

# Final Rule Implementing U.S. Outbound Investments Restrictions Goes into Effect

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On October 28, 2024, the U.S. Department of Treasury (Treasury Department) published a final rule (Final Rule) setting forth the regulations implementing Executive Order 14150 of August 9, 2023 (Outbound Investment Order), creating a scheme regulating U.S. persons' investments in a country of concern involving semiconductors and microelectronics, quantum information technologies and artificial intelligence sectors[1]. According to the Annex to the Outbound Investment Order, China (including Hong Kong and Macau) is currently the only identified "Country of Concern". The Final Rule went effective on January 2, 2025.

## Who are the in-scope persons?

The Final Rule regulates the direct and indirect involvement of "U.S. Persons", which is broadly defined to include (i) any U.S. citizen, (ii) any lawful permanent resident, (iii) any entity organized under the laws of the United States or any jurisdiction within the United States, including any foreign branches of any such entity, and (iv) any person in the U.S.

The Final Rule requires a U.S. Person to take all reasonable steps to prohibit a "Controlled Foreign Entity", a non-U.S. incorporated/organized entity, from making outbound investments that would be prohibited if undertaken by a U.S. Person. As such, the Final Rule extends its influence over any Controlled Foreign Entity of such U.S. Person.

The Final Rule also prohibits a U.S. Person from knowingly directing a transaction that would be prohibited by the Final Rule if engaged by a U.S. Person.

## Which outbound investments are in-scope?

The "Covered Transactions" include investment, loan and debt financing conferring certain investor rights characteristic of equity investments, greenfield or brownfield investments and investment in a joint venture ("JV") or fund, relating to a "Covered Foreign Person" (as discussed below), as described below:

1. **Equity investment:** (i) acquisition of equity interest or contingent equity interest in a Covered Foreign Person; (ii) conversion of contingent equity interest (acquired after the effectiveness of the Final Rule) into equity interest in a Covered Foreign Person;
2. **Loan or debt financing:** provision of loan or debt financing to a Covered Foreign Person, where the U.S. Person is afforded an interest in profits, the right to appoint a director (or equivalent) or other comparable financial or governance rights characteristic of an equity investment but not typical of a loan;
3. **Greenfield/brownfield investment:** acquisition, leasing, development of operations, land, property, or other asset in China (including Hong Kong and Macau) that the U.S. Person knows will result in the establishment or engagement of a Covered Foreign Person; and
4. **JV/ fund investment:** (i) entry into a JV with a Covered Foreign Person that the U.S. Person knows will or plan to engage in covered activities; (ii) acquisition of limited partner or equivalent interest in a non-U.S. Person venture capital fund, private equity fund, fund of funds, or other pooled investment fund that will engage in a transaction that would be a Covered Transaction if undertaken by a U.S. Person.

## What are in-scope transactions and carve-out transactions?

The Final Rule identifies three categories of Covered Transactions involving covered foreign persons – Notifiable Transactions, Prohibited Transactions, and Excepted Transactions.

A “Covered Foreign Person” includes the following persons engaging in “Covered Activities” (i.e. Notifiable or Prohibited Activities identified in the Final Rule) relating to a Country of Concern:

1. A person of China, Hong Kong or Macau, including an individual who is a citizen or permanent resident of China (including Hong Kong and Macau and are not a U.S. citizen or permanent resident of the United States); an entity organized under the laws of China (including Hong Kong and Macau), or headquartered in, incorporated in, or with a principal place of business in China (including Hong Kong and Macau); the government of China (including Hong Kong and Macau); or an entity that is directly or indirectly owned 50% or more by any persons in any of the aforementioned categories.
2. A person directly or indirectly holds a board, voting rights, equity interests, or contractual power to direct or cause the management or policies of any person that derives 50% or more of its revenue or net income or incur 50% or more its capital expenditure or its operating expenses (individually or as aggregated) from China (including Hong Kong and Macau) (subject to a \$50,000 in minimum); and
3. A person from China (including Hong Kong or Maca) who enters a JV that engages, plans to or will engage in a Covered Activity.

## Notifiable and Prohibited Transactions

The Final Rule:

1. Requires U.S. Persons to notify the Treasury Department regarding transactions involving covered foreign persons that fall within the scope of Notifiable Transactions, and
2. Prohibits U.S. Persons from engaging in transactions involving Covered Foreign Persons that fall within the scope of Prohibited Transactions.

The underlying consideration for the delineation between a Notifiable Transactions and Prohibited Transactions hinges on how impactful it is as a threat to the national security of the United States — a

Notifiable Transaction contributes to national security threats, while a Prohibited Transaction poses a particularly acute national security threat because of its potential to significantly advance the military intelligence, surveillance, or cyber-enabled capabilities of a Country of Concern.

Specifically, a Notifiable Transaction necessarily involves the following Notifiable Activities, while a Prohibited Transaction necessarily involves the following Prohibited Activities:

Prohibited Activities	Notifiable Activities
<b>Semiconductors &amp; Microelectronics</b>	<ul style="list-style-type: none"> <li>- Develops or produces any electronic design automation software for the design of integrated circuits (ICs) or advanced packaging;</li> <li>- Develops or produces (i) equipment for (a) performing volume fabrication of integrated circuit, or (b) performing volume advanced packaging, or (ii) commodity, material, software, or technology designed exclusively for extreme ultraviolet lithography fabrication equipment;</li> <li>- Designs any integrated circuits that meet or exceed certain specified performance parameters[2] or is designed exclusively for operations at or below 4.5 Kelvin;</li> <li>- Fabricates integrated circuits with special characteristics;[3]</li> <li>- Packages any IC using advanced packaging techniques.</li> </ul>
<b>Quantum Information Technology</b>	<ul style="list-style-type: none"> <li>- Develops, installs, sells, or produces any supercomputer enabled by advanced ICs that can provide a theoretical compute capacity beyond a certain threshold;[4]</li> <li>- Develops a quantum computer or produces any critical components;[5]</li> <li>- Develops or produces any quantum sensing platform for any military, government intelligence, or mass-surveillance end use;</li> <li>- Develops or produces any quantum network or quantum communication system designed or used for certain specific purposes.[6]</li> </ul>
<b>Artificial Intelligence (AI)</b>	<ul style="list-style-type: none"> <li>- Develops any AI system that is designed or used for any military end use, government intelligence, or mass-surveillance end use;</li> <li>- Develops any AI system that is trained using a</li> </ul>

	quantity of computing power greater than (a) $10^{25}$ computational operations; and (b) $10^{24}$ computational operations using primarily biological sequence data.
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## Excepted Transactions

The Final Rule sets forth the categories of Excepted Transactions, which are determined by the Treasury Department to present a lower likelihood of transferring tangible benefits to a Covered Foreign Person or otherwise unlikely to present national security concerns. These include:

1. **Investment in publicly traded securities:** an investment in a publicly traded security (as defined under the Securities Act of 1934) denominated in any currency and traded on any securities exchange or OTC in any jurisdiction;<sup>[7]</sup>
2. **Investment in a security issued by a registered investment company:** an investment by a U.S. Person in the security issued by an investment company or by a business development company (as defined under the Investment Company Act of 1940), such as an index fund, mutual fund, or ETF;
3. **Derivative investment:** derivative investments that do not confer the right to acquire equity, right, or assets of a Covered Foreign Person;
4. **Small-size limited partnership investment:** limited partnership or its equivalent investment (at or below two million USD) in a venture capital fund, private equity fund, fund of funds, or other pooled investment fund where the U.S. Person has secured a contractual assurance that the fund will not be used to engage in a Covered Transaction;
5. **Full Buyout:** acquisition by a U.S. Person of all equity or other interests held by a China-linked person, in an entity that ceases to be a Covered Foreign Person post-acquisition;
6. **Intracompany transaction:** a transaction between a U.S. Person and a Controlled Foreign Entity (subsidiary) to support ongoing operations or other activities are not Covered Activities;
7. **Pre-existing binding commitment:** a transaction for binding, uncalled capital commitment entered into before January 2, 2025;
8. **Syndicated loan default:** acquisition of a voting interest in a Covered Foreign Person by a U.S. Person upon default of a syndicated loan made by the lending syndicate and with

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passive U.S. Person participation; and

9. **Equity-based compensation:** receipt of employment compensation by a U.S. Person in the form of equity or option incentives and the exercising of such incentives.

## **What is the knowledge standard?**

The Final Rule provides that certain provisions will only apply if a U.S. Person has Knowledge of the relevant facts or circumstances at the time of a transaction. “Knowledge” under the Final Rule includes (a) actual knowledge of the existence or the substantial certainty of occurrence of a fact or circumstance, (b) awareness of high probability of the existence of a fact, circumstance or future occurrence, or (c) reason to know of the existence of a fact or circumstance.

The determination of Knowledge will be made based on information a U.S. Person had or could have had through a reasonable and diligent inquiry, which should be based on the totality of relevant facts and circumstances, including without limitation, (a) whether a proper inquiry has been made, (b) whether contractual representations or warranties have been obtained, (c) whether efforts have been made to obtain and assess non-public and public information; (d) whether there is any warning sign; and (e) whether there is purposeful avoidance of efforts to learn and seek information.

## **Key points relating to the notification filing procedures**

A U.S. person’s obligation to notify the Treasury Department is triggered when they know relevant facts or circumstances related to a Notifiable Transaction entered into by itself or its Controlled Foreign Entity. U.S. Person shall follow the electronic filing instructions to submit the electronic filing at <https://home.treasury.gov/policy-issues/international/outbound-investment-program>.

The filing of the notification is time-sensitive. The filing deadline is no later than 30 days following the completion of a Notifiable Transaction or otherwise no later than 30 days after acquiring such knowledge if a U.S. Person becomes aware of the transaction after its completion. If a filing is made prior to the completion of a transaction and there are material changes to the information in the original filing, the notifying U.S. Person shall update the notification no later than 30 days following the completion of the transaction.

In addition to the detailed information requested under the Final Rule, a certification by the CEO or other designees of the U.S. Person is required to certify the accuracy and completeness in material respects of the information submitted.

## **What are the consequences of non-compliance?**

The Treasury Department may impose civil and administrative penalties for any Final Rule violations, including engaging in Prohibited Transactions, failure to report Notifiable Transactions, making false representation or omissions, or engaging in evasive actions or conspiracies to violate the Final Rule. The Treasury Department may impose fines, require divestments, or refer for criminal prosecutions to the U.S. Department of Justice for violations of the Final Rule.

U.S. Persons may submit a voluntary self-disclosure if they believe their conduct may have violated any part of the Final Rule. Such self-disclosure will be taken into consideration during the Treasury Department’s determination of the appropriate response to the self-disclosed activity.

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