

FCC Sets Sights on China

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As yet another example of the U.S. government's ongoing concerns about the potential vulnerability of U.S. telecommunications networks and supply chains, the FCC recently released a [Notice of Proposed Rulemaking \(NPRM\)](#) proposing to prohibit the use of funds disbursed from the Universal Services Fund (USF) to purchase equipment or services from any providers posing a national security threat to the U.S. The USF distributes funds and subsidies to companies who provide service to unserved and underserved locations and low-income consumers. The NPRM dovetails with recent governmental actions targeting perceived Chinese threats to U.S. telecommunications infrastructure, including [the passage of the National Defense Authorization Act \(NDAA\) for Fiscal Year 2018 \(which prohibits the Department of Defense from using the equipment or services of certain Chinese telecommunications companies\)](#), the [Committee on Foreign Investment in the United States' \(CFIUS\) blocking of chipmaker Broadcom's hostile takeover bid for Qualcomm](#), and [the Department of Commerce's denial of export privileges against a Chinese telecommunications manufacturer for seven years](#). It also precedes a [recent report by the Wall Street Journal on May 2, 2018](#) detailing the possibility of executive action by the Trump administration to restrict Chinese companies' ability to sell telecommunications equipment in the U.S. Chinese companies have already taken action as a result of this increased focus on Chinese telecommunications equipment, including one firm's [request for a stay](#) of a U.S. order banning American companies from selling to the firm.

The NPRM offers some potential insights into how the FCC might implement the proposed ban. USF fund recipients should focus on the following aspects of the NPRM:

- *Federal Agency Models.* The FCC appears to be interested in how other federal or civilian agencies (such as the Federal Regulatory Energy Commission or the Federal Housing Authority) who provide grants or funding have handled similar issues, and asks for comment on ways to model an approach that limits USF recipients' purchase of equipment or services from companies that cause national security concerns.
- *Types of Equipment and Services.* The FCC leaves open the possibility of a bright-line approach in which any purchase from companies identified as presenting national security risks are prohibited, but also seeks comment on limiting the scope of the rule to equipment and services that relate to network management or supply chain vulnerabilities.
- *Effective Date.* Although the FCC clarified that any rule would only apply prospectively, the NPRM appears to recognize that some kind of lead time will be necessary. Similarly, the

NPRM also addresses the impact of the proposed rule on multi-year contracts that frequently exist between USF recipients and equipment manufacturers. The FCC specifically asks for comment both on whether it should “grandfather” these contracts, as well as the potential for these contracts being covered by applicable “change-of-law” provisions that are common in commercial agreements.

- *Identifying Companies that Pose a National Security Threat.* The method for identifying what companies pose a national security threat to communications networks and supply chains will be the focal point of this proceeding. The FCC discusses several possibilities for identifying covered companies. One method would be to draw from the 2012 Spectrum Act and the NDAA and ban any company prohibited from bidding on a government contract or participating in an auction. The FCC also addresses the proposed Defending U.S. Government Communications Act, which would prohibit all federal agencies from purchasing equipment or services from certain Chinese companies as substantial components or a critical technology of a system. A simpler mechanism to implement the proposed rule mentioned by the FCC is a framework whereby covered companies are those barred by the NDAA. Such an approach would necessarily involve the maintenance of some kind of prohibited providers list, either by the FCC or an Executive Branch agency.
- *Enforcement and Non USF-Related Remedies.* The FCC also seeks comment on how to enforce the proposed rule, specifically asking if it should impose forfeitures in addition to the recovery of any funds disbursed in violation of the proposed rule. USF recipients should note that the NPRM (unlike the prior circulated draft version) specifically asks for comment on alternatives to restricting USF support, including steps concerning the removal or prospective deployment of equipment. We interpret this language to mean that the FCC is considering potentially more significant enforcement measures and sanctions.

Although we are still in the early stages of this rulemaking proceeding, there are at least three key takeaways affected companies and major actors should consider going forward:

1. **Continued Focus on China-Related Threats to U.S. Telecommunications Infrastructure.** Consistent with ongoing Congressional and Executive Branch concerns regarding China-related national security threats that have resulted in legislation, CFIUS action, and export control sanctions, it appears the FCC is now taking its place on the frontlines of a looming trade war with China. Traditionally, national security concerns have surfaced in the context of the Executive Branch’s “Team Telecom” review of transactions involving FCC licenses. It now appears the FCC is willing to take a much more proactive role in acting against potential or perceived threats to U.S. telecommunications infrastructure.
2. **Impact on Rural and Small Carriers.** Many USF recipients are small and rural carriers that could be disproportionately impacted by the proposed rule. These small and rural carriers are often more cost-sensitive and have much smaller legal departments than the major national carriers. The FCC appears to recognize this reality and specifically asked for comments on the impact of the proposed rule on small and rural carriers. Carriers should begin developing a regulatory strategy that demonstrates the potential impact of this rule on their ability to provide service in advance of the June 1st comment deadline.
3. **Impact on Efforts to Close the Digital Divide.** Chairman Pai has repeatedly said that closing the digital divide between those who have and do not have access to advanced telecommunications infrastructure and services is the [FCC’s top policy priority](#). It will be interesting to see how restricting USF recipients’ ability to utilize certain network equipment and infrastructure could negatively impact this priority, particularly in light of the fact that small and rural carriers frequently rely on these more cost-friendly network components that often come from China-based companies.

Comments in this proceeding are due June 1, 2018, with reply comments due July 2, 2018.

Eamon Tierney contributed to this article.

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