

Commerce Department Further Restricts Huawei Access to U.S. Technology Abroad and Expands Reach of Entity List

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International Trade Controls

On August 17, 2020, the Commerce Department's Bureau of Industry and Security ("BIS") released a [Final Rule](#) (the "August 17 Final Rule") significantly expanding U.S. export controls restrictions on certain non-U.S. items reexported, exported from abroad, or transferred (in-country) in transactions involving Huawei or its affiliates designated on the BIS Entity List (collectively, "Huawei"). Many of the affected items are semiconductor-related. The August 17 Final Rule further modifies [amendments to the Foreign-Produced Direct Product Rule](#) released on May 15, 2020 (the "May 15 Interim Final Rule") in response to public comments and, [according to BIS](#), to "prevent Huawei's attempts to circumvent U.S. export controls to obtain electronic components developed or produced using U.S. technology."

Most significantly, the August 17 Final Rule amends the Foreign-Produced Direct Product Rule under the Export Administration Regulations ("EAR") and Footnote 1 to the Entity List to broaden greatly the universe of items subject to BIS licensing requirements when Huawei is involved in the transaction, including in situations where Huawei did not produce or develop the underlying items. The August 17 Final Rule also designates 38 additional Huawei affiliates on the Entity List; allows the expiration of a prior Temporary General License, replacing it with a permanent, narrower authorization to supply security research to Huawei; and establishes a more permissive licensing policy for less sensitive telecommunications technology.

Also on August 17, BIS released a [separate Final Rule](#) amending the EAR licensing requirements for all parties on the Entity List (not limited to Huawei), clarifying that the relevant licensing requirements also apply when the Entity List-designated party plays a role other than consignee or end-user in a transaction, including as a purchaser or intermediate consignee.

Additional Huawei Export Restrictions

Revisions to Entity List Footnote 1

As explained in our [prior alert](#), the May 15 Interim Final Rule added a "footnote 1" to the Entity List stating that specified items may not be knowingly reexported, exported from abroad, or

transferred (in-country) to “footnote 1”-designated entities without BIS authorization.¹ The only Entity List entries tagged with the “footnote 1” designation are Huawei and each of its Entity List-designated affiliates.

The May 15 Interim Final Rule established two categories of covered items. As modified by the August 17 Final Rule, those two categories of covered items are:

- **Footnote 1(a):** Foreign-produced items that are the “direct product of ‘technology’ or ‘software’ subject to the EAR and specified in” a list of Export Control Classification Numbers (“ECCNs”)² describing a range of software and technology³; and
- **Footnote 1(b):** Foreign-produced items that are “produced by any plant or major component of a plant that is located outside the United States, when the plant or major component of a plant, whether made in the U.S. or a foreign country, itself is a direct product of U.S.-origin ‘technology’ or ‘software’ subject to the EAR” and described in the same list of ECCNs describing semiconductor-related software and technology.⁴
 - A note to this paragraph explains that a “major component of a plant” means “equipment that is essential to the ‘production’ of an item, including testing equipment.”⁵ In the August 17 Final Rule, BIS interpreted “essential” broadly, stating that “any equipment subject to the [ECCNs] specified in [Footnote 1] that is involved in any of the production stages is considered essential.”
 - A second note explains that “[a] foreign-produced item includes any foreign-produced wafer whether finished or unfinished.”⁶

These categories both expand the scope of the May 15 Interim Final Rule. Specifically, footnote 1(a) previously applied only when the items in question also were “produced or developed” by Huawei, and footnote 1(b) previously applied only when the items also were the direct product of technology or software produced or developed by Huawei. These criteria are now being removed, significantly expanding the universe of items subject to the Foreign-Produced Direct Product Rule with respect to Huawei.

In addition to these changes to Entity List Footnote 1, the August 17 Final Rule revises the EAR’s Foreign-Produced Direct Product Rule set forth at General Prohibition Three.⁷ In

¹ See footnote 1 to Supp. No. 4 to EAR Part 744.

² The covered software includes ECCNs 3D001, 3D991, 4D001, 4D993, 4D994, 5D001, and 5D991; and the covered technology includes ECCNs 3E001, 3E002, 3E003, 3E991, 4E001, 4E992, 4E993, 5E001, and 5E991.

³ See footnote 1(a) to Supp. No. 4 to EAR Part 744.

⁴ *Id.* paragraph (b) of footnote 1.

⁵ *Id.* note 1 to paragraph (b) of footnote 1.

⁶ *Id.* note 2 to paragraph (b) of footnote 1.

⁷ See EAR § 736.2(b)(3).

particular, revised General Prohibition Three now specifies that one “may not reexport, export from abroad, or transfer (in-country) without a license or license exception any foreign-produced item controlled under footnote 1” to an Entity List party with “knowledge” that (a) the 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 any entity with a footnote 1 designation”; or (b) a “footnote 1”-designated party, *i.e.*, Huawei, “is a party to any transaction involving the foreign-produced item, *e.g.*, as a ‘purchaser,’ ‘intermediate consignee,’ ‘ultimate consignee,’ or ‘end-user.’”⁸ The expanded list of transactions triggering General Prohibition Three is consistent with a broader change to the Entity List, not specific to Huawei, described further below.

Expanded List of Designated Huawei Affiliates

BIS also designated 38 additional Huawei affiliates on the Entity List and modified the details of several previously designated affiliates. The newly designated affiliates include various “Huawei Cloud” and “Huawei OpenLab” entities and Huawei Technologies R&D UK, an important Huawei research-and-development arm, among others.

Revised Licensing Policy

Although all Huawei affiliates on the Entity List continue to carry a “presumption of denial” licensing policy for all items subject to the EAR, BIS has introduced additional flexibility in the August 17 Final Rule for certain foreign-produced items involving less-advanced telecommunications technology.

Footnote 1 now explains that the “[s]ophistication and capabilities of technology in items is a factor in license application review; license applications for foreign-produced items controlled by this footnote that are capable of supporting the ‘development’ or ‘production’ of telecom systems, equipment and devices at only below the 5G level (*e.g.*, 4G, 3G, etc.) will be reviewed on a case-by-case basis.”⁹

Replacement of Temporary General License

An earlier Huawei-related temporary general license expired on August 13, 2020, and the August 17 Final Rule replaces it with a permanent, but significantly more limited, authorization. Exports to Huawei otherwise restricted by its Entity List designation now are authorized “when the disclosure to [Huawei] is limited to information regarding security vulnerabilities in items owned, possessed, or controlled by [Huawei] when related to the process of providing ongoing security research critical to maintaining the integrity and reliability of existing and currently ‘fully operational network’ and equipment.”¹⁰

⁸ *Id.* § 736.2(b)(3)(vi).

⁹ See note to introductory paragraph of Footnote 1 to Supp. No. 4 to EAR Part 744.

¹⁰ See Footnote 2 to Supp. No. 4 to EAR Part 744 (defining “fully operational network”).

Effective Date and Savings Clause

The August 17 Final Rule is effective immediately. Similar to the Interim Final Rule, the savings clause of the August 17 Final Rule provides two limited safe harbors:

- Items newly subject to footnote 1(a) “that were on dock for loading, on lighter, laden aboard an exporting or transferring carrier, or en route aboard a carrier to a port of export or to the consignee/end-user, on [August 17], pursuant to actual orders for exports, reexports, and transfers (in-country) to a foreign destination or to the consignee/end-user,” may proceed as not subject to the EAR, or under the previous license or license exception; and
- Items newly subject to footnote 1(b) that started “production” prior to August 17 may proceed as not subject to the EAR, or under the previous license or license exception “so long as they have been exported, reexported, or transferred (in-country) on or before September 14, 2020.”

Items in either category not meeting these safe harbor criteria require specific licensing from BIS.

Revised Licensing Requirements for All Entity List Parties

Also on August 17, 2020, BIS issued a [separate Final Rule](#) clarifying the licensing requirements for all Entity List-designated parties. These amendments apply to all such parties and are not limited to Huawei.

EAR Section 744.11(a) now clarifies that BIS licensing is required for parties designated on the Entity List regardless of their role in a transaction, *i.e.*, whether they play the role of purchaser, intermediate consignee, ultimate consignee, or end-user, as those terms are defined in the EAR.¹¹ This amendment adds “intermediate consignees” and “purchasers” to the list of roles for which an Entity List-designated party would require licensing, consistent with the treatment of parties designated on the separate BIS “Unverified List.”

Impact of the Rule Changes

The latest amendments to the Foreign-Produced Direct Product Rule continue to demonstrate the Trump Administration’s focus on restricting Huawei’s access to U.S. semiconductor technology. The expanded “footnote 1” coverage in the August 17 Final Rule reflects a conclusion that the earlier May 2020 amendments were insufficiently restrictive to achieve the Administration’s goals.

Given the prevalence of U.S. technology and software in semiconductor design and manufacturing equipment, the expanded scope of “footnote 1” will impose licensing requirements on a very broad range of non-U.S.-made semiconductor items when destined for

¹¹ See EAR § 744.11(a). The Final Rule also makes conforming changes to Section 744.11(a), and to Section 744.16(a).

Huawei. At the same time, the introduction of a more flexible licensing policy for supplying pre-5G telecommunications items to Huawei presents some opportunity to seek BIS authorization for less sensitive exports.

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Covington has deep experience advising clients on the legal, policy, and practical dimensions of U.S. export controls. We will continue to monitor developments in this area, and we are well positioned to assist clients in understanding how these developments may affect their business operations.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our International Trade Controls practice group:

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