

# President Trump Signs Hong Kong Autonomy Act, Issues Executive Order Authorizing Sanctions and Other Measures

July 16, 2020

On July 14, 2020, President Trump signed into law the [Hong Kong Autonomy Act](#) (“HKAA”) and issued a new [executive order](#), “The President’s Executive Order on Hong Kong Normalization” (the “**Order**”). Collectively, the HKAA and the Order put into place a framework for the U.S. government’s policy response to the enactment by the People’s Republic of China (“**China**” or the “**PRC**”) of the Law of the People’s Republic of China on Safeguarding National Security in the Hong Kong Administrative Region (the “**National Security Law**”).<sup>1</sup> Among other things, both the HKAA and the Order authorize the imposition of sanctions on foreign persons, including foreign financial institutions, engaged in certain conduct relating to Hong Kong. The U.S. government did not immediately impose any sanctions under these authorities, and President Trump did not provide any indications as to the likely timing or targets of sanctions in lengthy [public remarks](#) tied to his signing of the HKAA.

We provide below a summary of key features of the HKAA and the Order. While there is substantial uncertainty as to how these authorities will ultimately be implemented, we hope that U.S. and non-U.S. companies will find this summary useful as they assess how potential future sanctions may affect their business.

## The HKAA

The HKAA, which passed both the House and Senate with overwhelming and bipartisan support, authorizes, and eventually requires, the President to impose sanctions on foreign persons determined to have contributed to China’s actions in Hong Kong, as well as on foreign financial institutions determined to knowingly conduct significant transactions with such persons. The Act provides for a phased approach to the imposition of sanctions, triggered by the inclusion of a foreign person or foreign financial institution in reports required to be submitted to Congress.

### Reports to Congress

Specifically, section 5(a) of the HKAA requires the Secretary of State to, within 90 days of enactment (i.e., by **October 13, 2020**), submit to Congress a report (the “**Section 5(a) Report**”) identifying any foreign person the Secretary has determined is materially contributing to, has materially contributed to, or attempts to materially contribute to the failure of the government of China to meet its obligations under the 1984 Joint Declaration of the UK and PRC governments concerning Hong Kong (the “**Joint Declaration**”) or the Basic Law of the Hong Kong Special Administrative Region (the “**Basic Law**”).<sup>2</sup> The HKAA provides that a person “materially contributes” to such a failure if such person:

- took action that resulted in the inability of the people of Hong Kong:
  - to enjoy freedom of assembly, speech, press, or independent rule of law; or
  - to participate in democratic outcomes; or
- otherwise took action that reduces the high degree of autonomy of Hong Kong.

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<sup>1</sup> Davis Polk clients interested in more details concerning the National Security Law may contact the authors, or their usual Davis Polk contact, for further information prepared by attorneys in Davis Polk’s Hong Kong office.

<sup>2</sup> In particular, Congress found in Section 3(4) of the HKAA that “(f)oremost among the obligations of the Government of China to Hong Kong is the promise that, pursuant to Paragraph 3b of the Joint Declaration, “the Hong Kong Special Administrative Region will enjoy a high degree of autonomy, except in foreign and [defense] affairs.”

Following this initial report by the Secretary of State, the Secretary of the Treasury is required by Section 5(b) of the HKAA to submit to Congress a report (the “**Section 5(b) Report**”) identifying any foreign financial institution that knowingly conducts a significant transaction with a foreign person identified in the Section 5(a) Report.<sup>3</sup> This report is required to be submitted not sooner than 30 days, and not later than 60 days, following submission of the Section 5(a) Report. This staggered submission requirement appears intended to give foreign financial institutions a brief window in which to conclude or wind-down activities with persons identified in the Section 5(a) Report without risking the imposition of sanctions.

Updates to both reports are required on an ongoing basis.

Foreign persons or foreign financial institutions meeting criteria for inclusion in either of the above-described reports may be excluded from the report or subsequent updates to the extent that their identification in the report would compromise intelligence sources or methods or harm certain law enforcement equities. They may also be excluded or removed from the report or subsequent updates if the President determines that an action or transaction that would otherwise merit the person’s inclusion:

- does not have a significant and lasting negative effect that contravenes the obligations of China under the Joint Declaration and the Basic Law;
- is not likely to be repeated in the future; and
- has been reversed or otherwise mitigated through positive countermeasures taken by that foreign person.

The HKAA provides for the imposition of sanctions on persons named in the Section 5(a) Report and foreign financial institutions named in the Section 5(b) Report, as described below.

## Property Sanctions on Foreign Persons

Immediately upon inclusion of a foreign person in the Section 5(a) Report, the President may, but is not required to, impose sanctions on such person: (1) prohibiting any person from dealing in property subject to the jurisdiction of the United States in which the sanctioned foreign person has an interest,<sup>4</sup> and (2) in the case of individuals, denying visas to such person and excluding her or him from entry into the United States. The imposition of these sanctions becomes mandatory one year after the foreign person’s inclusion in the Section 5(a) Report or a subsequent update, unless the person is removed from the report in the intervening period for the reasons described above, or the President determines that waiver of the sanctions is in the national security interest.<sup>5</sup> Given the President’s authority to waive or terminate sanctions, and the Secretary of State’s ability to control the initial decision of whether to include a person in the Section 5(a) Report, the executive branch retains substantial discretion concerning the imposition of sanctions under the HKAA, notwithstanding their purportedly “mandatory” nature.

## Menu-Based Sanctions on Foreign Financial Institutions

For foreign financial institutions identified in the Section 5(b) Report, the HKAA provides for a phased imposition of menu-based sanctions. Within **one year** of the inclusion of a foreign financial institution in

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<sup>3</sup> The HKAA does not define what constitutes a “significant” transaction, but in other contexts, the U.S. Treasury Department’s Office of Foreign Assets Control indicates that it assesses whether a transaction is significant for purposes of secondary sanctions by considering the following factors: (1) the size, number, and frequency of the transaction(s); (2) the nature of the transaction(s); (3) the level of awareness of management and whether the transaction(s) are part of a pattern of conduct; (4) the nexus between the transaction(s) and a sanctioned person; (5) the impact of the transaction(s) on statutory objectives; (6) whether the transaction(s) involve deceptive practices; and (7) such other factors as deemed relevant on a case-by-case basis.

<sup>4</sup> Although not framed as such, this prohibition appears to be functionally equivalent to an asset freeze, and we expect that the President will implement it as an asset blocking sanction.

<sup>5</sup> Decisions by the President to waive or terminate sanctions against a person, or to remove a foreign person from the Section 5(a) Report, are subject to Congressional disapproval, though any resolution of disapproval would be effective only if it passed with sufficient support to override a Presidential veto.

the report or a subsequent update, the President is required to impose **at least five** of the following sanctions:

- The US Government may prohibit any US financial institutions from providing loans or credits to the foreign financial institution;
- The foreign financial institution is prohibited from being designated as a primary dealer in US Government debt instruments;
- The foreign financial institution is prohibited from serving as agent of the US Government or as repository for US Government funds;
- The President may prohibit any transactions in foreign exchange that are subject to US jurisdiction and in which said foreign financial institution has an interest;
- The President may prohibit any transfers of credit or payments between financial institutions or by, through, or to any financial institution, to the extent such transfers or payments are subject to US jurisdiction and involve the foreign financial institution;
- Asset blocking sanctions;
- Restriction of exports, reexports and transfers of commodities, software and technology as determined by the President and the Commerce Department;
- The President may prohibit any US person from investing in or purchasing significant amounts of equity or debt instruments of the foreign financial institution;
- Visa restrictions on corporate officers, principal or controlling shareholders of the foreign financial institution; and
- Imposition of any of the above sanctions on the financial institution's principal executive officers.

Within **two years** of the inclusion of the foreign financial institution in the report, **all** of the above sanctions must be imposed. As with the sanctions on foreign persons, the President may waive the imposition of sanctions against a foreign financial institution if determined to be in the national security interest, may remove an institution from the report without imposing sanctions for cause, and retains substantial discretion over the imposition of these sanctions, notwithstanding their characterization as "mandatory."

## The Order

The issuance of the Order complements the HKAA by providing authority to implement certain of the sanctions provided for under the HKAA, as well as sanctions provisions in the 2019 [Hong Kong Human Rights and Democracy Act](#).<sup>6</sup> However, the Order goes beyond the requirements of those two statutes to include additional bases for the imposition of sanctions authorized pursuant to the International Emergency Economic Powers Act ("**IEEPA**"),<sup>7</sup> in response to a newly declared national emergency concerning the situation in Hong Kong. In addition to authorizing the imposition of sanctions, the Order directs executive branch agencies to take a number of steps to eliminate differential treatment of Hong Kong and China under U.S. law, consistent with the Hong Kong Policy Act of 1992, as amended.<sup>8</sup> We address in turn below each of these two core elements of the Order.

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<sup>6</sup> Pub. L. 116-76 (November 27, 2019).

<sup>7</sup> 50 U.S.C. §§ 1701-1706.

<sup>8</sup> 22 U.S.C. §§ 5701-5732.

## Sanctions Provisions

Section 4 of the Order authorizes each of the Secretary of State or the Secretary of the Treasury, in consultation with the other, to impose asset blocking sanctions on foreign persons determined:

- to be or have been involved, directly or indirectly, in the coercing, arresting, detaining, or imprisoning of individuals under the authority of, or to be or have been responsible for or involved in developing, adopting, or implementing, the National Security Law;
- to be responsible for or complicit in, or to have engaged in, directly or indirectly:
  - actions or policies that undermine democratic processes or institutions in Hong Kong;
  - actions or policies that threaten the peace, security, stability, or autonomy of Hong Kong;
  - censorship or other activities with respect to Hong Kong that prohibit, limit, or penalize the exercise of freedom of expression or assembly by citizens of Hong Kong, or that limit access to free and independent print, online or broadcast media; or
  - the extrajudicial rendition, arbitrary detention, or torture of any person in Hong Kong or other gross violations of internationally recognized human rights or serious human rights abuse in Hong Kong;
- to be or have been a leader or official of an entity, including any government entity, that has engaged in, or whose members have engaged in, certain of the above activities,<sup>9</sup> or of an entity whose property and interests in property are blocked pursuant the Order.
- to have materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services to or in support of, any person whose property and interests in property are blocked pursuant to the Order;
- to be owned or controlled by, or to have acted or purported to act for or on behalf of, directly or indirectly, any person whose property and interests in property are blocked pursuant to the Order; or;
- to be a member of the board of directors or a senior executive officer of any person whose property and interests in property are blocked pursuant to this section.

The property and property interests in the United States or the possession or control of U.S. persons of persons determined to be subject to sanctions pursuant to the Order will be blocked, and U.S. persons will generally be prohibited from engaging in transactions with such persons unless licensed by OFAC or exempt. Section 7 of the Order provides for the imposition of visa sanctions on individuals sanctioned pursuant to the Order, as well as their immediate family members (spouses and children).

The designation prongs under the Order do not precisely match the criteria for inclusion in the Section 5(a) Report required by the HKAA, but are broad enough to encompass those criteria, meaning that the Order is likely to be used to implement any sanctions imposed on persons included in the Section 5(a) Report. Interestingly, however, the Order does not contain provisions specifically targeting foreign financial institutions, or provide authority to implement the full range of menu-based sanctions provided for in Section 7(b) of the HKAA, though it does provide for derivative designation authority that could be used to impose blocking sanctions against foreign persons, including foreign financial institutions, that

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<sup>9</sup> This designation prong does not authorize designation of leaders of entities determined to have engaged the extrajudicial rendition, arbitrary detention, or torture of any person in Hong Kong or other gross violations of internationally recognized human rights or serious human rights abuse in Hong Kong. It is not clear whether this omission is intentional or was an error

provide financial support or services to sanctioned persons.<sup>10</sup> It is possible that an additional executive order will be needed in the future in order to fully implement the HKAA.

## Other Provisions

In accordance with the Hong Kong Policy Act, which codified certain preferential treatment accorded to Hong Kong under U.S. law as in effect prior to July 1, 1997, but authorized the President to eliminate such preferences in the event that China took steps to erode Hong Kong's autonomy, section 1 of the Order declares that it is the policy of the United States to suspend or eliminate different and preferential treatment for Hong Kong to the extent permitted by law and in the national security, foreign policy, and economic interest of the United States. Section 2 of the Order suspends the application of the Hong Kong Policy Act's codification of preferred treatment for Hong Kong under statutes relating to immigration,<sup>11</sup> export controls,<sup>12</sup> national security reviews of foreign investment,<sup>13</sup> and customs rules of origin.<sup>14</sup> Section 3 of the order directs executive branch agencies to, within 15 days, commence steps to further the purposes of the Order, including:

- Amending regulations necessary to implement the President's suspension of the application of the Hong Kong Policy Act to the statutes specified in Section 2 of the Order;
- Revoking license exceptions and terminating export licensing suspensions that afford Hong Kong or Hong Kong persons differential treatment from China or Chinese persons;
- Amending regulations to eliminate the preference for Hong Kong passport holders as compared to PRC passport holders;
- Giving notice of intent to suspend or terminate certain agreements between the U.S. and Hong Kong relating to cooperation on law enforcement (including extradition), scientific and educational, and tax matters;
- Reallocating admissions within the refugee ceiling set by the annual Presidential Determination to residents of Hong Kong based on humanitarian concerns; and
- Proposing other steps for the President's consideration.

Even prior to the issuance of the Order, federal agencies had begun taking steps to eliminate differences in treatment between Hong Kong and China under U.S. law, with both the [Commerce](#) and [State](#) Departments announcing changes in export control policy towards Hong Kong under the Export Administration Regulations and International Traffic in Arms Regulations in late June. Companies that export or reexport to Hong Kong items subject to U.S. export controls should pay particular attention to these changes, and ensure that they are aware of and compliant with any newly applicable export licensing requirements.

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<sup>10</sup> Indeed, at least facially, the derivative designation authority provided under the Order is broader than the secondary sanctions provisions of the HKAA, as it is not limited to foreign financial institutions, and does not require that the provision of support or services be "significant" in order to be sanctionable.

<sup>11</sup> Specifically, section 103 of the Immigration Act of 1990 (8 U.S.C. § 1152 note), and sections 203(c), 212(l), and 221(c) of the Immigration and Nationality Act of 1952, as amended (8 U.S.C. §§ 1153(c), 1182(l), and 1201(c), respectively).

<sup>12</sup> Specifically, the Arms Export Control Act (22 U.S.C. 2751 et seq.), and the Export Control Reform Act of 2018 (50 U.S.C. §§ 4801 et seq.);

<sup>13</sup> Specifically, section 721(m) of the Defense Production Act of 1950, as amended (50 U.S.C. § 4565(m)).

<sup>14</sup> Specifically, 19 U.S.C. § 1304.

## Looking Forward

The prospect of significant U.S. sanctions targeting China clearly merits attention, given the substantial ties between the U.S. economy and financial system and both Hong Kong and China. Thus far, however, the U.S. sanctions response to China's enactment of the National Security Law and other policy concerns relating to China has been measured, notwithstanding increasingly harsh rhetoric. For example, **sanctions** imposed in early July against Chinese officials and government entities relating to conduct in Xinjiang province were narrowly targeted and largely symbolic, and did not extend, for example, to commercial entities that have previously been made subject to export controls restrictions for involvement in similar conduct. **News reports** that proposals for more substantial sanctions relating to Hong Kong have been rejected by the President suggest that, at least for now, this measured approach is likely to continue. Nonetheless, there is no guarantee that this will be the case, and affected U.S. and non-U.S. companies alike should carefully monitor the situation, and take account of both existing and future sanctions risks.

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