STEPHENSON HARWOOD (Singapore) Alliance

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SANCTIONS, EXPORT CONTROLS AND OTHER TRADE RESTRICTIONS

Overcompliance in a conflict-of-laws era: why "When in Doubt, Don't Perform" may no longer be the safest strategy.

This newsletter is atypical. It is not the standard "punchy" one- or two-page law firm bulletin. We thought about reducing it to that, but we think this particular topic deserves greater consideration and analysis. Please read on; we think you will find the effort worthwhile.

For many years, multinational companies have often adopted a simple, straightforward approach to sanctions risk: where a transaction raised sanctions concerns, the safest commercial response was often to reject payment, suspend performance or terminate the relationship, relying on broadly-drafted sanctions clauses to do so.

That approach was particularly understandable where the principal legal risk arose from U.S. sanctions. U.S. sanctions not only apply directly to U.S. persons, but also expose non-U.S. persons to secondary sanctions risks in certain circumstances. Non-U.S. financial institutions, in particular, have historically faced substantial U.S. sanctions enforcement actions, with penalties reaching billions of dollars.

Today, however, the legal landscape has fundamentally changed. China's Anti-Foreign Sanctions Law (2021) ("**AFSL**"), together with its Blocking Rules, Blocking Orders and other countermeasures, have created a competing legal regime.

Businesses may now face civil liability in China for implementing "foreign discriminatory restrictive measures" – we explain exactly what this means below. Depending on the circumstances, they may also be exposed to broader regulatory consequences under China's countermeasures regime, including designation under the AFSL Counter-Sanctions List, the Unreliable Entity List, the Malicious Entities List or other applicable restrictive measures.

The result is that, in matters that relate to China, the question is no longer just: "How do we avoid sanctions risks?" It has become: "How do we comply with international sanctions without violating China's countermeasures?"

EMERGING ARTICLE 12 JURISPRUDENCE: A GROWING LITIGATION RISK FOR OVER-COMPLIANCE

Article 12 of the AFSL provides that if any person or corporate entity implements or helps implement foreign discriminatory restrictive measures, and doing so harms the lawful rights and interests of a Chinese individual or corporate entity, the affected Chinese party may sue in a Chinese court and seek an order requiring the conduct to stop and compensation for its losses.

This appears to be regardless of what a contractual dispute resolution clause may say to the contrary.

Until recently, Article 12 of the AFSL was regarded as largely symbolic and no one seemed entirely sure what it encompassed. Within the past two years, however, at least three high profile cases have invoked Article 12 against parties that refused to perform contractual or corporate obligations because of foreign sanctions, export controls or other restrictive measures. Collectively and among other things, these cases demonstrate a startlingly broad range of what Chinese courts consider to be “foreign discriminatory restrictive measures” to which Article 12 claims can apply.

Brief summaries follow.

The Nanjing Maritime Court Case

The first reported case germane to Article 12 of the AFSL arose before the Nanjing Maritime Court in 2024.

The U.S. Office of Foreign Assets Control (**“OFAC”**) administers and enforces US sanctions. Following the addition of a Chinese shipbuilding contractor to OFAC’s Specially Designated Nationals and Blocked Persons List (the "**SDN List**"), its European counterparty refused to make an outstanding payment of approximately US$11.86 million, citing U.S. sanctions concerns. The Chinese shipbuilder then commenced proceedings under Article 12 and successfully obtained an interim preservation order arresting the vessel that was due to be delivered.

Although the dispute was ultimately resolved through court mediation after the European purchaser obtained an OFAC licence authorizing payment, the case demonstrated that Article 12 is not merely aspirational—it was used as an effective litigation tool to obtain interim relief, exert commercial pressure and bring non-Chinese counterparties back to the negotiating table.

The Shanghai Maritime Court Case

The second reported case, decided by the Shanghai Maritime Court and particularly important as it was selected by the Supreme People's Court as one of its six model maritime cases for 2025[1], marked the first substantive judicial interpretation of Article 12.

A Singaporean carrier refused to discharge cargo at the destination port after learning that the Chinese manufacturer had been included on the U.S. Bureau of Industry and Security ("**BIS**") Entity List and OFAC's Non-SDN Chinese Military-Industrial Complex Companies ("**NS-CMIC**") List. Taking the view that the exporter had not provided sufficient information to satisfy its sanctions due diligence requirements, the carrier declined to complete delivery. The carrier relied on sanctions concerns and contractual clauses to justify returning the cargo to Shanghai.

The court rejected that position, holding that the carrier's refusal to perform constituted the implementation of “foreign discriminatory restrictive measures,” enabling the Chinese party to utilise Article 12 of the AFSL. Perhaps more significantly, the court held that even if Singapore law governed the underlying contract, Article 12 could nevertheless apply as an overriding mandatory rule under Chinese conflict-of-laws principles. The decision signals that broad sanctions clauses and foreign governing law provisions may not necessarily shield a party from litigation under Article 12.

Wingtech Technology v. Nexperia

The most recent development is the pending Wingtech Technology v. Nexperia litigation before the Dongguan Intermediate People's Court, filed this May. Unlike the earlier cases, which concerned contractual non-performance, Wingtech seeks to hold its own Dutch subsidiary and senior management liable under Article 12 for complying with Dutch governmental and judicial measures that deprived the Chinese parent of effective control over the company following U.S. export control restrictions and Dutch economic security intervention (purportedly seeking to safeguard the European supply of semiconductors) . Wingtech, which acquired Nexperia in 2019, is reportedly seeking damages of approximately RMB 8 billion (approximately US$1.17 billion), making it probably the most significant Article 12 case to date, at least in monetary terms.

[1] China does not operate a common law system of binding judicial precedent, but if a case is cited by the Supreme People’s Court as a “model case,” this is a strong indicator to lower courts that its decision principles and outcome should be followed.

The case represents a significant expansion of Article 12 beyond contractual disputes and into the realm of corporate governance. It also raises novel questions regarding whether compliance with mandatory foreign governmental or judicial orders may itself constitute "implementing or assisting in implementing foreign discriminatory restrictive measures."

The decision is keenly awaited.

Taken together, these cases illustrate a clear trend. Chinese courts appear increasingly willing to accept Article 12 claims against private parties whose commercial decisions are driven by foreign sanctions, export controls or other restrictive measures that impact China-related trade, business and interests. The concept of "implementing or assisting in implementing foreign discriminatory restrictive measures" appears to be interpreted progressively more broadly. Indeed, one might take the view that hearing a case where a Chinese parent company is suing its own foreign subsidiary and senior management under Article 12 is an extraordinary and particularly noteworthy event.

Although many important legal questions remain unresolved—including whether Article 12 does indeed override parties' contractual choice of forum or arbitration agreement despite the AFSL containing no express provision conferring exclusive jurisdiction on Chinese courts or excluding foreign courts or arbitral tribunals (in contrast to certain Russian counter-sanctions legislation); the availability and effectiveness of anti-suit injunctions; and the recognition and enforcement of foreign arbitral awards where they conflict with Chinese judgments—the practical message is already clear. Organisations doing China-related business can no longer assume that a conservative sanctions compliance approach or a broadly drafted sanctions clause will shield them from all legal risk. In today's conflict-of-laws environment, over-compliance may itself expose companies to litigation in China.

WHEN DOES SANCTIONS COMPLIANCE BECOME OVER-COMPLIANCE?

Companies should now carefully distinguish between conduct that is legally-required and conduct adopted solely out of commercial caution or internal risk appetite. Doing so may help avoid unnecessary disputes and reduce the risk of litigation under Article 12.

The cases mentioned above provide their own lessons, in this regard:

1. **Understand The Measures That Have Been Applied**

   It is important to properly understand the restrictive measures that have been applied. For example, the placement of a Chinese company on the BIS Entity List affects its ability to receive, access and/or utilise US goods and technology. Likewise, placement on the NS-CMIC List imposes certain restrictions as regards its securities, but neither is a full asset freeze or absolute prohibition on any dealings, as is typically the case when a party is placed on the SDN List.

   Absolutely refusing to perform any contract whatsoever with the Chinese company under these circumstances could be characterised as unnecessary overcompliance which can then lead to exposures under Article 12 of the AFSL, which are entirely avoidable.

   This is not to suggest that commercial or reputational considerations are irrelevant. A business may decide, as a matter of corporate policy or risk appetite rather than strict legal need, not to engage with certain parties or transport certain cargo. Nevertheless, this now needs to be considered within the context of the AFSL when Chinese parties are involved.

2. Consider All Options

Designation as an SDN undoubtedly presents a more complex sanctions issue because U.S. persons are then generally prohibited from dealing with the blocked person and non-U.S. persons may face secondary sanctions exposure in certain circumstances, including when making payments to the SDN. Nevertheless, SDN designation does not necessarily mean that every contractual obligation must immediately cease. In other words, it is not necessarily "fatal".

In many OFAC sanctions programs, general licences authorize limited wind-down activities for a specified period—typically 30 days—following a new designation. Depending on the scope of the applicable licence, counterparties may be permitted to wind down existing contractual relationships, make or receive outstanding payments, divest interests, or take other steps necessary to terminate pre-existing transactions in an orderly manner. Where no general licence is available, parties may apply for a specific licence from OFAC, although the process can be lengthy and there is no guarantee that a licence will be granted.

It is also worth noting that, from a Chinese regulatory perspective, where a Blocking Order has been issued under China's Blocking Rules prohibiting compliance with certain foreign sanctions (such as an SDN designation), Chinese parties may apply to the Ministry of Commerce for an exemption from complying with the Blocking Order. If granted, the exemption permits compliance with the relevant foreign measures.

The Nanjing proceedings mentioned above illustrate the practical importance of considering these options before non-performance. During the litigation, the European purchaser ultimately obtained an OFAC specific licence authorizing payment, after which the parties reached a mediated settlement. While every case will depend on its facts and the applicable sanctions program, the outcome suggests that lawful avenues for performance or payment may remain available even after a counterparty becomes designated.

3. Time To Revisit Sanctions Clauses

One lesson from the recent Article 12 cases is that sanctions clauses should no longer be treated as automatic exit clauses. Many existing sanctions clauses were drafted when the principal legal concern was compliance with U.S., EU or UK sanctions. They therefore assume that sanctions obligations point in only one direction, giving parties broad discretion to suspend or terminate performance whenever sanctions concerns arise, often without requiring a careful assessment of whether performance is in fact legally prohibited.

That assumption is increasingly difficult to justify as regards to China-related business in today's conflict-of-laws environment. A refusal to perform may itself give rise to civil liability under Article 12 where it is found to implement or assist in implementing foreign discriminatory restrictive measures. Depending on the circumstances, businesses may also face broader regulatory consequences under China's counter-sanctions regime.

Sanctions clauses should therefore evolve from automatic non-performance mechanisms into tools for managing conflicting legal obligations. Rather than assuming that U.S., EU or UK sanctions dictate the outcome, companies should assess the competing legal risks in light of the transaction's jurisdictional nexus, place of performance, payment flows, personnel involvement, location of assets, and regulatory exposure.

Where Chinese anti-sanctions laws could create material legal risk, sanctions clauses should account for this including, where appropriate: (i) an express reservation that neither party is required to violate another applicable mandatory law, including China's AFSL and Blocking Rules/Blocking Orders; (ii) an obligation to consider lawful alternatives, such as licences, exemptions or alternative performance mechanisms, before suspending or terminating performance; and/or (iii) relief from liability only where performance is objectively prohibited after reasonable efforts have been made to identify a lawful solution.

PRACTICAL TAKEAWAYS

The emerging Article 12 cases do not suggest that companies should disregard U.S., EU or UK sanctions or export controls. Rather, they demonstrate that broad sanctions clauses and internal compliance policies, and a mere sanctions "concern" rather a definite sanctions issue, confirmed under proper expert assessment, should no longer be treated as automatic justifications for non-performance. In an environment of conflicting legal regimes, businesses should distinguish between what the law actually prohibits and what internal policy or commercial risk appetite merely prefers.

Before suspending performance, terminating a contract, or refusing payment or shipment due to sanctions, export controls or other trade restrictions, a business should carefully assess whether there is genuinely a legal requirement to do so and, if so, undertake additional consideration of the lawful alternatives that remain available, including licences, exemptions, transaction restructuring or other compliance mechanisms. Taking these steps at the outset is not merely a matter of good compliance practice—it may prevent unnecessary and costly disputes from arising in the first place.

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