# U.S. Government Releases Awaited "Section 889" Rule on Prohibition on "Use" of Covered Telecommunications Equipment by Federal Contractors

July 13, 2020

Government Contracts

On July 10, 2020, the U.S. Government's Federal Acquisition Regulatory Council ("FAR Council") released a prepublication version of the interim rule governing Section 889(a)(1)(B) of the John S. McCain National Defense Authorization Act for Fiscal Year 2019 (Pub. L. No. 115-232), and added some clarifications to definitions that impact Section 889(a)(1)(A), which went into effect in August 2019. The interim rule implements the statutory prohibition on the head of an executive agency contracting with (including extending or renewing a contract) any "entity" that "uses" "covered telecommunications equipment or services as a substantial or essential component of any system or as a critical technology of any system." Covered telecommunications equipment or services includes all telecommunications equipment or services produced and provided by Huawei Technologies Company or ZTE Corporation, and video surveillance and telecommunications equipment or services produced and provided by Hytera Communications Corporation, Hangzhou Hikvision Digital Technology Company, or Dahua Technology Company, or any subsidiaries or affiliates of the five entities. The prohibition and the interim rule for Section 889(a)(1)(B) become effective on August 13, 2020.

The FAR Council explicitly recognized that this prohibition applies to ***all*** U.S. Government (or "Government") contractors, domestic and international, spanning a wide array of industries including the "health-care, education, automotive, aviation, and aerospace industries; manufacturers that provide commercially available off-the-shelf (COTS) items; and contractors that provide building management, billing and accounting, and freight services." Beginning on August 13, 2020, every entity seeking to serve as a prime contractor to the U.S. Government will have to certify compliance with Section 889(a)(1)(B) or seek a waiver for additional time to comply, even if that company is not selling telecommunications equipment or services to the U.S. Government.

Leading up to the highly anticipated release of these regulations, compliance questions from industry focused on three key categories: (1) the definitions of ***"entity"*** and of ***"use"***; (2) precise compliance requirements and the level of diligence required; and (3) the application of and process for exceptions and waivers. Although the interim rule addresses all of these items in part, questions remain about how these requirements will be enforced, the steps industry must take to certify full compliance with Section 889(a)(1)(B), and the likelihood and length of time for waivers. Notwithstanding these questions, it is plain that the ability to comply with

Section 889 (or to obtain a waiver beyond August 13, 2020) will become a discriminator in the contracting process. Indeed, the regulations clearly state that urgent mission requirements may allow an agency to reasonably choose an offeror that does not require a waiver.

The interim rule will take effect in August 2020, but current and prospective government contractors have an important opportunity to engage with the FAR Council and other Government stakeholders, particularly on these open questions. Comments on the interim rule will be due 60 days following its publication in the Federal Register.

## I. Definitions of "Entity" and "Use"

a. Definition of "Entity"

Prior to the release of the rule, there was uncertainty about how the FAR Council would interpret the statutory term "entity." The interpretation of the term is important because it defines the scope of coverage of the rule—principally, whether the general prohibition on "use" of covered telecommunications equipment would be interpreted to include parents, subsidiaries, affiliates, subcontractors, and/or suppliers of the contracting party. The interim rule clarifies that, for now, the term "entity" refers to only the contracting party:

> The 52.204-25 prohibition under section 889(a)(1)(A) will continue to flow down to all subcontractors; however, as required by statute the prohibition for section 889(a)(1)(B) will not flow down because the prime contractor is the only "entity" that the agency "enters into a contract" with, and an agency does not directly "enter into a contract" with any subcontractors, at any tier.

Moreover, the FAR Council highlighted the ***possibility*** that the rule could later apply to entities beyond the contracting party. Specifically, the FAR Council is seeking comments on whether to expand the prohibition's scope to "the offeror and any affiliates, parents, and subsidiaries of the offeror that are domestic concerns, and expand the representation at 52.204-24(d)(2) so that the offeror represents on behalf of itself and any affiliates, parents, and subsidiaries of the offeror that are domestic concerns." If enacted, this change would be effective when the FAR Council seeks to finalize the proposed rule by August 13, 2021. It would significantly expand the scope of compliance obligations for prime contracts with affiliates in the United States. Further, because the contemplated language is limited to affiliates, parents, and subsidiaries that are "domestic concerns," the change could have a disparate impact on foreign and domestic companies.

b. Definition of "Use"

The new rule does not clarify all aspects of what is meant by "use" of covered telecommunications equipment or services. In fact, the FAR Council did not include a definition of the term, and instead simply repeated the general statutory requirement that agencies are prohibited from "entering into a contract, 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 FAR Council did make the notable statement that the prohibition on use applies "***regardless of whether that usage is in performance of work under a Federal contract.***" This confirms that even ***commercial*** activities that bear no connection to

the contracting entity's performance of a federal contract are within the scope of the prohibition.

By clarifying that the prohibition on "use" only applies to the contracting party and not to any other "entity," the interim rule clarifies that the focus is on whether the prime contractor ***itself*** uses "covered telecommunications" equipment or services as a substantial or essential component of any system, or as critical technology as part of any system, whether or not used in support of commercial or Government related activities. The prime contractor will still need to ensure that it is not procuring any covered telecommunications equipment or services from its subcontractors, suppliers, and vendors for the prime contractor's use.

## II. Compliance Requirements

a. Application of the Rule

Contracting officers must include the updated clause when exercising options under any existing U.S. Government contract. Such an addition could present legal issues because the prohibition would not have existed in the contract at the time of contract execution, and the contractor may not have factored the impact of compliance into their prices for performance of those option periods. Absent a clause in the contract allowing the Government or prime contractor to unilaterally add new terms and conditions, such an addition to an existing contract/subcontract would ordinarily require a bilateral modification and consideration. In fact, the interim rule recognizes the need for consideration when it noted that modifications to existing U.S. Government IDIQ contracts must be done in accordance with FAR 1.108(d).

Nonetheless, the prohibition is a statutory mandate, so Government contractors may find themselves at an impasse if the parties cannot agree to the addition of the clause. Similarly, for General Service Administration and Veterans Affairs schedules and similar contracts, a failure to agree to the new clause could lead to the Government dropping a company's products from the schedules with limited notice. Such an impasse could potentially be resolved by a waiver for additional time to comply, which we discuss in more detail later in this alert.

b. Compliance Plans

Although not an explicit requirement of the rule, the FAR Council has outlined an expectation for contractors to prepare plans in the first year that demonstrate how they are complying with the new requirements. In the rule's preamble, the FAR Council stated, "[a]s a strictly contractual matter, an organization's failure to submit an accurate representation to the Government constitutes a breach of contract that can lead to cancellation, termination, and financial consequences. Therefore, it is important for contractors to develop a compliance plan that will allow them to submit accurate representations to the Government in the course of their offers." If contractors make inaccurate representations, they could face liability for breach of contract, and could even face charges of violating the False Statements Act and/or the False Claims Act, which have significant civil, administrative, and even criminal consequences.

The FAR Council signaled that the following elements should be part of the compliance plan developed by any entity:

1. **Regulatory Familiarization.** Read and understand the rule and necessary actions for compliance.
2. **Corporate Enterprise Tracking.** The entity must determine through a reasonable inquiry whether the entity itself uses "covered telecommunications" equipment or services as a substantial or essential component of any system, or as critical technology as part of any system. This includes examining relationships with any subcontractor or supplier for which the prime contractor has a Federal contract and uses the supplier or subcontractor's "covered telecommunications" equipment or services as a substantial or essential component of any system. A reasonable inquiry is an inquiry designed to uncover any information in the entity's possession—primarily documentation or other records—about the identity of the producer or provider of covered telecommunications equipment or services used by the entity. A reasonable inquiry need not include an internal or third-party audit.
3. **Education.** Educate the entity's purchasing/procurement, and materials management professionals to ensure they are familiar with the entity's compliance plan.
4. **Cost of Removal (if the entity independently decides to).** Once use of covered equipment and services is identified, implement procedures if the entity decides to replace existing covered telecommunications equipment or services and ensure new equipment and services acquired for use by the entity are compliant.

   [***Note***: Unlike some other recent telecommunications supply chain security actions, Section 889 does not provide for Government funds to underwrite a "rip and replace" campaign.]
5. **Representation.** Provide representation to the Government regarding whether the entity uses covered telecommunications equipment and services and alert the Government if use is discovered during contract performance.
6. **Cost to Develop a Phase-out Plan and Submit Waiver Information.** For entities for which a waiver will be requested, (1) develop a phase-out plan to phase-out existing covered telecommunications equipment or services, and (2) provide waiver information to the Government to include the phase-out plan and the complete laydown of the presence of the covered telecommunications equipment or services.

c. Reasonable Inquiry

The interim rule requires a contractor to represent to the Government that after conducting a "reasonable inquiry," it does or does not "use covered telecommunications equipment or services, or use any equipment, system, or service that uses covered telecommunications equipment or services." "Reasonable inquiry" is a new term, which was not included in the statute. It means "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."

This one definition raises at least three compliance challenges. First, the scope of "any information in the entity's possession" is ambiguous because it does not specify

whether this could include every email and conversation that an employee has with a supplier. The preamble to the interim rule indicates that it is "primarily documentation or other records." But, "any information" could also be read to cover publicly available information, especially given the significant press coverage on issues surrounding national security concerns with the telecommunications supply chain. Second, the terms "producer" and "provider" are not defined in the regulation, but the common usage of the term "producer" would include the manufacturer of the product. (The regulation may have included both terms because the manufacturer (producer) and seller (provider) often are two different companies.) Given the pervasiveness of white-labeling in the information technology industry, contractors would be wise to consult their vendors and suppliers of telecommunications equipment and services to verify that they are free of covered equipment or services. Finally, the language that "excludes the need" for internal or third party audits appears to alleviate the need for any type of reverse engineering.

For purposes of complying with Section 889(a)(1)(A), contractors may already be conducting supply chain diligence with regard to delivery of products and services to the Government, but a question remains as to how broadly to extend this type of diligence for the entity's own use of telecommunications equipment and services for purposes of complying with Section 889(a)(1)(B). A contractor should consider conducting some measure of due diligence under Section 889(a)(1)(B), especially if it has a reasonable basis to question the accuracy or completeness of supplier or subcontractor documentation.

## III. Exceptions and Waivers

### a. Exceptions

Section 889 includes two exceptions to the prohibition on the use or procurement of covered technologies at Subsections 889 (a)(2)(A) and (B). First, Subsection 889(a)(2)(A) provides an exception that allows U.S. Government agencies to procure services that rely on connections with covered telecommunications equipment so long as those connections are limited to backhaul, roaming, or interconnection arrangements. Notably, this exception applies only to a Government agency that is contracting with an entity to provide a service. The interim rule notes that "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" (emphasis added). In other words, the Government cannot contract "with a contractor that uses covered telecommunications equipment or services to obtain backhaul services from an internet service provider, unless a waiver is granted."

The interim rule defines "backhaul," "roaming," and "interconnection arrangements" for the first time to "provide clarity regarding when an exception to the prohibition applies." The definitions fit with a common understanding of these terms. Broadly speaking, these three terms cover instances when an entity is borrowing service from another entity. The interim rule notes that the definitions were developed based on existing telecommunications regulations and case law and consultation with subject matter experts.

- **Backhaul** is defined as the "intermediate links between the core network, or backbone network, and the small subnetworks at the edge of the network." Essentially, backhaul is the transportation of traffic between networks. For

example, this would include connecting cell phones/towers to the core telephone network. The definition notes that backhaul can be wireless or wired.

- **Roaming** is defined as "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."
- **Interconnection Arrangements** are defined as "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…or sharing data and other information resources." For example, this would include the connection of a customer of telephone provider A to a customer of telephone company B.

Second, Subsection 889(a)(2)(B) provides an exception for covered telecommunications equipment that cannot route user data traffic, redirect user data traffic, or permit visibility into any user data or packets that such equipment transmits or otherwise handles. "Route," "redirect," "user data," and "packets" are technical terms, and they remain undefined in the interim rule. Regardless of how these terms are ultimately applied, the statute uses the term "***cannot***," rather than "do not." This structure suggests that the Government will apply the exception narrowly, by examining the equipment's capabilities and functionalities, regardless of whether the equipment is actually being used for those functions. Only if the equipment is physically or logically incapable of performing the tasks will it fit into this exception.

b. Waivers

Contractors should familiarize themselves with the waiver process, as that process will be key to obtaining new contracts, and/or keeping existing contracts subject to extension or renewal, that involve the use of covered telecommunications equipment or services. In general, a waiver may be granted by an agency head only one time, and only until August 13, 2022. Once the waiver period expires, compliance is mandatory. Although Section 889 allows an entity to receive a national security waiver from the Office of the Director of National Intelligence ("ODNI"), we expect those waivers to be rare.

The waiver process will be conducted on an ***agency-by-agency basis***. Although a government-wide waiver process was contemplated as an alternative, the FAR Council ultimately determined that each agency best understood its own "unique mission needs" and "unique security concerns and vulnerabilities." Where a contractor sells the same products or services to multiple agencies, the contractor must initiate the waiver request with the contracting officers in each agency responsible for the potential contract. Different agencies may come to different conclusions on whether to initiate a waiver process or grant a waiver.

The readiness of agencies to process and consider waiver requests remains an open question. We understand that some waiver applicants have experienced a months-long process when seeking waivers under Section (a)(1)(A). These delays may have been caused by growing pains associated with establishing the new waiver process when Section 889 was still in its infancy, but the estimate of "a few weeks" in the interim rule is overly optimistic.

In fact, the new regulations for waivers under Section (a)(1)(B) introduce additional bureaucratic processes, including a novel, 15-day "notice-and-wait" period, during which the agency head must notify ODNI and the Federal Acquisition Security Council. Neither this specific 15-day waiting period nor the general requirement to consult with ODNI during agency-level waiver deliberations were included in the statute. These additional processes will slow the waiver process in general by a minimum of 15 days, to account for the time between the agency's determination and the approval of a waiver. An agency may waive the notice and consultation requirements only in the case of an emergency or national disaster.

Based on these new requirements, contractors must undertake advance planning. Mechanically, the waiver process is initiated by the contracting officer. If the contractor is unable to certify compliance with (a)(1)(B) ***at the time a bid is submitted***, it will be presumed that a waiver will be required for that contractor. A contracting officer may choose not to initiate the waiver process, and the regulations contain no avenue for recourse or appeal of this decision. To determine whether to initiate the formal waiver process, "market research" must be conducted by the agency, and contracting officers must incorporate feedback received from interested offerors during the acquisition process. The interim rule does not explicitly address whether waiver requests can be submitted outside of the submission of a proposal.

In sum, as noted above, the ability to comply with Section 889 (or to obtain a waiver beyond August 13, 2020) will become a discriminator in the contracting process. Indeed, the regulations clearly state that urgent mission requirements may allow an agency to reasonably choose an offeror that does not require a waiver.

If the contracting officer determines that a waiver is required to make an award, the contractor must submit a waiver request with detailed elements, as required by the statute: (1) a ***compelling justification*** for the additional time to comply; (2) a ***full and complete laydown*** of the presence of covered telecommunications or video surveillance equipment or services; and (3) a ***phase-out plan to eliminate*** such covered telecommunications equipment or services from the entity's systems. The contractor is permitted to include all the information it would need for a waiver with its proposal but it is not required until the contracting officer makes a determination to start the waiver process. Nonetheless, contractors who anticipate needing a waiver should begin preparing the information in advance to include with their proposals or to be ready to respond quickly so as to not cause any self-imposed delays to a process with many steps.

## IV. Comment Period

Contractors have an important opportunity to engage with the Government now. There will be a 60-day comment period for the interim rule. Any comments received during this period will be considered by the FAR Council in formulating the final rule.

The FAR Council laid out a specific set of questions in the interim rule, seeking data on a number of categories including the fully-burdened costs of compliance, business impacts stemming from compliance, the scope of industry's current use of covered telecommunications equipment or services, and suggested steps for identifying and removing covered telecommunications equipment or services. As many of these questions would involve proprietary information, the FAR Council has directed commenters to

include the phrase "Business Confidential" at the top of any page containing sensitive information.

One area that industry will want to pay close attention to is the ***potential expansion of scope*** under the final rule discussed above to require that the prohibition also apply to any of an entity's affiliates, parents, and subsidiaries of the entity that are domestic concerns, so that the entity represents on behalf of itself and any affiliates, parents, and subsidiaries whether they use covered telecommunications equipment or services. This would effectively redefine "entity" even more broadly. The FAR Council is seeking comments on the impacts of such an expansion of scope.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our firm:


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