

July 7, 2020

Hong Kong Autonomy Act

U.S. Congress Passes Sanctions Bill in Response to Chinese National Security Law

SUMMARY

On July 2, the U.S. Senate passed H.R. 7440 (the “Hong Kong Autonomy Act” or “the Act”), which, once it becomes law, will require the Executive Branch to impose sanctions against foreign individuals and financial institutions¹ determined to be “involved in the erosion of certain obligations of China with respect to Hong Kong.”²

The Hong Kong Autonomy Act would require the Executive Branch to file reports with Congress identifying individuals and entities³ determined to be “materially contributing” or attempting to materially contribute to any failure by the Chinese government to uphold its obligations under the Sino-British Joint Declaration⁴ or the Hong Kong Basic Law,⁵ which together “clarify certain obligations and promises that the Government of China has made with respect to the future of Hong Kong” as codified “in a legally-binding treaty.”⁶ The Act would also require reports to Congress that identify any foreign financial institutions determined to have knowingly conducted a “significant transaction” with persons identified in the report described in the previous sentence.⁷ The Act provides for elective sanctions on persons and entities identified in the report upon publication of the report, and mandatory sanctions after one year from inclusion in the report, unless certain conditions are satisfied. Foreign financial institutions would be subject to mandatory sanctions after one year, unless certain conditions are satisfied.

The Act was passed unanimously by both the Senate and the House of Representatives and has been sent to President Trump to sign into law. Given the overwhelming bi-partisan support for the Act in both the House and the Senate, it appears likely to take effect later this month.

KEY PROVISIONS OF THE ACT

A. EXECUTIVE REPORTS TO CONGRESS

The Act requires the Executive Branch⁸ to submit reports to Congress identifying:

- **Foreign persons.** Any foreign individual or entity determined by the Secretary of State, in consultation with the Secretary of the Treasury, to be materially contributing to, or that has materially contributed to, or attempted to materially contribute to the failure of the Government of China to meet its obligations under the Joint Declaration or the Basic Law.⁹
- **Foreign Financial Institutions.** Any foreign financial institution determined by the Secretary of the Treasury, in consultation with the Secretary of State, to knowingly¹⁰ conduct a significant transaction with a foreign person identified in the report on foreign persons.

The report on foreign persons would be required not later than 90 days after the date of enactment of the Act. The report identifying foreign financial institutions would be required not earlier than 30 days and not later than 60 days after the Secretary of State submits the report on foreign persons to Congress. Following these initial reports, the Act would require that the reports are updated in an ongoing manner, with resubmissions accompanying the annual report to Congress under Section 301 of the United States-Hong Kong Policy Act of 1992.

B. SANCTIONS

Foreign Persons

The Act provides for two sanctions upon any foreign person who appears in a report:

- Foreign persons who are individuals may be subject to exclusion from the United States.
- Foreign persons (individuals or entities) may be subject to financial sanctions essentially equivalent to designation as a blocked person (*i.e.*, sanctions that would preclude transactions with U.S. persons and freeze all property in control of U.S. persons).

Immediately after a foreign person's inclusion in a report, sanctions would be permissive; however, after one year from the date of a report, the sanctions would become mandatory unless the President issues a national security waiver or terminates the application of sanctions and removes the foreign person from the report because the Secretary of State, in consultation with the Secretary of the Treasury, has determined that the actions taken by the foreign person: (1) do not have a significant and lasting negative effect that contravenes the obligations of China under the Joint Declaration and the Basic Law; (2) are not likely to be repeated in the future; and (3) have been reversed or otherwise mitigated through positive countermeasures taken by that foreign person.¹¹

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Foreign Financial Institutions

A “menu” of ten sanctions could be imposed on foreign financial institutions identified in a report. They are:

- **(1) Loans from United States Financial Institutions.** The United States Government may prohibit any United States financial institution from making loans or providing credits to the foreign financial institution.
- **(2) Prohibition on Designation as Primary Dealer.** The Board of Governors of the Federal Reserve System and the Federal Reserve Bank of New York would not be permitted to designate, or permit the continuation of any prior designation of, the foreign financial institution as a primary dealer in United States Government debt instruments.
- **(3) Prohibition on Service as a Repository of Government Funds.** The foreign financial institution would not be permitted to serve as agent of the United States Government or serve as repository for United States Government funds—*i.e.*, the financial institution would not be permitted to take or hold U.S. government deposits.
- **(4) Foreign Exchange.** The President may prohibit any transactions in foreign exchange that are subject to the jurisdiction of the United States and in which the foreign financial institution has any interest.
- **(5) Banking Transactions.** The President may prohibit any transfers of credit or payments between financial institutions or by, through, or to any financial institution, to the extent that such transfers or payments are subject to the jurisdiction of the United States and involve any interest of the foreign financial institution—*i.e.*, the financial institution would be cut off from the United States and U.S. dollar transactions.
- **(6) Property Transactions.** The President may prohibit any person from conducting property transactions with U.S. persons (*i.e.*, pursuant to an OFAC designation). This is the equivalent of the sanction applicable to foreign persons described above.
- **(7) Restriction on Exports.** The President may restrict or prohibit exports of goods, technology, or services, directly or indirectly, from the United States to the foreign financial institution, including U.S. banking services.
- **(8) Ban on Investment in Equity or Debt.** The President may prohibit any United States person from investing in or purchasing significant amounts of equity or debt instruments of the foreign financial institution.
- **(9) Exclusion of Corporate Officers.** The President may direct the Secretary of State to deny a visa to, and the Secretary of Homeland Security to exclude from the United States, any alien that the President determines is a corporate officer or principal of, or a shareholder with a controlling interest in, the foreign financial institution.
- **(10) Sanctions on Principal Executive Officers.** The President may impose on the principal executive officer or officers of the foreign financial institution, or on individuals performing similar functions and with similar authorities as such officer or officers, any of the first eight sanctions described above that are applicable.

Like the sanctions applicable to foreign persons who appear in a report, the sanctions for foreign financial institutions are permissive upon the foreign financial institution’s inclusion in a report.¹² Mandatory sanctions are applicable by one year from the date of inclusion—not later than one year after the foreign financial institution’s inclusion in a report, the Act requires the President to impose not fewer than five of the ten “menu” sanctions. If the foreign financial institution is not removed by the process of Presidential

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waiver or removal described above, then not later than two years after inclusion in a report, the President would be required to subject the foreign financial institution to the full “menu” of all ten sanctions.

Although sanctions against financial institutions are presented as a “menu” of available sanctions, in practical effect, the “menu” may only provide limited flexibility. Sanctions (5), (6), and (7) are each tantamount to a complete exclusion from the U.S. financial system and the U.S. dollar. It is possible that, in the first instance, five of the less powerful of the available sanctions could be imposed to limit potentially crippling impacts to an institution. However, it is also possible that U.S. and other large international banks could institute compliance measures that further impact the sanctioned institution’s ability to operate. Even the initial identification in a report—before the imposition of any sanctions—could have a significant impact on an identified institution.

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ENDNOTES

- 1 The term “financial institution” means a financial institution specified in 31 U.S.C. 5312(a)(2), which is extremely broad and includes, among other things, an insured bank, a commercial bank or trust company, a private banker, an agency or branch of a foreign bank in the United States, any credit union, a thrift institution, a broker or dealer registered with the Securities and Exchange Commission, a broker or dealer in securities or commodities, an investment bank or investment company, a currency exchange, an issuer, redeemer, or cashier of travelers’ checks, checks, money orders, or similar instruments, an operator of a credit card system, an insurance company, a loan or finance company, a travel agency, a licensed money transmitter, persons involved in real estate closings or settlements, as well as “any business or agency which engages in any activity which the Secretary of the Treasury determines, by regulation, to be an activity which is similar to, related to, or a substitute for any activity in which any business described” therein, and “any other business designated by the Secretary whose cash transactions have a high degree of usefulness in criminal, tax, or regulatory matters.”
- 2 116th Congress, 2d Session, H.R. 7440, Hong Kong Autonomy Act, Preamble.
- 3 The bill refers to the establishment of “a clear and unambiguous set of penalties with respect to foreign persons . . . involved in the contravention of the obligations of China under the Joint Declaration and the Basic Law and the financial institutions transacting with those foreign persons.” H.R. 7440, Section 4, paragraph (3).
- 4 The term “Joint Declaration” means the Joint Declaration of the Government of the United Kingdom and Northern Ireland and the Government of the People’s Republic of China on the Question of Hong Kong, done at Beijing on December 19, 1984.
- 5 The term “Basic Law” means the Basic Law of the Hong Kong Special Administrative Region of the People’s Republic of China.
- 6 H.R. 7440, Section 3.
- 7 The bill would require the Secretary the Treasury, in consultation with the Secretary of State, to submit to the appropriate congressional committees and leadership a report that “identifies any foreign financial institution that knowingly conducts a significant transaction with a foreign person identified” in a report submitted to Congress by the Secretary of State. H.R. 7440, Section 5(b).
- 8 With respect to foreign persons, the Secretary of State, after consultation with the Secretary of the Treasury (H.R. 7440, Section 5(a)); with respect to foreign financial institutions, the Secretary of the Treasury, after consultation with the Secretary of State (H.R. 7440, Section 5(b)).
- 9 A foreign person “materially contributes” to “the failure of the Government of China to meet its obligations under the Joint Declaration or the Basic Law if the person—(1) took action that resulted in the inability of the people of Hong Kong—(A) to enjoy freedom of assembly, speech, press, or independent rule of law; or (B) to participate in democratic outcomes; or (2) otherwise took action that reduces the high degree of autonomy of Hong Kong.” H.R. 7440, Section 5(g).
- 10 “The term ‘knowingly,’ with respect to conduct, a circumstance, or a result, means that a person has actual knowledge of the conduct, the circumstance, or the result.” H.R. 7440, Section 2(9).
- 11 Congress has the ability to override any such national security waiver or Presidential termination via a “disapproval resolution”—*i.e.*, a “joint resolution disapproving the waiver or termination of sanctions with respect to a foreign person that contravenes the obligations of China with respect to Hong Kong or a foreign financial institution that conducts a significant transaction with that person” under section 8 of the Act. H.R. 7440, Section 8(e)(1)(A).
- 12 H.R. 7440, Section 7(c).

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