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BIS Introduces Significant Restrictions on Huawei

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May 25, 2020 — On May 19, 2020, the U.S. Department of Commerce, Bureau of Industry and Security ("BIS"), published an amendment to the Export Administration Regulations ("EAR") that will significantly restrict Huawei's ability to use U.S. technology and software to design and manufacture its semiconductors abroad. Before the change, foreign manufacturers could use U.S.-controlled equipment and technology to make and sell most products without being subject to U.S. export controls. The new rule expands the EAR's foreign-produced direct product rule so that certain categories of products (including semiconductors and chipsets) that are a direct product of certain U.S. technology or software (or that are made using equipment that is a direct product of that same technology or software) will require a license to be exported, re-exported, or transferred to Huawei or its many non-U.S. affiliates. Although structured as an interim final rule that became effective on May 15, 2020, BIS is accepting industry comments through July 14, 2020.

This rule amends General Prohibition Three, also known as the foreign-produced direct product rule. Generally speaking, that rule makes certain items produced outside of the United States subject to U.S. export controls under the EAR, for export to a specified list of countries, if those items are the direct product of, or are the direct product of a plant or plant component made from, certain national security controlled U.S.-origin technology or software. While the new rule largely leaves the scope of the existing foreign-produced direct product rule unchanged, it adds a further restriction for certain parties on the Entity List maintained by BIS. (The Entity List identifies persons reasonably 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.)

Specifically, the new rule marks certain parties on the Entity List with a "footnote 1" designation; only Huawei and its non-U.S. affiliates have a footnote 1 designation under the new rule. Footnote 1 provides that non-U.S. persons may not export, re-export, or transfer certain items to a party with a footnote 1 designation without a license if those items (1) are the direct product of, or are produced by a plant or major component of a plant made from certain U.S. origin technology and software classified under Categories 3 (electronics), 4 (computers), or 5 (telecommunications) of the Commerce Control List; (2) the items are produced or developed by an footnote 1 party (i.e., Huawei); and (3) the non-U.S. person has knowledge that item is destined for a footnote 1 entity (i.e., Huawei).

The categories of products captured under the rule most notably include semiconductors and chips controlled under Category 3. Although there were initial concerns that the Trump Administration's move could cause broad disruptions to the global semiconductor industry (including U.S. companies), the actual rule appears to be narrower. In particular, the rule appears to only be triggered when an item is produced or developed by Huawei or one of its affiliates using the specified U.S.-origin technology or software and the exporter has knowledge that the item is destined for Huawei or one of its affiliates.

The most significant impact of the rule is likely to be on Huawei's chip division, known as HiSilicon, which is also a footnote 1 party on the Entity List along with its various affiliated companies. The effect of the rule is likely to deny HiSilicon access to two critical aspects of its chip production: (1) chip design software (the leading brands of which originate from the U.S.) and (2) access to foundries that manufacture semiconductors, the most advanced of which use U.S. equipment.

The success of Huawei and HiSilicon is key to China's plan to modernize its economy from a manufacturing-dependent model to one focused on advanced technologies – known as the Made In China 2025 plan. However, amid concerns that Huawei's advancement using U.S. technology could benefit the People's Liberation Army under China's policy of civil-military fusion, Huawei has increasingly been under fire from U.S. regulators. For example, in May 2019, BIS added Huawei and its affiliates to its Entity List, which required a license before items subject to the EAR could be transferred to the company or its affiliates. The new rule is largely a response to Huawei's efforts to circumvent those restrictions by having foundries – such as Taiwan Semiconductor Manufacturing Co. – manufacture its chips a small enough proportion of U.S. origin content to fit within the existing de minimis exception, so that the resulting products would not be subject to the EAR and could be transferred to Huawei without a license from BIS. By expanding the foreign-produced direct product rule, chips manufactured for Huawei using U.S. technology or software (or equipment made using U.S. technology or software) are now subject to the EAR, regardless of the amount of U.S.-origin content actually used in the chip.

Although the rule became effective on May 15, 2020, BIS is accepting comments through July 14, 2020. Companies that may be affected by the rule, especially in ways unintended by BIS, should therefore consider submitting feedback. Such comments could help shape and tailor a future, final version of the rule.

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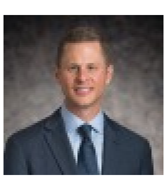

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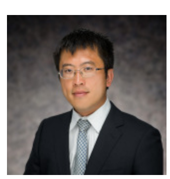

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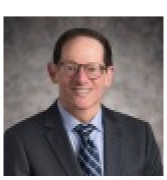

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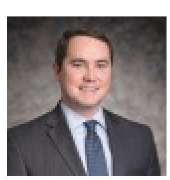

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