

# Commerce Department Adds 77 Companies and Individuals to the Entity List, Many in China, and Issues Huawei FAQs

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International Trade Controls

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On December 18, the U.S. Department of Commerce's Bureau of Industry and Security ("BIS") released a [Final Rule](#) ("the Rule"), effective immediately, adding 77 entities to the BIS Entity List. The majority of these entities are in China, and include, among others, the Semiconductor Manufacturing International Corporation ("SMIC") and the drone company SZ DJI Technology Co., Ltd. ("DJI"). The new additions also include entities in Bulgaria, France, Germany, Hong Kong, Italy, Malta, Pakistan, Russia, and the United Arab Emirates.

Exports, reexports, and transfers (in-country) of any items subject to the Export Administration Regulations ("EAR") to the listed entities, or when a listed entity is otherwise a party to the transaction, now require prior BIS licensing, even for non-sensitive EAR99 items (e.g., ordinary commercial products). Items subject to the EAR include commodities, software, and technology originating in or exported from the United States, as well as certain non-U.S.-origin items that contain controlled U.S.-origin content or are the direct products of sensitive U.S. technology or software. Subject to a few exceptions below, BIS has instituted a policy of a presumption of denial of export license applications for most items to the listed entities.

The designations were effective December 18, 2020 and will be published in the Federal Register on December 22, 2020.

The large tranche of designations of Chinese entities is the latest in a series of measures the Trump Administration has directed at China, including measures that have been imposed since the November 3, 2020 U.S. election and have been aimed at the military-civil fusion in China. Other recent actions include, for instance, President Trump's November 12 Executive Order prohibiting U.S. persons from engaging in any transaction in publicly traded securities, or any securities that are derivative of, or are designed to provide investment exposure to such securities, of "Communist Chinese military companies." (See our recent alert [here](#).) This Rule also continues the Trump Administration's focus on human rights in China, this time with particular emphasis on the collection of genetic material and high-technology surveillance.

Also on December 18, BIS posted [new Frequently Asked Questions \("FAQs"\)](#) related to BIS's prior designation on the Entity List of Huawei Technologies Co., Ltd. and many of its non-U.S. affiliates (collectively, "Huawei"). The publication of the FAQs had been long awaited, as they

address questions related to the August 2020 expansion of the EAR's foreign-produced direct product rule to cover a broader range of items exported, reexported, or transferred to Huawei.

### **Basis for Entity List Designations**

The Entity List, maintained as Supplement No. 4 to Part 744 of the EAR, identifies legal and natural persons believed to be involved, or to pose a significant risk of being or becoming involved, in activities contrary to the national security or foreign policy interests of the United States. BIS explains in the Rule that it has reasonable cause to believe that the listed entities have been or may become involved in such activities.

#### China and Hong Kong Designations

The majority of entities added to the Entity List in the Rule are located in China. The specific reasons cited by BIS for designation to the Entity List vary.

SMIC and ten related entities were designated because of "China's military-civil fusion (MCF) doctrine and evidence of activities between SMIC and entities of concern in the Chinese military industrial complex." One of these related entities is Hong Kong-based.

Four Chinese entities (AGCU ScienTech Inc. ("AGCU ScienTech"); China National Scientific Instruments & Materials Co., Ltd. ("CNSIM"); DJI; and Kuang-Chi Group) were designated for the "abusive genetic collection" from and "high-technology surveillance" of individuals within China, as well as the "export of items...that aid repressive regimes around the world."

China Communications Construction Company Ltd. and four other companies were designated for reasons related to "China's efforts to assert its unlawful maritime claims" and "to reclaim and militarize disputed outposts in the South China Sea."

A significant part of the designations were 25 research academies, institutes, and a test center associated with the China State Shipbuilding Corporation Ltd., as well as the Beijing Institute of Technology and four other Chinese entities "for acquiring and attempting to acquire U.S.-origin items in support of programs for the People's Liberation Army." The Beijing University of Posts and Telecommunications was also added to the Entity List for its "research and development, and production, of advanced weapons and advanced weapons systems in support of People's Liberation Army modernization."

Finally, the interagency End-User Review Committee responsible for reviewing the evidence that led to the designations also added one entity, Tongfang NucTech Technology Ltd., for reasons related to nonproliferation—namely, that it produced "lower performing equipment" that impaired U.S. efforts to counter illicit international trafficking in nuclear and other radioactive materials, including efforts that are part of cargo screening—and two entities and five individuals for reasons related to the "theft of trade secrets from U.S. corporations."

#### Non-China Designations

In addition to the Chinese entities listed above, entities in several other countries also were added to the Entity List for, among other reasons, providing aircraft parts without the necessary licenses to Mahan Air, an entity on the List of Specially Designated Nationals and Blocked Persons maintained by the Treasury Department's Office of Foreign Assets Control. Several entities also were designated, according to BIS, for seeking to evade license requirements and divert U.S.-origin items to unauthorized recipients.

## Impact of Entity Listing Designations

These Entity List designations mandate BIS licensing for all exports, reexports, and transfers (in-country) of any item subject to the EAR to the listed entities, or if a listed entity is otherwise a purchaser, intermediate consignee, ultimate consignee, or end user to the transaction. Moreover, license exceptions otherwise available under the EAR are suspended with respect to the listed entities, and BIS has instituted a license review policy of a presumption of denial for export license applications for all items, subject to a few exceptions for certain entities detailed below.

All commodities, software, and technology that are subject to U.S. jurisdiction under the EAR—including common EAR99 items not identified on the EAR's Commerce Control List—require licensing prior to their supply by any person, including by non-U.S. persons, to any of the listed entities as a result of the designations. Items “subject to the EAR” include all items located in or exported from the United States, and all items produced in the United States, wherever located. Furthermore, non-U.S.-made items that contain more than *de minimis* amounts of controlled U.S.-origin content also are subject to the EAR. Non-U.S.-made items destined for China, including destined to the listed entities, require BIS licensing if their value is made up of more than 25% controlled U.S.-origin content, where that content is itself subject to BIS licensing requirements for export to or reexport to China.<sup>1</sup>

Finally, certain non-U.S.-produced items that meet the narrow conditions to constitute “direct products” of certain types of sensitive U.S. software or technology also are subject to the EAR, even if those non-U.S. items were produced and are located abroad and contain no or less than *de minimis* controlled U.S.-origin content. Additionally, items produced at a non-U.S. manufacturing plant or by a major manufacturing plant component can be subject to the EAR if the plant or plant component was a product of certain sensitive U.S. software or technology.<sup>2</sup>

The Entity List designations apply only to the listed entities (including branches and operating divisions) and their representatives, because Entity List designations do not automatically extend to non-listed subsidiaries or separately incorporated affiliates of listed persons. However, when dealing with a non-listed subsidiary or affiliate of a listed entity, under longstanding BIS guidance, companies should exercise heightened caution to ensure that the party with which they are dealing is in fact separately incorporated (and not part of the listed entity), that it is not

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<sup>1</sup> Notwithstanding this general 25% *de minimis* threshold, non U.S.-made items are “subject to the EAR” if they contain any amount of certain types of U.S. content. Such content includes, for example, U.S.-origin components classified under a “600 series” or “9x515” Export Control Classification Number (“ECCN”), when destined for countries subject to U.S. arms embargos, such as China. There similarly are no *de minimis* levels for any non-U.S.-origin encryption technology that incorporates U.S.-origin encryption controlled under ECCN 5E002.

<sup>2</sup> A broader version of this foreign-produced direct product rule applies to exports, reexports, and transfers to Huawei, as discussed below. BIS has not applied that broader foreign-produced direct product rule to exports, reexports, and transfers to these newly listed entities or to other entities on the Entity List, besides Huawei.

a front or shell company for the listed entity, and that it will not otherwise divert items subject to the EAR to a listed entity.

The Rule contains a limited savings clause allowing items that were en route aboard a carrier to a port of export or reexport as of the date of publication of the Rule in the Federal Register, pursuant to actual orders for export or reexport to a foreign destination, to proceed to that destination under a license exception or without a license if they would have been so eligible prior to the effective date of the Rule.

### License Review Policy – Exceptions

BIS has imposed a license review policy of a presumption of denial for certain items going to SMIC and the ten related entities. The policy applies to items “uniquely required for production of semiconductors at advanced technology nodes (10 nanometers and below, including extreme ultraviolet technology).” The review policy is case-by-case for all other items to SMIC and related entities.

With regards to AGCU ScienTech, CNSIM, DJI, and Kuang-Chi Group, BIS has imposed a license review policy of a presumption of denial for most items, but case-by-case review for applications to export, reexport, or transfer to these entities “items necessary to detect, identify and treat infectious disease.”

BIS has imposed the license review policy set forth in 15 C.F.R. § 744.2(d) for two entities in Pakistan: Geo Research and Link Lines (Pvt.) Limited. Section 744.2(d) sets out a non-exclusive list of nine wide-ranging factors that guide the U.S. government in its review of these license applications. These factors are intended to assess nuclear proliferation concerns, and include factors such as the appropriateness of the commodities, software, or technologies to the stated end use and whether the stated end use is appropriate to the end user.

### **Entity List Revisions**

As part of the new Rule, BIS also revised the Entity List to update the aliases and addresses for two entities: China Shipbuilding Group 722nd Research Institute and Oriental Engineers Pvt. Ltd. Finally, BIS removed several entities from the list: Ben Gurion University (Israel) and Dow Technology Co. LLC, Hassan Dow, and Modest Marketing LLC (United Arab Emirates).

### **Huawei-Related FAQs**

The new FAQs provide significant clarifications regarding BIS’s interpretation of the [August 2020 Foreign-Produced Direct Product Rule](#) (“FDP Rule”) (summarized in our previous [client alert](#)), which expanded the scope of EAR jurisdiction over foreign-produced items that are exported, reexported or transferred with “knowledge” that 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 Huawei, or where Huawei is a party to any transaction involving the foreign-produced item. The FAQs were long awaited, given the complexity of the FDP Rule, and BIS advised in releasing the FAQs that they are “subject to amendment” and exporters should “check back frequently for updates.”

Some of the more significant clarifications in the FAQs are as follows:

- *FAQ 9* confirms that the FDP Rule generally does not require a license for the servicing or repair of an item lawfully exported prior to the August 2020 FDP Rule, although other

provisions of the EAR may apply and replacement parts that are subject to the FDP Rule that are for Huawei equipment may require licensing.

- *FAQ 12* states that “incorporation of a part that is subject to the EAR pursuant to the FDP rule does not necessarily make the larger foreign product subject to the EAR.” This guidance suggests that BIS does not consider that mere incorporation of a part subject to the FDP rule (if it were sent directly to Huawei) automatically makes an end-item subject to the FDP Rule (e.g., the end item is not considered to have been “produced by” the equipment that produced the part, under Footnote 1(b) of the FDP Rule). However, the export, reexport, or transfer of such a part that is an FDP to another party with “knowledge” that the part is to be incorporated into a part, component, or equipment for Huawei still requires licensing. *FAQ 7* provides an example of this, explaining that a wafer that is subject to the FDP Rule requires licensing when exported abroad to a finished integrated circuit manufacturer with “knowledge” that the integrated circuit or higher-level assembly containing the integrated circuit (and wafer) is for Huawei. See *also* *FAQ 13.a*.
- *FAQ 20* states that where a distributor has a license to provide products to a listed Huawei entity, a company supplying products to the distributor does not need to get a separate license. This and other guidance, such as *FAQ 16*, appear relevant in analogous situations, e.g. where a company is supplying components to a downstream manufacturer which has a license to supply the end-item to a listed Huawei entity, then the supplier and the downstream manufacturer do not both need to obtain licensing.
- *FAQ 24* confirms that if U.S. software is used in the product engineering stage of producing a cellphone, “[t]he direct product would be whatever the software produces. In most cases the direct product of the U.S. software would be the product design, which may be subject to paragraph (a) of the FDP Rule.” This guidance may be relevant in analogous situations where U.S. technology, software, or hardware is used to produce an item at an early stage of the engineering or production process. However, it also would be important to take into account *FAQ 14*, which states that when integrated circuits are designed in the United States, the integrated circuits themselves are subject to paragraph (a) of the FDP Rule.

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We are well-positioned to advise on the export controls issues related to these latest actions, and more broadly on the trade controls and human rights dimensions of doing business in China and internationally. If you have any questions concerning the material discussed in this client alert, please contact the following members of our International Trade Controls practice:

<b><u>Stephen Bartenstein</u></b>	+1 202 662 5471	<a href="mailto:sbartenstein@cov.com">sbartenstein@cov.com</a>
<b><u>Eric Carlson</u></b>	+1 202 662 5253	<a href="mailto:ecarlson@cov.com">ecarlson@cov.com</a>
<b><u>Dan Feldman</u></b>	+1 202 662 5494	<a href="mailto:dfeldman@cov.com">dfeldman@cov.com</a>
<b><u>Peter Flanagan</u></b>	+1 202 662 5163	<a href="mailto:pflanagan@cov.com">pflanagan@cov.com</a>
<b><u>Corinne Goldstein</u></b>	+1 202 662 5534	<a href="mailto:cgoldstein@cov.com">cgoldstein@cov.com</a>
<b><u>Alan Larson</u></b>	+1 202 662 5756	<a href="mailto:alarson@cov.com">alarson@cov.com</a>
<b><u>Peter Lichtenbaum</u></b>	+1 202 662 5557	<a href="mailto:plichtenbaum@cov.com">plichtenbaum@cov.com</a>
<b><u>Lisa Peets</u></b>	+44 20 7067 2031	<a href="mailto:lpeets@cov.com">lpeets@cov.com</a>
<b><u>Stephen Rademaker</u></b>	+1 202 662 5140	<a href="mailto:srademaker@cov.com">srademaker@cov.com</a>
<b><u>Eric Sandberg-Zakian</u></b>	+1 202 662 5603	<a href="mailto:esandbergzakian@cov.com">esandbergzakian@cov.com</a>
<b><u>Kimberly Strosnider</u></b>	+1 202 662 5816	<a href="mailto:kstrosnider@cov.com">kstrosnider@cov.com</a>
<b><u>David Addis</u></b>	+1 202 662 5182	<a href="mailto:daddis@cov.com">daddis@cov.com</a>
<b><u>David Lorello</u></b>	+44 20 7067 2012	<a href="mailto:dlorello@cov.com">dlorello@cov.com</a>
<b><u>Alden Fletcher</u></b>	+1 202 662 5212	<a href="mailto:afletcher@cov.com">afletcher@cov.com</a>

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