

## AT LONG LAST: TREASURY ISSUES IMPLEMENTING REGULATIONS ON OUTBOUND U.S. INVESTMENTS

On October 28, 2024, the U.S. Department of the Treasury ("**Treasury**") issued a final rule (the "**Final Rule**") providing the regulations for the new "**Outbound Investment Security Program**." The Final Rule implements the August 9, 2023 [Executive Order](#) ("**EO**")<sup>1</sup> 14105, "Addressing United States Investments in Certain National Security Technologies and Products in Countries of Concern." As described in further detail below, the Final Rule (1) requires U.S. persons to notify Treasury of certain direct or indirect transactions with "Covered Foreign Persons" (which includes Chinese persons and entities in the PRC, Hong Kong, and Macau) involving specified groups of sensitive technologies and products; and (2) prohibits U.S. persons from engaging, directly or indirectly, in other such transactions. The Final Rule takes effect on January 2, 2025, and will apply to transactions with a completion date on or after January 2, 2025.

The Final Rule comes after more than a year of rulemaking under EO 14105 and follows the August 9, 2024, Advanced Notice of Proposed Rulemaking ("**ANPRM**") and June 21, 2024, Notice of Proposed Rulemaking ("**NPRM**"). As the Treasury [Press Release](#) and [Fact Sheet](#) describe, the Final Rule identifies the subsets of technologies and products within the (i) semiconductors and microelectronics, (ii) quantum information technologies; and (iii) artificial intelligence ("**AI**") sectors and fully implements the Outbound Investment Security Program, designed to disrupt the ability of "countries of concern"<sup>2</sup> to obtain financial and intangible benefits to develop sensitive technologies counter to U.S. national security.

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<sup>1</sup> Treasury Press Release at 3.

<sup>2</sup> "Countries of concern" currently include China, Hong Kong, and Macao.

## I. WHO DOES THE FINAL RULE APPLY TO

As we previously described in our alert and blog post on the NPRM (available [here](#) and [here](#)), the Final Rule applies to all "**U.S. Persons**", globally, which includes "any United States citizen or lawful permanent resident, entity organized under the laws of the United States or any jurisdiction within the United States, including any foreign branch of any such entity, or any person in the United States."<sup>3</sup> The definition of U.S. Person remains unchanged from the NPRM.

The Final Rule applies to direct or indirect U.S. Person involvement in "**Covered Transactions**"<sup>4</sup>, which includes, among other transactions, certain U.S. Person equity interests, greenfield investments, debt financing where the lender obtains certain management or governance rights, real estate transactions, and LP interests in pooled investment funds (in certain circumstances), involving "**Covered Foreign Persons**."

**Covered Foreign Persons** include Chinese persons and entities (including the PRC, Hong Kong and Macau) engaged in certain activities related to the defined subsets of technologies and products. Under the Final Rule, such persons would include:

- individuals who are citizens or permanent residents of China (including the PRC, Hong Kong and Macau) and not also a U.S. citizen or permanent resident of the United States;
- entities organized under the laws of, or headquartered, incorporated in, or with a principal place of business in, China;
- the government of China and persons acting on the government's behalf; and
- entities directly or indirectly owned, in aggregate, 50% or more by any of the above categories, regardless of location.

Additionally, the Final Rule captures certain transactions involving an entity that has a voting interest, board seat, equity interest, or holds any power to direct or cause the direction of the management or policies in a covered foreign person where more than 50 percent of one of several key financial metrics of the entity is attributable to such covered foreign person.

## II. WHAT DOES THE FINAL RULE APPLY TO

The Final Rule includes **prohibition** and **notification requirements**.

**Prohibitions:** The Final Rule prohibits U.S. persons from engaging, directly or indirectly, in certain Covered Transactions with Chinese Persons involving specified products and technologies in the (i) semiconductors and microelectronics, (ii) quantum information technologies; and (iii) AI sectors.

Additional information on prohibited transactions is included in the chart below.

**Notifications:** U.S. persons are required to notify Treasury for certain other transactions, under a notification process described in the final rule. This includes completing and submitting an electronic form on Treasury's Outbound Investment

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<sup>3</sup> Final Rule at § 850.229.

<sup>4</sup> Defined at Final Rule at 93-94.

Security Program website within specified timelines.<sup>5</sup> More specifically, the Final Rule requires U.S. persons to (i) file notifications no later than 30 days following the closing of a Covered Transaction,<sup>6</sup> or (ii) where a U.S. Person does not have "knowledge" (defined as actual knowledge, an awareness of a high probability, or reason to know)<sup>7</sup> at the time of a transaction, within 30 days of acquiring actual knowledge after a transaction completion date.<sup>8</sup> Unlike submissions under the Committee on Foreign Investment in the United States ("**CFIUS**") regulations, notifications are not subject to a review and approval process.

However, the Final Rule provides Treasury authorization to request additional information, including documents, related to the notified transaction.

Notably, a Covered Transaction that may otherwise be only subject to the notification requirements will be prohibited when such transactions include the involvement of a Covered Foreign Person that is on one of several U.S. government lists, such as the Department of Commerce's Bureau of Industry and Security ("**BIS**") Entity List, the BIS Military End User List (or meets the BIS definition of a "Military Intelligence End User"), the Office of Foreign Assets Control list of Specially Designated Nationals ("**SDN List**"), the Department of the Treasury's list of non-SDN Chinese Military Industrial Complex Companies ("**NS-CMIC List**"), or has been designated as a foreign terrorist organization by the Secretary of State under 8 U.S.C. 1189.<sup>9</sup>

Notification and prohibition requirements extend to certain indirect U.S. person transactions, including transactions by a U.S. person's "controlled foreign entity." For example, a U.S. person must submit a notification for a transaction conducted by its "controlled foreign entity" if the transaction falls into the category of those which would require notification for the U.S. person to engage in directly. U.S. persons are also required to take "all reasonable steps" to prohibit and prevent controlled foreign entities from completing a transaction that would be prohibited if undertaken by the U.S. person. The Final Rule includes factors that Treasury will consider when determining whether a U.S. person took such steps.

Finally, the Final Rule imposes other obligations on U.S. persons related to certain Covered Transactions. This includes prohibiting U.S. persons from knowingly directing non-U.S. persons to engage in an otherwise prohibited transaction.

A summary of the prohibition and notification requirements in the Final Rule is included in the chart<sup>10</sup>, below:

Type of Technology	Prohibited Transactions	Notifiable Transactions
<b>Semiconductors and Microelectronics</b>	Covered transactions related to certain electronic design automation software; certain	Covered transactions related to the design, fabrication, or packaging of integrated circuits not

<sup>5</sup> Treasury will provide additional information about the electronic filing process prior to when the Final Rule takes effect.

<sup>6</sup> Final Rule at § 850.403.

<sup>7</sup> Final Rule at § 850.216.

<sup>8</sup> Final Rule at § 850.404.

<sup>9</sup> Final Rule at 116-17; § 850.224(m).

<sup>10</sup> Treasury Fact Sheet at 4.

	<p>fabrication or advanced packaging tools; the design or fabrication of certain advanced integrated circuits; advanced packaging techniques for integrated circuits; and supercomputers are prohibited.</p>	<p>otherwise covered by the prohibited transaction definition are subject to a notification requirement.</p>
<p><b>Quantum Information Technologies</b></p>	<p>Covered transactions related to the development of quantum computers or production of any critical components required to produce a quantum computer; the development or production of certain quantum sensing platforms; and the development or production of certain quantum networks or quantum communication systems are prohibited.</p>	<p>None.</p>
<p><b>Certain AI Systems</b></p>	<p>Covered transactions related to the development of any AI system designed to be exclusively used for, or intended to be used for, certain end uses are prohibited. In addition, covered transactions related to the development of any AI system that is trained using a quantity of computing power greater than <math>10^{25}</math> computational operations, or trained using primarily biological sequence data and a quantity of computing power greater than <math>10^{24}</math> computational operations, are prohibited.</p>	<p>Covered transactions related to the development of any AI system not otherwise covered by the prohibited transaction definition, where such AI system is: designed or intended to be used for certain end uses or applications; or trained using a quantity of computing power greater than <math>10^{23}</math> computational operations, are subject to a notification requirement.</p>

### III. ARE THERE ANY EXCEPTIONS

The Final Rule includes exceptions for certain transactions, provided all required conditions are met, including but not limited to the following types of transactions<sup>11</sup>:

- **"Publicly traded securities:** *An investment by a U.S. person in a publicly traded security or a security issued by a registered investment company, such as an index fund, mutual fund, or exchange-traded fund;*
- **Certain LP investments:** *A U.S. person's investment made as an LP in a venture capital fund, private equity fund, fund of funds, or other pooled investment fund, if such investment is \$2,000,000 or less or if the U.S. person has received a contractual assurance that its capital will not be used by the fund to engage in what would be a prohibited or notifiable transaction;*
- **Derivatives:** *A U.S. person's investment in certain derivative securities;*
- **Buyouts of country of concern ownership:** *A U.S. person's full buyout of all country of concern ownership of an entity, such that the entity does not constitute a covered foreign person following the transaction;*
- **Intracompany transactions:** *An intracompany transaction between a U.S. person and its controlled foreign entity to support operations that are not covered activities or to maintain ongoing operations with respect to covered activities that the controlled foreign entity was engaged in prior to January 2, 2025;*
- **Certain pre-Final Rule binding commitments:** *A transaction fulfilling a binding, uncalled capital commitment entered into prior to January 2, 2025;*
- **Certain syndicated debt financings:** *Where the U.S. person, as a member of a lending syndicate, acquires a voting interest in a covered foreign person upon default and the U.S. person cannot initiate any action vis-à-vis the debtor and is not the syndication agent;*
- **Equity-based compensation:** *A U.S. person's receipt of employment compensation in the form of an award or grant of equity or an option to purchase equity in a covered foreign person, or the exercise of such option; and*
- **Third-country measures:** *Certain transactions involving a person of a country or territory outside of the United States may be excepted transactions where the Secretary of the Treasury determines that the country or territory is addressing national security concerns related to outbound investment and the transaction is of a type for which associated national security concerns are likely to be adequately addressed by the actions of that country or territory."*

However, any transaction which otherwise would qualify for an exception but affords a U.S. Person certain rights that are not standard minority shareholder protections does not qualify as an excepted transaction.<sup>12</sup>

<sup>11</sup> Final Rule at § 850.501; Treasury Fact Sheet at 3.

<sup>12</sup> Treasury Fact Sheet at 3; Final Rule at § 850.501.

In addition to the above, the Final Rule also provides a process for a U.S. Person to seek an exemption from notification and prohibition requirements if the Covered Transaction is deemed to be in the national interest of the United States.<sup>13</sup> This request will be reviewed and actioned by the Secretary of the Treasury, in consultation with the Secretary of Commerce, the Secretary of State, and other relevant agencies.

#### **IV. WHO WILL ADMINISTER THE OUTBOUND INVESTMENT SECURITY PROGRAM**

The newly-announced Office of Global Transactions within Treasury's Office of Investment Security will administer the Outbound Investment Security Program.<sup>14</sup>

#### **V. WHAT ARE THE POSSIBLE PENALTIES**

Under the Final Rule, Treasury would have the power to, among other things: (1) investigate and make requests for information from parties related to a notifiable or prohibited transaction "at any time," including through holding hearings, examining witnesses, receiving evidence, taking depositions, and requiring by subpoena the attendance and testimony of witnesses and production of documents; (2) nullify, void, or compel the divestment of a prohibited transaction entered into after the regulations issued under the EO take effect; and (3) refer potential criminal violations to the U.S. Department of Justice for prosecution.

Violations of the Final Rule will be subject to civil and criminal penalties as set forth in the International Emergency Economic Powers Act ("**IEEPA**"). As of the issuance of the Final Rule, the maximum civil penalty for a violation is the greater of approximately \$370,000 or twice the value of the transaction that is the basis of the violation.<sup>15</sup> Violations may also be referred to the Department of Justice for criminal prosecution. Criminal penalties can reach up to \$1 million and 20 years imprisonment (for individuals).

#### **CONCLUSION**

The Final Rule is the culmination of (at least) two years of efforts by the U.S. Government to implement the Outbound Investment Security Program as part of a wider strategy to limit U.S. investments that pose threats to U.S. national security. It imposes targeted but significant new regulatory obligations on U.S. Persons investors. It is critical for investors, globally, to consider how this Final Rule might influence their investment plans and to establish processes for identifying potentially covered transactions, including for rejecting prohibited transactions and submitting required notifications, as necessary. Non-U.S. companies with U.S. person employees, directors, owners, investors, and other U.S. person involvement, are advised to consider implementing risk-based recusal procedures and consider other risk-based mitigation for the U.S. person employees, directors, and owners.

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<sup>13</sup> Treasury Fact Sheet at 3; Final Rule at § 850.502.

<sup>14</sup> Treasury Fact Sheet at 3.

<sup>15</sup> Treasury Fact Sheet at 5; Final Rule at Subpart G (§§ 850.701 – 850.704).

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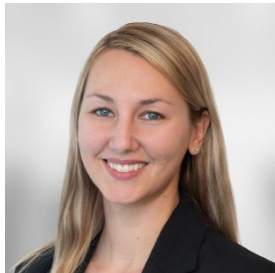
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