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Treasury Issues Proposed Regulations to Restrict and Track US Outbound Investment in China

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TREASURY ISSUES PROPOSED REGULATIONS TO RESTRICT AND TRACK US OUTBOUND INVESTMENT IN CHINA

Almost a year after President Joseph Biden issued an executive order requiring new regulations to restrict and track US investment in China, the US Department of the Treasury released proposed rules. The draft regulations are generally consistent with the advance notice of proposed rulemaking that was issued concurrent with the executive order in August 2023, and confirm that, in addition to prohibiting certain investments, the new regulatory regime will impose significant compliance requirements on both US investors and on the funds and companies that receive US investment. In advance of the final rules being promulgated, potentially affected parties should prepare for the effect on their operations and consider what additional measures will be needed to adapt and comply with the new regulatory regime.

BACKGROUND

The US Department of the Treasury (Treasury) released a notice of proposed rulemaking (NPRM) on June 21, 2024, seeking public comment on regulations to implement Executive Order (EO) 14105, issued on August 9, 2023. EO 14105, titled "Addressing United States Investments in Certain National Security Technologies and Products in Countries of Concern," declared a national economic emergency to address the threat posed by "countries of concern"—currently, China (including Hong Kong and Macau)—that seek to develop and exploit sensitive technologies or products critical for military, intelligence, surveillance, or cyber-enabled capabilities.

As discussed in the preface of the NPRM, the US government has determined that investments by US persons are often more valuable because they convey capital as well as "intangible benefits" which help companies succeed. For example, US investors may provide companies with managerial assistance, access to investment and talent networks, market access, enhanced standing and prominence, and additional financing. When these benefits further the development of sensitive technologies or products that enhance the military, intelligence, surveillance, or cyber-enabled capabilities of a country of concern, the government has concluded that these efforts harm the national security of the United States.

The NPRM was preceded by an advanced notice of proposed rulemaking (ANPRM), which was released concurrently with EO 14105 on August 9, 2023 and introduced the areas of potential regulation, discussed high-level concepts such as notification and prohibition of outbound investment, and indicated that the new process would not operate as a "reverse CFIUS" as many had been referring to it.

Although, for the most part, the NPRM does not deviate from what the ANPRM signaled the government envisioned, there are still some notable differences. For example, the NPRM refines the scope of the regulations, including with respect to transactions involving artificial intelligence (AI) systems, and participation in limited partnership investments. Additionally, and consistent with the Biden administration's focus on multilateral engagement, the rule also proposes a new exception for certain types of transactions with or involving a person from a country or territory outside of the United States that has instituted similar measures aimed at regulating outbound investments, as designated by Treasury.

Finally, the NPRM formalizes the "knowledge" standard previewed by the ANPRM, indicating that the proposed rules would apply to the actions (or inactions) of US persons having an awareness of specific, relevant facts and circumstances related to a given transaction. This includes situations in which a US person has awareness of a "high probability" that a circumstance might occur or could have learned of that circumstance "through a reasonable and diligent inquiry." While Treasury explicitly appears to have modeled the definition on the definition used in US export controls, the application of a subjective knowledge standard will likely pose challenges in the investment context.

This report first outlines the new regulatory framework proposed by the NPRM, starting with a summary of certain key definitions. The scope of notifiable and prohibited transactions is addressed in the following section, violations are addressed thereafter. Finally, we discuss some of the main takeaways for investors and other affected parties.

KEY DEFINITIONS

Although all of the definitions laid out in the proposed rules are relevant, summarized below are four key definitions: US person; covered foreign person; covered transaction; and knowledge. Each alone, and all four together, form the foundation for the scope of the outbound investment review process and the national security concerns that process reflects.

US Person

As drafted, the proposed rules apply specifically to the conduct of US persons, leading to a threshold question: Is a "US person" involved in a given transaction? If not, then the rules would not apply. Under the proposed rules, and similar to the formulation used by US export control regimes, a "US person" includes (1) a US citizen or lawful permanent resident, (2) any entity organized under the laws of the United States or any jurisdiction within the United States, and (3) any person in the United States.

Regarding the third category, the NPRM notes that Treasury is concerned that persons who are neither US citizens nor US lawful permanent residents may still accrue knowledge, experience, networks, and other intangible assets while in the United States, which could directly or indirectly benefit a covered foreign person. These persons—whether students, visa holders, travelers, or others—fall within the scope of the proposed rules while located in the United States, but commentary to the proposed rules indicates that these persons would *not* be subject to the requirements when physically located outside of the United States. This distinction is surprising in light of the formulation of the proposed rules to address the intangible benefits that can be "conveyed" by US persons. Implementation of this aspect of the definition could be the subject of further guidance, whether in the form of regulatory language or informal agency guidance, such as frequently asked questions.

Covered Foreign Person

The proposed rules require Treasury to either prohibit or require notification of certain transactions involving a "covered foreign person," a term that refers to a person from a country of concern engaged in activities related to certain industries defined in the regulations. As of the publication of this article and under the EO, China (including Hong Kong and Macau) is the only country of concern listed.

The NPRM outlines three sets of circumstances under which a person would be classified as a covered foreign person:

- A person from a country of concern who is directly engaged in a covered activity would be considered a covered foreign person.
- A person not directly from a country of concern or engaged in a covered activity but having a significant relationship with a person from a country of concern engaged in a covered activity would also be classified as a covered foreign person. This relationship must meet the following two conditions:

    - The person must hold a specified interest in the person from a country of concern, such as a voting interest, board seat, equity interest, or contractual power to direct management or policies.
    - More than 50% of the first person's revenue, net income, capital expenditure, or operating expenses must be attributable to the person from a country of concern engaged in a covered activity. This includes aggregated interests in multiple persons from a country of concern (although different types of interests held by the same party are not aggregated).
- A person from a country of concern participating in a joint venture with a US person, where the joint venture is engaged in a covered activity, would be considered a covered foreign person. The involvement in the joint venture itself causes the person from a country of concern to be classified as a covered foreign person.

According to the NPRM, Treasury seeks to capture entities with significant financial connection to those engaged in covered activities to prevent the transfer of intangible benefits to persons from countries of concern. The proposed rules intentionally do not include a de minimis threshold for defining a covered foreign person and does not define how to calculate "significant" financial connections—definitional gaps which can increase compliance uncertainty and, ultimately, costs. Additionally, and consistent with requests in other rulemakings, Treasury received, but declined to develop, publish, and maintain a public list of covered foreign persons, noting the challenges with keeping the list current, a difficulty that could lead to evasion through corporate restructuring.

Covered Transaction

The NPRM proposes defining a "covered transaction" to include a US person's direct or indirect acquisition, leasing, or development of operations, land, property, or other assets in a country of concern if it establishes a covered foreign person or pivots an existing entity's operations into a new covered activity. This includes the acquisition of an equity interest or financial instrument convertible to an equity interest in a covered foreign person, and the provision of convertible debt financing or debt financing that grants management or governance rights. The conversion of contingent equity interest or convertible debt is also covered, with both the original acquisition and conversion being subject to the regulations.

Importantly, the NPRM specifies that a transaction will be treated as a covered transaction if the relevant US person "knows" at the time of the transaction that it involves or will result in the establishment of a covered foreign person or will result in a person of a country of concern engaging in a new covered activity. As further discussed in detail below, "knowledge" includes both actual knowledge and reason to know of the relevant facts or circumstances, meaning that a US person with reason to know these facts would not be excused from obligations or liability. For example, a US person acquiring a manufacturing facility in a country of concern with the intent to retrofit it for a covered activity, and having secured financing based on this future activity, would likely be engaging in a covered transaction. Similarly, a US person investing as a limited partner in a pooled fund with a known history of investing in the AI sector in a country of concern, where the fund later engages in a covered transaction, would also be considered a covered transaction at the time of its investment. Therefore, a fund's investment history may be another area in which investors need to conduct due diligence in order to comply with outbound investment regulations.

The NPRM does not exclude other activities such as university-to-university research collaborations, the sale of goods and services, or the licensing of intellectual property, as the definition is crafted to refer to a narrow set of specific transaction types. However, transactions undertaken for official US government business by employees, grantees, or contractors are not considered covered transactions under the proposed rules.

Other notable covered transactions include the following:

- Greenfield (establishment of a business in a new jurisdiction) and brownfield (establishment of a new business at a facility with existing operations) investments are included when a US person's acquisition, leasing, or development of operations, land, or assets in a country of concern is intended to establish a covered foreign person or pivot to a new covered activity. The US person's intent is sufficient in these cases, even if the specific knowledge is absent at the time of the transaction, although the government might still attempt to rebut the person's claimed intent based on particular facts. The NPRM explains that this is to ensure that activities aimed at establishing a covered foreign person or engaging in new covered activities in a country of concern are regulated, as these can convey intangible benefits to a covered foreign person.
- Participation in joint ventures with persons from countries of concern if the joint venture will engage in a covered activity is generally covered. Similar to greenfield and brownfield investments, a US person's intent is presumptively sufficient to extend jurisdiction over the transaction. This includes situations where a covered foreign person does not exist at the time of the transaction but may result from the joint venture.
- Investments made by a limited partner into non-US-person pooled investment funds are covered if it is possible for the US person to know, through a reasonable and diligent inquiry, that the fund likely will invest in a person of a country of concern engaged in specified sectors. While it will generally not be possible for a limited partner—or the fund itself—to know what portfolio companies and other investments will ultimately be made, they could, for example, know the sectors and geography of where investment is intended. If the pooled fund undertakes a transaction that would be a covered transaction if made by the US person directly, and the US person knew that the pooled fund likely would invest in a person of a country of concern engaged in any of the three covered sectors, then:
    - if it is a notifiable transaction, then it must be notified to Treasury within 30 calendar days of the notifiable event because certain transactions may require multiple notifications (e.g., the acquisition of a contingent equity interest and subsequent conversion into an equity interest each could constitute a separate covered transaction that requires notification); and
    - if the pooled fund undertakes a prohibited transaction, then, if completed, the US person's investment would violate the proposed rules.

Both direct and indirect transactions are covered, regardless of the number of intermediary entities involved. For example, if a US person purchases shares in a special purpose vehicle that acquires an equity interest in a covered foreign person, knowing this at the time of the transaction, it would be viewed as a covered transaction.

Knowledge

The proposed rules establish a "knowledge" requirement, which involves an awareness of specific circumstances, or its likelihood of existence (whether through unintentional or deliberate ignorance). Under the proposed rules, the existence of "knowledge" is based on whether a US person has or had an awareness of the relevant facts and circumstances at a specific time. If so, then liability may arise depending upon whether a required notification was submitted or a transaction was completed. "Knowledge" of a fact or circumstance means

- actual knowledge that a fact or circumstance exists or is substantially certain to occur;

- 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.

As with other regulations, the proposed rules do not define "awareness" or "high probability," leaving those terms to be interpreted and applied by the parties involved in the transaction. Because the government might later second-guess parties' interpretation and application of the rules, companies and their counsel will need to use sound judgment in their compliance efforts.

The proposed rules also note that whether a person has or had knowledge at the time of a given transaction will be based on the information a US person had or could have had through "reasonable and diligent" inquiry. This aligns with the definition of "knowledge" within the Export Administration Regulations (EAR), which qualifies both positive "knowledge" that a circumstance exists or is substantially certain to occur, and awareness of a high probability of its existence or future occurrence.[1] The proposed rules draw some of their language from the EAR, which provides that awareness may be inferred from the conscious disregard of known facts and willful avoidance of facts.[2] As with the EAR, however, these terms are sufficiently flexible that awareness can vary from transaction to transaction, and companies and their counsel will need to apply the rules based on the specific facts of each transaction.

Thus, the proposed rules do not impose liability on a US person's participation in a transaction with all attributes of a covered transaction if that US person did not know it involved or would result in a covered transaction. However, failure to conduct reasonable diligence before undertaking the transaction may be evidence that the person had, or should have had, reason to know of such fact or circumstance, in which case the prohibition or notification requirement would still apply.

Treasury expands on the various factors that may indicate "knowledge" under the proposed rules, including an assessment of the US person's efforts to conduct due diligence on the participating entities and the nature of the transaction. These factors appear in other regulatory programs as well, so again Treasury is not writing on an entirely blank slate. Such measures include a combination of diligence, contractual protections, and how the US person's approach evolves or adapts through the acquisition of additional information. These considerations include the following:

1. The inquiry a US person, its legal counsel, or its representatives have made regarding an investment target or relevant counterparty, including questions asked as of the time of the transaction
2. The contractual representations or warranties the US person has obtained or attempted to obtain from the investment target or relevant counterparty regarding the transaction's status as a covered transaction and the investment target or relevant counterparty's status as a covered foreign person
3. The effort by the US person at the time of the transaction to obtain available non-public information relevant to determining the transaction's status as a covered transaction and the investment target or relevant counterparty's status as a covered foreign person, and efforts to obtain and review such information

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[1] 15 C.F.R. Part 772.1

[2] *See id.*

4. Available public information, efforts to obtain and review such information, and the consistency of other available information with such publicly available information
5. Whether the US person, its legal counsel, or its representatives have purposefully avoided learning or sharing relevant information
6. The presence or absence of warning signs, including evasive responses or non-responses from an investment target or relevant counterparty to questions or refusal to provide information, contractual representations, or warranties
7. The use of public and commercial databases to identify and verify relevant information about an investment target or relevant counterparty

SCOPE OF NOTIFIABLE AND PROHIBITED TRANSACTIONS

The NPRM establishes two ways in which outbound investment would be regulated:

- **Notification** of specific investments by a US person in a covered foreign person engaged in covered activities pertaining to specified categories of technologies and products.
- **Prohibition** on certain types of investment by a US person in a covered foreign person engaged in covered activities pertaining to other specified categories of technologies and products.

Rather than adopting a wholesale prohibition, bright line licensing requirement, or case-by-case review, the regulatory regime would provide a framework for parties to analyze their legal obligations related to contemplated transactions. This results in significant time savings for Treasury, as it will not be engaged in a CFIUS-type process with a case-by-case review approach.

Notifiable Transactions

The proposed rules would require a US person engaged in a covered transaction to provide a notification to Treasury of certain types of covered transactions that are not prohibited. By requiring notification, Treasury seeks to increase visibility into investments involving technologies and products relevant to national security threats. This information will be used to help identify sector trends and capital flows, inform policy development, and guide the implementation of the outbound investment program and other relevant government programs. An open question remains with respect to the additional extent that existing regulatory programs (e.g., the Entity List) may be adapted to further the foreign policy goals of the proposed rules.

- **For semiconductors and microelectronics**, the proposed rules would require notification of transactions related to the design, fabrication, or packaging of integrated circuits not otherwise classified as prohibited transactions.
- **For AI systems**, notification is required for transactions related to the development of AI not classified as prohibited, particularly if designed for government intelligence, mass surveillance, or military use. This also includes AI intended for cybersecurity, digital forensics, penetration testing, or robotic control, and AI trained with significant computational power (e.g., integer or floating-point operations), with thresholds under consideration at 10^{23}, 10^{24}, or 10^{25} operations. The proposed rules reflect further consideration of AI system development based on design and intended use, incorporating

technical parameters for computational power. Treasury is considering feedback on AI models, especially those involving frontier AI, and seeks alternatives to ensure that definitions precisely address national security concerns. This includes potentially adjusting computational thresholds and considering specialized AI models, techniques to enhance AI performance, and other relevant factors to better capture activities that pose security risks.

The proposed rules do not include any notifiable transactions related to supercomputers or quantum computers.

Prohibited Transactions

The proposed rules would prohibit US persons from engaging in certain covered transactions posing a significant national security risk.

- **Advanced Integrated Circuit Design and Equipment**: Prohibits investment in covered foreign persons developing or producing electronic design automation software for integrated circuits or advanced packaging. The prohibition also covers the development or production of certain front-end semiconductor fabrication equipment designed for volume fabrication of integrated circuits, equipment for volume advanced packaging, or items exclusively for use in or with extreme ultraviolet lithography fabrication equipment.
- **Advanced Integrated Circuit Design and Production**: Prohibits investment in covered foreign persons designing integrated circuits that meet or exceed certain advanced technical thresholds identified by the Bureau of Industry and Security of the Department of Commerce, or integrated circuits designed for operation at or below 4.5 kelvin. The prohibition includes the fabrication of advanced integrated circuits meeting specified technical criteria and the packaging of integrated circuits using advanced packaging techniques.
- **Supercomputers**: Prohibits investment in covered foreign persons developing, installing, selling, or producing any supercomputer enabled by advanced integrated circuits with 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.
- **Quantum Computers and Components**: Prohibits investment in covered foreign persons developing quantum computers or producing critical components required to produce a quantum computer, such as dilution refrigerators or two-stage pulse tube cryocoolers.
- **Quantum Sensors**: Prohibits investment in covered foreign persons developing or producing quantum sensing platforms designed for military, government intelligence, or mass-surveillance end uses. The proposed rules include an end-use limitation to appropriately scope this activity to national security threats.
- **Quantum Networking and Communication Systems**: Prohibits investment in covered foreign persons developing or producing quantum networks or communication systems designed for scaling up quantum computers, secure communications such as quantum key distribution, or military, government intelligence, or mass-surveillance applications. The proposed rules include an end-use limitation to address national security threats.

- **AI Systems**: Prohibits investment in covered foreign persons the development of AI systems for military, intelligence, or mass-surveillance applications. This includes AI systems trained with high computing power, especially using biological sequence data.

Treasury also used the proposed rules to explicitly highlight that transactions with entities on US government restricted party lists, such as the Entity List, are prohibited if they involve covered foreign persons engaged in any covered activity. This is due to the inherent national security risks associated with these entities, and signals a significant expansion of existing authorities to achieve new foreign policy objectives.

The NPRM invites public comments on the scope of the proposed notification requirements and prohibitions, particularly regarding the computational power thresholds for AI systems and whether certain approaches should apply to notifiable rather than prohibited transactions.

Excepted Transactions and Exemptions

The proposed rules also include specific exceptions and exemptions for transactions that would otherwise be covered:

- Investments in publicly traded securities or securities issued by investment companies, such as index funds, mutual funds, or exchange-traded funds.
- Investments made as limited partners or equivalents in venture capital funds, private equity funds, funds of funds, or other pooled investment funds. The NPRM provides two alternative formulations for this exception, and invites comment on which to adopt. The first involves sufficiently passive investments that comprise no more than 50% of the fund's assets under management. The second option involves investments of no more than $1 million.
- Full buyouts by US persons of all country of concern ownership in an entity are included, ensuring the entity is no longer considered a covered foreign person post-transaction.
- Intracompany transactions between a US parent and a majority-controlled subsidiary to support ongoing operations or other non-covered activities.
- Transactions fulfilling binding, uncalled capital commitments made before August 9, 2023.
- Acquisition of voting interests in covered foreign persons upon default by US persons as members of a lending syndicate, provided they cannot initiate any action against the debtor and do not have a lead role in the syndicate.
- Transactions with or involving persons from countries or territories outside the United States, where Treasury determines that the country or territory addresses national security concerns posed by outbound investments and the transaction type's associated national security concerns are likely to be adequately addressed by the country's actions.

A "national interest exemption" may be granted by Treasury, in consultation with other relevant agencies, based on the impact on national security, such as effects on critical supply chains.

VIOLATIONS

The Outbound Order requires Treasury, in coordination with other agencies, to investigate and pursue civil penalties in the case of potential violations of the proposed rules, including the following:

- Taking any action prohibited by the proposed rules;
- Failing to take any action required by the proposed rules within the timeframe and manner specified;
- Making materially false or misleading representations when submitting any information required by the proposed rules; and
- Taking any action that evades, avoids, or has the purpose of evading or avoiding any of the prohibitions of the proposed rules.

Under the proposed rules, engaging in a prohibited transaction could be treated similarly to failing to file the required notification of a notifiable transaction. Further, the failure to update such notification, either as a separately reportable event or with the acquisition of previously unavailable information required under the proposed rules, attaches an ongoing obligation for US persons to consider whether or when a previous certification must be updated to avoid a separate violation. This approach draws directly from the EAR.[3]

Penalties

Violations of the proposed rules are subject to civil and criminal penalties depending upon the conduct at issue based on Section 206 of the International Emergency Economic Powers Act (IEEPA). IEEPA provides for a maximum civil penalty not to exceed the greater of $368,136 subject to adjustment for inflation, or an amount that is twice the amount of the transaction that is the basis of the violation with respect to which the penalty is imposed.[4] Under the proposed rules, Treasury may impose a civil penalty on any violator and refer potential criminal violations to the US Department of Justice.

Divestment

In addition to civil monetary and criminal penalties, the proposed rules articulate that Treasury, in consultation with the heads of relevant agencies, may take action to nullify, void, or otherwise compel divestment of any prohibited transaction entered into after the effective date of the rule—August 9, 2023.

Voluntary Self-Disclosure

In conjunction with the potential for civil or criminal penalties and divestment, the proposed rules allow for "any person" who has engaged in conduct that may constitute a violation to submit a voluntary self-disclosure to Treasury. As with other voluntary disclosure opportunities provided by the Departments of Justice, Commerce, and State, Treasury may take such disclosure into account as a mitigating factor in determining the appropriate response, including the potential imposition of penalties if it is determined that there was, in fact, a violation.

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[3] Compare the draft rule in Section 850.406 (Notice of material omission or inaccuracy) with 15 C.F.R. § 764.2(g)(2) ("All representations, statements, and certifications made by any person are deemed to be continuing in effect. Every person who has made any representation, statement, or certification must notify BIS, and any other relevant agency, in writing, of any change of any material fact or intention from that previously represented, stated, or certified, immediately upon receipt of any information that would lead a reasonably prudent person to know that a change of material fact or intention has occurred or may occur in the future.").

[4] 89 Fed. Reg. 2139 (Jan. 12, 2024).

The required form of the voluntary self-disclosure must: (1) be a written notice, (2) describe the conduct that may be a violation, (3) identify each involved person, and (4) include, or be followed "within a reasonable period of time" by, a report of "sufficient detail to afford a complete understanding of the conduct that may constitute the violation." Disclosing parties must also timely respond to any follow-up inquiries by Treasury.

However, similar to other regulatory regimes, mitigation credit may be lessened or even withheld depending on the timing and contents of a voluntary self-disclosure. For example, the proposed rules clarify that the identification of a violation to Treasury may nevertheless not be considered a voluntary self-disclosure in any one or more of several circumstances specified in the NPRM, such as if the disclosure includes materially false or misleading information; if the disclosure is not self-initiated; if the disclosure is a response to an administrative subpoena or other inquiry from Treasury or another government agency; and if the filing is made pursuant to a required notification under the proposed rules, including §§ 850.403 (Notification of post-transaction knowledge) or 850.406 (Notice of material omission or inaccuracy).

MAIN TAKEAWAYS AND NEXT STEPS

The proposed rules introduce several key considerations and obligations for US persons involved in transactions with foreign entities, particularly those from countries of concern. A significant aspect is the increased due diligence burden. US persons will need to perform and document their "reasonable and appropriate" due diligence measures (including for example, through contractual assurances) to ensure that transactions do not inadvertently involve covered foreign persons or activities.

The inclusion of the "knowledge" standard in the proposed rules is also crucial for assessing how new regulations would impact the process of completing deals. This standard will determine the new types of due diligence companies need to conduct, and the new provisions they may need to include in contracts and other deal documents. Investors and their counsel will need to ask appropriate questions during due diligence and obtain contractual representations or warranties from a target business about its status as a covered foreign person based on the diligence findings. Investors will not be able to avoid accountability simply because the target business does not respond to questions or provide adequate responses; rather, stonewalling or non-responsive answers to diligence requests may be a red flag that should (and in certain cases, must) be addressed.

Additionally, the enhanced recordkeeping requirements under the proposed rules mandate new considerations when engaging in due diligence. US persons are required to maintain detailed and contemporaneous documentation of their due diligence efforts rather than after-the-fact summaries or recollections of what was exchanged. This involves comprehensive records of inquiries made, contractual representations obtained, discussions with counterparties and other experts, and efforts to gather both public and non-public information relevant to the transaction. Further, parties should document both responses and non-responses (or declinations) to assess whether or to what extent any red flags may exist.

Similar to the broader US government emphasis on voluntary disclosure of suspected or actual wrongdoing, the proposed rules also emphasize the importance of voluntary disclosures following the closing of a transaction or covered event. US persons are encouraged to submit voluntary self-disclosures of potential violations, which may serve as a mitigating factor in enforcement actions. Investors will therefore need to be prepared to consider providing detailed voluntary disclosures if they identify any non-compliance with the regulations, including descriptions of the conduct and involved parties.

Compliance with the proposed rules will likely result in increased transaction costs for US persons. In the cost estimate included in the NPRM, Treasury estimated that 60 investors and 106 transactions annually would potentially be involved in covered transactions under the outbound investment regulations, although Treasury doubled those numbers for purposes of its cost estimate. The costs for investors will likely arise from the need for enhanced due diligence, legal consultations, and the potential requirement for notifications or divestment in certain scenarios. Entities should therefore budget for these additional expenses and include compliance measures into their integration planning processes.

The NPRM invites public comments, with a deadline of August 4, 2024. Although the NPRM does not give any indication of when the final rules will be issued, Treasury's budget request to Congress for Fiscal Year 2025 indicated that Treasury anticipated implementing the outbound investment program in 2025. Therefore, while US person investors and other entities are not immediately affected, they should begin planning—if they have not already done so—for the new compliance measures described above that will come with the new regulations. In addition, investors should be cognizant of the types of investment that will no longer be legal under the new regulations, and plan accordingly.

Although the regulations will only apply to US person investors, companies in other countries should also be prepared for indirect effects on them. Chinese companies involved in the three listed sectors will plainly see the availability of US capital become restricted. In addition, funds located in other countries may need to limit their investment in affected Chinese companies, if they want the funds to be able to receive US investment. Such investment funds, however, may be able to take advantage of the exceptions specified in the proposed rules for investment by US entities as limited partners under certain circumstances.

The new outbound investment regulations will be a significant change, and will impact many businesses both within and outside the United States. However, the preview of the likely regulations contained in the NPRM will greatly aid businesses and their counsel in determining the potential impact on their operations, and in promptly developing plans to minimize that impact as much as possible.

While in government, David Plotinsky was involved in the White House and interagency discussions regarding outbound investment regulation.

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