Insight

Trump’s Political Tax on Nvidia Chips to China

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Executive Summary

- The Trump Administration recently announced a deal with Nvidia to allow the company to sell to China its H20 chips, which were designed to comply with previous export restrictions, overriding the Trump Administration’s own export controls put in place due to national security concerns.
- While reversing course on export controls could be justified as a policy matter, the impetus for the change instead appears to be an agreement for Nvidia to pay the U.S. government 15 percent of its revenue from chips sales in China, casting doubt onto the national security justifications of the action.
- If the Trump Administration continues to leverage U.S. national security for its own benefit, policymakers could inadvertently ignore legitimate national security risks under the assumption that the claimed risks are again just leverage for the administration.

Introduction

In late July, the Trump Administration announced a reversal of federal policy banning the sale of Nvidia H20 chips — a lesser performing chip designed to comply with existing export controls — to China, originally put in place to protect the national security of the United States. In August, however, details emerged that cast doubt on the justifications for the reversal: In exchange for allowing Nvidia to sell its chips to China, Nvidia promised to pay the U.S. government 15 percent of the revenue from sales to China.

The decision highlights a concerning trend that suggests the Trump Administration is willing to ignore national security risks for its own gain. Earlier this year, the administration

outright ignored a federal ban on Tik Tok, allowing the app to continue operation. This decision came despite the fact that the only reason the law survived First Amendment scrutiny was because of the serious national security risk the app poses to Americans. Similarly, the Trump Administration previously reversed course on a merger between Nippon Steel and U.S. Steel after the firms agreed to give the U.S. government significant control over the combined firms. Now, after years of arguing that export controls are necessary to outpace Chinese artificial intelligence (AI) development, the Trump Administration has reversed course on its own export controls in exchange for 15 percent of revenue on Nvidia's sale of the chips to China. (Note, the administration also gave a similar deal to Nvidia rival chipmaker AMD, that exports chips to a lesser extent). Revising existing export controls could achieve national security goals, such as by allowing Nvidia to scale up its production and ensure American chips become the international standard. But in revising the rules in exchange for a cut of the profits, the Trump Administration's action casts doubt on the security justifications of the policy in the first place.

The administration's actions will have major implications for tech policy moving forward. In almost every technology policy issue area, policymakers are arguing that government action is needed to defend our national and economic security. But this administration continues to reverse course on issues of national security when politically expedient. Thus, as Congress considers future legislation, arguments about national security could hold less weight, regardless of the merits of the argument. As a result, lawmakers could ignore legitimate national security risks thinking the administration is simply crying wolf.

Export Controls on AI

To maintain the U.S. advantage in AI, the federal government has used export controls as a tool to restrict access to AI chips to other countries, particularly China, based on the assumption that this approach may help maintain the technological edge the United States holds over other countries.

Increased global tension over the possession and distribution of chips started in 2018 when the Trump Administration cut off Chinese chipmaker Fujian Jinhua Integrated Circuit from its U.S. suppliers. Since then, the United States has been implementing restrictions on the export of chips, including in 2022, when it restricted China's access to Nvidia's A100 and H100 chips – which are high-performance GPUs optimized for AI and other high-performance computing (HPC) applications. More recently, the Biden Administration introduced the Framework for Artificial Intelligence Diffusion, which outlined the U.S. position on the global diffusion of AI through the levying of AI export controls on more countries and introduced controls on closed AI model weights, the parameters that define how an AI model learns. The framework established three tiers of countries with different

levels of access: Tier 1 countries (the United States and 18 key partners) have no restrictions; Tier 2 countries (150 other nations) can receive exports only through companies that have joined the data center authorization program or have obtained individual licenses; and Tier 3 countries (arms-embargoed countries), which remain under strict export restrictions.

Nvidia developed the H20 chip specifically to target the Chinese market and comply with the Biden-era export controls. The H20's computer power is only 15 percent of the H100, and much of the chip's functionality had been eliminated to ensure Chinese AI developers couldn't outpace U.S. firms. Despite the restrictions, the Trump Administration blocked the sale of these chips to China in April, arguing the action is necessary to safeguard U.S. national and economic security.

Taxing Exports of AI Chips

The Trump Administration reversed course on the H20 chip in late July, a move largely tied to trade negotiations with China.

In isolation, the decision to allow the sale of the chips doesn't necessarily raise concerns. As American Action Forum has previously highlighted, widespread restrictions on the sale of chips and AI models could stifle innovation and limit opportunities for U.S. firms in global markets. U.S. export controls severely limit AI companies' ability to operate in Tier 2 countries, discouraging global customers who may turn to alternative suppliers with fewer barriers, such as China. Further, by relying on fixed, rigid categories that consider countries' chip accessibility in tiers, the United States often fails to adapt quickly enough to the fast-paced advancements in AI. Finally, allowing some level of increased security risks from the sale of H20 chips could be offset by security benefits from accessing rare earth materials in a trade deal, and the relative tradeoffs are exactly the type of calculation the Trump Administration should be exploring.

The deal wasn't in isolation, however, and in early August the full picture became clear. In exchange for allowing Nvidia to sell these chips in China, Nvidia agreed to pay what amounts to a 15 percent export tax on the chips, casting doubt on the security justifications for the export restrictions.

This decision highlights a concerning trend in the administration. Previously, Congress passed a law banning the application TikTok, largely due to the national security concerns the Chinese-owned app presented. Yet TikTok is still operating in the United States because the Trump Administration refuses to enforce the law, going so far as to pressure application store operators to keep the app listed despite being a clear violation of the law. And beyond

the technology sector, the administration previously reversed course on a merger between Nippon Steel and U.S. Steel after the firms agreed to give the U.S. government significant control over the combined firms.

These decisions suggest two possible rationales, either of which is concerning: the security concerns used to justify these protections were overstated, or the administration is willing to ignore the security risks to Americans to gain leverage and control over different sectors of the economy.

Broader Policy Implications

U.S. policymakers should not ignore the national security risks that China presents, but as the Trump Administration appears to repeatedly ignore these risks for its own gain, it will become more difficult to convince policymakers that national security risks justify regulatory intervention. Currently, almost every technology policy area has at least some national security component to it, such as the Federal Communications Commission banning a variety of Chinese equipment and some in Congress calling for a national privacy law often relying in part on cybersecurity and thus national security justifications.If a new security risk arises that justifies congressional action, lawmakers may be reluctant to pass legislation if they feel that they have been misled about security risks in the past.

Further, Congress should carefully consider future grants of authority to the executive branch. If the Trump Administration – or any administration – makes deals regardless of security concerns, and that go beyond congressional delegation of authority, what other deals may come through in the future? China could get a deal soon on TikTok because the administration wants to use it in trade negotiations, and Japan got a deal with Nippon Steel by giving the Trump Administration significant control over the combined entities. If Congress has security concerns, lawmakers should be skeptical of granting even more authority to the White House moving forward.