

Chinese blocking rules

What to expect



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INTRODUCTION

In the past years, the US has forcefully targeted China with different trade measures, including sanctions and export control rules effectively restricting US and Chinese trade, and in particular targeted trade in technology and related products, as well as Chinese investments in the US and US investments in Chinese companies.

China is now taking certain counter actions comparable to the EU and Russian reactions against what is by China perceived as too far-reaching extra-territorial US measures. One of these actions is the adoption of blocking rules, which more or less mirrors the EU's Blocking Statute – a response to US extra-territorial export control and sanctions against Cuba and Iran.

1. HIGHLIGHTS AND ISSUES OF THE BLOCKING RULES

On 9 January 2021, the Chinese Ministry of Commerce (“**MOFCOM**”) issued effective immediately the Rules on Counteracting Unjustified Extra-territorial Application of Foreign Legislation and Other Measures (the “**Blocking Rules**”). The Blocking Rules, together with the Unreliable Entity List¹ and the Measures for the Security Review of Foreign Investment², can be seen as a package of joint countermeasures against extra-territorial sanctions and export control restrictions (particularly from the US) impacting business with Chinese companies and individuals.

An official English version of the Blocking Rules is available [here](#).

1.1 What is on the radar?

The Blocking Rules are intended to target the extra-territorial application of a foreign law and measure (“**Foreign Law**”) that “violates international law or the basic principles of international relations” and “unjustifiably prohibits or restricts normal economic, trade and related activities” between citizens, legal persons and other organisations of China (“**Chinese Persons**”) and a third country (or region) or its citizens, legal persons or other organisations (“**Foreign Persons**”). Identified and targeted Foreign Laws may be assessed and blocked as outlined below. So far, no Foreign Laws have been identified and no Blocking Orders (as defined below) have been issued.

1.2 Who would fall under the jurisdiction of the Blocking Statute?

Based on a literal reading, the Blocking Rules do not capture transactions between two Chinese Persons or two Foreign Persons. It is however not clear whether the Blocking Rules would capture a Chinese affiliate of a Foreign Person or an oversea affiliate of a Chinese Person.

Take the example of Chinese domestic transactions. If a Chinese subsidiary of a Foreign Person refuses to deliver

Chinese goods to another Chinese company, because the goods in question are subject to US export control rules (e.g. re-export of US origin technology), the Blocking Rules may not apply if both parties to the transaction are deemed Chinese Persons.

Similarly, uncertainty remains as to whether an oversea affiliate of a Chinese Person (such as a subsidiary of a Chinese parent established in the EU) is regarded as a Chinese Person or a Foreign Person and consequently whether the Blocking Rules would apply in such situations.

As the Blocking Rules are newly released, and yet to be implemented and enforced, it will be important to follow the development on how these provisions will be interpreted and applied.

1.3 How will Foreign Laws be identified (Blocking Orders)?

The authority responsible for implementing the Blocking Rules is a working committee composed of various governmental departments led by MOFCOM (the “**Working Committee**”). The Working Committee examines and determines whether the extraterritorial application of a Foreign Law is “unjustified”, by taking the following factors into account:

- Whether international law or the basic principles of international relations are violated;
- Potential impact on China's national sovereignty, security and development interests;
- Potential impact on the legitimate rights and interests of Chinese parties; and
- Other (unspecified) relevant factors.

The Working Committee is granted considerable discretion in its decision-making. Once the Working Committee has determined that a Foreign Law has an “unjustified” extra-territorial application, MOFCOM will issue an order to prohibit the “recognition of, the execution of, and the

¹ Promulgated by MOFCOM in September 2020.

² Jointly promulgated by Chinese National Development and Reform Commission and the MOFCOM in December 2020.

compliance with” such foreign legislation or measures (a “**Blocking Order**”).

If MOFCOM has issued a Blocking Order, the Working Committee may nevertheless, depending on the circumstances, suspend or withdraw an issued Blocking Order, which echoes the Working Committee’s extensive discretionary power.

The EU Blocking Statute, in comparison, applies only to the specific set of laws specified in its annex. The Chinese model appears to be more open-ended by issuing Blocking Orders from time to time, and may eventually target substantially a larger number of Foreign Laws.

1.4 Are there any exemptions available?

A Chinese Person may seek an exemption (“**Exemption**”) from the Blocking Order by submitting a written application to MOFCOM. MOFCOM will decide whether to grant an exemption within 30 days, or a shorter period under urgent circumstances.

The EU Blocking Statute has a similar exemption mechanism without however stipulating the timeframe.

Notably, it is not specified if a Foreign Person is also entitled to file an application for an Exemption. It can be reasonably expected that a Foreign Person, as opposed to a Chinese Person, may be in greater need of getting an Exemption, in order to proactively avoid underlying risks. It remains to be seen if, in the implementation of the Blocking Rules, the authorities will deliberately deny Foreign Persons the possibility to request an Exemption, or whether this will be left blank for future legislation.

1.5 Reporting Obligation

A Chinese Person is obliged to report to MOFCOM within 30 days upon it “being caught in the position” where a Foreign Law³ prohibits or restricts its ability to engage in “normal economic, trade and related activities” with a Foreign Person.

A comparable reporting requirement, including the 30-day reporting obligation, is also found in the EU Blocking Statute. The EU Blocking Statute aims however only at specific foreign laws in its annex, while there is no such limitation under the Blocking Rules.

1.6 Administrative Penalty

Failure to comply with a Blocking Order or reporting obligation could potentially result in such Chinese Persons receiving an administrative warning, order of rectification and/or fine. The amount of such fines are however not quantified in the Blocking Rules. It is not clear if this

entails another discretionary power or if it merely leaves the amount to be quantified in later regulations.

1.7 Compensation of Loss

As under the EU Blocking Statute, a Chinese Person can make claims for damages before a Chinese court and require compulsory enforcement against a “person at issue” who:

- has complied with the Foreign Law that is subject to a Blocking Order unless an Exemption has been obtained; or
- has benefited from a judgement or ruling made in accordance with the Foreign Law subject to a Blocking Order.

However, some practical elements are missing under the Blocking Rules, namely, the scope of compensation and how to calculate loss, enforcement measures against a Foreign Party, and associated legislation⁴ etc. We anticipate that Chinese courts will face both theoretical and practical challenges when dealing with these types of claims.

As a general comment on enforcement in China (including that of the administrative penalty as above), Chinese courts and authorities (including MOFCOM) usually do not proactively enforce claims against a Foreign Person due to practicalities and lack of international cooperation. However, it is in practice not uncommon that a Chinese affiliate of a Foreign Person may be caught (by tax or environmental audits etc.) even though it may not be directly involved in a situation captured by the Blocking Rules. With this said, a Foreign Person should still be aware of the potential risks entailed by the implementation and application of the Blocking Rules as long as it maintains a business presence or exposure in China.

1.8 Support from the Government

If a Chinese Person suffers “significant loss” from complying with a Blocking Order e.g. by refusing to comply with the blocked Foreign Law, the Chinese government may provide “necessary support” to the Chinese Person depending on the situation.

The Blocking Rules do not elaborate on the types of necessary support that may be relevant. As this measure is not further specified in the Blocking Rules, it may be questioned whether this is intended more as a form of political message rather than an actual ground for businesses to claim and receive support, e.g. through any tax benefits or financial subsidies which generally are common ways of support from the Chinese government.

³ Although not specified, logically, such Foreign Law shall refer to a Foreign Law that has not been previously listed in a Blocking Order.

⁴ Noting that compensation of loss needs to be placed into a suitable legal ground under Chinese legislation such as the Chinese Civil Code, and by theory a provision in the Blocking Rules may not suffice in a civil lawsuit.

2. WHAT SHOULD A FOREIGN PERSON DO?

For now the Blocking Rules only constitutes a high-level framework and many aspects remain to be clarified. Nonetheless, the adoption of these rules clearly indicates the Chinese government's determination and ambition to counter unfavourable foreign laws that negatively affect Chinese Persons. Going forward, only further legislative action and actual precedents of enforcement will reveal what real implication the Blocking Rules will have. These rules may play an increasingly important part in the daily compliance of multinational companies with business relating to China.

At this stage, European multinationals with business in China should consider the following:

- Monitor: The Blocking Rules will become effective and implemented through Blocking Orders. Thus, monitoring any indications of which foreign laws and regulations are being considered by the Working Committees and MOFCOM for such designation is crucial.
- Assess risks: Some Foreign Persons may in the future face a dilemma of being subject to both the Blocking Rules (and the Blocking Orders) and Foreign Law. In such case it becomes absolutely crucial to weigh and compare the risks resulting from both regimes.
- Proper paperwork: Properly worded sanction and/or trade control related clauses in documentation will become increasingly important, and it may be necessary to re-negotiate and re-draft the existing clauses and contracts.
- Make proper reporting: Chinese affiliates of Foreign Persons may in some situations have to report to MOFCOM to comply with the above-mentioned reporting obligation. When making such a reporting, it should be carefully considered to what extent the disclosure shall be made and it may be necessary to set a proper firewall between the Chinese affiliate and the Foreign Person and their respective business.
- Prepare negotiation strategies: It can be reasonably foreseen that some Chinese Persons may take advantage of the Blocking Rules in future negotiations with Foreign Persons.

This article is not construed to interpret the Blocking Rules under the Chinese domestic legal system. instead, this report examines the Blocking Rules' applicability to multinational companies based on a literal reading of certain provisions thereof and interpreting those provisions based on principles of public international law. It is distributed solely for informational purposes and should not be regarded as legal advice. The article may be quoted as long as the source is specified.

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