

# Financing CCP's Surveillance State



## *Krach's Campaign to Protect the American Investor*

By Michael Mink January 19, 2020

### **Championing the American Investor**

Under Secretary of State Keith Krach has championed the cause to protect the average American from unknowingly funding the Chinese Communist Party's human rights abuses. Krach believes that "most Americans have no idea that their own money—held in pension funds, 401Ks, and brokerage accounts—is



financing Chinese companies that support China's military, security, and intelligence apparatus, as well as human rights abuses on an epic scale, such as those in Xinjiang. Through a web of subsidiaries, index funds, financial products and lack of proper disclosure, the average American investor is involuntarily supporting Chinese companies."

*As long as these subsidiaries retain access to America's capital markets, the PRC's military will continue to be financed on the backs of American workers.*

### **Advising U.S. Businesses**

On July 1, 2020, Krach sent a letter to all U.S. CEOs, asserting their duty to establish governance principles when it comes to investing in entities that directly or indirectly facilitate human rights abuses. He urged pension funds, mutual funds, insurance companies, venture capital firms, institutional investors, and emerging index funds to disclose Chinese investments to their constituents.



*Krach stated that Chinese companies' financial practices are opaque for a reason and do not comply with Sarbanes-Oxley transparency provisions, which puts all investors at risk.*

## Calling on University Endowments



On August 18, 2020, Krach also sent a letter to the governing boards of universities, alerting them to the CCP companies on the entity list or that contribute to human rights violations poses to university endowments.

Krach's warning to the governing boards of higher education institutions extended to guidance regarding risk reduction due to China's financial practices. He advised, "Divesting would be prudent in the likely outcome that enhanced listing standards lead to a wholesale delisting of PRC firms from U.S. exchanges by the end of next year. Holding these stocks also runs the high risks associated with PRC companies having to restate financials." He urged them to consider publicly disclosing Chinese holdings to their campus communities, "especially the PRC companies in emerging markets index funds."

*Krach told the endowment boards that they "have a moral obligation, and perhaps even a fiduciary duty, to ensure that your institution has clean investments and clean endowment funds."*

## Informing Pension Holders

On December 8, 2020, Krach issued a U.S. Department of State fact sheet titled "US Investors Are Funding Malign PRC Companies on Major Indices." The Thrift Savings Plan's governing board study revealed that a majority of pension funds use the MSCI emerging market index as



their investment guide, including: The 401k's of all 10 largest publicly traded U.S. companies; 10 top federal contractors; All 20 of the largest state pension plans; All six of the largest target-date mutual-fund providers with holdings of \$1.9 trillion as of June 2019; The Pension Benefit Guaranty Corporation with \$131 billion in pension insurance reserves.

*Malign PRC companies are being financed with the help of the \$10.7 trillion invested in more than 5,000 U.S. pension systems through the use of emerging market index funds.*

## Forewarning Stock Exchange Delistings



Krach's December 8th fact sheet highlighted that CCMCs, China Mobile, China Telecom and China Unicom are on the New York Stock Exchange and warned investors that these Chinese companies stocks have increased risk due to being subject to sanctions, public protests, trade restrictions, boycotts, delisting

and other punitive measures that jeopardize their business and profitability. On January 7, 2021, The NYSE announced the delisting of the three major Chinese telecommunications firms. China Telecom Corp. shares dropped 9.4%, China Mobile Ltd. fell 7.2%, closing at their lowest since 2008 and 2006. China Unicom declined 11%.

*Bloomberg noted, "As far back as August, Undersecretary of State Keith Krach wrote a letter warning universities to divest from Chinese firms ahead of possible delistings."*

## Tracking Index Providers

On December 8, 2020, Krach issued a U.S. Department of State fact sheet titled "US Investors Are Funding Malign PRC Companies on Major Indices" listed 13 PRC firms on the Commerce Entity List and 35 parent-level "Communist Chinese military companies" CCMCs and 71 affiliates' on the DOD's List of CCMCs that are included in the MSCI, FTSE and

	MSCI China A Index	MSCI EM Index	MSCI ACWI Index	FTSE Emerging Index	FTSE All World Index
CCMCs and Affiliates Identified	35	59	61	74	76
Deletions Announced to Date	6	10	10	10	10
Percentage Announced to Date	17%	17%	16%	14%	13%

Bloomberg emerging market index funds. Krach emphasized that these Chinese companies are engaging in activities contrary to the national security interests of the US which included supporting PRC military development, human rights abuses and surveillance violations.

*While the recent decisions by index providers to remove several Chinese military companies are welcoming, those firms "are the tip of an iceberg of the 1,000 subsidiary companies," said Under Secretary Krach in his prepared press remarks.*

## Cautioning Financial Institutions



On January 14, 2020, Krach issued a U.S. Department of State fact sheet titled “Communist Chinese Military Companies Listed Under E.O. 13959 Have More Than 1,100 Subsidiaries” expanding the list to 44 parent-level CCMCs 1,108 subsidiaries cross referenced to

MSCI’s and FTSE’s major indexes that are prohibited for US investment and requires divestment. Krach stressed that ample notice have been given to compliance officers and risk managers about disclosing the material risk associated to their constituents. Krach warns CEOs and their boards about their legal duty to be in compliance and take action to minimize any negative effect on their clients’ holdings due to imminent divestment.

*Ample warning has been given to public and private equity compliance officers and risk managers to understand and disclose to their constituents the material risk associated with investments identified in the Executive Order. CEOs and their boards now have a legal duty to implement and be in full compliance with the Executive Order. They also may have a fiduciary duty to take decisive action to minimize any negative effect on their clients’ holdings due to the imminent divestment of CCMCs. Best practices in material risk mitigation, disclosure, and transparency are essential to proper corporate governance.*

## Enlisting the Press

Krach asked the press to shine the light of transparency on the CCP’s efforts as a matter of national security to ensure that the American people are not used as fundraising tools of an authoritarian state hostile to U.S. interests. He asked journalists to tell American investors to



call their fund manager about any CCMC investments in their portfolio to guard against potential losses due to immanent divestment.

*Please tell American citizens who are investors and pension holders that their fund manager should notify you if your investments are contributing to the Chinese Party’s military buildup, the surveillance state, and human rights abuses. If you have not been notified by January 30th, call them. Ask them if you are exposed. If you are exposed, ask them the name of the companies, the amount and when you will be divested. Then ask them why they do not directly and clearly disclose to you. If they do not get a satisfactory answer, best to find a new fund manager.*

## ***Inspiring Civil Society***



On January 18, 2020, Krach sent a letter to all civil society organizations saying that they have always been leaders in exposing the world's inequities and injustices. "It is critical,"

Krach said, "that you remain at the forefront of the shared effort to secure the free world against the CCP's rising authoritarianism and genocide." Linking the various dimensions of authoritarian risks, combining the actions of the social, education, business and government sectors, and uniting under the global Clean Network Alliance of Democracies creates a network effect that has the power to be an exponential force for good in promoting democratic principles over authoritarianism.

*Your organizations have the ability to codify Clean Values into ESG standards that will serve as an example to the world. It is paramount that you partner only with organizations that are not financing the CCP's egregious behavior and genocide."*

## ***Perpetuating Government Policy***

Krach has been a vocal advocate within the U.S. Government for continuity of policy concerning the multiple lists for companies of foreign advisories. At a press conference, he gave the example that only 7 of the 44 companies on the Defense Department's list of Communist Chinese military companies are on the Commerce Department's Entity List. He recommended harmonizing the various agency lists to advance



U.S. national security and address the unprecedented scale of the challenge the country is facing. He asserted that if a company is barred from receiving sensitive technology, then it should not be obtaining U.S. investment either. Krach also argued for better coordination with allies in Korea, Japan, and Europe. He also claimed that issuing licenses for the sake of a company's profits, over national security is short sighted.

*There is important work to be done on continuity of policy in aligning the Defense Department list of CCMCs with the Commerce Department Entity List, and the Military End User list.*