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Hua-Wait a Minute: Entity Designation Affects Non-U.S. Manufacturers' Exports to China Tech Giant

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On May 16, 2019, a sweeping U.S. export control rule went into effect that will impact the U.S. tech industry, but may also create an outsized risk for non-U.S. manufacturers. The rule, issued by the U.S. Department of Commerce, Bureau of Industry and Security (BIS) adds Huawei Technologies Co., Ltd. (Huawei) and 68 of its affiliates to the Entity List. That designation effectively prohibits the export, reexport, and retransfer of all U.S.-origin "items subject to the Export Administration Regulations (EAR)" to those entities. The designation arises from a U.S. government finding that the restrictions are warranted on U.S. national security and foreign policy grounds.

The De Minimis Rule

For companies in the United States, the effect of the rule is straightforward: virtually all items manufactured in the United States are "subject to the EAR." (The biggest exception is military items, which are already subject to a total export prohibition for China under the International Traffic in Arms Regulations.) But the seemingly straightforward Entity List prohibition becomes a little more complicated for manufacturers outside the United States. The source of that complication is the *de minimis* rule.

Effects on Non-U.S. Manufacturers

Under the *de minimis* rule, U.S. export controls are applied to certain foreign-made products. The *de minimis* rule provides that a foreign-made commodity is subject to the EAR if that foreign-made commodity contains more than 25% controlled U.S.-origin content by value. The rule does not count so-called EAR99 items or other items that do not require a license (NLR items) to the final destination. That means that some low-level U.S.-origin software, technology, or commodities do not count in the 25% *de minimis* threshold.

We won't delve into the details here, but if you make a product outside the United States that incorporates U.S. parts, components, or technology, or bundles U.S.-origin software, U.S. export controls may apply to the export of your product from *outside the United States* to Huawei in China. If the relevant controls apply, the foreign manufacturer (and any other person wherever located) is prohibited from exporting the item to Huawei.

Turning the Screws

For now, the application of the *de minimis* rule is straightforward: foreign made product with 25% or less controlled U.S.-origin content – no EAR, no worry.

Currently, the 25% de minimis threshold does not count U.S.-origin content that does not require a license to the item's final destination. Consider, however, what would happen if, for exports to Huawei, BIS took into account that all U.S.-origin content would require a license *to Huawei*. That would mean counting EAR99 and NLR items in the 25%. That would restrict an enormous number of foreign-made goods that use commercial, off-the-shelf U.S. parts and technology, from being sold to Huawei.

BIS has not published guidance or clarification on how the Entity List additions will intersect with the de minimis rule. However, we understand that, in the past, BIS and the Office of Export Enforcement have considered regulations interpretations that would prevent companies from exploiting the de minimis to "laundering" U.S.-origin input items in non-U.S. end-products.

The Takeaway

At this point, non-U.S. manufacturers that sell to Huawei or other designated entities would do well to assess the amount of U.S.-origin content they use in their products. If the value of that content, including U.S.-origin technology and software, approaches 25%, those companies would be well advised to carefully account and record the U.S.-origin value in that product. It is likely that BIS will be looking carefully for U.S. items and technology being re-exported to the newly designated entities.