

# United States Establishes New “Outbound Investment Program” Targeting Certain Investment Activities in China

11 August 2023

On August 9, 2023, U.S. President Joe Biden signed an [Executive Order](#) “Addressing United States Investments in Certain National Security Technologies and Products in Countries of Concern” (the “Order”). The Order, which has been long anticipated, is aimed at outbound U.S. investments and the “intangible benefits that accompany such investments” in the high-end Chinese technology sectors. The Order, specifically targets the People’s Republic of China and the Special Administrative Regions of Hong Kong and Macau and results from a determination by U.S. authorities that China’s strategies to exploit advanced technologies or products to enhance its military, intelligence, surveillance and cyber-enabled capabilities threatens the national security of the United States.

Concurrent with the issuance of the Order, the U.S. Treasury Department (“Treasury”) issued an Advance Notice of Proposed Rulemaking (“Advance Notice”) to solicit feedback about the regulatory framework to effect and implement the Order. The Advance Notice provides a mere bare-bones framework for implementing the Order and asks for feedback on more than 80 questions, the responses to which will help guide Treasury on how it should proceed.

Comments on the Advance Notice are due within 45 days of the publication of the document in the Federal Register. We believe that publication will happen on Monday, which will mean that written comments will be due by September 28, 2023. We anticipate that many interested parties will file comments, which Treasury will need to consider to advance the regulatory process.

## KEY TAKEAWAYS

- *First*, and foremost, the Order and the Advance Notice do not establish immediate restrictions or compliance obligations. Rather, the Advance Notice represents an initial step in what is likely to be a long regulatory process of framing and defining the limits set forth in the Order and implementing them. Once comments are received on the Advance Notice, Treasury will need to consider them and then issue

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a proposed rule, which too will be subject to a further notice and comment period. Given this process, we would not anticipate a final regime to be in place until some time in 2024.

- *Second*, the Order and Advance Notice do not signal that all China-facing transactions will be restricted. Rather, three sectors are of concern:
  - **Semiconductors and Microelectronics.** The focus is on technology that enables the design and production of advanced integrated circuits and the installation or sale to third-party customers of certain supercomputers.
  - **Quantum Information Technologies.** The focus is on the end uses of specific and advanced quantum information technologies and products. Mainly, the U.S. government is concerned with the development of quantum computers and components, quantum sensors and quantum networking and communication systems that could enable capabilities that compromise encryption and other cyber security controls and military communications.
  - **Artificial Intelligence.** For sensitive technologies and products in the AI systems category, the U.S. Government is concerned with the development of AI systems that enable the military modernization of countries of concern – including weapons, intelligence and surveillance capabilities – and that have applications in areas such as cyber security and robotics.

The Order and Advance Notice suggest that certain transactions involving these sectors will require notice to Treasury and others will be prohibited. (The Biden Administration's focus on only these three sectors and not others, such as biotechnology and energy, has drawn criticism from some quarters.)

- *Third*, the limits on notice requirements and restrictions on transactions will apply to "U.S. persons" engaged in "covered transactions" with "a covered foreign person." Each of these key terms will require definition, and Treasury has sought comment on how these terms should be scoped.
  - **U.S. Persons.** This term is proposed to include U.S. incorporated entities and U.S. citizens and permanent residents and any person in the United States. Treasury also has signaled that, in the investment management context, it intends to capture situations in which a U.S. person acts as general partner or manages an offshore fund.
  - **Covered Transactions.** Transactions proposed to be covered include acquisitions of equity interests, provision of debt financing with a convertible feature,

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greenfield investments and establishments of joint ventures. Importantly, the Advance Notice suggests that certain transactions may be specifically “excepted.” Excepted transactions may include passive investments that do not raise meaningful U.S. national security implications, such as investments in publicly traded securities, index funds and mutual funds. The Advance Notice proposes that limited partner investments in a pooled investment vehicle would qualify for the exception if (a) the limited partner is passive and “cannot make managerial decisions” and does not have an ability “to influence or participate in” the fund’s decision making or operations, and (b) the investment is below a de minimis threshold to be determined by Treasury.

- **Covered Foreign Persons.** Treasury suggests that this term would include entities (a) engaged in the above-noted activities with a principal place of business or organized in China and (b) with subsidiaries and branches engaged in such activities and that, individually or in the aggregated, compromise more than 50% of the entity’s consolidated revenue, net income, capital expenditure or operating expenses.
- *Fourth*, the Advance Notice signals that whatever program Treasury adopts will not be retroactive. Treasury, however, has said that it may, after final regulations have been implemented, seek information about transactions entered into after the Executive Order.
- *Fifth*, Treasury has indicated that it is not considering a strict liability regime, as applies in the U.S. sanctions context. Rather, it anticipates conditioning compliance based on a person’s “actual or constructive knowledge.” The knowledge element would, thus, cover what a U.S. person knows or “reasonably should know based on publicly available information” and appropriate due diligence. This approach suggests that, in the future, firms will need to consider compliance steps, which may include appropriate due diligence and representations and warranties in transactions.
- *Sixth*, as currently conceived, the notice for covered transactions will need to be filed within 30 days post closing of a transaction. The notice, which will require detailed transactional information, will be kept confidential. Treasury does not currently suggest that a notice will be used to delay or substantively review transactions on a case-by-case basis. That said, the Advance Notice asks for comments on what options Treasury should consider in a case in which it is notified of a transaction that would be considered prohibited and whether, in this situation, Treasury should order divestment or impose civil penalties.

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## REACTIONS AND POSSIBLE FUTURE STEPS

The Order and Advance Notice may not represent the final word on this topic. The U.S. Congress is actively considering legislation—the Outbound Investment Transparency Act—that would codify the Order and may go further. To that end, some in Congress have expressed disappointment that the Biden Administration did not include greater restrictions and may seek to do so through the legislative process. Interested parties should monitor these developments.

International reaction has varied. A spokesman for the Chinese embassy in Washington was quoted as saying “China opposes the U.S.’s overuse of national security to politicize and weaponize trade, scientific and technological issues and deliberately making obstacles to normal economic and trade exchanges and technological cooperation.”<sup>1</sup> According to press reports, the European Commission has said it recognizes the significance of the topic covered by the Order and will assess whether to replicate the approach.<sup>2</sup>

In the coming weeks, industry participants and their trade associations will take steps to assess the impact the Order and forthcoming regulations may have on their dealings in China. As noted above, we expect many to comment on the Advance Notice.

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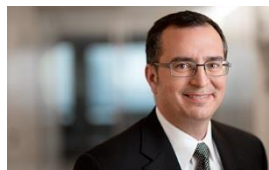
We will continue to monitor developments and provide additional updates as warranted. Please do not hesitate to contact us with any questions.

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<sup>1</sup> Wall Street Journal, “Biden Restricts U.S. Investment in China” (Aug. 9, 2023), [https://www.wsj.com/articles/u-s-to-ban-some-investments-in-china-71f519d6?mod=world\\_lead\\_story](https://www.wsj.com/articles/u-s-to-ban-some-investments-in-china-71f519d6?mod=world_lead_story).

<sup>2</sup> Reuters, “EU to analyse US tech curbs in China, says issue also key to Europe” (Aug. 10, 2023) <https://www.reuters.com/article/usa-china-investment-eu-idCAKBN2ZL0P8>.

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