



Asia Under Fire of US Sanctions

Ivan Timofeev

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Introduction

For quite a long time Asia occupied a special place in international sanctions policy. Most of the restrictive measures were aimed against North Korea. The international community represented by the UN Security Council reached a rare consensus on the North Korean nuclear missile programme. There were differences among the Security Council members on the extent of pressure on Pyongyang. They made up for these differences by supplementing Security Council restrictions with their own unilateral sanctions as they saw fit. The United States has been the most active initiator of unilateral sanctions against North Korea. Until recently, Pyongyang was the main target of restrictions imposed by major regional players. However, the situation has undergone a tangible change in the past few years.

First, to compel other countries to observe the imposed restrictions, the US authorities have begun to introduce secondary sanctions against foreign citizens and companies for cooperation with North Korea. The US Department of the Treasury blacklisted companies from Russia, China, and some other countries. Although damage from secondary sanctions has been minimal, Moscow and Beijing have criticized their use against companies in the foreign jurisdiction. Nevertheless, the US authorities are increasingly resorting to secondary sanctions. The risks of secondary sanctions are linked to the restrictions imposed on North Korea and some other states, for instance, Iran.

Second, the growing competition between the United States and China is making Beijing a potential target of US sanctions. In the late 1980s, the US and European countries imposed a large package of restrictions on China, but by the early 2000s most of them were cancelled owing to the rapid growth of economic ties. For the time being, sanctions against China are in their infancy. Fines imposed by the US Department of the Treasury on the Chinese ZTE and the case against Huawei acquired a serious political tinge but did not go beyond secondary sanctions until recently – both companies were ‘punished’ for their alleged ties with Iran in violation of US sanctions against it. Nevertheless, restrictions against Chinese telecommunication giants follow in the wake of the growing technological competition between the US and China. Under the circumstances, sanctions may be used as an instrument of technological deterrence. Sanctions were also imposed on China for its military-technical cooperation with Russia. This practice may continue in the future.

Third, China may resort to reciprocal restrictions. Up to now, Beijing has preferred to refrain from using sanctions. Restrictions have been sooner imposed informally, which has also produced political results. At the same time, the growth of China’s economic power and the exacerbation of political differences in the region may well compel China to adopt a tougher and more open policy of economic restrictions.

Fourth, for various reasons, other countries in the region are becoming involved in a policy of unilateral sanctions. For instance, Japan remained a major trading partner to Iran

for a long time despite US sanctions. Washington resumed unilateral sanctions against Iran and cancelled exemptions for Japan and other US partners, thereby toughening its policy against them. The same applies to India, which also lost its exemptions on Iranian oil and may well be targeted by US sanctions for its defence cooperation with Russia.

Finally, fifth, large regional players start thinking about insurance mechanisms in case the US dollar is turned into a weapon and the US uses its unique position in the global financial system for political ends. Such debates, not to mention practical actions, are in the initial stage. The same applies to Europe where the issue of financial sovereignty has become more urgent due to the US withdrawal from the nuclear deal with Iran and large fines imposed by the US Department of the Treasury on European companies. At present, it is more a matter of tactical measures. However, in the future this issue may become more topical, especially if the political competition between the US and China exacerbates.

Are these changes a sign of fundamental upheavals in regional affairs or are they just momentary fluctuations of no strategic importance? Will the US policy of sanctions lead to irreversible political consequences or will national governments and companies comply with the American demands? Will sanctions facilitate the adoption of systemic measures on the protection of financial sovereignty or will the region's governments and companies prefer working in the usual environment of US leadership? We will try to answer these questions in the context of the afore-mentioned changes.

What Kind of Sanctions Are We Talking About?

The concept of sanctions includes a fairly wide range of restrictive measures and requires a clear conceptual framework. To begin with, economic sanctions are different from trade wars. These two concepts are often confused in the Asian region, especially when it comes to relations between the US and China. In fact, they differ both in goals and in methods. Trade wars are aimed to achieve economic advantages for national producers. Tariff regulation is the main means of carrying out a trade war. Countries can remain partners and even allies, but still wage major trade wars. Sanctions, on the contrary, pursue mainly political goals. The initiating country aims to have the target country make specific political concessions or change its political course. Accordingly, methods vary. Sanctions may come in the form of bans on certain imports or exports, on technology transfer, financial transactions, investment, lending, etc. Trade wars and sanctions have a different legal basis at the level of national legislation. The same applies to purely bureaucratic process: individual departments are usually in charge of imposing sanctions.

There are several types of restrictive measures. The first type includes sanctions imposed by the UN Security Council on the basis of Article 41, Chapter VII of the UN Charter. Strictly speaking, such sanctions have the fullest international legitimacy, as they are introduced on behalf of the international community in accordance with the rules agreed upon by all its members. However, the bulk of restrictive measures belong to a different type – unilateral sanctions. Such measures are imposed by a single country, a group of countries, or an international organization based on national legislation and without approval of the UN Security Council. The US has introduced the bulk of such measures in the past century and made recourse to sanctions more often than all other countries and international organizations taken together.¹ This is not accidental. Sanctions are often imposed by economically developed countries which enjoy significant economic superiority over target countries.

There are other reasons for the popularity of unilateral measures. In the case of the UN, the decision to impose restrictions must be taken by the Security Council based on consensus. Adoption of resolutions may be protracted or delayed, and the phrasing is often a rounded trade-off. On the contrary, an individual state can impose sanctions promptly, and the measures can be exceptionally harsh. The speed of decision-making on sanctions at the UN and, for example, in the office of the US president differs tremendously. Such differences become even more pronounced when a decision is implemented. Over the past two decades, the UN has done a lot of work to improve the mechanisms for implementing sanctions decisions.² However, the organization is experiencing a shortage of financial and human resources. Different restrictive measure programmes vary significantly in terms of the resources and personnel available to them. Even more difficulties arise at the level of individual countries' reporting on the implementation of UN decisions. The quality of reports varies significantly and, in some cases, they are submitted only after major delays. National states, especially superpowers, never run into such problems. For the purposes of implementing sanctions, the US today has the best-trained interdepartmental staff, which is fully supplied with finances, personnel, information, and other important resources.

Countries can remain partners and even allies, but still wage major trade wars

Unilateral measures can also be grouped in several sets. First, comprehensive sanctions should be distinguished from targeted or 'smart' sanctions. Comprehensive restrictions are rarely used today as they lead

¹ Hufbauer, G, Schott, J, Elliott, K & Oegg, B, 2009, 'Economic Sanctions Reconsidered', Third Edition, Peterson Institute for International Economics, p. 89.

² See: Biersteker, T, Eckert, S & Tourinho, M, 2016, 'Targeted Sanctions. The Impacts and Effectiveness of United Nations Actions', Cambridge University Press.

to serious social ramifications, while their influence on the political course of the target country is not guaranteed. Targeted sanctions are used more often today and are aimed at particular representatives of political elites or economic sectors that are vital for the target country.

Another important classification involves dividing sanctions into primary and secondary. Primary restrictions often imply the inclusion of particular individuals or legal entities on sanctions lists based on political decisions of the initiating country's government, its parliament, or a specific department. The law of the US and the EU implies a partial or complete ban on economic transactions with the persons on the lists. The ban applies to citizens of the initiating country and the organizations operating within its jurisdiction.

In the narrow sense, secondary sanctions include extraterritorial restrictions against foreign individuals or organizations found to have violated sanctions regimes. In a broad sense, they can be called 'sanctions for violating sanctions' imposed on any company or individual. Such measures are mostly used by the United States. Due to the important role of the dollar in the global financial system, the US authorities can track transactions around the world. Secondary sanctions are often imposed for using the US financial system (any dollar-denominated transaction may count) in relations with individuals or organizations under sanctions. However, the decision on imposing secondary sanctions may be made for other reasons, including the ones established by intelligence, such as, transshipment of goods prohibited for import or export on the high seas or delivery of such goods through third countries or companies.

Secondary sanctions per se may also involve different tools. First, there is including a company or a person violating an existing regime of restrictions in the sanctions lists. In other words, the violator of sanctions is equalized in status with the objectives of primary sanctions. This is a radical measure designed to completely exclude the offender from the international financial system and to significantly limit its operations in the international arena. Often, such companies are no longer able to conduct regular international activities. They remain doomed to work with a country under sanctions. A more flexible measure implies using fines against violators. A fine harms the company but does not remove it from international activities. Such measures are highly effective and are used against major global companies and small firms alike. Regardless of their size, companies that have been fined do not commit violations in the future.³

³ See: Timofeev, I, 2019, 'Rethinking Sanctions Efficiency. Evidence from 205 Cases of the U.S. Government Enforcement Actions against Business', *Russia in Global Affairs*, vol. 17, no 3, July–September. Available from: <https://eng.globalaffairs.ru/number/Rethinking-Sanctions-Efficiency-20213>

Is North Korea the Main Target?

The use of sanctions in the Asia-Pacific Region was linked to North Korea for a long time. The international community represented by the UN Security Council and major countries individually tried to use restrictions to compel the North Korean leaders to give up their nuclear missile programme. Sanctions against Pyongyang are one of the most paradoxical cases. North Korea was subjected to the toughest sanctions. A broad international coalition was formed that used all its pressure to achieve unprecedented isolation of the country. Notwithstanding, Pyongyang still succeeded in carrying out its nuclear missile programme while its economy and the political system withstood the pressure.

After the end of the Cold War, long-term security guarantees became an acute issue for North Korea. However, North Korean nuclear missile ambitions were unacceptable for all key regional players. They undermined the non-proliferation regime and were bound to increase potential losses and costs in the event of a real armed conflict. The six-party talks ended in failure. Pyongyang decided to up the ante and launched a series of missile and nuclear tests in 2006. Despite the differences between the participants in the six-party talks, the international community unanimously opposed North Korean tests and made sanctions a key instrument in curbing the country's nuclear missile programme. The UN adopted a record number of resolutions and used more personnel and funds on sanctions against North Korea than on most other restrictions in its history.

The sanctions against North Korea escalated as the country continued to conduct missile and nuclear tests. Ten resolutions were adopted since 2006. Each new round of tests led to tougher sanctions. Thus, in 2006 a ban was imposed on supplies of arms, any nuclear- and missile-related products, and luxury items. Financial sanctions were introduced against organizations involved in the nuclear missile programme (UN Security Council Resolution 1718). After new tests in May 2009, they were supplemented with additional financial restrictions and inspections of commercial vessels (Resolution 1874). In 2012–2013, personal sanctions were adopted against a number of individuals and organizations. Tougher financial measures and restrictions were imposed on the efforts of North Korean foreign missions to circumvent sanctions (resolutions 2087 and 2094). All these measures were further toughened in 2016 after new tests and statements by North Korean leaders

on the development of the hydrogen bomb. They were supplemented with restrictions on export items vital for North Korea: coal, ore, steel, and rare earth metals (resolutions 2270 and 2321). Finally, four resolutions (2356, 2371, 2375, and 2397) were adopted in 2017 in one go. A ban was imposed on the admission of migrant workers from North Korea, stronger export and import restrictions as well as financial and other sanctions were adopted. In parallel, a number of states, for instance, South Korea, Japan, EU countries, and Australia, introduced unilateral restrictions. The US adopted the toughest and most detailed unilateral measures. They were enacted both by a series of presidential executive orders (13466, 13551, 13570, 13687, 13722, and 13810), and by laws approved by US Congress (PL 114-122 in 2016 and PL 115-44 in 2017, which is well known in Russia).

It is widespread practice to introduce unilateral sanctions in parallel with UN Security Council resolutions. The US and its allies often resort to it, as distinct from China and Russia, which usually do not go beyond UN Security Council resolutions. However, the simultaneous existence of UN sanctions and unilateral restrictions has given rise to a unique problem. US unilateral sanctions are extraterritorial. In other words, Washington imposes them both on its own citizens and on foreign nationals. In these circumstances, such restrictions began to be applied to Russian and Chinese individuals and companies that the US government suspected of violating sanctions. Therefore, these unilateral sanctions created a potential conflict within the UN Security Council. For the time being, they have not done much damage, but they are gradually becoming system-wide. Adopting unilateral secondary sanctions, the Americans proceeded both from their own laws and from UN sanctions.⁴

Here are some vivid examples of US secondary sanctions against Russia and China over the North Korean restrictions. For instance, Chinese industrial company Dandong Hongxiang Industrial Development and four of its top executives⁵ were put on the US Specially Designated Nationals List (SDN-list) in September 2016. The company is located in the city of Dandong, Liaoning province, near the border with North Korea. Three other Dandong-based companies selling metals and raw materials were put on the SDN-list

⁴ 'Updated Guidance on Addressing North Korea's Illicit Shipping Practices', 2019, March 21. US Department of the Treasury. Available from: https://www.treasury.gov/resource-center/sanctions/Programs/Documents/dprk_vessel_advisory_russian_04052019.pdf

⁵ 'Non-proliferation Designations. Specially Designated Nationals List Update', 2016, September 26, Office of Foreign Assets Control, US Department of the Treasury. Available from: <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20160926.aspx>

in August 2017. Then, the same happened to seven more companies from China, Singapore, and Namibia, as well as Russia's Gefest-M. Six individuals, including four Russians, were put on the same list. Not long before this, in June 2017, the Americans added to it three more Russian companies (Independent Oil Company, Ardis-Bearings, and Primornefteprodukt) and one more Russian citizen.⁶ In November 2017, four other companies from Dandong were put on the same list.⁷ In August 2018, they blacklisted Dandong Zhongsheng Industry and Trade and the Russian Agrosoyuz Bank.⁸ Several days later, the same happened with Russian Profinet, Chinese Dalian Sun Moon Star International Logistics Trading and a company from Singapore. A number of Russian logistics companies and their vessels were put on the SDN-list in the same month, including Gudzon Shipping, PML, and Vela-Marine.⁹ According to the Americans, most violations are linked to the delivery and sale of banned products – coal, oil products, metals, and seafood. In some cases, these products are simply transhipped from one vessel to another at sea.

Chinese and Russian diplomats protested against the blacklisting of companies and individuals by the Americans, but not a single case triggered a serious political crisis. Strictly speaking, the scale of US secondary sanctions against Chinese and Russian companies is fairly modest. At present, the US Department of the Treasury has blacklisted only 94 Chinese companies. Some of them represent foreign companies that are under US sanctions for other reasons. This also applies to the Russian Vnesheconombank (VEB) – Asia, which was subjected to sectoral restrictions as part of the Ukrainian sanctions package. The Chinese office of the Belarusian Belneftekhim is on the list of sanctions against Belarus. With few exceptions, these companies can hardly be called large or strategic. In all, 32 companies are

The volume and political consequences of the US secondary sanctions over Iran are much stronger in comparison with sanctions over North Korea

⁶ 'North Korea Designations and Updates; Non-proliferation Designations and Updates; Democratic Republic of the Congo Designations; Counter Terrorism Removals', 2017, June 1, Office of Foreign Assets Control, US Department of the Treasury. Available from: <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20170601.aspx>

⁷ 'North Korea Designations; Counter Terrorism Designation Removal', 2017, November 21, Office of Foreign Assets Control. US Department of the Treasury. Available from: <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20171121.aspx>

⁸ 'North Korea Designations; Non-proliferation Designation', 2018, August 3, Office of Foreign Assets Control, US Department of the Treasury. Available from: <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20180803.aspx>

⁹ 'Cyber-related Designations; North Korea Designations', 2018, August 21, Office of Foreign Assets Control, US Department of the Treasury. Available from: <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20180821.aspx>

under sanctions against North Korea. Another seven are blacklisted due to non-proliferation issues that are often linked to North Korea. These companies are practically invisible on the scale of the Chinese economy. Only 74 Chinese citizens are on the US blacklist, including 34 on the North Korean case and 12 on the case of non-proliferation.

There are many more Russian names on the US blacklists – 408 companies and 122 individuals, but most of them were subjected to sanctions over Ukraine or Syria, as well as cybersecurity, alleged interference in elections, or human rights violations. Only 11 companies and 11 individuals were subjected to sanctions over North Korea. Importantly, the US did not limit its North Korean sanctions only to Russia and China, so it can hardly be accused of a national bias.

As for the fines imposed on companies for violating US sanctions, North Korea plays an even smaller role in this respect. In the past ten years, not a single Russian or Chinese company has been subjected to fines for violating sanctions against North Korea – however, fines were imposed on two American companies. In 2015, Navigators Insurance paid \$271,800 for insuring vessels that were blacklisted over the North Korean programme, as well as insurance transactions related to Iran, Cuba, and Sudan.¹⁰ The most ludicrous case happened with US company E.L.F. Cosmetics in January 2019. It bought a consignment of eyelash cosmetics from two Chinese companies that had bought the products from North Korean suppliers. The ill-starred company admitted the violation on its own free will and paid a fine of \$996,000.¹¹

To sum up, US secondary sanctions for violating restrictions against North Korea have not yet led to a serious aggravation of relations with China, Russia, or any other country. However, this may happen in the future. This is clear from the experience of secondary sanctions over Iran, which have had a much stronger impact on US–Chinese relations.

¹⁰ 'Navigators Insurance Company Settles Potential Liability for Apparent Violations of Multiple Sanctions Programs', 2015, August 6, Office of Foreign Assets Control, US Department of the Treasury. Available from: https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20150806_navigators.pdf

¹¹ 'E.l.f. Cosmetics, Inc. Settles Potential Civil Liability for Apparent Violations of the North Korea Sanctions Regulations', 2019, January 31, Office of Foreign Assets Control, US Department of the Treasury. Available from: https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190131_elf.pdf

Iranian Nuclear Problem: The Fallout in US–China Relations

Sanctions against Iran are very similar to restrictions against North Korea. In order to contain Iran's nuclear programme, the UN Security Council has adopted a number of resolutions as well. Since 2006, the sanctions' intensity has been increasing as Iran made progress in its nuclear projects. The first resolution (1696) was a warning, but the next one (1737) already contained bans on supplying materials that could be used in a nuclear programme. In 2007, the number of restrictions was expanded by Resolution 1747. The sanctions were used both against individuals and organizations involved in the nuclear programme and the Islamic Revolutionary Guards Corps. Restrictions on arms deliveries to Iran and financial sanctions in the form of an appeal to international institutions to refrain from lending to Iran were introduced. In 2008, Iranian banks operating abroad came under restrictions, a policy was introduced to inspect ships and aircraft when there are grounds to suspect their involvement in the nuclear programme (Resolution 1803). Finally, in 2010, against the backdrop of Tehran's latest achievements in uranium enrichment, financial, trade, and transport restrictions were tightened significantly (Resolution 1929). The resolution also indicated the relationship between oil trade revenue and nuclear programme development. Although the resolution did not impose restrictions on Iranian oil imports, this point was widely used by individual countries in unilateral restrictions.

Just like in the case of North Korea, the US imposed more unilateral sanctions than any other country. Washington widely used sanctions immediately after the Islamic Revolution of 1979. The Americans were the first to launch a campaign to deter Iran's nuclear projects through sanctions back in 1995. European and Asian allies of the US were reluctant to join Washington's sanctions and occasionally sabotaged them openly. Therefore, the internationalization of sanctions in the UN Security Council was a great boost for US diplomacy. Congress supported the executive branch by adopting a series of laws on Iran over 20 years (PL 104-172 in 2006, PL 111-195 in 2010, PL 112-158 in 2012, PL 112-239 in 2013, PL 114-17, and PL 115-44 in 2017) and approving a large number of presidential executive orders. Importantly, the sanctions concerned the nuclear programme and missile projects, human rights, suspicions of supporting terrorism, etc. They were much tougher compared to UN

resolutions. It was about a ban on investing in the oil and gas sector, supplying fuel, and then importing crude oil from Iran.

The US was making vigorous and quite successful efforts to internationalize its sanctions. The EU came up with a package of unilateral measures, and a number of countries adopted US requirements concerning limitations on purchases of Iranian oil, as well as financial and other restrictions (for example, India and Japan). These measures caused serious damage to Iran and were among the factors for signing the Joint Comprehensive Plan of Action (JCPOA) in 2015 and adopting UN Security Council Resolution 2231. However, in 2018, the US unilaterally withdrew from the JCPOA, while maintaining the extraterritorial nature of its sanctions. In other words, while in the case of North Korea unilateral US measures coexisted with the UN sanctions regime, large-scale unilateral and extraterritorial sanctions against Iran were imposed by the Americans and no one else. At the same time, the volume and political consequences of the US secondary sanctions over Iran are much stronger in comparison with sanctions over North Korea.

Over the past ten years, the US sanctions regime against Iran has been violated much more often compared with other sanctions. Iran accounts for 107 out of 312 violations, which were fined by the US Treasury Department. To put that in perspective, Cuba had 67 such violations, Sudan – 58, the weapon of mass destruction (WMD) countering programme – 16, Burma – 15, the drug trafficking countering programme – 14, and other programmes – under ten each. American and European companies accounted for the bulk of violations, with the Europeans paying 83% of all fines.

The Chinese looked pretty modest against this background. There were only a few investigations completed during 2009–2019 or currently underway.¹² Two of them are relatively small. In 2018, Yantai Jereh Oilfield Services Group was fined by the US Treasury Department for supplying equipment to the Iranian oil industry. The case was recognised as ‘flagrant’, that is, it had a number of aggravating circumstances, including attempts by the management to cover up non-compliance with sanctions, the systematic nature of violations, the company’s deliberate actions, etc. Eventually, the company agreed to pay a fine of \$2.7m and obtained only a small discount for cooperation with the Americans during the

¹² Timofeev, I, 2019, ‘Rethinking Sanctions Efficiency. Evidence from 205 Cases of the U.S. Government Enforcement Actions against Business’, *Russia in Global Affairs*, vol. 17, no 3, July–September. Available from: <https://eng.globalaffairs.ru/number/Rethinking-Sanctions-Efficiency-20213>

investigation.¹³ Another case is related to the Chinese branch of the US Company Stanley Black & Decker. The Chinese subsidiary supplied Iran with industrial equipment unbeknownst to the parent company in the United States. The US-based headquarters found out about the fact of violations and voluntarily reported it to the US authorities. The penalty was relatively small compared to the volume of transactions and amounted to \$1.8m.¹⁴ These cases did not cause any political fallout.

The cases involving the telecommunications companies ZTE and Huawei caused by far more repercussions. An investigation against ZTE was triggered by supplying equipment containing US-made components to Iran. Therefore, the investigation was conducted both by the Department of the Treasury and the Department of Commerce. The case was recognised by the US as 'flagrant' as it involved many aggravating circumstances. ZTE's actions to circumvent US sanctions were identified as pre-planned. The situation was further aggravated by repeated attempts of the management to cover up the violations. Moreover, according to the Americans, this continued even after the US authorities opened the investigation.¹⁵ Eventually, the company cooperated with the Department of the Treasury and the Department of Commerce, accepted their terms, and paid enormous fines. By 2018, the fines totalled \$2.29bn.¹⁶

The Huawei case has provoked an even bigger political crisis. It has not been settled yet and has led to a number of major consequences. The US administration accused the Chinese telecoms giant of exporting equipment with US-made parts to Iran. The problem was therefore taken up by the Departments

China will opt for technological autonomy, although Chinese companies will still have to accept US conditions in the medium term

¹³ 'Yantai Jereh Oilfield Services Group Co., Ltd. Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations', 2018, December 12, Office of Foreign Assets Control, US Department of the Treasury. Available from: https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20181212_jereh.pdf

¹⁴ 'Stanley Black & Decker, Inc. Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations Committed by its Chinese-Based Subsidiary Jiangsu Guoqiang Tools Co. Ltd', 2019, March 27, Office of Foreign Assets Control, US Department of the Treasury. Available from: https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190327_decker.pdf

¹⁵ 'Zhongxing Telecommunications Equipment Corporation Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations', 2017, March 7, Office of Foreign Assets Control, US Department of the Treasury. Available from: https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20170307_zte.pdf

¹⁶ 'Secretary Ross Announces \$1.4 Billion ZTE Settlement; ZTE Board, Management Changes and Strictest BIS Compliance Requirements Ever', 2018, US Department of Commerce, June 7. Available from: <https://www.commerce.gov/news/press-releases/2018/06/secretary-ross-announces-14-billion-zte-settlement-zte-board-management>

of Treasury and Commerce. The Department of Justice soon joined the case. It is only seldom that several regulators become simultaneously involved in an investigation, which is evidence of the seriousness of the suspected violations. In December 2018, Huawei's chief financial officer Meng Wanzhou was detained in Canada at the request of the US. She was charged with financial fraud allegedly intended to evade US economic sanctions on Iran. On May 15, the US Department of Commerce blacklisted Huawei for actions against US national security interests. In effect, it curtailed Huawei's transactions with US companies, which spelled big problems for the Chinese giant because of its close technological ties with its American partners.

Yet, the Huawei restrictions have led to major losses for US businesses as well. On May 20, the Department of Commerce issued a Temporary General License authorizing transactions with Huawei in four specific areas. This has left the Chinese company in limbo, because the license should be renewed every 90 days and can be revoked at any time. Meanwhile, Huawei was charged with industrial espionage. In that context, US President Donald Trump signed the Executive Order on Securing the Information and Communications Technology and Services Supply Chain¹⁷ to declare a national emergency with respect to 'an unusual and extraordinary threat to the national security, foreign policy, and economy of the United States'. China was not mentioned directly but it is obviously the target of that order. In other words, the Huawei case has given an official start to large-scale US actions that could lead to sanctions in the field of information against China and other countries, including Russia.

Beijing promptly gave a harsh response to the US and Canada, including the arrest of two Canadian nationals. However, Huawei, like many other sanctioned companies, refrained from politicizing the matter. The investigation is not over yet, but Huawei will likely try to settle the US claims, most probably by paying huge fines. But it would be the lesser of two evils, because settling the claims would allow Huawei to remain in the market and to continue its cooperation with American companies.

This is a landmark case, because Chinese companies are now viewed as a threat in the United States. In China, the US sanctions are seen as an attempt to hamper China's technological progress, especially considering that the United States has done everything in its power to persuade other countries to ban the Chinese companies' 5G projects. The main result of this campaign may be that China will opt for technological autonomy, although Chinese

¹⁷ 'Executive Order on Securing the Information and Communications Technology and Services Supply Chain', 2019, May 15, The White House. Available from: <https://www.whitehouse.gov/presidential-actions/executive-order-securing-information-communications-technology-services-supply-chain/>

companies will still have to accept US conditions in the medium term. Tactically, the Americans can force their will on Chinese companies. However, strategically, China will strive for autonomy, so that eventually the United States will lose the Chinese market, with all the ensuing consequences for American business.

One more landmark case was the addition of the China Ocean Shipping Company (COSCO) to the SDN-list. COSCO is suspected of transporting Iranian oil in violation of US sanctions. This is not an ordinary case, because the Americans have applied an extraordinary measure against COSCO, banishing it from the sphere of international transactions. The company is facing serious problems with dollar-denominated payments, port services, insurance, etc. The sanctions have also affected COSCO's partners. Again, the Chinese authorities' response was low-key, but behind this apparent calm, stormy clouds of strategic confrontation with the United States may be gathering.

A US–China Conflict?

The US sanctions against China are often regarded as being closely linked to the trade war. In fact, these are different processes with differing goals, means, norms, and even officials in charge. The sanctions are much closer to political issues, even if they are based on economic restrictions. While trade wars may well be waged between partners, an escalation of sanctions is a sign of more fundamental problems in relations, particularly if sanctions cease to be episodic and crystallize into a strategy.

Several factors can influence the conversion of the anti-China sanctions into a strategy. First, there is a history of restrictions against China. Beijing came under brutal sanctions in 1947 and had to live with them until the late 1960s, when they started being watered down. But after the Tiananmen Square events, the US and Europe built up pressure again (Public Law 101-246 of 1990 and the European Council's 1989 Madrid Declaration). During the 1990s, the restrictions tapered off due to the rapid growth of economic interdependence and effective lobbying by both Chinese business and US partners. Only a small set of restrictions survived by 2000, mostly those in the area of arms and military equipment supplies. However, the 'strategic memory' or the 'historical track' associated with sanctions against China persists to this day. It is debatable to what extent this factor can influence political decision-making. Nevertheless, with all else being equal, the confrontational 'track' feeds rivalry at a new stage in relations.

SANCTIONS AND TRADE WARS

Trade War



Aimed to gain economic advantage through tariff and non-tariff barriers

Sanctions



Aimed to achieve political goals and behaviour change of the target country

Primary restrictions are imposed on target country's legal entities and individuals

Secondary restrictions are imposed on third countries' legal entities and individuals for violating the sanctions regime

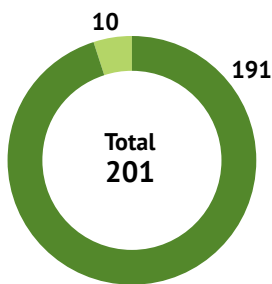
UN Security Council sanctions have full international legitimacy

Unilateral sanctions are imposed by a country or a group of countries on others

US Secondary Sanctions in 2009–2019

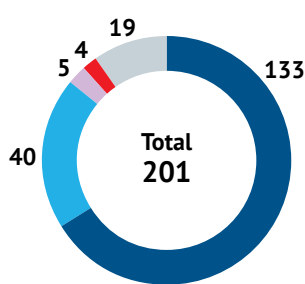
Breakdown of cases for violation of the US Department of the Treasury's sanctions

Fines



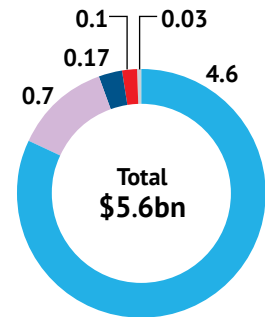
■ Against companies
■ Against individuals

Fines by country



■ US
■ EU
■ Switzerland
■ China
■ Others

Sum of fines, \$bn



■ EU
■ US
■ Switzerland
■ China
■ Others

Source: based on data from US Department of the Treasury.

The second factor is related to incidents in the digital sphere. Unlike in the Huawei case, the US concerns have to do with national security rather than economic rivalry or breaches of the sanctions regime against third countries. The first wakeup call was an incident in 2015, when hackers, who, as the US believed, were working for the Chinese government, stole millions of files of US citizens. The political scandal was hushed up. But Barack Obama reacted by signing Executive Order 13694 introducing a state of emergency, authorizing the government to impose sanctions against cybercrime suspects, both organizations and individuals, from any country. Since then, there have been no high-profile digital incidents between China and the US. However, an institutional mechanism designed to combat the threat has already been put in place and working.

Unlike Washington, Beijing prefers to introduce informal and indirect restrictions

The third factor is China's defence cooperation with Russia. In this area, China comes under PL 117-44 Countering America's Adversaries Through Sanctions Act (CAATSA), which envisages sanctions for military-technical cooperation with Moscow. In September 2018, the US Department of the Treasury put the Equipment Development Department of the Chinese Central Military Commission, along with its director, Li Shangfu, on the SDN-list for their S-400 and Su-35 deals with Russia. The actual damage from these moves is infinitesimal and the measures are more likely to be meant as a signal. It would have passed unnoticed, were it the only restriction imposed on China. But in the context of other sanctions it is rather a 'link in a chain', although the US bureaucracy could hardly have meant it to be one.

The fourth factor is China's increased military and political activity in the South China Sea. So far, the United States has not imposed sanctions in this connection. But there were discussions to this effect in the expert community.¹⁸ The political controversy in the South China Sea continues and prospectively may even intensify something that increases the likelihood of US sanctions. There are contradictions over other regional security issues as well, including Taiwan.

The fifth factor has much to do with the domestic political dynamics in the United States. Congress may come up with an initiative to contain China. Although Congress and the administration largely see eye to eye on China, the legislators may put forward more radical proposals than the executive is ready to accept. Thus far, China is mentioned in current bills and resolutions

¹⁸ See, for example, Cooper, Z & Lorber, E, 2016, 'Sanctioning the Dragon: Using Statecraft to Shape Chinese Behavior', *National Interest*, March/April, p. 36-42.

in connection with countervailing its economic, information, and political influence, the need to form a coalition with countries in the region,¹⁹ the problem of Tibet,²⁰ Hong Kong,²¹ etc. In any event, Congress is unlikely to cushion possible complications in bilateral relations.

Beijing's own attitude to what is happening is the key to assessing the prospects for further escalation. While the US has long referred to China as a threat and applied sanctions concerning certain episodes, the Chinese stance seems more cautious. Until recently, Beijing disregarded the sporadic use of sanctions against some of its citizens and companies. The United States is yet to design a separate programme of sanctions against China similar to the one that exists in relation to Russia. So far, Washington has not given cause for China to openly opt for an aggravation. But Beijing is certain to be considering possible measures to counteract the US sanctions. If anything, China's strategy will be influenced by the specific nature of its sanctions policy. Unlike Washington, Beijing prefers to introduce informal and indirect restrictions. A case in point is an actual ban on access to the Chinese market for certain South Korean companies in connection with Seoul's plans to buy US THAAD systems. At the same time, China openly declared that it could impose sanctions on US companies if they supplied weapons to Taiwan.

Chinese leaders may be toying with the idea of introducing a package of preventive measures. Some of these are being discussed by US experts,²² although it is still unclear to what extent Beijing is ready to use them. A few measures can be outlined.

- Identifying companies and individuals that might be targeted by restrictions if the US takes similar steps, imposing selective restrictions on these companies and individuals. The key restriction is a denial of access to the Chinese market.
- Using vulnerabilities in the US economy, including America's huge debt.
- Ban on certain exports to the US.

¹⁹ 'S. 2547. To State the Policy of the United States with Respect to the Expansion of Cooperation with Allies and Partners in the Indo-Pacific Region and Europe Regarding the People's Republic of China', 2019, 116th Congress, 1st Session, September 25, The US Congress. Available from: <https://www.congress.gov/bill/116th-congress/senate-bill/2547/text?q=%7B%22search%22%3A%5B%22China%22%5D%7D&r=6&s=3>

²⁰ 'S. 2539. To Modify and Reauthorize the Tibetan Policy Act of 2002, and for other Purposes', 2019, 116th Congress, 1st Session, September 24, The US Congress. Available from: <https://www.congress.gov/bill/116th-congress/senate-bill/2539/text?q=%7B%22search%22%3A%5B%22China%22%5D%7D&r=8&s=3>

²¹ 'H.Res.543 – Stand with Hong Kong Resolution', 2019, September 25, 116th Congress (2019-2020), The US Congress. Available from: <https://www.congress.gov/bill/116th-congress/house-resolution/543/text?q=%7B%22search%22%3A%5B%22China%22%5D%7D&r=17&s=3>

²² See, for example, Nephew, R, 2019, 'China and Economic Sanctions: Where does Washington Have Leverage?', Brookings Report, September. Available from: <https://www.brookings.edu/research/china-and-economic-sanctions-where-does-washington-have-leverage/>

- Introducing targeted restrictions against US allies, or, conversely, establishing special relations with them in some sectors contrary to Washington's position.
- Accelerated import substitution to oust US goods and technologies.
- Stepping up support for the sanctions-hit adversaries of the US. The case in point is a politically motivated, purposeful assistance rather than a breach of US sanctions regimes to maximize profits.

If the latter happens, the nature of Chinese moves to violate the US sanction regimes will be fundamentally changed. Deals with sanctioned countries may become a systematic state-supported policy – poles apart from today's isolated episodes stemming from corporate initiative or error.

China will also work to gradually transform the world financial system so as to undermine the domination of the US dollar and preclude its use as a political tool. One of the fundamental consequences of the anti-sanctions course (provided the Chinese leadership chooses it) will be a sharp rise in the state involvement in the economy and foreign trade. Paradoxically, the US sanctions may lead to the erosion of the norm-setting principles promoted by Washington. Instead of market relations that are widespread, if somewhat specific, within the Chinese business community, the United States will have to deal with an economy swayed by the state regulators.

Nevertheless, these developments are not yet preordained, if increasingly likely. A collapse of economic ties will harm both China and the US. For this reason, the sides are certain to refrain from any excessively abrupt moves. Beijing may choose a more moderate course, avoiding isolation and focusing on multilateral diplomacy, the more so as the United States has made its sanctions policy much more unilateral in recent years.

Washington will find it more difficult to persuade its allies and partners to help it to contain China

One of the most glaring examples is Washington's withdrawal from the JCPOA and its efforts to make the international business community abide by US sanctions. This policy tends to cause dissatisfaction with the United States among both rivals and allies. The extraterritorial sanctions are hitting European businesses hard. They have also affected the interests of such countries as Japan, India, and South Korea, which have recently been stripped of exemptions to buy Iranian oil. We can hardly expect a system-wide, consolidated, and effective protest against US sanctions in the foreseeable future. It is even less likely that this protest could be headed by China. However, Washington will find it more difficult to persuade its allies and partners to help it to contain China or support US sanctions if full-scale rivalry comes underway.

For a long time, US sanctions targeted countries that Washington branded as 'rogue states'. In a number of cases, the UN Security Council supported these restrictions, particularly when it was necessary to stop the proliferation of nuclear missile technologies or nuclear weapons. But Washington's unilateral restrictions and extraterritorial sanctions are increasingly affecting major players. China is becoming the main target in Asia. Until recently, the problem amounted to episodic fines and secondary sanctions against individuals and select companies. Their overall number was not high, and the US actions were not causing political problems. Today, however, the situation is changing. Containing China has become an agenda in its own right for the United States, increasing the risk of sanctions and China's retaliation. Chinese leaders are wielding a wide range of levers. An escalation of sanctions is fraught with grave damage to US–China relations.

Nevertheless, a confrontational scenario is not yet preordained. The United States may preserve its leadership, at least in the medium term, possessing as it does great potential for using economic restrictions to achieve political goals. However, the abuse of sanctions and unilateral moves, like the withdrawal from the JCPOA, will erode support for the US even from its allies. The financial sovereignty rhetoric may be converted into specific strategies. China has greater capability than anyone else for implementing them. It is quite likely that an awareness of the need for a coalition game and multilateral diplomacy will prevail in Washington. The point of no return has not been passed yet.

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