
Hughes Hubbard & Reed

The White House Imposes Limited Restrictions on Outbound U.S. Investments to China

Client Advisories

Hughes Hubbard & Reed LLP • A New York Limited Liability Partnership
One Battery Park Plaza • New York, New York 10004-1482 • +1 (212) 837-6000

Attorney advertising. Readers are advised that prior results do not guarantee a similar outcome. No aspect of this advertisement has been approved by the Supreme Court of New Jersey. For information regarding the selection process of awards, please visit <https://www.hugheshubbard.com/legal-notices-methodologies>.

August 14, 2023 – On August 9, 2023, President Biden signed an [Executive Order Addressing United States Investments in Certain National Security Technologies and Products in Countries of Concern](#) (the “Order”), which declares a national emergency to address the national security threat to the United States posed by “countries of concern” engaging in a comprehensive, long-term strategy to develop and exploit sensitive or advanced technologies and products that are critical to such country’s military, intelligence, surveillance, or cyber-enabled capabilities. In an Annex to the Order, the President identified the People’s Republic of China (“China”)—along with the Special Administrative Regions of Hong Kong and Macau—as a country of concern. The President may modify the Annex and update the list of countries of concern in the future.

The Order directs the Department of the Treasury (“Treasury”) to issue a new regulatory program requiring (i) notification of or, in more narrow circumstances, (ii) prohibition against outbound investments by U.S. persons into certain Chinese firms involved in “covered national security technologies and products” within the semiconductors and microelectronics, quantum information technologies, and artificial intelligence sectors. The Order complements existing authority to review inbound U.S. investment conducted by the Committee on Foreign Investment in the United States (“CFIUS”).

On August 9, 2023, the Treasury issued an [Advance Notice of Proposed Rulemaking \(“ANPRM”\)](#) to provide transparency and clarity concerning the intended scope of the program. The ANPRM solicits public comments on 83 separate questions regarding the development and eventual implementation of the Order, which must be received by 45 days after publication of the ANPRM in the Federal Register (scheduled for August 14, 2023). Treasury’s timeline for implementing the outbound investment review program is not entirely clear, but the new program will likely not go into effect for at least several months.

Background

The Order is part of a broader effort by the Biden Administration to enhance existing policy tools and develop new policy initiatives aimed at maintaining U.S. leadership in technologies critical to national security, while preventing the exploitation of the U.S.'s open economic ecosystem in ways that could undermine the national security of the United States. (We discussed in a previous [alert](#) the evolving role of CFIUS in maintaining U.S. economic and technological leadership). Also, on October 7, 2022, the U.S. Department of Commerce ("Commerce") issued sweeping export controls restricting the flow and limiting China's ability to develop these categories of sensitive technologies and products. (We summarized the October 7 rule in a previous [alert](#)). According to the ANPRM, the Order seeks to address remaining risks presented by outbound U.S. investments, which could potentially enable China to develop critical military, intelligence, surveillance, or cyber-enabled capabilities and which are not sufficiently addressed by existing national security policy tools.

The Order not only seeks to restrict the flow of U.S. capital to certain Chinese firms engaged in sensitive technologies and products but also the intangible benefits that typically accompany such investments, including, "enhanced standing and prominence, managerial assistance, access to investment and talent networks, market access, and enhanced access to additional financing." The ANPRM notes that the Order also seeks to increase the U.S. Government's visibility, highlight trends, and inform future policy developments related to U.S. person transactions involving the defined technologies and products.

The delay in issuing the order—the White House was expected to issue the Order earlier this year—reflects the complexity of identifying categories of notifiable and prohibited sensitive goods and technologies. The Biden Administration and members of Congress considering similar legislation also faced considerable pressure from business interests against the imposition of wider restrictions on outbound U.S. investments in China. Treasury has sought to target the scope of the restrictions to those transactions most likely to pose a risk to national security. According to the ANPRM, Treasury anticipates that transactions covered by the program would include certain acquisitions of equity interests (e.g., mergers and acquisitions, private equity, and venture capital), greenfield projects, joint ventures, and certain debt financing transactions by U.S. persons in these few limited but highly sensitive sectors. The ANPRM also seeks comment related to the parameters of covered and excepted transactions with an eye towards providing clarity, avoiding unintended consequences, and focusing on transactions of highest concern.

Overview of Notifiable and Prohibited Transactions

The Order directs Treasury to issue regulations prohibiting or requiring notification of certain types of outbound investments by U.S. persons involving covered foreign persons, which the Order defines as persons of a country of concern who are engaged in activities, as identified in the regulations issued under this order, involving one or more covered national security technologies and products. The Order defines "covered national security technologies and products" as sensitive technologies and products determined to be critical for the military, intelligence, surveillance, or cyber-enabled capabilities of China in the semiconductors and microelectronics, quantum information technologies, and artificial intelligence sectors. The Order further directs Treasury to identify categories of notifiable and prohibited transactions involving sensitive technologies and products within each sector.

Notifiable transactions are those Treasury determines—in consultation with Commerce and, as appropriate, the heads of other relevant agencies—*may contribute* to the threat to the national security and prohibited transactions are those determined to *pose a particularly acute* national security threat because of their potential to significantly advance the military, intelligence, surveillance, or cyber-enabled capabilities of countries of concern. Thus, prohibited transactions are meant to be focused on military, defense, and intelligence applications. The ANPRM proposes broad categories of notifiable and prohibited transactions for each of the identified sectors but solicits public input on the specific contours of each definition.

Moreover, the Order provides Treasury broad authority to do the following:

- investigate and make requests for information relative to notifiable or prohibited transactions from parties to such transactions or other relevant persons at any time, including through the use of civil administrative subpoenas;
- nullify, void, or otherwise compel the divestment of any prohibited transaction entered into after the effective date of the regulations issued under this order; and
- refer potential criminal violations of this order or the regulations issued under this order to the Attorney General.

The Order also authorizes Treasury to issue regulations prohibiting U.S. persons from “knowingly directing transactions” if such transactions would be prohibited transactions under the Order if engaged in by a U.S. person.

Finally, the Order authorizes Treasury to issue regulations requiring U.S. persons to:

- notify Treasury of any transaction by a foreign entity controlled by such U.S. person that would be a notifiable transaction if engaged in by a U.S. person; and
- take all reasonable steps to prohibit and prevent any transaction by a foreign entity controlled by such U.S. person that would be a prohibited transaction if engaged in by a U.S. person.

The ANPRM notes that the program’s regulations will carve out several categories of “excepted transactions” that present a lower likelihood of concern. Notably, Treasury is considering including passive investments in funds managed by non-U.S. persons as an “excepted transaction.” Further, the ANPRM notes that Treasury anticipates the definition of “covered transaction” will exclude the following activities:

- university-to-university research collaborations;
- the procurement of material inputs for any of the covered national security technologies or products (such as raw materials);
- intellectual property licensing arrangements;
- bank lending; the processing, clearing, or sending of payments by a bank;
- underwriting services;
- debt rating services; prime brokerage; global custody;
- equity research or analysis; or
- other services secondary to a transaction.

According to the ANPRM, the Treasury does not anticipate that the program will entail a CFIUS-like, case-by-case review of U.S. outbound investments; but rather expects that the transacting parties will have the obligation to determine by themselves whether a given transaction is prohibited, subject to notification, or permissible without notification. Treasury is considering requiring that notifications be filed no later than 30 days following the closing of a covered transaction.

The ANPRM notes that Treasury is considering penalizing the following:

- failure to timely notify a transaction;
- undertaking a prohibited transaction; and
- making material misstatements in, or material omissions from, information filed with Treasury.

Conclusion

The Order is part of a broader effort by the Biden Administration to enhance existing policy tools and develop new policy initiatives aimed at maintaining U.S. leadership in technologies critical to national security. The Order seeks to address remaining risks presented by outbound U.S. investments, which may enable China to develop critical military, intelligence, surveillance, or cyber-enabled capabilities.

The Order directs Treasury to issue regulations requiring U.S. persons to notify Treasury or be prohibited from undertaking transactions with a covered foreign person that is engaged in certain defined activities involving covered national security technologies and products that may contribute to the threat to the national security of the United States. These requirements would not apply to a U.S. persons engaged in an excepted transaction.

Treasury anticipates that the program will not entail a case-by-case, CFIUS-like review. Rather, involved parties will be required to determine by themselves whether the subject transaction is prohibited, subject to notification, or permissible without notification.

Treasury issued an ANPRM concurrently with the Order, which provides transparency and solicits public comments concerning the intended scope and eventual implementation of the Order. Treasury's timeline for implementing the regulations is unknown but the outbound investment program will not go into effect for at least several months.

U.S. individuals and companies concerned with the impact of the upcoming regulations should provide written comments on the ANPRM by September 28, 2023.

Related People



Sean M. Reilly



Jan Dunin-Wasowicz



Anna Hamati



John Hannon



Justin Campbell

Related Areas of Focus

Sanctions, Export Controls & Anti-Money Laundering