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Federal Government Moves to Bar Contractors from Using Certain Chinese Telecommunications and Video Surveillance Services or Equipment

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On July 14, 2020, the Federal Acquisition Regulatory (“FAR”) Council published an [interim rule](#) restricting federal government contractors from using, in their own systems, certain covered telecommunications and video surveillance equipment and services from designated Chinese companies, such as Huawei Technologies Company (“Huawei”). Subsequently on July 28, 2020, the Department of Defense published a [memorandum](#) further explaining some of the nuances of the rule. Despite calls for a delayed effective date to facilitate compliance, the interim rule is scheduled to take effect on August 13, 2020.

The rule implements Section 889(a)(1)(B) of the [John S. McCain National Defense Authorization Act for Fiscal Year 2019 \(Pub. L. 115-232\)](#) (“FY 2019 NDAA”) and extends the restrictions already in effect beyond the telecommunications supplies and services the federal government actually acquires from contractors. Contractors have until September 14, 2020, to submit comments before the interim rule is finalized, and both prime contractors and subcontractors considering new federal contracts, or extensions or renewals under existing agreements, would be well-advised to examine their enterprises and supply chains before certifying their compliance.

The View from Washington

The interim rule is an extension of the FY 2019 NDAA, which became law in August 2018 and already restricts direct federal purchases of covered equipment and services as of August 2019. Nonetheless, the publication of the interim rule still could place further strain on the increasingly fractious relationship between the U.S. and

China insofar as it represents another salvo aimed at Huawei and similar Chinese companies. Huawei, in particular, already is the primary target of numerous U.S. government actions affecting both inbound and outbound transactions, including its addition to the BIS Entity List, which severely restricts Huawei's ability to procure items subject to U.S. export and reexport controls.

In addition to the federal procurement prohibitions set forth in Section 889, Huawei, among others, seems likely to be deemed a "foreign adversary" for purposes of transactions with U.S. parties concerning Information and Communications Technology and Services. A proposed rule authorizing the U.S. Department of Commerce to review and potentially block or unwind such transactions retroactive to May 2019 was published in late November 2019, but has not yet been finalized.

Key Features of the Interim Rule

The interim rule implements Section 889(a)(1)(B) of the FY 2019 NDAA, providing, e.g., that executive agencies are prohibited from:

entering into, or extending or renewing, a contract with an entity that uses any equipment, system, or service that uses covered telecommunications equipment or services as a substantial or essential component of any system, or as critical technology as part of any system.

The restrictions apply, e.g., to solicitations issued on or after August 13, and any resultant contracts, as well as to solicitations issued prior to August 13, provided the resulting award occurs after that date.

Covered Telecommunications Equipment or Services

"Covered telecommunications equipment or services" is defined to mean:

- Equipment produced by Huawei or ZTE Corporation (or any subsidiary or affiliate of such entities);
- For the purpose of public safety, security of government facilities, physical security surveillance of critical infrastructure, and other national security purposes, video surveillance and telecommunications equipment produced by Hytera Communications Corporation, Hangzhou Hikvision Digital Technology Company ("Hikvision"), or Dahua Technology Company ("Dahua") (or any subsidiary or affiliate of such entities);¹

- Telecommunications or video surveillance services provided by such entities or using such equipment; or
- Telecommunications or video surveillance equipment or services produced or provided by an entity that the Secretary of Defense, in consultation with the Director of National Intelligence or the Director of the Federal Bureau of Investigation, reasonably believes to be an entity owned or controlled by, or otherwise connected to, the government of a “covered foreign country,” which is defined as the People’s Republic of China.

Substantial or Essential Component

The term “substantial or essential component” means any component necessary for the proper function or performance of a piece of equipment, system or service.

Critical Technologies

Section 889 adopts the definition of “critical technologies” provided in the Foreign Investment Risk Review Modernization Act of 2018, which expanded the jurisdiction of the Committee on Foreign Investment in the United States. Such technologies include, in particular, certain items subject to the prevailing U.S. export controls regimes, including any “emerging” or “foundational” technologies identified by the U.S. Department of Commerce in accordance with the Export Control Reform Act of 2018.

Use

Though the definitions above track those set forth at Section 889(a)(1)(A) of the FY 2019 NDAA, the term “use” is unique to Section 889(a)(1)(B) and is the crux of its more expansive restriction. It is neither defined in the FY 2019 NDAA nor the interim rule and, as drafted, could result in prime contractors and their subcontractors being barred on the basis of even attenuated or ancillary use of covered equipment. For example, on June 10, Under Secretary of Defense for Acquisition and Sustainment Ellen Lord testified that the provision potentially could invalidate a major prime contractor as a result of the use of a subcontractor “six or seven levels down the supply chain” of “one camera in a parking lot.”

Due in part to the risks of such an expansive interpretation, the U.S. Department of Defense, several members of Congress, and key industry stakeholders have advocated for a delayed implementation date beyond August 13, though thus far to no avail. For example, though amendments were offered to the FY 2021 NDAA in both

the House and the Senate to extend the deadline, currently it appears they will not be voted on until September.

Exceptions

There are two exceptions to the prohibitions: one for certain third-party connection services such as backhaul, roaming and interconnection agreements; and another for certain equipment without the ability to route or redirect user data traffic, or have visibility into user data.

An agency may contract with an entity “to provide a service that connects to the facilities of a third-party, such as backhaul,² roaming,³ or interconnection arrangements.”⁴ This exception applies only to an agency that is contracting with an entity to provide a service. Therefore, the exception does not apply to a contractor’s use of a service that connects to the facilities of a third-party, such as backhaul, roaming, or interconnection arrangements. As a result, executive agencies are prohibited from contracting with a contractor that uses covered telecommunications equipment or services to obtain backhaul services from an internet service provider, unless a waiver is granted.

Further, an entity may procure “telecommunications equipment that cannot route or redirect user data traffic or [cannot] permit visibility into any user data or packets that such equipment transmits or otherwise handles.”

Key Compliance Considerations

If implemented on time as drafted, Under Secretary Lord testified that the new restrictions stand to pose a meaningful compliance burden, in light of the “heavy lift” to identify covered equipment. A contractor’s failure to abide by the requirements set forth in the interim rule could be construed as a material misrepresentation or breach of contract that potentially could lead to termination, as well as financial penalties. In addition, knowing noncompliance could potentially expose a contractor to liability under the civil False Claims Act.

Prime Contractors

The interim rule requires that the party executing the contract with the federal government (“offeror”) provide the representation at Section 52.204-24 as to whether it uses covered telecommunications equipment or services. If so, it is required to make certain disclosures regarding, e.g., the manufacturer of the equipment and a detailed

description of the same. Importantly, the offeror is to make this representation after conducting a “reasonable inquiry,” which is defined as:

an inquiry designed to uncover any information in the entity’s possession about the identity of the producer or provider of covered telecommunications equipment or services used by the entity that excludes the need to include an internal or third-party audit.

Subcontractors

The prohibitions set forth in Section 889(a)(1)(B) expressly do not flow down to subcontractors because, according to the FAR Council, the prime contractor is the only entity with which an agency contracts. However, as the “reasonable inquiry” standard imposed on prime contractors expressly requires that they make a representation as to equipment or services “used by the entity,” it seems prime contractors could very well extend their due diligence to the subcontractors and/or seek a parallel representation from them, even if the prohibitions nominally do not flow down.

The FAR Council apparently also is considering the expansion of the scope of the prohibitions detailed in the interim rule to any affiliates, parents and subsidiaries of an offeror that are domestic entities. Presumably, this is regardless of whether any of these entities is reasonably expected to participate in the performance of a federal contract.

The proposed expansion of the prohibitions to entities affiliated with the offeror is unsurprising given that the use by a prime contractor of covered equipment is prohibited even if that equipment has no nexus to the performance of a contract.

Waivers

The interim rule also establishes an agency-initiated process that authorizes case-by-case waivers that would expire no later than August 13, 2022. The submission of an offer following an affirmative representation regarding the use of covered equipment essentially will constitute a waiver request, which the FAR Council anticipates likely will take agencies a few weeks to process. Agencies reasonably may decline to initiate the waiver process and proceed to make awards to contractors not requiring waivers. Note that there is also the possibility of a waiver without an expiration date, though the authority to issue it vests with the Director of National Intelligence separate and apart from the interim rule.

Key Takeaways

- The interim rule is the latest iteration in the U.S. government's comprehensive effort to insulate government agencies from Chinese-supplied telecommunications and other equipment citing national security concerns.
- Despite efforts to extend the effective date of the interim rule, including amendments to the FY 2021 NDAA which could be heard in September, and efforts that still could be taken up as part of stimulus legislation in relation to COVID-19, it now appears likely that the requirements will take effect on August 13.
- Accordingly, prime contractors should undertake to identify the possible use of covered equipment throughout their supply chains and subcontractors should also be prepared for prime contractors to make inquiries or request certifications.
- Comments on the interim rule are due by September 14 and provide an opportunity for contractors to detail the likely significant compliance burdens attendant to the implementation of the interim rule with the aim of having the FAR Council address the impact of these burdens on industry.

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1. Hikvision and Dahua also appear on the Entity List.[↩](#)

2. The term "backhaul" means "intermediate links between the core network, or backbone network, and the small subnetworks at the edge of the network (e.g., connecting cell phones/towers to the core telephone network). Backhaul can be wireless (e.g., microwave) or wired (e.g., fiber optic, coaxial cable, Ethernet)." [↩](#)

3. The term "interconnection arrangements" means "arrangements governing the physical connection of two or more networks to allow the use of another's network to hand off traffic where it is ultimately delivered (e.g., connection of a customer of telephone provider A to a customer of telephone company B) or sharing data and other information resources."[←](#)

4. The term "roaming" means "cellular communications services (e.g., voice, video, data) received from a visited network when unable to connect to the facilities of the home network either because signal coverage is too weak or because traffic is too high."[←](#)

Authors

Mario Mancuso, P.C.

Partner / Washington, D.C. / New York

Ivan A. Schlager, P.C.

Partner / Washington, D.C.

Daniel J. Gerkin

Partner / Washington, D.C.

H. Boyd Greene IV

Partner / Washington, D.C.

Jeremy Iloulian

Associate / Washington, D.C.

Sanjay José Mullick

Partner / Washington, D.C.

Anthony Rapa

Partner / Washington, D.C.

Robert S. Ryland

Partner / Washington, D.C.

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