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Risky Business: The Top Four Risks Companies Face When Doing Business With China and How to Address Them

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While the U.S. and Chinese business communities continue to have a mutually beneficial relationship, the reality is that the bilateral political discourse is becoming more strained. Both governments are implementing measures to protect their domestic interests and this affects business.

How are companies supposed to navigate these new challenges? With the Lunar New Year holiday slowdown upon us, it is a good time for strategic business planning to reduce exposure to these risks.

1. Ensure No Sanctions or Related Restrictions Apply

Sanctions affecting business with China are evolving. Currently, there are no general or broad prohibitions on doing business with China, but effectively, many U.S. government agencies are using controls to create a broad, overlapping and expanding regulatory regime. For example,

- Under the new Hong Kong Sanctions program, multiple Chinese and Hong Kong officials have become restricted parties with whom U.S. persons cannot directly or indirectly transact.
- Prohibitions on investing in securities and derivatives of Communist Chinese Military-Industrial Companies or CMICs require that U.S. investors be cognizant of where their money goes.
- In tandem with other U.S. government regimes, sanctions and trade controls are expanding restrictions on transacting with Chinese entities within the military/intelligence-industrial complex, the Chinese government (and some affiliated entities), those entities undermining democracy or raising human rights concerns, and entities taking part in activities that are deemed to conflict with U.S. foreign policy or national security aims.
- Additionally, more expansive prohibitions apply to contractors and subcontractors doing business within the U.S. government procurement space.

As this matrix of restrictions grows, U.S. companies will need to create effective policies to

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identify applicable prohibitions and implement responsive procedures. One of the most important steps in this process is running restricted party screenings to know exactly with whom a company is doing business and whether those parties are restricted. This applies to everyone in the supply chain, from offshore contractors to suppliers and customers.

2. Understand the Applicable Export Controls Regime and Watch for New Technology Controls

Export control laws create national security-based restrictions on exporting goods, software and technologies to foreign persons and locations. These regimes are already extensive, but continue to expand. Back in 2018, Congress passed the Export Control Reform Act, which included a process for evaluating and increasing controls on emerging and foundational technologies. This act is expected to result in stricter controls in 2022 on the following technology exports to China:

- AI.
- Biotechnology.
- Microprocessor technology.
- Additive manufacturing.
- Advanced materials.
- Advanced surveillance.
- Robotics.
- Logistics tech.

Additionally, the U.S. government has already revoked Hong Kong's special status, meaning that U.S. export controls for China now also apply to Hong Kong, and the Department of Commerce recently expanded licensing requirements for exports intended for military/intelligence end-uses and end-users in China. Together, these changes create a clear trend toward stricter trade controls for exports to China. Thus, companies should evaluate if their long-term goals and strategic business plans must change.

3. If Considering Accepting Chinese Investment, Understand How CFIUS' Requirements and Oversight Capabilities May Affect Your Transaction

The Committee on Foreign Investment in the U.S. (CFIUS) has oversight power over foreign investment into the United States, and if it identifies a national security concern, can require companies to either mitigate the concerns or unwind investment transactions. One such concern is foreign access to U.S. critical technology.

Given the strained relationship between China and the U.S., Chinese investments are certainly under additional CFIUS scrutiny. So, if a company is considering taking foreign investment or entering into a merger or joint venture with a foreign party, it is important to consider: 1) whether the transaction could trigger a review based on a potential foreign investor's access to U.S. persons' data, critical technologies, or U.S. critical infrastructure or other potential national security concerns; and 2) how the company can prepare for such a review by mitigating potential national security risks.

4. Understand the Effect of Increased Supply Chain Regulation and Identify Areas That Can be Streamlined

Federal agencies now are prohibited from purchasing or contracting with companies that use certain Chinese-covered telecommunications equipment. There are now human rights-based import restrictions on products from China's Xinjiang region. And, there are no immediate plans to remove the 75% to 25% additional import tariffs on many Chinese products. Additionally, the Biden administration plans to further address supply chain vulnerabilities in the following areas:

- Medical supplies and equipment.
- Energy and grid resilience technologies.
- Semiconductors.
- Key electronics and related technologies.
- Telecommunications infrastructure.
- Key raw materials.

Any such measures would likely further impose limits or restrictions on trade with China. Thus, it is imperative that U.S. companies audit their supply chains, identify where vulnerabilities lie and restructure where possible to reduce the risk of violations or excessive costs.

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