

ZTE Export Privileges to Be Reinstated Under Terms of New Settlement Agreement

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The U.S. Department of Commerce announced yesterday that it has reached a new settlement agreement with Chinese telecom giant ZTE to replace the denial order that the Commerce Department's Bureau of Industry and Security (BIS) activated on April 15, 2018. The denial order, which prohibited U.S. producers from supplying even common, off-the-shelf EAR99 and other low-level technology electronic components and commercial software to ZTE, sent shockwaves throughout the global telecommunications industry and threatened to put ZTE, China's second-largest telecommunications equipment manufacturer, out of business. The new settlement agreement will reinstate ZTE's export privileges in exchange for ZTE's agreement to pay a \$1.4 billion fine, replace its entire management team, and retain a team of compliance specialists embedded within ZTE for ten years. The timing for ZTE's reinstatement is uncertain, but Wiley Rein will continue to monitor this matter closely.

Background

On March 23, 2017, ZTE entered into a settlement agreement with the U.S. government to settle civil and criminal allegations that ZTE violated U.S. sanctions and export control laws by illegally shipping U.S.-origin products to Iran and North Korea. As part of that agreement, ZTE agreed to pay a combined penalty of up to \$1.19 billion and agreed to not commit any further violations under penalty of having its export privileges revoked for a seven-year period.^[1] The settlement agreement also subjected ZTE to mandatory, periodic reporting. Pursuant to this requirement, on February 2, 2018, the U.S. government requested a status report on individuals who ZTE had previously indicated were disciplined as part of the company's efforts to respond to the violations that gave rise to the settlement

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agreement. ZTE's status report showed that the company had provided false information regarding its disciplinary efforts and had not undertaken to correct its prior false statements until after receiving the February 2, 2018 information request. As a result, BIS activated the seven-year denial order and placed ZTE on the Denied Persons List. This move effectively cut ZTE off from U.S. components and software and had far-reaching, global impacts on network operators and consumers with ZTE mobile phones.

New Agreement Will Replace Denial Order with Harsh Penalties

Under the terms of the new settlement agreement, ZTE will be required to pay a \$1 billion fine and place an additional \$400 million in suspended penalty escrow before ZTE will be removed from the Denied Persons List. The \$1.4 billion penalty is in addition to the \$892 million that ZTE paid as part of the 2017 settlement agreement, resulting in a total penalty amount of \$2.29 billion. ZTE will also be required to replace its entire board of directors and executive leadership team and to retain a BIS-selected team of special compliance coordinators for ten years. The agreement includes a new ten-year suspended denial order that BIS will be able to activate if ZTE commits any additional violations during the ten-year probationary period.

Decision is Facing Strong Pushback in Congress

The Administration's decision to lift the denial order on ZTE in exchange for the new settlement agreement is facing a strong rebuke in Congress, which has already introduced several ZTE-targeted amendments to pending legislation over the past few weeks. For example, Senator Chris Van Hollen (D-MD) recently introduced an amendment that has since been incorporated into the Senate's National Defense Authorization Act (NDAA) bill that would prohibit President Trump from modifying the penalties on ZTE unless and until he certifies to Congress that ZTE has fully complied with U.S. law for a period of one year. And, soon after the Department of Commerce announced the new settlement agreement, Sens. Tom Cotton (R-AR), Van Hollen, and Chuck Schumer (D-NY) introduced a bipartisan amendment to the NDAA that would reinstate the penalties on ZTE once the NDAA is signed into law and require the President to make certain certifications before lifting the penalties. Senator Mark R. Warner (D-VA), Vice Chairman of the Senate Select Committee on Intelligence and a member of the Senate Banking and Finance Committees, also released a statement highlighting the U.S. government's broader national security concerns regarding ZTE.

Apart from potential Congressional action, we caution that it is critical for companies to wait until the Department of Commerce officially removes ZTE from its Denied Persons List prior to resuming activities with ZTE covered by the current denial order.

[1] ZTE paid \$892 million of the combined penalty amount, as the remaining \$300 million was suspended during the seven-year probationary period.