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Fiscal Year 2023 National Defense Authorization Act Muddies the Water on Whether Chinese Semiconductor Ban Applies to Contractors

*By Robyn N. Burrows**

In this article, the author explains that it remains unclear whether a Chinese semiconductor ban applies to government contractors.

In October 2022, a proposed amendment to the FY 2023 National Defense Authorization Act (NDAA) was introduced to prohibit contractors from selling certain Chinese semiconductor technologies to federal agencies and from using these same covered products and services. This measure was added through Section 5949 of the NDAA.

Thereafter, the House of Representatives passed a compromise version of the NDAA, which appears to scale back the semiconductor ban by applying it only to federal sales of covered products and services, without also banning contractors from using them. However, the explanatory statement accompanying the NDAA suggests contractors (including their affiliates and subsidiaries) may ultimately be prohibited from using covered semiconductor technologies—which would raise a host of compliance and implementation concerns.

COMPROMISE VERSION OF NDAA LIMITS SEMICONDUCTOR BAN TO FEDERAL SALES

Section 5949 bans semiconductor products and services from Semiconductor Manufacturing International Corporation, ChangXin Memory Technologies, and Yangtze Memory Technologies Corp., plus their subsidiaries and affiliates. This ban was modeled after the supply chain restrictions from Section 889, which prohibit contractors from selling and using covered telecommunications and video surveillance equipment from five Chinese telecom companies.

Like Section 889, Section 5949 originally contained Part A and Part B prohibitions banning contractors from selling covered semiconductor products and services to the government (Part A) and also from using these same technologies (Part B). Structurally, the compromise version of Section 5949 retains Parts A and B, but both parts prohibit federal sales of covered semiconductor products and services:

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- Prohibition on Use or Procurement.

(1) IN GENERAL.—The head of an executive agency may not—

(A) procure or obtain, or extend or renew a contract to procure or obtain, any electronic parts, products, or services that include covered semiconductor products or services; or

(B) enter into a contract (or extend or renew a contract) with an entity to procure or obtain electronic parts or products that use any electronic parts or products that include covered semiconductor products or services.

Notably absent is any prohibition against contractors using covered semiconductor products or services. The “use” prohibition in Part B only bans agencies from procuring electronic parts and products that use covered semiconductor products or services. The elimination of a true use ban may have been in response to lobbying efforts by the semiconductor industry, as reflected in a November 22 letter¹ from a coalition of defense, technology, and business trade groups to lawmakers on the Senate Armed Services Committee.

NDAAs’ JOINT EXPLANATORY STATEMENT—RULEMAKERS EXPECTED TO EXTEND BAN TO CONTRACTORS

Despite what appears to be a more limited semiconductor ban in Section 5949, contractors should not assume that the ban, once implemented, will only apply to their federal sales. In particular, the “Joint Explanatory Statement” accompanying the NDAA states Congress’ expectation that the FAR Council implement rulemaking that extends Section 5949 to prohibit contractors from using covered semiconductor products:

We note that the intent of Congress in advancing this proposal is that, in serving federal supply chains, Federal contract recipients and their suppliers (including domestic and foreign subsidiaries, affiliates, distributors, and intermediaries) should not utilize companies connected to foreign countries of concern that threaten national security, such as Semiconductor Manufacturing International Corporation, Yangtze Memory Technologies Corp, and ChangXin Memory Technologies, or any other company identified under this section (including any affiliate, subsidiaries, successor, distributor, or intermediary thereof). . . .

With regard to the regulations to be prescribed by this Federal Acquisition Regulatory Council, the intent of this provision is to include both

¹ <https://www.uschamber.com/security/supply-chain/coalition-letter-on-section-889-of-the-ndaa>.

*contractors and suppliers, to the extent possible under the Federal Acquisition Regulation[.]*²

While the text of Section 5949 only prohibits federal sales of covered semiconductor technologies, the joint explanatory statement reflects a Congressional intent that the ban be extended to use by contractors and suppliers—including their domestic and foreign subsidiaries and affiliates. This would be more onerous than Part B of Section 889, which currently only applies to the prime contracting entity and excludes affiliates, subsidiaries, and subcontractors. As noted by trade groups, covered entities would be required to trace their supply chain down to the component level to identify any covered semiconductor equipment used in the contractor’s enterprise. Additional diligence would be required to identify whether third parties (such as payroll, accounting, or logistics support) use covered products or services.

Congress’ disjointed approach to Section 5949 may have resulted from industry pressure against applying Part B to the semiconductor supply chain (achieved through the text of Section 5949), combined with a legislative desire to impose a “use” ban similar to Section 889 (as reflected in the Joint Explanatory Statement). The FAR Council will need to address these conflicting provisions during the rulemaking process. Until then, the scope of the ban remains unclear. Given the potential impact of an industry ban on using these semiconductor technologies, contractors should closely monitor and participate in future rulemaking.

² Emphasis added.

