

U.S. Department of Commerce announces expansion of foreign direct product rule restricting Huawei's access to certain foreign-produced items

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On 15 May 2020 the U.S. Department of Commerce announced an [Interim Final Rule](#) that would expand the scope of the foreign direct product rule set forth in General Prohibition Three's (GP 3), further restricting transfers to China's Huawei Technologies Co. Ltd. and its affiliates (collectively, Huawei) that have been designated on the Commerce Department, Bureau of Industry and Security's (BIS) Entity List. According to BIS, the purpose of the rule is to protect U.S. national security by extending U.S. export controls jurisdiction to certain non-U.S. items when destined for Huawei. The expansion is intended to counter Huawei's efforts to undermine U.S. export controls by restricting the use of U.S. technology and software to design and manufacture semiconductors abroad for Huawei. In its [press release](#), the Commerce Department made clear that these new restrictions are aimed primarily at HiSilicon, Huawei's chip design arm. HiSilicon relies on foundries located outside of mainland China to produce certain high-end five nanometer (nm) and seven nm chips, which are used in mobile phones and 5G base stations.

BIS is amending the longstanding foreign direct product rule in GP 3 and the Entity List in the Export Administration Regulations (EAR) to target Huawei's acquisition of foreign-produced items, including semiconductors, that are the direct product of certain U.S. software and technology. Under this new rule, the prior foreign direct product rule has been significantly expanded to cover new transactions involving foreign-produced items that were previously not controlled to Huawei. Specifically, the rule restricts the knowing reexport, export, or transfer (in-country) to certain listed Huawei entities of:

1. Foreign-produced items produced or developed by Huawei that are the "direct product" of specified EAR-controlled software or technology.
2. Foreign-produced items that are both:
 - a) Produced using certain equipment that is the "direct product" of specified U.S.-origin software or technology.
 - b) The "direct product" of software or technology produced or developed by Huawei.

Also on 15 May the Commerce Department announced a [Final Rule](#) extending Huawei's Temporary General License (TGL) through 13 August 2020. The TGL permits certain activities, including those necessary for the continued operation of existing networks and equipment as well as the support of existing mobile services, including cybersecurity research critical to maintaining the integrity and reliability of existing and fully operational networks and equipment. In the accompanying [press release](#), the Commerce Department noted that it expected this to be the final extension of the TGL.

The rule significantly expands export controls on Huawei

Since 16 May 2019 when Huawei was added to the BIS Entity List (with other Huawei affiliates subsequently added on 19 August 2019), the export, reexport, or transfer (in-country) to Huawei of items subject to U.S. export controls has required a license from BIS, including U.S.-origin items and foreign-produced items with a certain amount of controlled U.S.-origin content. Under the initial Entity List designation, Huawei could still receive foreign-produced items that were not subject to the EAR, including items manufactured outside the United States using U.S. technology or equipment (unless such technology or equipment was highly controlled for national security reasons). These new rules are intended to close what the U.S. government views as a gap regarding Huawei's access to items made outside the United States with certain specified U.S.-origin technology or software (e.g., chip designs fabricated at non-U.S. foundries that rely on U.S. technology or software in their production equipment, techniques, and processes). These restrictions are unique to Huawei for now, but could be expanded to include additional companies in the future.

In particular, BIS has imposed additional licensing requirements on two categories of foreign-produced items where one knows or has reason to know that the items will be exported, reexported, or transferred (in country) to Huawei entities listed on the Entity List.

Restrictions on items produced by Huawei that are the direct product of certain technology or software

Foreign-produced items produced or developed by Huawei that are the direct product of technology or software subject to the EAR that is controlled under Export Control Classification Numbers (ECCNs) specified in the rule. For example, if Huawei develops an integrated circuit design using technology or software, such as Electronic Design Automation software, that is controlled under one of the specified ECCNs, that integrated circuit design also becomes subject to the EAR and requires an export license if destined to another listed Huawei entity.

In this example, the foreign-produced item is the integrated circuit design developed by Huawei. While the input technology or software used by Huawei in the development process, such as the Electronic Design Automation software, must be subject to the EAR and covered by one of the specific ECCNs set forth in the rule, the resulting integrated circuit design is subject to the EAR and requires a license for transfer to another listed Huawei entity regardless of the classification of the integrated circuit design.

Restrictions on third party production of items based on Huawei designs or technology

Foreign-produced items that are both: 1) produced by a plant (or major component of a plant) outside the United States, where that plant (or major component of a plant) is a direct product of U.S.-origin technology or software that is controlled under one of the specified ECCNs and 2) direct products of software or technology produced or developed by Huawei.

For example, if Huawei sends a chip design to a manufacturer for fabrication (regardless of whether that chip design was made using EAR software or not), and the manufacturer fabricates that chip in a plant outside the United States using equipment that is the direct product of U.S.-origin technology or software controlled under one of the specified ECCNs (e.g., U.S. equipment

developed using certain U.S. technology or software), the finished chip is subject to the EAR and requires an export license if destined to a listed Huawei entity.

Another example is if Huawei sends a chip design to a manufacturer for fabrication, *and* the manufacturer fabricates that chip in a plant outside the United States using a plant design based on ECCN 3E002 technology from the United States, the finished chip is subject to the EAR and requires an export license if destined to a listed Huawei entity.

The expansion applies to activities involving certain specified technology and software

The relevant ECCNs for purposes of this rule (as described above) are set forth in Categories 3, 4, and 5 of the Commerce Control List (CCL) and include items subject to national security (NS) and/or anti-terrorism (AT) controls:

- Technology or software controlled under ECCNs 3E001, 3E002, 3E003, 4E001, 5E001, 3D001, 4D001, or 5D001 (subject to NS and AT controls).
- Technology controlled under ECCNs 3E991, 4E992, 4E993, or 5E991 (subject to AT controls only).
- Software controlled under ECCNs 3D991, 4D993, 4D994, or 5D991 (subject to AT controls only).

The rule includes a savings clause for certain items already in transit or production

Although the Interim Final Rule is effective immediately, the rule includes a savings clause for certain items already in transit or in production. The savings clause applies differently depending on whether the items are produced by Huawei itself or by third parties using a Huawei design.

- Items produced by Huawei itself may only proceed without a license or in reliance upon prior license exception eligibility if, on 15 May 2020, they were already 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, pursuant to actual orders for exports, reexports, and transfers (in-country) to a foreign destination or to the consignee/end-user.
- Items produced in a non-U.S. plant using a Huawei design, provided that production started prior to 15 May 2020, are not subject to the EAR and therefore may be exported, reexported, or transferred (in-country) within 120 days of the effective date of the rule (i.e., before midnight on 14 September 2020).

Next steps

As both rules are effective immediately, U.S. exporters should be prepared to comply with the expansion of the foreign direct product rule and extension of the Entity List as of 15 May 2020. Any comments on this Interim Final Rule should be addressed to BIS by 14 July 2020.

BIS has also advised that it does not intend to renew Huawei's TGL after its next expiration on 13 August 2020. Therefore, any U.S. firms that have business arrangements with Huawei or are users of Huawei equipment should review their compliance obligations in light of these changes.

For further information or assistance, please contact any of the Hogan Lovells lawyers identified below.

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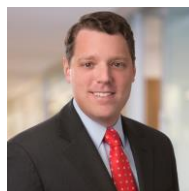
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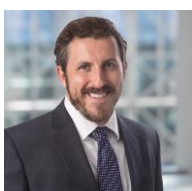
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