Making Xinjiang Sanctions Work

Policy Brief No. 4 – Western sanctions

Based on *Making Xinjiang Sanctions Work*, July 2022[i]

Can economic sanctions address Xinjiang forced labour? The Xinjiang Sanctions research project seeks to answer this question. Drawing on 3 original datasets containing over 12,000 datapoints, confidential interviews and a year of research, this Policy Brief series summarises key findings from the research. For further analysis, and the references and authorities supporting the statements in these Policy Briefs, see the project's main research study at www.xinjiangsanctions.info.

The Xinjiang Sanctions Policy Brief series:

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Key research findings

- Governments have adopted 239 measures in response to Xinjiang forced labour (as of June 2022), according to the Xinjiang Sanctions Government Measures (XJS-GMS, v. 4.0) dataset, available at www.xinjiangsanctions.info.
- 60 per cent of these have been adopted by the United States. Canada, the UK, the EU and the EU's EFTA partners account for the remainder.
- Import and export controls are the most numerous measures, but are currently focused in the US and Canada. Asset freezes and travel restrictions are being used by a broader set of countries.
- While the US has measures in place against 108 targets, elsewhere the target sets are a small fraction of this size.
- 36 per cent of all measures target just 4 individuals (senior CCP officials in XUAR) and 3 entities (including the XPCC).
- Import bans are increasingly popular. The US has instituted bans on imports of a range of goods from Xinjiang, and since 21 June 2022 has applied a rebuttable presumption that supply-chains passing through Xinjiang are tainted by forced labour, under the *Uyghur Forced Labor Prevention Act* (UFLPA). Importers will have to provide clear and convincing evidence that the goods they are seeking to import were not made in whole or in part with forced labour if they include any components from Xinjiang.
- The value of shipments detained by US authorities in this way increased from USD 0.218 million in FY 2018 to USD 227 million for the first 6 months of FY 2022, and is expected to increase now that the UFLPA is in force.
- Canada has a similar forced labour import ban in place, not limited to Xinjiang, and has begun enforcing it. Australia and the EU are contemplating adopting similar arrangements.
- At least 7 countries have asset freezes and travel restrictions in place for entities connected to Xinjiang forced labour. Many of these were adopted in two coordinated sanctions 'rounds', one in January 2021 and another in March 2021 that accounts for more than a quarter of all measures adopted to date.
- Several countries have adopted export controls, with a particular focus on surveillance technology.
- Canada, the EU, UK and US have issued official guidance to businesses that may be exposed to Xinjiang forced labour risk.
- Capital market controls are extremely limited and having little impact. Some investors are voluntarily beginning to take action, such as heightened due diligence and active engagement, but shareholder action is in its infancy and other investors are clearly happy to hold equities and debt issued by firms tied to Xinjiang forced labour.
- U.S. holdings of Chinese securities have surged 57.5 percent from USD 765 billion in 2017 to as much as USD 1.2 trillion in 2020. Vanguard's investments in Xinjiang reportedly tripled between 2018 and 2021, and institutional investors outside the US own shares in many Chinese firms sanctioned by the US.

Why is this important?

- Understanding what Xinjiang sanctions are in place and how they are operating is critical to analysing their impact and likely success.
- This study and the associated datasets on www.xinjiangsanctions.info provide the first compilation, taxonomy and analysis of Xinjiang sanctions.
- The datasets are already in use by several global banks and retailers, which use them to support compliance and policy analysis.

Research overview

The Xinjiang Sanctions Government Measures (XJS-GMS, v. 4.0) dataset, available at www.xinjiangsanctions.info, currently identifies 318 measures adopted or under consideration by 7 governments in response to Xinjiang forced labour. At the time of writing (June 2022), 239 of these measures were in force, 43 proposed but not yet in force, and 36 expired. 60 per cent of all measures in force have been adopted by the United States (see Figure 1, below).

There has been a steady acceleration in the pace of adoption of measures since 2018 (see Figure 2). Import and export restrictions account for the largest share of measures in force, although asset and property restrictions, as well as travel restrictions, have been put in place by a wider group of countries. Only the US and Canada currently have import or export controls in place in response to Xinjiang forced labour (see Figure 3).

While US measures are directed at 108 distinct targets, outside the US sanctions cluster around a small number of individuals and entities, including the XPCC (Figure 4).

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Figure 1: Measures in force by jurisdiction

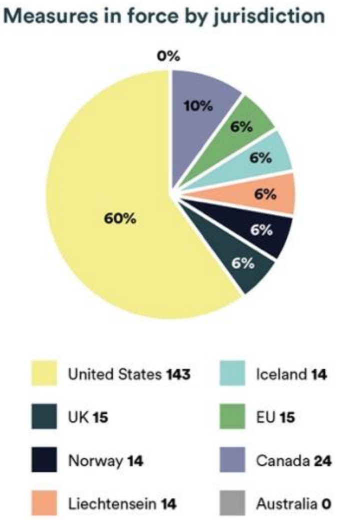


Figure 2: Year-on-year activity on Xinjiang forced labour measures

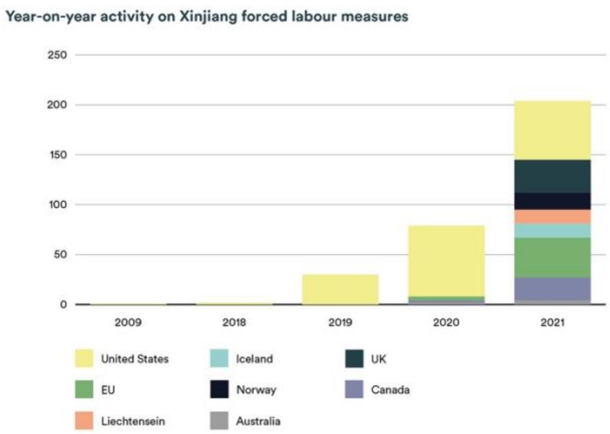
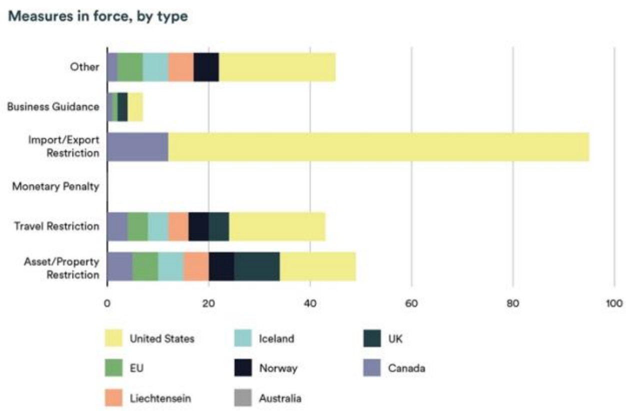


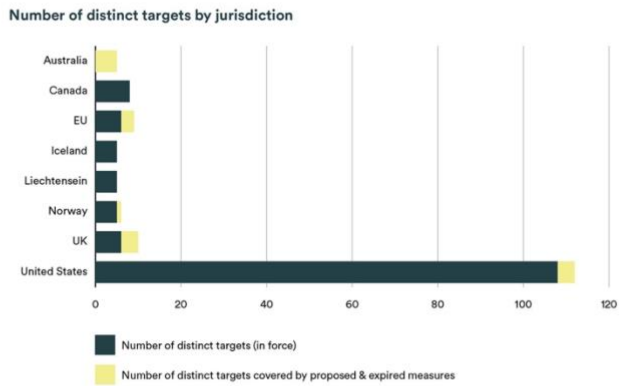
Figure 3: Measures in force, by type



Import restrictions

US Customs and Border Protection (CBP) has detained hundreds of millions of dollars worth of goods reasonably suspected to be made with Xinjiang forced labour, through Withhold Release Orders (WROs) issued under section 307 of the *Tariff Act* of 1930. Such detentions can be based either on US CBP's own initiative or receipt of information from the public. An importer hit with a WRO can either reroute the shipment to a foreign market or seek to persuade CBP that the goods were not in fact made with forced labour. CBP can also seize cargoes where it finds conclusively that they were made with forced labour.

Figure 4: Number of distinct targets by jurisdiction



The US has adopted numerous WROs relating to Xinjiang, including WROs addressing the XPCC's involvement in the cotton trade (since November 2020), banning import of all cotton and tomatoes produced in Xinjiang (January 2021), and targeting several Xinjiang entities centrally involved in the solar energy supply-chain (June 2021). Between 2016 and 2018 only USD 6.3 million worth of forced labour goods were seized by CBP. As of early 2019, just 6 of CBP's 62,450 personnel were charged with enforcing section 307 of the Tariff Act. But enforcement is now ramping up significantly. CBP now has over 20 enforcement personnel at headquarters, and tens of millions of dollars of funding is being put in place to increase enforcement. The value of shipments detained under section 307 of the Tariff Act has consequently risen from USD 0.218 million in FY 2018 to USD 227 million for the first 6 months of FY 2022.

Since 21 June 2022, under the *Uyghur Forced Labor Prevention Act*, the US has applied a rebuttable presumption that *all* goods made in whole or in part in Xinjiang were made with forced labour, which also applies to entities using Xinjiang forced labour elsewhere in China. To import goods from Xinjiang or these firms, importers must comply with due diligence and evidentiary guidance established under the Act and provide "clear and convincing" evidence that the goods were not made with forced labour. Companies have pushed for implementation arrangements minimising the regulatory burden they face, arguing for fast-track and trusted trader arrangements, a phasing in of evidentiary requirements, and heads ups on priority enforcement areas. Numerous companies, including Nike, Coca Cola, Apple, Gap, Campbell Soup, Kraft, JinkoSolar, BP and HSBC lobbied Congress while the bill was being considered.
Canada recently put in place a general ban on imports of goods made with forced labour and appears to have begun enforcing it. Australia and the EU are also considering import bans and are actively looking at the US experience for insights about how to design and implement their own

arrangements. The European Parliament has proposed a ban that applies not only to imports but also goods made with forced labour inside the European common market.

Asset freezes and travel restrictions

All countries that have adopted Xinjiang sanctions have adopted asset freezes and travel restrictions. Many of these were adopted in two coordinated sanctions 'rounds', one in January 2021 and another in March 2021, with the latter accounting for more than a quarter of all measures adopted to date. US financial sanctions are imposed primarily through inclusion of targets in the list of Specially Designated Nationals and Blocked Persons – known as the SDN List – controlled by the US Treasury's Office of Foreign Assets Control (OFAC). Addition to the list leads to US banks and financial institutions freezing assets; restrictions on access to US visas, which are handled through the State Department; and bans on dollar-based transactions, even outside the US.

Export controls

Several countries, including the US and UK, have export controls in place. These prevent the export of specified technologies or goods to designated entities, particularly those associated with the XPCC, and with surveillance technologies used in repression and detention of minorities in the VSETC system. The most powerful of these is the US Department of Commerce Bureau of Industry & Security's Entity List (the 'Entity List'), which formally impacts US persons. It further impacts non-US persons through the "foreign direct product rule", which allows the US to restrict provision of certain American goods and services to third party foreign persons that do not voluntarily comply with Entity List restrictions. This creates a strong incentive for foreign entities including financiers, insurers and shippers to refrain from business with entities on the US Entity List.

Business guidance

Canada, the EU, the UK and US have issued guidance or advisories to business laying out expectations relating to the identification and management of risks associated with doing business in Xinjiang, or with entities connected to Xinjiang. Several of these advisories warn business against relying on third-party audits to identify forced labour risks. Moreover, both the US and EU guidance mention investor risks.

Capital market sanctions

There are relatively few controls in place on investment in companies connected to Xinjiang forced labour. This is somewhat surprising, given that studies suggest financial sanctions are generally more effective than trade-based sanctions; and the potential leverage capital market sanctions could offer over Chinese organisations. Capital markets could thus still emerge as a flashpoint in efforts to address Xinjiang forced labour. The European Parliament has, for example, refused to move forward with the EU-China Comprehensive Agreement on Investment until Beijing addresses Xinjiang forced labour concerns. This does not however work to restrict existing capital flows between the EU and China, but only to prevent the adoption of measures that would expand those flows in certain ways.

Investors face challenges identifying company ties to Xinjiang forced labour. Some jurisdictions, notably the US, have contemplated disclosure rules for such risks, but none have yet been adopted. Under the UN Guiding Principles on Business and Human Rights, investors have human rights due diligence obligations, even where merely offering custodial services for clients' securities. But many capital market actors, such as UBS and HSBC, seem to continue purchasing equities issued by firms that are known to be connected to Xinjiang forced labour. Development finance actors seem to be undertaking some heightened due diligence and engagement efforts in response to Xinjiang forced labour. Members of US Congress have raised concerns with the World Bank and the US development finance entity about continued support for firms connected to Xinjiang forced labour. Some institutional investors, including Investor Alliance for Human Rights and Investors Against Slavery and Trafficking APAC, are undertaking targeted active engagement efforts with companies. Shareholder actions related to Xinjiang forced labour are however scarce, though they have been organised at Apple, Disney and Nike. In fact, some institutional investors, such as Blackrock, seem to be using their votes to *endorse* Chinese firms' continued participation in the Poverty Alleviation through Labour Transfers programme.

The most significant controls are in the US. Designation on the US SDN List prevents US persons investing in or buying the debt of designated companies, and the companies of which designated companies own 50 per cent or more. Under Executive Order 14032, the US has also created the Non-SDN Chinese Military-Industrial Complex Companies List, which has been used to target some Xinjiang-related entities. Together, these measures have led to a small number of firms being removed from the equity and bond indices that are tracked by Exchange Traded Funds and other financial products worth trillions of dollars. Yet with the XPCC having holdings in 862,000 entities worldwide, these controls may only be scratching the surface. Moreover, U.S. holdings of Chinese securities have surged 57.5 percent from USD 765 billion in 2017 to as much as USD 1.2 trillion in 2020, the same period that forced labour has emerged as a major problem in Xinjiang. Chinese firms with ties to Xinjiang forced labour have raised hundreds of millions of dollars in IPOs and debt *after* being sanctioned by the US. The US fund manager, Vanguard, appears to have tripled its investments in Xinjiang between 2018 and 2021. Some of these investments are even integrated into Vanguard's ESG offerings, despite the evidence that doing business in Xinjiang places firms at high risk of exposure to forced labour. And even where US capital flows are impeded, other investors can easily step in. Pension and sovereign funds in Australia, Canada, New Zealand, Norway and UK are all reportedly invested in Chinese firms designated by the US as off limits for US investors

[i] James Cockayne, *Making Xinjiang Sanctions Work: Addressing forced labour through coercive trade and finance measures* (Nottingham: University of Nottingham, 2022).

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