

# Commerce Tightens Huawei Restrictions; Aims to Close Loopholes

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On August 17, 2020, the U.S. Commerce Department's Bureau of Industry and Security (BIS) released two new rules ramping up the export restrictions on Huawei, its affiliates, and other prohibited parties (the public inspection copies are available [here](#) and [here](#)). Both rules are effective immediately and aim to strike a major blow against Huawei—particularly its access to advanced chips. The measures also may cause significant disruptions to consumers, network operators, and chipmakers, among others, and could spur retaliatory action by the Government of China.

Collectively, the rules (1) add 38 additional Huawei companies to BIS's Entity List; (2) remove the Temporary General License (TGL) that formerly allowed certain transactions with Huawei and replace it with a more limited, permanent authorization for security research and disclosure; (3) tighten the loopholes in BIS's special foreign direct product rule applicable to Huawei and its affiliates designated on BIS's Entity List in an effort to cut off Huawei's chip supply; and (4) amend the Entity List generally to make clear that the prohibitions apply when such entities are acting as a purchaser, intermediate consignee, ultimate consignee, or end-user. A brief overview of each of these changes is provided below.

## Background

BIS administers the U.S. Export Administration Regulations (EAR), which are the U.S. export controls on commercial, dual-use, and less sensitive military items. Starting in May 2019, BIS added Huawei and more than 100 of its affiliates to its Entity List. By placing Huawei on the Entity List, BIS prohibited exports, reexports, and transfers of U.S. goods, software, and technology, including common, off-the-shelf

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Export Controls and Economic Sanctions  
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electronic components and commercial software as well as basic, low-level EAR99 technology, to Huawei. The Huawei export ban is far-reaching and also extends to certain foreign-made products that incorporate controlled U.S. content or are direct products of U.S. technology or software.

### **Addition of 38 Huawei Companies to the Entity List**

On August 17, 2020, BIS added an additional 38 affiliates in 21 countries, including several “Cloud” and “OpenLab” affiliates, to its Entity List. As such, effective immediately, exports, reexports, and transfers of U.S. items and certain foreign-produced items that are subject to BIS’s export controls (either because they contain above *de minimis* controlled U.S.-origin content or are subject to the direct product rule described below) to or involving these entities are generally prohibited without BIS authorization.

### **Removal of TGL and Addition of Permanent Authorization for Certain Cybersecurity-Related Transactions**

BIS formerly had authorized limited exceptions to the broad export ban via a TGL. Among other activities, the TGL permitted certain transactions with Huawei that were necessary (1) to maintain and support existing and currently fully operational networks and equipment, and (2) to provide service and support to existing Huawei personal consumer electronic devices (*e.g.*, phones, tablets, smart watches, mobile hotspots, and similar personally-owned equipment) and Customer Premises Equipment (*e.g.*, network switches, residential Internet gateways, set-top boxes, home networking adapters, and other personally-owned equipment that enable consumers to access network communications services and to distribute them within their residence or small business).

The TGL has expired and these authorizations are no longer in place, which could have significant ramifications for network operators around the world. BIS noted that it “never intended all of the provisions of the TGL to be permanent authorizations. Instead, the goal of the TGL was to allow time for companies and persons to shift to other sources of equipment, software, and technology (*i.e.*, those not produced by Huawei or one of its listed affiliates).”

Recognizing the importance of addressing and combating cybersecurity threats, BIS added a permanent authorization in the EAR allowing companies to continue to engage in certain cybersecurity research and vulnerability disclosures involving Huawei, which had also been permitted under the now-expired TGL. This authorization allows parties to disclose to listed Huawei entities information regarding security vulnerabilities in items owned, possessed, or controlled by a listed entity as part of an effort to provide ongoing security research that is critical to maintain the integrity and reliability of existing and currently fully operational networks and equipment. A “fully operational network” means a third party (non-Huawei) network that is providing services to that third party’s customers.

### **Revisions to the Foreign Direct Product Rule**

Certain foreign-manufactured products can be “subject to the EAR” and trigger the Huawei export ban if the foreign-manufactured items are the direct products of U.S. technology or software, or a complete plant or any major component of a plant made from U.S. technology. Historically, the foreign direct product rule has been

limited in scope, requiring that both the U.S. technology or software as well as the final foreign-manufactured products be controlled for “national security” reasons under the EAR, a fairly small subset of products and technology that does not include, for example, smartphones, mass market chipsets, and similar consumer products.

On May 15, 2020, BIS amended its foreign direct product rule in an effort to further limit Huawei’s access to U.S. technology, including from foreign semiconductor manufacturers that rely on U.S. technology or software, such as U.S. Electronic Design Automation software or U.S. production or testing equipment. Nonetheless, the May rule contained certain loopholes that allowed Huawei to continue to benefit from U.S. semiconductor technology and software.

As such, BIS has again revised the rule to impose a license requirement on certain foreign-produced items where Huawei is involved in the transaction, as follows:

- First, in order for the revised foreign direct product rule to apply, the foreign-produced item must meet one of the following requirements:
  - (1) *Direct Product of Specified U.S. Technology or Software*: The foreign-produced item must be a direct product of technology or software subject to the EAR and specified in certain Export Control Classification Numbers (ECCNs) in Categories 3, 4, and 5 in the Commerce Control List (CCL);<sup>1</sup> or
  - (2) *Direct Product of a Plant or Major Component of a Plant*: The foreign-produced item must be produced by a plant or major component of a plant (*i.e.*, equipment involved in any of the production stages, including testing equipment) that is located outside the United States, when the plant or major component of the plant, whether made in the United States or abroad, itself is a direct product of the above-specified Category 3, 4, or 5 U.S.-origin technology or software.
- Second, the person must have “knowledge” (actual knowledge or reason to know) of one of the following circumstances:
  - (1) The foreign-produced item will be incorporated into, or will be used in the production or development of any part, component, or equipment produced, purchased, or ordered by a listed Huawei entity; or
  - (2) A listed Huawei entity is a party to any transaction involving the foreign-produced item, *e.g.*, as a purchaser, intermediate consignee, ultimate consignee, or end-user.

BIS’s modifications are intended to eliminate loopholes that had allowed Huawei to continue to benefit from U.S. technology, including language in the prior iteration of the rule that required that the foreign-produced items be “destined” to Huawei, seemingly allowing chips and other items to be incorporated into Huawei products if such products were transferred directly to the ultimate customer, and language that formerly required production or development by Huawei, which did not necessarily capture multi-party designs. BIS also clarified that a foreign-produced item captured by the controls above can include both finished or unfinished foreign-produced wafers.

With respect to licensing, BIS generally will review licenses involving these foreign-produced items under a presumption of denial, with the exception of items capable of supporting the development or production of telecom systems, equipment, and devices at only below the 5G level, which will be reviewed on a case-by-case basis.

### **Revisions to the Scope of General Entity List Prohibitions**

Consistent with the Huawei-related changes, BIS also revised the EAR such that the Entity List prohibitions for any company apply when that entity is a party to the transaction, *i.e.*, not only as an ultimate consignee or end-user that receives the items, but also as a purchaser or intermediate consignee. BIS described this as a “clarification” because certain Entity List *Federal Register* notices previously included this broad language. However, BIS had previously published guidance permitting companies to use a listed entity as a freight forwarder (*i.e.*, an intermediate consignee), although the agency warned that engaging such an entity required added caution and due diligence to ensure that the items would not be diverted.

Wiley continues to closely monitor Huawei-related developments and the impacts and unintended consequences of the U.S. government’s crackdown on Chinese telecom companies. Should you have any questions, please do not hesitate to contact one of the attorneys listed on this alert.

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<sup>1</sup> The covered ECCNs are 3D001, 3D991, 3E001, 3E002, 3E003, 3E991, 4D001, 4D993, 4D994, 4E001, 4E992, 4E993, 5D001, 5D991, 5E001, and 5E991.