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## The Nature Of The Chinese Unreliable Entity List

The Ministry of Commerce of the People's Republic of China ("MOFCOM") issued the Provisions on the Unreliable Entity List<sup>1</sup> (MOFCOM Order No. 4 of 2020, hereinafter referred to as the "UEL Provisions") on September 19, 2020. On February 16, 2023, MOFCOM designated Lockheed Martin Corporation and Raytheon Missiles & Defense as the first two unreliable entities and decided to impose a range of sanctions on them<sup>2</sup>.

The UEL Provisions articulates two sides of the same coin – with **investigations on one side**, and **sanctions on the other**. The recent designation of the afore-mentioned American companies as unreliable entities serves as an example of direct sanctions. Nevertheless, in our opinion, the UEL Provisions is fundamentally concerned with investigations.

### 1. The side of investigations features procedural and substantive rules

Articles 5 to 7 of the UEL Provisions provide clear guidance on the competent authority, main procedures, and key considerations for investigations when an investigation of a targeted entity is under way. Article 5 specifies the competent authority in charge of and the initiation process for such an investigation. Article 6 explains the investigation method to be employed, as well as the suspension, termination, and resumption of the investigation proceedings under certain

<sup>1</sup> <http://english.mofcom.gov.cn/article/policyrelease/questions/202009/20200903002580.shtml>.

<sup>2</sup> <https://www.chinadaily.com.cn/a/202302/16/WS63ee175ca31057c47ebaf3c0.html>.

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circumstances. And Article 7 illustrates the key factors that the competent authority will consider in determining the reliability of an entity subject to investigation.

In terms of the competent authority, the UEL Provisions entrusts the working mechanism of UEL, a cross-agency body, as the competent authority under the UEL Provisions. As MOFCOM is the core agency of the working mechanism, it is reasonable to consider MOFCOM as the main authority in charge of conducting UEL investigations.

Despite the concise wording, these articles stipulate the rights and obligations of both the competent authority and respondents. First, the UEL Provisions imposes mandatory procedural obligations on the competent authority. For example, the UEL Provisions requires the competent authority to ensure transparency in investigations by releasing the initiation notice and notice to the public. Second, respondents also have the right to defend themselves of their own will before the competent authority. If respondents choose to respond before the competent authority, we believe that legitimate procedural and substantive rights under Chinese trade laws will be automatically triggered and conferred on the interested parties.

With respect to the factors to be considered, Article 7 requires the competent authority to look into a range of important factors before deciding on the unreliability of a targeted entity. These factors include (1) the degree of danger to national sovereignty, security, or development interests of China; (2) the degree of damage to the legitimate rights and interests of enterprises, other organizations, or individuals of China; (3) whether being in compliance with internationally accepted economic and trade rules; and (4) other factors that shall be considered. Given the complexity of these factors, a thorough analysis, including comparison, contrast, and counterfactual analysis, may be necessary for the competent authority to reach factual findings.

Regarding the investigation method, the UEL Provisions clearly outlines the methods that the competent authority may adopt. Article 6 explicitly lists three types of methods available, including inquiring, consulting, and copying documents. When necessary, the competent authority is also empowered to deploy “other necessary means”. Given the scope of the investigations, the competent authority may resort to

plenty of means in its arsenal to conduct such investigations.

## **2. On the side of sanctions, there still stands a chance of investigations**

Article 8 of the UEL Provisions authorizes the competent authority to impose direct sanctions on targeted entities “where the facts about the actions taken by the relevant foreign entity are clear”. However, even when direct sanctions are imposed, there may still be room for investigations.

In such scenarios, “facts” remain the top issue under investigation. As the UEL Provisions requires established facts about the actions taken by relevant entities before the competent authority can impose direct sanctions, it is reasonable to assume that the competent authority has already conducted an investigation and drawn relevant conclusions about the facts and the alleged actions. Further, even if the “facts” are already clearly exhibited, the targeted entity may still present defenses to elaborate on the condition, context and scope of its actions, as well as other mitigating factors that may reduce the negative impact of the alleged actions and alleviate the unreliability of the entity.

The other issue worth investigating is the factors that lead to the designation of the targeted entity as “unreliable”. Article 7 of the UEL Provisions identifies the negative effects of the alleged actions on national interests, business interests, and consistency of international economic and trade rules as the factors for the competent authority to consider when making a determination.

Therefore, even under the scenario of direct sanctions, investigations are still possible to establish the facts. Additionally, the targeted entity may present a defense that challenges the competent authority’s conclusion about its alleged actions.

## **3. The sanctions are based on the results of an investigation**

The UEL Provisions enables the competent authority to structure comprehensive measures to sanction an entity when relevant investigations are concluded. Hence, an investigation may wind up with sanctions slapped against an entity.

One of the most important aspects of the investigation process is the amount of fines to be imposed. For example, as outlined in the first UEL designation, the amount of fine is directly linked to the contract value of certain arms sales. Therefore, in order

to quantify the fine, the competent authority needs to find out the scope and timespan of the sales as well as the contract value of the sales under investigation. It is reasonable to assume that calculation of the fine must be based on established facts. In addition, when viewed through the lens of other trade laws, certain facts need to be factored in to decide whether a fine to be imposed is appropriate. Therefore, an investigation of relevant facts is warranted.

### **Our Perspective**

The UEL Provisions is a new administrative tool that MOFCOM can utilize in trade law areas to protect and promote national interests as well as business interests. While the UEL functions in resemblance to the Specially Designated Nationals And Blocked Persons List (“SDN List”), the UEL Provisions gives weight to investigations in its implementation and enforcement. Considering the nature and purpose of the UEL Provisions, the UEL tends to be an administrative tool and investigation is a critical component of the UEL’s administrative function, providing a platform for interested parties to voice their opinions and defend their rights.

With legal rights and obligations clearly articulated under the UEL Provisions, the UEL Provisions ensures that the competent authority conducts investigations in a transparent and accountable manner. The competent authority may utilize the investigation process to hear comments and arguments from the respondents and other interested parties. The respondents and other interested parties have the opportunity to participate in the investigation process and defend their legitimate rights. As such, the UEL Provisions provides a framework for transparent and accountable investigations that respect the rights and obligations of all parties involved; it also ensures that the competent authority considers all relevant information before making a determination, which leads to a more reasonable and just outcome.

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