

Multinationals with Operations in China May Be Feeling Caught Between a Rock and a Hard Place

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The growing economic and political tension between the U.S. and China has placed multinationals with operations in China in a tenuous position – comply with U.S. sanctions laws, and in return, suffer economic backlash, or worse, from the Chinese government or consumers.

In recent months, China has taken several steps seemingly targeted at disincentivizing compliance with U.S. and other foreign laws, including enacting the *Provisions on the Unreliable Entity List* (“**UEL**”), the *Measures on Obstructing the Unjustified Application of Foreign Laws and Measures* (the “**Blocking Measures**”), and the *Anti-Foreign Sanctions Law* (“**AFSL**”), as well as enacting the *Data Security Law* and *Personal Information Protection Law* (collectively, “**Data Laws**”). In September 2021, China also signaled a reinvigorated anti-corruption campaign with a multi-agency announcement of newly issued “**Guidelines**.” Beyond these legislative acts, Chinese agencies, media, and celebrities participated in a series of negative campaigns targeted at multinationals adhering to U.S. sanctions laws – Swedish clothing company H&M, U.S. chipmaker Intel, and U.S. retail warehouse entity Sam’s Club (owned by Walmart). The most recent negative publicity came directly from the Chinese government as China’s anti-corruption enforcement agency, the Central Commission for Discipline Inspection (“**CCDI**”), added fuel to the growing disincentivizing fire. In an article on the CCDI website, it said that the alleged removal of products from Xinjiang province by Sam’s Club “reveals stupidity and short-sightedness, and will surely have its own bad consequences.”

This level of increased activities focused on multinationals with operations in China should serve as a reminder of the need for effective preparation, oversight, and compliance.

In 2020, the Chinese Ministry of Commerce (“**MOFCOM**”) issued the UEL, a list-based counter sanction that allows the Chinese government to impose punitive measures against foreign entities that endanger China’s sovereignty, national security, or development interests, or that suspend normal transactions or apply discriminatory measures against Chinese enterprises, organizations, or individuals. In January 2021, MOFCOM issued the Blocking Measures, which allow the Chinese government to create a “Prohibition Order” regarding foreign laws, measures, or sanctions which would prohibit compliance with such measures to the detriment of a Chinese party and countermeasures could be applied.

On July 10, 2021, China enacted the AFSL, elevating its counter-sanction regime from regulation to the level of law. The AFSL serves as a means of deflecting and disincentivizing the growing use of sanctions and other laws or

enforcement actions by foreign governments believed to be against Chinese interests. Put succinctly, the AFSL prohibits individuals and companies from complying with foreign laws China perceives to be “discriminatory restrictive measures” against China’s national interests, requiring these same individuals and entities to cooperate and implement Chinese countermeasures. The AFSL (the official Chinese version [here](#) and a crowd-sourced translation is available [here](#)) creates a mechanism through which individuals and organizations (including foreign-invested entities along with affiliated individuals and entities) can be added to a countermeasure list and subjected to certain retaliatory measures for their roles in “interfering with the internal affairs of China” in ways that are deemed “in violation of international law and basic principles of international relations.”

In the brief period since its enactment, China has already utilized the AFSL to counter-sanction U.S. individuals and organizations. First, in response to the U.S. government’s July 16, 2021 addition of seven people to the Hong Kong Business Advisory and Treasury Specially Designated Nationals list, China responded by sanctioning several U.S. individuals, including former Secretary of Commerce, Wilbur Ross, and Human Rights Watch’s China director, Sophie Richardson. Thereafter, following the U.S. Senate’s December 16, 2021, passage of the revised Uyghur Forced Labor Prevention Act and subsequent U.S. Treasury sanctioning of several Chinese companies for involvement in Xinjiang, China retaliated on December 21, 2021, with sanctions against four members of the U.S. government’s Commission on International Religious Freedom.

During this same period, on September 1 and November 1, 2021, the China Data Laws came into effect. The purported purpose of the Data Laws is to prevent harm to China’s national security, public interest, or the lawful rights and interests of Chinese citizens or organizations. The practical application of these laws, however, create disincentives for entities and individuals to comply with U.S. and other foreign laws. In general, the Data Laws apply extraterritorially to data processing and security, placing restrictions and requirements on the cross-border transfer of certain types of company data and personal information. Violations of these restrictions or requirements can result in civil, administrative, and even criminal punishments. The disincentive to comply with U.S. and other foreign laws is most evident in the requirements for entities and individuals to inform Chinese government agencies prior to the production of any data to foreign governments in relation to any foreign investigation or enforcement action, and possibly even in some civil litigation discovery, and to the extent production is allowed, those same entities and individuals must utilize Chinese government procedures for the act of production.

And, finally, in the midst of the implementation of the Data Laws, on September 8, 2021, a consortium of Chinese governmental entities – the China Central Discipline Inspection Committee, National Supervision Committee, CPC Central United Front Work Department, CPC Central Political Legal Committee, Supreme People’s Court, and Supreme People’s Procuratorate – announced that they had jointly issued the Guidelines, an internal policy statement related to anticorruption enforcement. Although the official policy statement is an internal document and therefore not available to the public, the public joint announcement made clear the Guidelines related to an increased emphasis, and cooperative approach among Chinese government entities, on the investigation of bribery – both bribe-receivers and bribe-givers. Presently, it is unclear whether U.S. or foreign entities will ultimately be the target of this increased focus on anti-corruption and related cooperation amongst Chinese government agencies; however, the heightened risk of potential blacklisting for violators, carbon copy prosecutions, and stricter approaches to confiscation as a result of the Guidelines, do appear targeted toward foreign enterprises.

THE RISK OF BLACKLISTING

Per the Guidelines, the Chinese government will explore implementation of a blacklist system for companies and individuals found to have paid bribes in China. While it is unclear how this blacklist system will be implemented, multiple avenues appear to already exist, such as the UEL or social credit system, as well as the existing ability to revoke business licenses. Once blacklisted, a company or an individual will face significant challenges in conducting business in or with China. The risk of blacklisting is not limited to violations arising from bribes to public officials, but can arise from commercial bribery, currently prohibited by China’s *Anti-Unfair Competition Law*. The Guidelines do not specify a materiality threshold related to the seriousness of the wrongdoing, although the CCDI has stated that it has prepared detailed provisions regarding the blacklisting system. Whether, or when, these thresholds may become public is unknown.

THE RISK OF CARBON COPY PROSECUTIONS

While not widely publicized, China has utilized carbon copy prosecutions (or administrative investigations) in response to public settlements with non-Chinese authorities involving conduct in China for several years. Recognizing the already existing risk of completing a lengthy government investigation only to be summoned for an additional investigation by Chinese government agencies for the same conduct, the recent anti-foreign enforcement activities, in particular, the Data Laws, by the Chinese government should serve as a warning that this risk is not simply theoretical. As previously highlighted, the Data Laws provide the Chinese government with an additional arrow in its quiver – the ability to investigate and find liability for complying with foreign subpoenas for China-based data. The application of the Data Laws serves as a double-edged sword. Whether a company elects to notify the Chinese government in advance of producing China-based data in a foreign enforcement action, as required by the newly enacted Data Laws, or whether a company elects to violate the Data Laws and willfully produce data without prior notification, the company may face some Chinese government response. In either circumstance, the current environment suggests a carbon-copy prosecution is likely to be initiated.

STRICTER AND BROADER APPROACH TOWARDS TARGETS, MITIGATION, CONFISCATION, AND COOPERATION

The new Guidelines represent a more aggressive approach by the Chinese government in terms of targeting those who pay bribes, as opposed to China's historical focus on the recipients of bribes – Chinese officials, and in terms of increasing penalties for those involved in bribes. With respect to enhanced penalties, any property or other benefit gained through the use of bribes will be subject to potential confiscation, while any access to government officials or qualifications, such as licenses to operate in China, will be subject to potential revocation or cancellation. Additionally, receiving credit for “mitigating circumstances” will be harder to obtain. Currently, credit or mitigation is usually applied if the bribe-payer actively cooperates with the investigation or self-reports wrongdoing. The Guidelines, however, emphasize the need to manage the acute risks of bribery before the conduct occurs. In other words, simply cooperating after the failure to manage the risk without putting in controls to prevent the bribes in the first place is unlikely to present a case for “mitigating circumstances.” While these enhanced restrictions do appear more in-line with enforcement actions under the FCPA, they can also be interpreted as measures that are consistent with China's interest in penalizing outsiders.

PUBLIC RELATIONS RISKS

Public relations challenges are an ever-present risk for multinational companies operating in China. Some may remember the crisis faced by European grocer, Carrefour, in the months leading up to the 2008 Olympics, or the nationwide campaign against Japanese businesses in 2005. Recently, multinationals adhering to U.S. sanctions and foreign laws have been targeted by Chinese agencies, media, and celebrities in print, television, and social media in a series of negative campaigns. The targets of these negative campaigns have included some very prominent names, including Nike, H&M, Intel, and Sam's Club.

In March 2021, the U.S., Britain, Canada, and the E.U. announced sanctions against Chinese officials related to the treatment of Uyghurs in Xinjiang province. Shortly after, numerous fashion brands, including Nike and H&M, were trending in Chinese social media with netizens calling for widespread boycotts. When allegations were raised that Intel requested its suppliers to avoid products from Xinjiang, a similar backlash was sparked. During the 2021 holiday season, a significant amount of coverage related to stories of netizens destroying Christmas decorations in Beijing. More recently, in mid-January, the CCDI published a scathing article accusing U.S. retail giant Walmart Inc and its Sam's Club chain of “stupidity and shorted-sightedness” after social media users alleged that Sam's Club had removed Xinjiang-sourced products from its stores and website. The article appeared to be directed at placing pressure on the company, as it discussed the amount of money the company has made in China, suggesting that it should take a stance on the issue.

The Sam's Club series of events may be the most telling with respect to the Chinese government's efforts to disincentivize compliance with foreign laws. Typically, informal political position statements or calls for public action from the Chinese government come through publications such as the *Global Times* or news agencies such as Xinhua. A statement from the CCDI is unique and of concern because the CCDI is the Party's enforcement arm for misconduct by Party members. This means that a statement on the CCDI website is intended for the Party and government officials, yet that intent appears distorted here. While China did spend 2020 and 2021 establishing a

counter-sanctions regime, utilizing those tools would likely have also punished Chinese economic interests. Using the CCDI website as a tool in this context appears to have been motivated by a desire to avoid this unwanted result.

THE TAKEAWAY

The recent flurry of activity and continuing international tensions suggests a very real risk that China may initiate retaliatory investigations against foreign companies. As more FCPA resolutions have encompassed alleged bribery in China, and current indicators do not suggest the risk of bribery in China has reduced, companies should be making concerted efforts to monitor their business activities within China. Beyond anti-corruption, the potential breadth of retaliatory investigations is broad, including tax, unfair competition, data security, and anti-monopoly, etc. Companies at risk of finding themselves in the middle of the U.S.-China Xinjiang dispute, or any other international tensions, should consider moving forward any planned business audits, developing contingency plans with triage teams, and conducting trainings that present best practices and strategies for handling the first moments of an investigation.

Winston's White Collar and Regulatory Teams are able to help companies prepare for the unexpected during these turbulent times, including preparation of contingency plans, local triage teams, investigation training, and preemptive audits (sanctions, tax, anti-corruption, AML, etc.).

9 Min Read

Authors

[Cari Stinebower](#)

[Jacob Harding](#)

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Cari Stinebower



Jacob Harding

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