SZ)

- ❖ NetPosa is the parent company of SenseNet, which supplies China's Skynet Project surveillance system with facial recognition tracking services across public spaces in Xinjiang. The company's chairman serves on a Ministry of Public Security committee that sets national security technology standards.

⁵⁹ <https://www.axios.com/chinese-coronavirus-test-maker-agreed-to-build-a-xinjiang-gene-bank-f82b6918-d6c5-45f9-90b8-dad3341d6a6e.html>

⁶⁰ https://www.wsj.com/articles/western-companies-get-tangled-in-chinas-muslim-clampdown-11558017472;http://www.chinadaily.com.cn/a/201808/14/WS5b72a6a1a310add14f385ba2_4.html

⁶¹ http://news.cnr.cn/native/gd/20180814/t20180814_524331653.shtml

⁶² <https://www.nytimes.com/2019/07/02/technology/china-xinjiang-app.html>

Shenzhen Shenwang Vision Technology Co., Ltd. (SenseNet)*Subsidiary of NetPosa Technologies Ltd. (300367.SZ)*

- ❖ SenseNet is a joint venture between NetPosa and SenseTime Group that supplies China's Skynet Project with facial recognition tracking services across public spaces in Xinjiang.

Zhejiang Dahua Technology Co., Ltd. (002236.SZ)

- ❖ Dahua Technology provides video surveillance products and services used in machine vision, video conferencing, professional drones, and RFID systems. It has received over a billion dollars in contracts for video surveillance and security projects in the XUAR, including facial recognition and data storage systems.⁶³

Hangzhou Hikvision Digital Technology Co., Ltd. (002415.SZ)

- ❖ Hikvision is one of the world's largest manufacturers of video surveillance products, with a full line including CCTV cameras, DVRs, and video management software. It has equipped several detention facilities in Xinjiang and won hundreds of millions of dollars worth of security contracts in the region. Hikvision also operates a research center in Xinjiang and has worked on Uyghur-specific AI image and video projects at a paramilitary base in Urumqi.⁶⁴

Iflytek Co., Ltd. (002230.SZ)

- ❖ Iflytek (stylizes as iFlytek) produces speech recognition software and products, including the first AI open platform for smart hardware developers in China. It has supplied voiceprint collection systems to Kashgar police in Xinjiang and partnered with the Xinjiang Public Security Bureau and with telecommunications companies to integrate voice pattern data into surveillance systems.⁶⁵

Xiamen Meiya Pico Information Co. Ltd. (300188.SZ)

- ❖ Meiya Pico produces digital forensics and cybersecurity products and services, including technology to detect Uyghur and Islamic symbols in photos, an app reportedly used by police to extract smartphone data from individuals, and a range of drones.⁶⁶ It has

⁶³ http://www.its114.com/html/2017/changshangyaowen_0217/84407.html; <https://ipvm.com/reports/xinjiang-dahua-hikvision>

⁶⁴ <https://ipvm.com/reports/hik-xj-pap>

⁶⁵ <https://www.reuters.com/article/us-china-xinjiang-mit-tech-insight/risky-partner-top-u-s-universities-took-funds-from-chinese-firm-tied-to-xinjiang-security-idUSKCN1TE04M>; <https://www.hrw.org/news/2017/10/22/china-voice-biometric-collection-threatens-privacy>

⁶⁶ <https://www.scmp.com/tech/start-ups/article/3017688/what-you-need-know-about-meiya-pico-chinas-low-profile-forensics>; <https://www.rfa.org/mandarin/yataibaodao/shaoshuminzu/hc-11272018150156.html>

provided the Xinjiang Police College with drone flight training for reconnaissance and patrol assignments, and is working with the Xinjiang Public Security Bureau's cybersecurity corps to build a cybersecurity training base.⁶⁷

Below are Chinese companies that allegedly employ Uyghur workers through forced labor and training programs in the XUAR, and supply surveillance and data technology to implement mass surveillance and detention programs in the XUAR, that are publicly traded but have not been added to the Entity List or other U.S. sanctions regimes:

Suzhou Good-Ark Electronics Co., Ltd. (002079.SZ)

- ❖ Good-Ark Electronics manufactures semiconductor products sold in China and in other countries. According to a 2017 agreement, Good-Ark agreed to employ 500 Uyghur workers following their completion of an education and training program that has been characterized as a detention and indoctrination program.⁶⁸ As of 2019, the company's Shandong factory employed a number of Uyghurs that had been transferred from Xinjiang.⁶⁹

Shandong Ruyi Woolen Garment Group Co., Ltd. (002193.SZ)

- ❖ Ruyi Group is the largest textile manufacturer in China and has ownership stakes in major international brands like Bally and SMCP (which owns Sandro, Maje, and Claude Pierlot). It reportedly employs 2,000 Uyghur workers across three countries in Xinjiang and has production links to several villages and households.⁷⁰ The company is also known as Shandong Ruyi Technology Group.

Jiangsu Guotai Guosheng Co. Ltd.

Subsidiary of Jiangsu Guotai International Group (002091.SZ)

- ❖ Jiangsu Guotai is a clothing and textile producer that supplies a number of international brands, including Abercrombie & Fitch, American Eagle, Target, Tommy Hilfiger, Costco, DKNY, Macy's, Kohl's, and Walmart. A satellite factory of Shandong Zoucheng Guosheng reportedly employs over 3,500 Uyghurs, making it one of the largest beneficiaries of the forced labor and training program in the XUAR.⁷¹

⁶⁷ <http://www.xjpcedu.cn/info/1161/1864.htm>; <http://stock.jrj.com.cn/2018/08/10000024944213.shtml>

⁶⁸ <http://archive.ph/3e0G3>; <https://www.harderrlp.com/wp-content/uploads/2020/04/Dkt-1-Complaint.pdf>

⁶⁹ <http://archive.ph/jXzgL>

⁷⁰ <http://archive.ph/q9VgW>; <http://archive.ph/73ip1>

⁷¹ <http://archive.ph/q9VgW>

Avary Holding (Shenzhen) Co., Ltd. (002938:SZ)

- ❖ Avary Holdings designs and manufactures printed circuit boards used in various communications, computing, and consumer electronic products. It employs about 111 Uyghurs at its Jiangsu factory that were transferred from Xinjiang, and has participated in programs seeking additional Uyghur labor transfers.⁷²

SAIC Motor Corporation Ltd. (600104.SS)

- ❖ SAIC's luxury car brand Roewe Group, which sells domestic vehicles overseas under the British MG Motor brand, employs rural laborers from Xinjiang at its Jiangsu factory.⁷³

Haoxiangni Health Food Co., Ltd. (002582.SS)

- ❖ Formerly known as Haoxiangni Jujube, the company produces dried jujube (Chinese date) and other food products using Uyghur labor at factories in both Henan province and the XUAR.⁷⁴

Youngor Textile Holdings Co., Ltd.Subsidiary of Youngor Group Co. Ltd. (600177.SS)

- ❖ Along with various subsidiaries that also operate in Xinjiang, Youngor produces textiles and textile machinery for several international brands including Calvin Klein, Gap, Lacoste, LL Bean, and Uniqlo. Over 2,000 Uyghur workers had been transferred from Xinjiang to Youngor factories in Anhui province, and the company has expressed interest in employing additional workers from the XUAR.⁷⁵

Suzhou Keda Technology Co., Ltd. aka Kedacom (603660.SS)

- ❖ Kedacom manufactures video conferencing, surveillance, and analytics technology, and has developed a platform for the Xinjiang Public Security Department's Safe City Network, connecting cities and districts across the XUAR.⁷⁶ Kedacom also worked with an unspecified Xinjiang detention center to set up an integrated security management system with video surveillance and digital interrogation capabilities.⁷⁷

⁷² <http://archive.ph/L5G9i>

⁷³ <http://archive.ph/lhdVC>

⁷⁴ <http://archive.ph/RZhne>

⁷⁵ <http://archive.ph/jsyEC>

⁷⁶ <http://data.eastmoney.com/notices/detail/603660/AN201512280012506620,JU4JThCJThGJU1JUI3JTIFJUU3JUE3JTkxJU4JUJFJUJF.html>

⁷⁷ <https://www.kedacom.com/cn/newskd/4035.jhtml>

Tongfang RIA Co., Ltd.

Subsidiary of Tsinghua Tongfang Co., Ltd. (600100.SS)

- ❖ Tongfang RIA supplies IC card and RFID technology for products including electronic reader machines and access control systems. The Aksu detention center in Xinjiang uses Tongfang RIA technology for its high-security key cards, gate management, and prison access control system.⁷⁸

Leon Technology Co., Ltd. (300603.SZ)

- ❖ Leon Technology provides security system and communications network engineering and services, and primarily operates in Xinjiang. Past projects include implementing China Mobile's smart technology data system across the XUAR that encompasses education, healthcare, digital payments, transportation, and governance, and China Mobile's cloud computing data center project in Karamay.⁷⁹ Leon Technology also set up a smart policing joint venture with SenseTime Group in 2017, known as Tangli Technology.⁸⁰

⁷⁸ <http://www.thtfria.com.cn/index.php?c=content&a=show&id=180>

⁷⁹ <https://www.msbcsc.com/viewnews-2277480.html>; <http://www.3snews.net/smartcity/260000035951.html>

⁸⁰ <https://www.ft.com/content/38aa038a-5f4f-11e9-b285-3acd5d43599e>

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