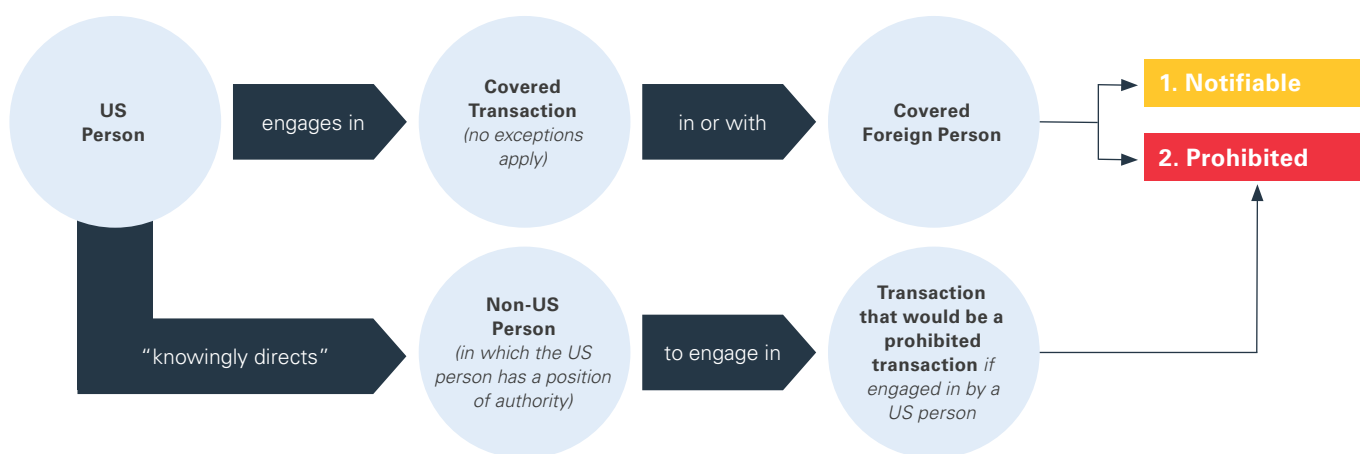


On October 28, 2024, the Department of the Treasury’s (Treasury) Office of Investment Security issued a [final rule](#)¹ (“Final Rule” or “Outbound Investment Regulations”) containing the regulations that will implement, effective on January 2, 2025, an outbound investment regulatory regime that captures certain types of US person-involved investments in, or with, Chinese interests if the investment involves any of three key technology areas: quantum information technologies, semiconductors and microelectronics, and certain artificial intelligence (AI) technologies. US and non-US companies involved in or planning to participate in one or more of the key technology areas must be intimately familiar with the scope and application of these regulations to avoid liability. The regulations create new due diligence obligations on such businesses, and non-compliance is subject to the same severe penalties as Office of Foreign Asset Control (OFAC) sanctions violations. This publication provides a summary of the Outbound Investment Regulations established by the Final Rule, and offers considerations for enterprises potentially affected by the new regulatory program.

Overview of the Outbound Investment Regulatory Program

The Outbound Investment Regulations implement the August 9, 2023, Executive Order that mandated Treasury to address investments with “countries of concern” and involving certain technologies and products critical to national security.² In the Executive Order, the President identified only China as a “country of concern,” but the President has the authority to designate other countries in the future.

Under the Final Rule, certain outbound investments by, or in some cases under the direction of, US persons will be prohibited or subject to notification requirements. How to comply with the requirements will depend on whether a “US person” is engaged in a “covered transaction” with a “covered foreign person,” as each of these terms are defined in the Outbound Regulations.



1. Scope of “US Persons” Compliance Obligations

The Final Rule pushes compliance onto “US persons.” A US person includes any United States citizen, lawful permanent resident, any entity organized under the laws of the United States, and any person physically in the United States. As discussed further below, the Final Rule also reaches US persons through their controlled non-US entities (i.e., foreign subsidiaries).

The Final Rule requires US persons to exercise “reasonable and diligent inquiry” to obtain “knowledge” as to whether relevant facts or circumstances exist concerning potentially relevant transactions. The knowledge standard under the Final Rule mirrors that employed under the Export Administration Regulations (EAR)³ and includes “an awareness of a high probability of a fact or circumstance’s existence or future occurrence, or reason to know of a fact or circumstance’s existence.”⁴ And as with compliance under the EAR, the presence of contractual assurances to prevent violations of the Outbound Regulations is one of the key factors Treasury will consider in ascertaining whether a US person undertook “reasonable and diligent inquiry” in relation to the knowledge standard.⁵

¹ *Provisions Pertaining to US Investments in Certain National Security Technologies and Products in Countries of Concern* (to be codified at 31 C.F.R. Part 850).

² Exec. Order No. 14,105 *Addressing United States Investments in Certain National Security Technologies and Products in Countries of Concern*, 88 Fed. Reg. 54867 (Aug. 9, 2023).

³ See 15 C.F.R. 772.1.

⁴ 31 C.F.R. § 850.216.

⁵ 31 C.F.R. § 850.104(c)(2).

Further, the Final Rule includes the refusal to make contractual assurances as a “warning sign” (i.e., a red flag), among those indicia that can contribute to creating a presumption of “knowledge” by a US person.⁶ The compliance obligation does not stop at only the actions of the US person. Under the Final Rule, US persons will be responsible for: (a) taking steps to ensure controlled non-US entities do not engage in transactions that would be prohibited if done by US person; and (b) for “knowingly directing” transactions by non-US persons.

(a) US Persons to Push Down Compliance to Non-US Subsidiaries

The Final Rule requires that a “US person shall take *all reasonable steps* to prohibit and prevent any transaction by its controlled foreign entity that would be a prohibited transaction if engaged in by a US person.”⁷ Treasury will consider the following factors to determine the adequacy of compliance measures of the US parent, and its controlled entity with regard to the Outbound Investment Regulations: compliance agreements between the US person and its controlled foreign entity; the existence and exercise of shareholder rights by the US person with respect to the controlled foreign entity; the existence and implementation of periodic training and internal reporting requirements; and the implementation, periodic review, and documented testing of appropriate internal controls. These factors will be crucial to Treasury’s findings of violations of US persons through their controlled foreign entities, as well as in the determination of appropriate penalties and enforcement measures.⁸

(b) US Persons Cannot “Knowingly Direct” Investments by Non-US Persons

Treasury has defined “knowingly directing” as when a US person “has authority, individually or as part of a group, to make or substantially participate in decisions on behalf of a non-US person, and exercises that authority to direct, order, decide upon, or approve” a transaction. The Final Rule states that this authority “exists when a US person is an officer, director, or otherwise possesses executive responsibilities at a non-US person.”⁹

2. Types of “Covered Transactions” that Fall Within the Regulations

(a) Types of Covered Investments

The new program includes acquisitions of equity or contingent interests, greenfield and brownfield investments, joint ventures, certain investments made as a limited partner, and certain debt financing transactions by US persons. The program also includes the conversion of contingent interests that were acquired after the Final Rule goes into effect. Further, the program includes “indirect” transactions, including a US person’s use of an intermediary entity to undertake a transaction that would otherwise be subject to prohibition or notification.¹⁰

(b) Excepted Transactions

Excepted transactions include US investments into publicly-traded securities, index funds, mutual funds, exchange-traded funds, certain investments made as a limited partner, complete buyouts, certain intracompany transfers of funds from a US parent to its foreign subsidiary, committed but uncalled capital investments, and compensation for individual employment in the form of equity awards or stock options.¹¹ However, Treasury indicated that any investment that affords a US person rights beyond standard minority shareholder protections, such as membership or observer rights, nomination rights, or involvement in substantive business decisions, will not be excepted.¹² Additionally, the Secretary of the Treasury may designate additional transaction types as excepted transactions, in consultation with the Secretary of Commerce and the Secretary of State.¹³

6 31 C.F.R. § 850.104(c)(6).

7 31 C.F.R. § 850.302(a) (*emphasis added*).

8 31 C.F.R. § 850.302(b).

9 31 C.F.R. § 850.303.

10 31 C.F.R. § 850.210.

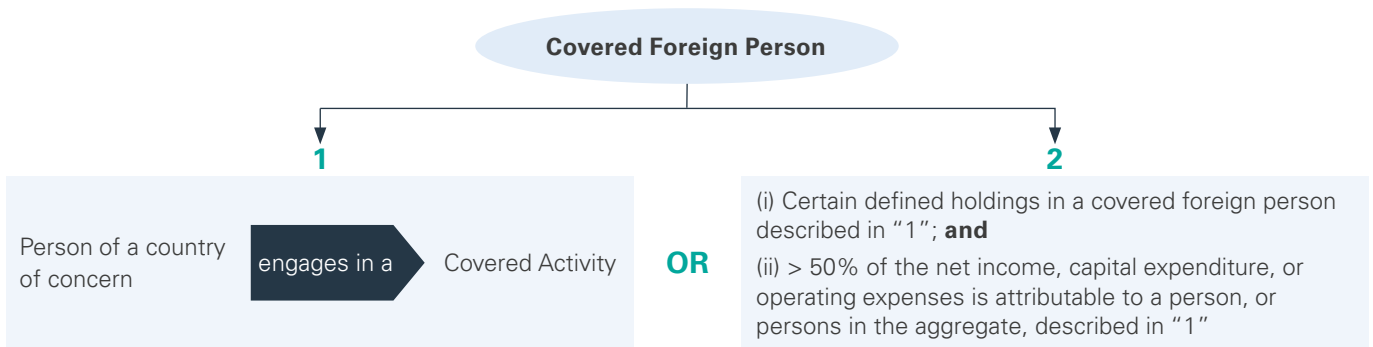
11 31 C.F.R. § 850.501(a – f).

12 31 C.F.R. § 850.501(a).

13 31 C.F.R. § 850.501(g).

(c) Understanding “Covered Foreign Persons”

Understanding whether a party is a “covered foreign person” is essential to understanding compliance obligations, requiring reasonable due diligence to assess. The Final Rule provides for two ways in which a party could be a “covered foreign person,” either because of the party’s activities or because the party has some control over a covered foreign person and meets certain economic metrics in relation to that holding.



First, a covered foreign person is any “person of a country of concern” (i.e., any entity organized under the laws of or having a principal place of business in China or being majority-owned by Chinese individuals or entities) that is engaged in a “covered activity.” A covered activity is any of the activities that falls within the parameters of a notifiable transaction or a prohibited transaction (see summary chart of such activities attached to this publication).

Second, a covered foreign person also includes any person that directly or indirectly holds certain rights, or interest in a covered foreign person described above and through that holding derives or incurs certain economics on an annual basis, as follows:

Directly or indirectly hold: <ul style="list-style-type: none"> • Board seat; • Voting or equity interest (unless an “excepted transaction”); or • Any contractual power to direct or cause the direction of the management or policies 	Economic impact from the holding: <ul style="list-style-type: none"> • > 50 percent of revenue or net income • > 50 percent of capital expenditure • > 50 percent of operating expenses
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(d) Identified “Covered Transactions” Subject to Prohibition or Notification

As provided in the EO, the Final Rule identifies certain functions relating to particular national security technologies and products which constitute “covered activities” and can cause a transaction to be a “covered transaction” under the Final Rule. A covered transaction may include a technology or product related to:

- **Semiconductors and Microelectronics**
 - **Prohibited transactions** – Software for electronic design automation, equipment for volume fabrication of integrated circuits (ICs), equipment for volume advanced packaging of ICs, inputs for extreme ultraviolet lithography fabrication equipment, advanced IC design, advanced IC fabrication, advanced IC packaging and supercomputers.
 - **Requires notification** – Any other IC fabrication or packaging not otherwise prohibited.
- **Quantum Information Technologies**
 - **Prohibited Transactions** – Quantum computers and components, quantum sensing platforms, and quantum network or quantum communication systems.
 - **Requires Notification** – No separate requirement for quantum information technologies stated in the Final Rule.
- **Artificial Intelligence (AI) Systems**
 - **Prohibited transactions** – AI systems designed to be exclusively used for, or intended to be used for, military, intelligence or surveillance end uses; and AI systems trained using certain quantities of computing power.
 - **Requires notification** – AI systems not otherwise prohibited and designed or intended to be used for certain end uses or applications, or AI systems trained using certain quantities of computing power.

If the relevant foreign person or joint venture engaged in the covered activity falls within certain US restricted party lists, the covered transaction is prohibited (versus there being a notification requirement). These restricted party lists include: the EAR’s Entity List and Military End User List; Treasury’s Specially Designated Nationals and Blocked Persons (SDN) List and Non-SDN Chinese Military-Industrial Complex Companies (NS-CMIC List); or and the list of entities designated as a foreign terrorist organization by the Secretary of State.

A summary chart of the above activities is attached to this article and provides definitions and technology parameters of the Final Rule in greater detail.

3. Notification Review Process

For transactions requiring notification, the Final Rule requires US persons to file through a portal hosted on Treasury's website no later than 30 days following closing of the transaction. The notification requires information about the parties (both the US person and the covered foreign person), details of the transaction/investment, and the covered national security technologies and products. Treasury will post instructions on how to file a notification its [Outbound Investment Security Program website](#) prior to the effective date of the rule (Jan. 2, 2025).

In cases where a US person acquires actual knowledge after the completion date of a transaction that the transaction would have been covered under the regulations, the US person is required to file a notification "promptly" and not later than 30 calendar days after acquiring the actual knowledge. This post-transaction notification is required for covered transactions that would have been either notifiable or prohibited transactions. A post-transaction notification contains the same information as a standard filing with additional requirements for the US person to explain when they became aware of the covered transaction and what pre-transaction diligence occurred. A note to the Final Rule indicates that upon reviewing the facts of a post-transaction notification, Treasury may nevertheless determine that the US person had actual knowledge of the transaction's status prior to the closing.

4. Penalties and Enforcement Actions

Violations of the Final Rule (including attempts to violate or conspiracies to violate) may incur a civil penalty under the International Emergency Economic Powers Act (IEEPA) not to exceed the greater of (1) \$250,000 adjusted annually for inflation (currently \$368,136) or (2) twice of the amount of the covered transaction. IEEPA also contains a criminal penalty mechanism for willful violations of the regulations that include fines of not more than \$1 million imprisonment for natural persons of not more than 20 years, or both.

In addition to the civil and criminal penalties above, the Final Rule permits the Secretary of the Treasury to nullify, void, or compel divestment of any transaction that is "entered into" after the effective date and determined to be prohibited under the regulations.

Treasury may assess compliance with the Final Rule through monitoring third-party commercial data, reviewing internal government data, and initiating outreach to an involved entity. If Treasury identifies an instance of non-compliance it will coordinate with law enforcement agencies to investigate the apparent non-compliance and potentially initiate an enforcement action.

Policy Implications and What This Means for Legislative Efforts

The 2023 Executive Order signaled a major shift in how the US will manage its economic relationship with China, especially in how it keeps sensitive technologies out of reach. It and the Final Rule aim to protect this national security interest by limiting US investments that could help China advance in critical areas like quantum computing, semiconductors, and AI. US companies must now closely oversee not only their own actions, but also those of any foreign subsidiaries they control. This means more stringent rules on what they can do abroad, requiring US firms to keep a careful watch on all operations to avoid accidentally boosting China's capabilities in these high-stakes fields.

The Final Rule also ramps-up pressure on compliance. US individuals and companies have to be extra vigilant about whom they're investing in, and which areas are off-limits, especially when it involves Chinese entities working on technology with national security implications. Non-compliance could come with severe financial penalties, and the Treasury Department now has the power to roll back or force divestment from any transactions it deems a security risk. This new set of rules continues the long-standing trend we have observed under which the US has been increasingly relying on its economic instruments of national power to further its national security priorities—here, to ensure that US persons are not supporting, through investment activities, the development of sensitive technologies to help advance China's strategic interests.

Notably, the Final Rule comes amid ongoing debate among lawmakers about the most effective approach to outbound investment review more broadly. While there is bipartisan and bicameral consensus on the need for codification of outbound regulation, lawmakers have differing opinions on the best method. In the Senate, Senators Casey (D-PA) and Cornyn (R-TX) have proposed a notification-only system for US persons making investments or engaging in economic activities linked to North Korea, China, Russia, or Iran. This proposal would cover transactions across six sectors: advanced semiconductors and electronics, AI, quantum information science and technology, hypersonics, satellite-based communications, and networked laser scanning systems with dual-use applications—a more expansive list of sectors than in Treasury's Outbound Investment Regulations.

By contrast, House lawmakers continue to debate whether to codify a sectoral approach like the Executive Order and Senate proposal or list-based restrictions. Whether Congress can agree on a compromise approach, and how any future law may align with, expand, or even supersede the Treasury framework, remains unclear. Regardless, the Final Rule represents a significant new world in how stakeholders approach outbound investment, and that landscape will likely continue to evolve over the coming years.

Considerations for Potentially Affected Businesses

The Final Rule creates a new outbound investment regulatory program that goes into effect on January 2, 2025, applicable to businesses and investors operating in the key sectors identified: (1) semiconductors and microelectronics, (2) quantum information technologies, and (3) AI. The new regulatory program will require businesses to institute new compliance measures or risk significant penalties. At the outset, firms should assess whether any of their operations or investments (portfolio companies) are in any of the covered activity areas that could trigger compliance obligations and where within their organizations are “US persons,” if any. The answers to these questions will inform the level of compliance necessary. Due diligence processes to assess whether investment partners are covered foreign persons must be implemented, and new contractual representations and warranties should be used to satisfy the knowledge requirement under the Final Rule. Beyond the US, these measures will have an impact on non-US parties with connections to Chinese businesses involved in covered activities as they are likely to face heightened due diligence from US-based entities that are now required to establish knowledge that a deal is not a covered transaction.

Any party interested in learning more about the Final Rule should reach out to this article’s authors for further information.

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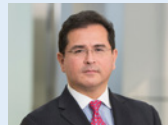
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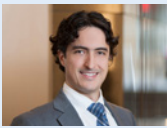
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US Outbound Investment Review Program Proposed Rule:

Activities Proposed to Be Subject to Prohibition or Notification

Pursuant to the [Final Rule](#), issued by the US Department of the Treasury (Treasury) on October 28, 2024 (to be codified at 31 C.F.R. Part 850), to implement the outbound investment review program mandated by President Joe Biden’s Executive Order “[Addressing United States Investments in Certain National Security Technologies and Products in Countries of Concerns](#)” (Exec. Order 14105, 88 Fed. Reg. 54867, Aug. 9, 2023). In the Final Rule, Treasury established prohibitions and notification requirements for US persons undertaking transactions with a covered foreign person engaged in the following activities:

Prohibited	Requires Notification
Semiconductors and Microelectronics	
Software for Electronic Design Automation – The development or production of any electronic design automation software for the design of integrated circuits (IC) or advanced packaging. (§ 850.224(a)).	No related category requiring notification
Equipment for volume fabrication of ICs – The development or production of any front-end semiconductor fabrication equipment designed for the volume fabrication of ICs, including equipment used in the production stages from a blank wafer or substrate to a completed wafer or substrate (i.e., the ICs are processed but they are still on the wafer or substrate). (§ 850.224 (b)(1)).	No related category requiring notification
Equipment for volume advanced packaging of ICs – The development or production of any equipment for performing volume advanced packaging. (§ 850.224 (b)(2)).	No related category requiring notification
Inputs for extreme ultraviolet lithography fabrication equipment – The development or production of any commodity, material, software or technology designed exclusively for use in or with extreme ultraviolet lithography fabrication equipment. (§ 850.224 (b)(3)).	No related category requiring notification
Advanced IC design – The design of any IC that meets or exceeds the performance parameters in Export Control Classification Number (ECCN) 3A090.a. in supplement No. 1 to Part 774 of the Export Administration Regulations (EAR) (15 C.F.R. part 774), or ICs designed for operation at or below 4.5 Kelvin. (§ 850.224(c)).	The design of any other IC not described in § 850.224(c) (§850.217(a))
Advanced IC Fabrication – The fabrication of logic ICs using a non-planar transistor architecture or with a technology node of 16/14 nm or less, including fully depleted silicon-on-insulator (FDSOI) IC (§ 850.224(d)(1));	The fabrication of any other IC not described in § 850.224(d) (§ 850.217(b))
Advanced IC Fabrication – The fabrication of NOT-AND (NAND) memory ICs with 128 layers or more (§ 850.224(d)(2));	

Prohibited	Requires Notification
<p>Advanced IC Fabrication – The fabrication of dynamic random-access memory (DRAM) ICs using a technology node of 18 nm half-pitch or less (§ 850.224(d)(3));</p>	<p>The fabrication of any other IC not described in § 850.224(d) (§ 850.217(b))</p>
<p>Advanced IC Fabrication – The fabrication of ICs manufactured from a gallium-based compound semiconductor (§ 850.224(d)(4));</p>	
<p>Advanced IC Fabrication – The fabrication of ICs using graphene transistors or carbon nanotubes (§ 850.224(d)(5));</p>	
<p>Advanced IC Fabrication – The fabrication of ICs designed for operation at or below 4.5 Kelvin. (§ 850.224(d)(6)).</p>	
<p>Advanced IC Packaging – The packaging of ICs in a manner that supports two-and-one-half dimensional (2.5D) or three-dimensional (3D) assembly of ICs, such as by directly attaching one or more die or wafer using through-silicon vias, die or wafer bonding, heterogenous integration, or other advanced methods and materials. (§ 850.224(e) and § 850.201).</p>	<p>Any other IC Packaging – The term “package” means to assemble various components, such as the IC die, lead frames, interconnects, and substrate materials to safeguard the semiconductor device and provide electrical connections between different parts of the die. (§ 850.217(c) and § 850.218).</p>
<p>Supercomputers – The development, installation, sale, or production of any supercomputer enabled by advanced ICs that can provide a theoretical compute capacity of 100 or more double-precision (64-bit) petaflops or 200 or more single-precision (32-bit) petaflops of processing power within a 41,600 cubic foot or smaller envelope. (§ 850.224(f)).</p>	<p>No related category requiring notification</p>
<p>Quantum Information Technologies</p> <p>A “quantum computer” is defined as a computer that performs computations that arness the collective properties of quantum states, such as superposition, interference, or entanglement. (§ 850.225)</p>	
<p>Quantum Computers and Components – Develops a quantum computer or produces any of the critical components required to produce a quantum computer such as a dilution refrigerator or two-stage pulse tube cryocooler. (§ 850.224(g)).</p>	<p>No separate notification requirement for quantum information technologies.</p>
<p>Quantum Sensing Platforms – Develops or produces any quantum sensing platform designed for, or which the relevant covered foreign person intends to be used for, any military, government intelligence, or mass-surveillance end use. (§ 850.224(h)).</p>	
<p>Quantum Network or Quantum Communication System – Develops or produces any quantum network or quantum communication system designed for, or which the relevant covered foreign person intends to be used for:</p> <p>(1) Networking to scale up the capabilities of quantum computers, such as for the purposes of breaking or compromising encryption;</p> <p>(2) Secure communications, such as quantum key distribution; or</p> <p>(3) Any other application that has any military, government intelligence, or mass-surveillance end use. (§ 850.224(i))</p>	

Artificial Intelligence (AI) Systems

Defined as “a machine-based system that can, for a given set of human-defined objectives, make predictions, recommendations, or decisions influencing real or virtual environments” i.e. a system that “(1) uses data inputs to perceive real and virtual environments; (2) abstracts such perceptions into models through automated or algorithmic statistical analysis; and (3) uses model inference to make a classification, prediction, recommendation, or decision.” Also “any data system, software, hardware, application, tool, or utility that operates in whole or in part using [such] a system.” (§ 850.202)

AI systems for military, intelligence or surveillance –

The development of any AI system that is designed to be exclusively used for, or which the relevant covered foreign person intends to be used for, any:

- (1) Military end use (e.g., for weapons targeting, target identification, combat simulation, military vehicle or weapon control, military decision-making, weapons design (including chemical, biological, radiological, or nuclear weapons), or combat system logistics and maintenance); or
- (2) Government intelligence or mass surveillance end use (e.g., through mining text, audio, or video; image recognition; location tracking; or surreptitious listening devices). (§ 850.224(j)).

AI systems trained using certain quantities of computer power –

The development of any AI system that is trained using a quantity of computing power greater than:

- (1) 10²⁵ computational operations (e.g., integer or floating-point operations); or
- (2) 10²⁴ computational operations (e.g., integer or floating-point operations) using primarily biological sequence data. (§ 850.224(k)).

AI systems for military, intelligence, surveillance, or cybersecurity –

The development of any AI system that is not described in the related category prohibitions (§ 850.224(j) or (k)) and that is:

- (1) Designed to be used for any military end use (e.g., for weapons targeting, target identification, combat simulation, military vehicle or weapons control, military decision-making, weapons design (including chemical, biological, radiological, or nuclear weapons), or combat system logistics and maintenance); or government intelligence or mass-surveillance end use (e.g., through incorporation of features such as mining text, audio, or video; image recognition; location tracking; or surreptitious listening devices);
- (2) Intended by the covered foreign person or joint venture to be used for cybersecurity applications, digital forensics tools; penetration testing tools; or the control of robotic systems; or
- (3) Trained using a quantity of computing power greater than 10²³ computational operations (e.g., integer or floating-point operations).

All notifiable covered activities are prohibited if the relevant foreign person or joint venture falls within any of the following US restricted party lists or designations

Engages in a covered activity, whether referenced in this section or § 850.217 and is:

- Included on the Bureau of Industry and Security’s **Entity List** (15 C.F.R. part 744, supplement no. 4)
- Included on the Bureau of Industry and Security’s **Military End User List** (15 C.F.R. part 744, supplement no. 7)
- Meets the definition of “**Military Intelligence End-User**” by the Bureau of Industry and Security in 15 C.F.R. 744.22(f)(2)
- Included on the Department of the Treasury’s list of Specially Designated Nationals and Blocked Persons (**SDN List**), or is an entity in which one or more individuals or entities included on the SDN List, individually or in the aggregate, directly or indirectly, own a 50 percent or greater interest (i.e., subject to the **OFAC 50% Rule**);
- Included on the Department of the Treasury’s list of Non-SDN Chinese Military-Industrial Complex Companies (**NS-CMIC List**); or
- Designated as a foreign **terrorist organization** by the Secretary of State under 8 U.S.C. 1189