



International Trade & Regulatory ADVISORY ■

MAY 20, 2020

Commerce Imposes New Export Control Restrictions on Huawei

On Friday, May 15, 2020, the U.S. Department of Commerce Bureau of Industry and Security (BIS) [issued new](#) sweeping export control rules aimed at limiting Huawei Technologies Co. Ltd. and its non-U.S. affiliates access to chips, chip designs, and other semiconductor-related items made with U.S.-origin software or technology, or made on U.S. or foreign-origin equipment designed from specified U.S.-origin software or technology. The move aims to further limit Huawei's access to the global supply of semiconductors and may impact foundries, integrated circuit (IC) design houses, and other chipset suppliers of Huawei around the globe. This action, amending the foreign-produced direct product rule, comes on the one-year anniversary of BIS designating Huawei and over 100 of its affiliates and subsidiaries on the Entity List and is effective immediately, though BIS will receive comments on the rule until July 14, 2020.

In a [press release](#), Commerce Secretary Wilbur Ross stated that “[d]espite the Entity List actions the Department took last year, Huawei and its foreign affiliates have stepped-up efforts to undermine these national security-based restrictions through an indigenization effort. However, that effort is still dependent on U.S. technologies.... We must amend our rules exploited by Huawei and HiSilicon and prevent U.S. technologies from enabling malign activities contrary to U.S. national security and foreign policy interests.”

Commerce also issued a 90-day extension of the temporary general license extending the expiration date from May 15, 2020 to August 13, 2020. However, Commerce [signaled](#) that this may be the final extension, stating that “companies and persons should be prepared to submit license applications to the Department to determine which, if any, activities will be authorized in the event that their TGL authorization is eliminated.”

What Is the Direct Product Rule and What Is Changing?

The Export Administration Regulations (EAR) extend U.S. jurisdiction over foreign-made items that exceed de minimis threshold levels of controlled U.S. content along with certain foreign-made items that are the *direct product* of certain U.S. technology or software.

General Prohibition Three of the EAR, 15 C.F.R. § 736.2(b)(3), establishes certain restrictions on the “reexport and export from abroad of the foreign-produced direct product of U.S. technology and software.” The term “‘direct product’ means the immediate product (including processes and services) produced directly by the use of technology or software.” Simply put, if, for example, a supplier in the United Kingdom uses a U.S.-origin specification or blueprint

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design to produce an IC, that IC *could* be the immediate product of the U.S.-origin technology and be subject to U.S. export controls.

Items subject to this prohibition, depending on the level of export control, may require a license or license exception from BIS to be exported, reexported, or transferred (in-country) . Historically, this prohibition has only applied to foreign-produced items that are subject to national security (NS) controls as designated by the applicable export control classification number (ECCN) of the Commerce Control List. In other words, if the foreign-made item was the direct product of technology or software and the technology or software as well as the foreign made item were not controlled for NS reasons, the item was not subject to the EAR and therefore could be exported, reexported, or transferred without regard to U.S. export controls.

BIS expansion of the direct product rule

Going forward, items that are the direct product of U.S. technology or software controlled for NS reasons, *and items that are the direct products of specified ECCNs, when destined to designated entities*, will be subject to the new foreign-produced direct product rule if there is “knowledge” that the item is destined to a listed entity. The specified ECCNs in this rule are:

CCL Product Groups	ECCNS
Category 3 – Electronics	3E001, 3E002, 3E003, 3E991, 3D001, 3D991
Category 4 – Computers	4E001, 4E992, 4E993, 4D001, 4D993, 4D994
Category 5 – Telecommunications	5E001, 5E991, 5D001, 5D991

This control will be listed in a new provision in Section 736.2(b)(3)(vi). Notably, the architecture of this new rule seems designed to allow BIS to simply use *footnotes* to impose unilateral controls by merely designating any technology or software ECCN deemed to be of concern. Entities on the Entity List with such footnote designations will be subject to the new (b)(3)(vi) provision.

Global Supply Chain Impacts

Foreign-made items that are direct products of technology or software

This new control impacts both Huawei and its suppliers. If a chipmaker or other supplier of an item has *knowledge* that the item is destined to a Huawei entity on the Entity List *and* the item is “produced or developed by any entity with a footnote 1 designation” *and* is the “direct product” of technology or software controlled by a specified ECCN, a license from BIS will now be required to transfer (in-country), export, or reexport that item. The rule appears at least partly targeted toward shipments between Huawei entities because it focuses on items produced by listed entities that are also destined for listed entities.

Again, the rule does not appear to cover all foreign-made items that are the direct product of the specified technology and software. Rather, only foreign-made items “produced or developed by” and destined to Huawei and its listed affiliates may be controlled. BIS does not define “produced or developed” anywhere within this new rule, an omission that may call for clarification or guidance. In the absence of such guidance, parties may consider looking to Part 772 of the EAR, which defines “production,” at least for purposes of the General Technology Note, as “all production stages, such as: product engineering, manufacture, integration, assembly (mounting), inspection, testing, quality assurance.” “Development,” at least for purposes of the General Technology Note, is defined as “related to all stages

prior to serial production, such as: design, design research, design analyses, design concepts, assembly and testing of prototypes, pilot production schemes, design data, process of transforming design data into a product, configuration design, integration design, layouts.”

Production Activities – Within this framework, “produced by” an entity seems somewhat susceptible to interpretation by mortals. For example, if HiSilicon engineers, integrates, or assembles, or potentially even if it inspects, tests, or engages in quality assurance on a chipset, *and* if the chipset is the immediate and direct product of U.S.-origin 3E001 technology or of other U.S. origin software or technology classified in the specified ECCNs, *and* the chipset is known to be destined for another listed entity, then the chipset would be subject to the EAR and restricted from transfer to the other listed entities even though they are affiliates of HiSilicon.

Development Activities – In the development context, for example, if an IC (1) is designed or its prototypes assembled and tested, or its integration or layout designed or analyzed, or pilot production schemes are arranged by HiSilicon or other listed Huawei affiliates; (2) is the immediate and direct product of U.S.-origin 3E001 technology or of other U.S.-origin software or technology classified in the specified ECCNs; and (3) it is destined for another listed entity, then that IC would be subject to the EAR and restricted from transfer. This restriction could apply when the IC is actually put into production by non-Huawei entities or fabs based on the development by listed entities using the listed U.S.-origin software or technology.

Commercial-off-the-shelf items developed without any requirements or influence or development by any listed Huawei entity, even if derived in part from the specified U.S.-origin technology or software, appear to be outside the scope of this new rule. Companies that have developed or are developing products outside the U.S. based on their own design or specifications are encouraged to ensure that the development history of that product is fully documented to prevent downstream restrictions.

Secretary Ross’s concern about indigenization of IC and related technology development by listed entities notwithstanding, the new rule could potentially have the effect of spurring a renaissance of independent, non-listed entity development and production of items that will not be subject to the EAR under this rule. Moreover, the new rule necessitates an increasing focus on what exactly it means to be the immediate product produced directly by the use of certain technology or software. The words “immediate” and “direct” must at least mean that tangential use of a particular software or technical information in the course of making or, say, testing an item, would not make that item the “direct product” of the technology or software.

Foreign-made items that are direct products of a plant or major component of a plant

The new control also captures any item produced outside the U.S. by any plant or major component of a plant if the plant or major component of the plant is a direct product of the specified U.S.-origin technology or software and the foreign-made item is the direct product of software or technology produced or developed by a listed entity. A “major component” of a plant means that the equipment *is essential to the production* of an item to meet the specification of any design produced or developed by designated entities, including testing equipment.

Thus, the new rule appears to control foreign-made items manufactured on U.S.-origin equipment – or foreign-produced equipment that itself is a direct product of the specified U.S.-origin technology or software – even if the design of the foreign-made end item is not U.S.-origin. As an example: a foundry manufactures an IC based on a Huawei specification (no U.S.-origin technology); that IC is now subject to the EAR if it is manufactured on certain U.S.-origin equipment *or* on foreign-made equipment that is the direct product of certain U.S.-origin technology or software.

Suppliers in this industry now need to consider the pedigree of major plant components (i.e., equipment) used during the manufacturing, testing, and qualification process and whether they are the direct product of the specified U.S. software or technology. It may prove to be very difficult to ascertain the classification and origin of the technology or software used to develop and manufacture, for example, plasma etching machinery, especially if that equipment was originally sourced from outside the U.S. While there might not be a prohibition on exporting or transferring such equipment itself (if destined to a non-Huawei entity), there is now a prohibition on exporting, reexporting, or transferring items made on such equipment, if those items are themselves the direct product of software or technology produced or developed by a listed entity and destined to Huawei.

Again, the rule only targets deliveries to listed Huawei entities, and only of items that are the direct product of software or technology produced or developed by those entities. In other words, the use of the U.S.-origin machine or major plant component alone is not enough to trigger this additional restriction. This should be a relief to major equipment manufacturers and foundries outside the U.S., though the rule targets the prevalence of foundries and other manufacturers in the IC supply chain using customer designs and software tools to make finished products, and the practical impact will need to be assessed.

What Should Industry Do Next?

Foundries and other manufacturers of semiconductors need to take *immediate action* to review these new export control rules if they supply Huawei, its non-U.S. affiliates, or its subcontractors. Foundries that have not conducted an export classification review of items produced because the chip design was not based on U.S.-origin technology should consider evaluating production machinery and equipment used to manufacture or test those items and confirm if the equipment is the direct product of specified U.S.-origin technology or software.

In particular, co-development and co-production with Huawei listed entities, the deployment of Huawei designs, and the use of software, technology, and other tools from Huawei to produce items may make such items subject to the EAR depending on the use and application of U.S.-origin technology, software, and equipment. The reach of this rule is already being felt by Taiwan Semiconductor Manufacturing Co Ltd., one of the world's largest chipmakers, which recently announced that all new orders from Huawei have been stopped.

Items produced with U.S.-origin technology or software will be subject to EAR licensing requirements if shipped *after* May 15, 2020. Shipments of foreign-produced items that are direct products of plants or major components of plants as identified above and were in "production" before May 15, 2020 may proceed as not being subject to the EAR provided they are exported, reexported, or transferred (in-country) before September 14, 2020.

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