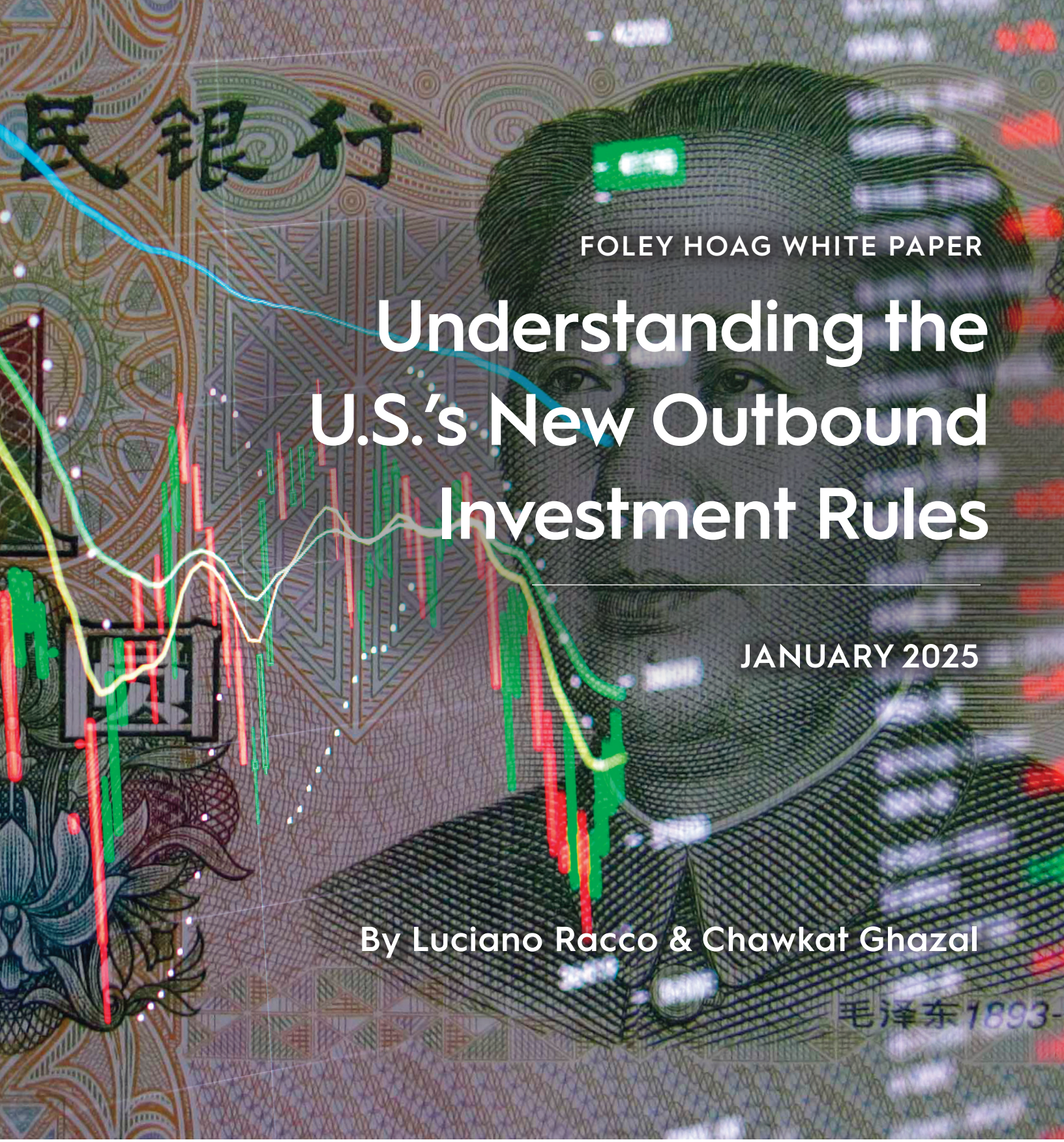

FOLEY HOAG WHITE PAPER

Understanding the U.S.'s New Outbound Investment Rules

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I. Introduction

Effective in January 2025, the U.S. Department of the Treasury issued a final rule (colloquially known as "Reverse CFIUS") implementing the Outbound Investment Program, which prohibits U.S. persons from making certain investments involving a defined set of technologies (currently certain semiconductors/microelectronics, quantum computing, and artificial intelligence systems) with persons from countries of concern (currently only China) that pose a national security threat to the United States. Additionally, the Outbound Investment Program requires U.S. persons to notify the Treasury Department of certain other transactions involving persons from countries of concern that may contribute to a threat to U.S. national security. Despite some referring to the Outbound Investment Program as "Reverse CFIUS," the program differs significantly in that there is no pre-approval process by the U.S. Government as is the case with mandatory filings that must be submitted and reviewed by the Committee on Foreign Investment in the United States ("CFIUS") prior to closing for certain inbound investments by foreign persons in U.S. businesses. Both U.S. and non-U.S. investors alike should familiarize themselves with the requirements of the Outbound Investment Program.

While the list of targeted countries currently only includes China, it may be expanded in the future to include other countries that the U.S. perceives as posing a national security threat. The covered technologies currently fall into three categories that could also be expanded in the future: semiconductors and microelectronics, quantum information technologies, and artificial intelligence. The Outbound Investment Program took effect on January 2, 2025. Given the extraterritorial reach of the rule, businesses in the United States and abroad will need to adopt new diligence measures and other internal policies and procedures to comply with its requirements.

II. Whose Investments are Impacted?

A. U.S. Persons

Every U.S. person is required to comply with the provisions of the Outbound Investment Program. For the purposes of the Outbound Investment Program, the term "U.S. persons" includes:

1. any United States citizen or lawful permanent resident;
2. any entity organized under the laws of the United States or any jurisdiction within the United States, including any foreign branch of such an entity;
3. and any person located in the United States, regardless of their country of citizenship.

Treasury has clarified that, while a U.S. subsidiary of an entity incorporated outside of the U.S. is a U.S. person, simply having a U.S. subsidiary or U.S.-based employees does not make the foreign parent a U.S. person as well.

B. Foreign Entities Controlled by U.S. Persons

The Outbound Investment Program requires U.S. persons to take "all reasonable steps to prohibit and prevent" their controlled foreign entities from engaging in transactions that would be prohibited if undertaken by a U.S. person. The rule also requires U.S. persons to notify the Treasury Department of any notifiable transaction carried out by a controlled foreign entity.

The term *controlled foreign* entity means any entity incorporated in, or otherwise organized under the laws of, a country other than the United States of which a U.S. person is a parent.

For purposes of this term, the following rules shall apply in determining whether an entity is a parent of another entity in a tiered ownership structure:

(1) Where the relationship between an entity and another entity is that of parent and subsidiary, the holdings of voting interest or voting power of the board, as applicable, of a subsidiary shall be fully attributed to the parent.

(2) Where the relationship between an entity and another entity is not that of parent and subsidiary (*i.e.,* because the holdings of voting interest or voting power of the board, as applicable, of the first entity in the second entity is 50 percent or less), then the indirect downstream holdings of voting interest or voting power of the board, as applicable, attributed to the first entity shall be determined proportionately.

(3) Where the circumstances in paragraphs (b)(1) and (2) of this section apply (*i.e.*, because a U.S. person holds both direct and indirect downstream holdings in the same entity), any holdings of voting interest shall be aggregated for the purposes of applying this definition, and any holdings of voting power of the board shall be aggregated for the purposes of applying this definition. Voting interest shall not be aggregated with voting power of the board for the purposes of applying this definition.

In the event a controlled foreign entity engages in a prohibited transaction, the Treasury Department will consider several factors to determine whether the U.S. person took all reasonable steps to prohibit and prevent the entity from engaging in the transaction. The factors the Treasury Department will evaluate include:

(a) The execution of compliance agreements related to the final rule between the U.S. person and its controlled foreign entity;

(b) The existence and exercise of governance or shareholder rights by the U.S. person over the controlled foreign entity, where applicable;

(c) The implementation of periodic training and internal reporting requirements by the U.S. person at its controlled foreign entity concerning compliance with the final rule;

(d) The development and use of appropriate, documented internal controls, including internal policies, procedures, or guidelines that are periodically reviewed internally by the U.S. person and its controlled foreign entity; and

(e) The implementation of a documented process for testing and/or auditing internal policies, procedures, or guidelines.

It is important to note that the factors listed above are non-exhaustive, and the Treasury Department may consider other factors not listed to determine whether the U.S. person took "all reasonable steps" to prohibit and prevent its controlled foreign entity from engaging in the unauthorized transaction.

III. How will U.S. Individuals and Entities be Expected to Comply with the Outbound Investment Rules?

A U.S. person's knowledge of certain facts or circumstances is generally a pre-requisite for the obligations under the Outbound Investment Program to apply. The Treasury Department therefore anticipates that U.S. persons should be able to comply with the Outbound Investment Program through a reasonable and diligent transactional due diligence and compliance process. The analysis of whether the Outbound Investment Program applies is independent of whether other U.S. Government rules or restrictions apply (or not). A U.S. person who fails to undertake a reasonable and diligent inquiry prior to a transaction may be responsible for knowledge that could have been acquired had the U.S. person undertaken such an inquiry.

The Outbound Rule further prohibits U.S. persons from "knowingly directing" a transaction by a non-U.S. person if, at the time of the transaction, the U.S. person knows that the transaction would be prohibited if engaged in by a U.S. person. A U.S. person "knowingly directs" a transaction when they have the authority, individually or as part of a group, to make or substantially participate in decisions on behalf of a non-U.S. person and exercise that authority to direct, order, decide upon, or approve a transaction. This authority exists when a U.S. person serves as an officer, director, or holds executive responsibilities at a non-U.S. entity, which could bring into scope the activities of many non-U.S. entities that would not otherwise be subject to the outbound investment rules. A senior Treasury official has confirmed that the non-U.S. person employer of a U.S. person who knowingly directs a prohibited transaction does not itself face liability under the Outbound Rule.[1] The senior Treasury official also confirmed that the prohibition on U.S. persons "knowingly directing" transactions only applies to prohibited transactions, not those that are merely notifiable.

The Outbound Investment Program does not restrict a U.S. person from working at any entity that receives investment that is subject to the Outbound Investment Program, nor does it restrict a U.S. person from working at an entity making such an investment. However, the Outbound Investment Program requires a U.S. person's recusal from participation in certain activities to avoid violating this prohibition, including:

(a) Participating in formal approval and decision-making processes related to the transaction, including making recommendations;

(b) Reviewing, editing, commenting on, approving, or signing relevant transaction documents; and

(c) Engaging in negotiations with the investment target or the relevant transaction counterparty, such as a joint venture partner.

The Treasury has made clear that the Outbound Investment Program is "not intended to create an ongoing obligation for a U.S. person to monitor or prevent post-transaction changes to an investment target's activities," however, an investment target's pivot to a covered activity could raise implications under the Outbound Investment Program if a. "the U.S. person had knowledge at the

[1] Comments attributed to senior Treasury officials came during a conference held by the U.S. Department of the Treasury on the Outbound Investment Program on December 9, 2024.

time of the transaction regarding the later corporate pivot into a covered activity, including whether the U.S. person had" or b. "should have had an awareness of a high probability of a fact or circumstance's existence or future occurrence." In either case, the transaction would be a notifiable transaction or a prohibited transaction, depending on the covered activity involved. Further, pursuant to section 850.403, "if following a transaction a U.S. person later acquires 'actual knowledge' of a fact or circumstance that, if known to the U.S. person at the time of the transaction, would have resulted in a notifiable transaction or a prohibited transaction, the U.S. person will be required to submit a notification within 30 days of acquiring such knowledge. Section 850.403 requires 'actual knowledge' of a fact or circumstance and does not include 'reason to know,' as the intention is not to create a requirement to conduct continuing diligence or actively monitor the activities of the target of the transaction after the completion date for purposes of section 850.403, assuming that a 'reasonable and diligent inquiry' had been conducted at the time of the transaction." See FAQ III.3.

Below is a list of examples provided by the Treasury Department describing situations where a U.S. person would be knowingly directing a prohibited transaction.

Example 1: A U.S. person is a corporate officer at Company I, a non-U.S. person operating company incorporated in a foreign jurisdiction. The U.S. person's role includes substantial participation in investment decisions related to Company I's strategic acquisitions, including as a member of the investment committee that votes on whether to undertake potential investments. The U.S. person participates in deliberations among Company I's leadership about whether to undertake a share purchase in Company J, a privately-held covered foreign person that develops a quantum computer. Following these deliberations, the U.S. person votes in favor of the share purchase and knows at the time of the vote that the share purchase would be a prohibited transaction if undertaken by a U.S. person. The U.S. person has knowingly directed an otherwise prohibited transaction under the Outbound Investment Program, because such person has authority to make or substantially participate in decisions as part of a group on behalf of Company I and has exercised that authority to direct a transaction that would be prohibited if engaged in by a U.S. person.

Example 2: A U.S. person is an accountant employed at Company K, a company that is not a U.S. person, and does not have the authority to make decisions on behalf of the company. Per instructions from Company K's management, the U.S. person accountant undertakes financial due diligence in support of a potential corporate investment into a covered foreign person that would be a prohibited transaction if engaged in by a U.S. person. Company K then makes the investment. Absent additional facts, the U.S. person employee has not knowingly directed an otherwise prohibited transaction under the Outbound Investment Program, because the U.S. person employee did not have the authority to make decisions on behalf of Company K.

Example 3: A U.S. person serves on the management committee at a pooled investment fund that is not a U.S. person. The fund makes an investment into a covered foreign person that would be a prohibited transaction if performed by a U.S. person. While the management committee reviews and approves all investments made by the fund, the U.S. person recuses themself from the deliberations related to the particular investment, the decision-making, the work on relevant transaction documents, and negotiations with the investment target; absent additional facts, the U.S. person has not knowingly directed an otherwise prohibited transaction.

Treasury further provided guidance that "where an advisory board or committee has the authority to approve or disapprove certain transactions, such as those where conflicts of interest are present, the advisory board or committee would have the authority to 'make or substantially participate in decisions' of the pooled investment fund. In cases where an advisory board or committee approves a transaction that would be a covered transaction if undertaken by a U.S. person, a U.S. person that participates in the advisory board or committee would be liable for 'knowingly directing' such a transaction unless they recuse themself." The Treasury Department has stated that U.S. persons are not prohibited from working at an entity that receives an investment that is subject to the Outbound Investment Program, nor are U.S. persons restricted from working at an entity making such an investment.

IV. Which Foreign Entities Are Subject to Investment Restrictions?

An entity subject to investment restrictions is referred to under the Outbound Investment Program as a "covered foreign person." The term covered foreign person means:

1) A person of a country of concern that engages in (e.g., designs, fabricates, packages, develops, or produces) a covered activity (see the activities described in sections 850.217 and 850.224); or

2) A person that directly or indirectly holds a board seat on, a voting or equity interest in (other than through securities or interests that would satisfy the conditions of the excepted transactions under § 850.501(a) if held by a U.S. person, which is discussed further in section VII below), or any contractual power to direct or cause the direction of the management or policies of any person or persons of a country of concern that engages in a covered activity or through which it:

    (i) Derives more than 50 percent of its revenue individually, or as aggregated across such persons from each of which it derives at least $50,000 (or equivalent) of its revenue, on an annual basis;

    (ii) Derives more than 50 percent of its net income individually, or as aggregated across such persons from each of which it derives at least $50,000 (or equivalent) of its net income, on an annual basis;

    (iii) Incurs more than 50 percent of its capital expenditure individually, or as aggregated across such persons from each of which it incurs at least $50,000 (or equivalent) of its capital expenditure, on an annual basis; or

    (iv) Incurs more than 50 percent of its operating expenses individually, or as aggregated across such persons from each of which it incurs at least $50,000 (or equivalent) of its operating expenses, on an annual basis.

3) A person of a country of concern that participates in a joint venture with a U.S. person, where the U.S. person knows at the time of entrance into the joint venture that the joint venture will engage, or plans to engage, in a covered activity. Note that the Outbound Rule does not define "joint venture," but in the commentary to the final rule, Treasury indicates

> that "the Treasury Department refers to the plain English meaning of the term, i.e., as involving the contribution of capital and/or assets by two parties and the sharing of profits and losses. The term as generally understood in the market does not cover 'any business relationship'."

Treasury has stated it does not currently intend to publish a list of entities identified as covered foreign persons.

Below is a list of examples provided by the Treasury Department describing situations where a foreign person would be considered a "covered foreign person" under the Outbound Investment Program:

> **Example 1:** Company L is an entity incorporated outside of a country of concern and is not itself engaged in any covered activity. Company M is incorporated in a country of concern and engages in a covered activity and is therefore a covered foreign person. Company L holds a small equity interest in Company M, and more than 50 percent of Company L's capital expenditures are attributable to Company M for the most recent year for which audited financial statements are available at the time of a relevant investment by a U.S. person in Company L. Because Company L holds an equity interest in Company M and more than 50 percent of Company L's capital expenditures are attributable to Company M, Company L is a covered foreign person under the Outbound Investment Program.
>
> **Example 2:** Company N holds a 10 percent equity interest in Company O, a covered foreign person, and income from Company O comprises 30 percent of Company N's net income, and such income from Company O is above $50,000 for the most recent year for which audited financial statements for Company N are available. In addition, Company N holds a 10 percent equity interest in Company P, a covered foreign person, and income from Company P comprises 21 percent of Company N's net income, and such income from Company P is above $50,000 for the most recent year for which audited financial statements for Company N are available. Company N is a covered foreign person under the Outbound Investment Program, because Company O and Company P are each a covered foreign person in which Company N holds an equity interest, income for Company N derived from each of Company O and Company P is at least $50,000, and, in the aggregate, the income from Company O and Company P comprises 51 percent of the net income of Company N for the most recent year for which audited financial statements are available.
>
> **Example 3:** Assume the same facts as in Example 2, except that none of Company N's net income is attributable to Company O, and instead, 30 percent of Company N's capital expenditures are attributable to Company O for the most recent year for which audited financial statements for Company O are available. Absent additional facts, Company N is not a covered foreign person under the Outbound Investment Program, because the percentage of capital expenditures attributable to Company O and the percentage of net income attributable to Company P are not aggregated (because they are different financial metrics), and neither the percentage of Company N's capital expenditures attributable to Company O, nor the percentage of Company N's net income attributable to Company P is more than 50 percent.

Example 4: Company Q is incorporated and headquartered outside of a country of concern and its principal place of business is outside of a country of concern, but 50 percent of its equity is held by a person of a country of concern. Company Q engages in a covered activity. Company Q therefore is a person of a country of concern under the Outbound Investment Program, and because it is a person of a country of concern that engages in a covered activity, Company Q is also a covered foreign person.

Example 5: Company R is incorporated in a country of concern but is not engaged in a covered activity. Company R is wholly owned by Company S, which is incorporated in a country of concern and is engaged in a covered activity. Even though Company R is a person of a country of concern and is wholly owned by a covered foreign person, absent additional facts, Company R is not a covered foreign person.

A. Person of a Country of Concern

As of today, China is the only country that is designated as a country of concern. The definition of a "person of a country of concern" is:

(a) Any individual that:

(1) Is a citizen or permanent resident of a country of concern;
(2) Is not a U.S. citizen; and
(3) Is not a permanent resident of the United States;

(b) An entity with a principal place of business in, headquartered in, or incorporated in or otherwise organized under the laws of a country of concern;

(c) The government of a country of concern, including any political subdivision, political party, agency, or instrumentality thereof; any person acting for or on behalf of the government of a country of concern; or any entity with respect to which the government of a country of concern holds individually or in the aggregate, directly or indirectly, 50 percent or more of the entity's outstanding voting interest, voting power of the board, or equity interest, or otherwise possesses the power to direct or cause the direction of the management and policies of such entity (whether through the ownership of voting securities, by contract, or otherwise);

(d) Any entity in which one or more persons identified in paragraph (a), (b), or (c) of this section, individually or in the aggregate, directly or indirectly, holds at least 50 percent of any of the following interests of such entity: outstanding voting interest, voting power of the board, or equity interest; or

(e) Any entity in which one or more persons identified in paragraph (d) above, individually or in the aggregate, directly or indirectly, holds at least 50 percent of any of the following interests of such entity: outstanding voting interest, voting power of the board, or equity interest.

Treasury has provided multiple examples where an entity that does not have the above-mentioned attributes still can be considered "a person of a country of concern" including:

- Company A is incorporated and headquartered outside of a country of concern and its principal place of business is outside of a country of concern. A ministry of the government of a country of concern controls Company A, including possessing the power to direct or cause the direction of Company A's management and policies. Company A is therefore a person of a country of concern under section 850.221(c).

- Company B is incorporated and headquartered outside of a country of concern and its principal place of business is outside of a country of concern. Each of six citizens of a country of concern, each of whom is not a U.S. citizen or U.S. permanent resident, is a voting director on the board of Company B. Company B has ten directors on its board, each with equal voting power. Company B is therefore a person of a country of concern under section 850.221(d), because 60 percent of the voting power of Company B's board is held in the aggregate by persons of a country of concern.

- Company C is incorporated and headquartered outside of a country of concern and its principal place of business is outside of a country of concern. Company D, a person of a country of concern under section 850.221(b), holds 60 percent of the voting power of the board of Company C. Company C is therefore a person of a country of concern, because at least 50 percent of its outstanding voting interest is held by a person of a country of concern.

V. Technologies Targeted

The Outbound Investment Program applies to investments in persons from countries of concern engaged in "covered activities." Treasury has clarified that purchasing an item or service does not, alone, constitute engaging in a covered activity. Currently, the three targeted industries are semiconductors and microelectronics, quantum information, and artificial intelligence. Not all investments in these sectors are subject to the Outbound Investment Program, and we note that the term "artificial intelligence" or "AI" is often used in marketing materials to encompass far wider range of activity than is targeted by Treasury. Below is a table providing additional information about the activities targeted within these sectors. Under the rule, some investments in "covered activities" are prohibited, while others only require submitting a notification to the Treasury Department.

Industry	*Prohibited* Investments in Chinese Companies that are:	*Notification Required* for Investments in Chinese Companies that are:
Semiconductors and Microelectronics	• Developing or producing any electronic design automation software for the design of integrated circuits or advanced packaging. • Developing or producing any: (1) Front-end semiconductor fabrication equipment designed for performing the volume fabrication of integrated circuits, including equipment used in the production stages from a blank wafer or substrate to a completed wafer or substrate; (2) Equipment for performing volume advanced packaging; or (3) Commodity, material software, or technology designed exclusively for use in or with extreme ultraviolet fabrication equipment. • Designing any integrated circuit that meets or exceeds the performance parameters in Export Control Classification Number 3A090.a in supplement No. 1 to 15 CFR part 774, or integrated circuits designed for operation at or below 4.5 Kelvin. • Fabricating any of the following: (1) Logic integrated circuits using a non-planar transistor architecture or with a production technology node of 16/14 nanometers or less, including fully depleted silicon-on-insulator (FDSOI) integrated circuits; (2) NOT-AND	• Designing any integrated circuit that is not described in the prohibited category. • Fabricating any integrated circuit that is not described in the prohibited category. • Packaging any integrated circuit that is not described in the prohibited category.

Industry	*Prohibited* Investments in Chinese Companies that are:	*Notification Required* for Investments in Chinese Companies that are:
	(NAND) memory integrated circuits with 128 layers or more; (3) Dynamic random-access memory (DRAM) integrated circuits using a technology node of 18 nanometer half-pitch or less; (4) Integrated circuits manufactured from a gallium-based compound semiconductor; (5) Integrated circuits using graphene transistors or carbon nanotubes; or (6) Integrated circuits designed for operation at or below 4.5 Kelvin. • Packaging any integrated circuit using advanced packaging techniques.	
Quantum Information	• Developing, installing, selling, or producing any supercomputer enabled by advanced integrated circuits 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. • Developing a quantum computer or producing any of the critical components required to produce a quantum computer such as a dilution refrigerator or two-stage pulse tube cryocooler. • Developing or producing any quantum network or quantum communication system designed for, or which the relevant covered foreign person intends to be used for: (1) Networking to scale up the capabilities of quantum computers, such as for the purposes of breaking or compromising encryption; (2) Secure communications, such as quantum key distribution; or (3) Any other application that has any military, government intelligence, or mass surveillance end use.	• None

Industry	*Prohibited* Investments in Chinese Companies that are:	*Notification Required* for Investments in Chinese Companies that are:
Artificial Intelligence Systems	• Developing[2] any AI system that is designed to be exclusively used for, or which the relevant covered foreign person intends to be used for: Military end use[3] (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 incorporation of features such as mining text, audio, or video; image recognition; location tracking; or surreptitious listening devices). • (k) Developing any AI system that is trained using a quantity of computing power greater than: (1) 10^25 computational[4] operations (e.g., integer or floating-point operations); or (2) 10^24 computational operations (e.g., integer or floating-point operations) using primarily biological sequence data.	• Developing any AI system that is not described in the prohibited category 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 any of the following: (i) cybersecurity applications; (ii) digital forensics tools; (iii) penetration testing tools; or (iv) the control of robotic systems; or (3) Trained using a quantity of computing power greater than 10^23 computational operations.

[2] Treasury has clarified that a person "develops" an AI system when engaging "in any stages prior to serial production" including "designing an AI system or making substantive modifications with respect to a third-party AI model or machine-based system, such as removing security measures or safeguards of the third-party AI model." See FAQ II.1. A senior Treasury official stated that mere use of a commercial off-the-shelf AI model does not constitute development of an AI system, but that customizing, configuring, or fine tuning such a model would be development activities.

[3] When assessing whether an AI system meets any of the end-uses identified in the final rules, Treasury has stated that "different versions of an AI system, including adaptations, derivatives, subsequent generations, or successor systems, should be assessed as distinct AI systems since the designed end-use or capabilities of a successor system could vary from a prior version." See FAQ II.1.

[4] Treasury has stated that "computation thresholds for AI systems should be calculated by aggregating the quantity of computing power measured in computational operations (for example, integer or floating-point operations) required to train a given AI system. For instance, the computational operations required to train an AI system that is a combination of smaller, pre-trained AI models would be the summation of the computational operations required to train each component model of the AI system. Similarly, developing an AI model based on the transfer of knowledge from one model to another would include the computational operations required to train both models." See FAQ IV.1.

Treasury has stated that "computation thresholds for AI systems should be calculated by aggregating the quantity of computing power measured in computational operations (for example, integer or floating-point operations) required to train a given AI system. For instance, the computational operations required to train an AI system that is a combination of smaller, pre-trained AI models would be the summation of the computational operations required to train each component model of the AI system. Similarly, developing an AI model based on the transfer of knowledge from one model to another would include the computational operations required to train both models." See FAQ IV.1.

A transaction that would otherwise only be notifiable, becomes prohibited if the covered foreign person meets any of the following criteria:

- is included on the Bureau of Industry and Security's ("BIS") Entity List;
- is included on BIS's Military End User List;
- meets the definition of "Military Intelligence End-User" established by BIS in 15 CFR § 744.22(f)(2);
- is included on the Treasury Department'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;
- is included on the Treasury Department's list of Non-SDN Chinese Military Industrial Complex Companies; or
- is designated as a foreign terrorist organization by the Secretary of State under 8 U.S.C. 1189.

VI. Covered Transactions

Under the Outbound Investment Program, the definition of covered transactions means a U.S. person's direct or indirect:

1. Acquisition of an equity interest or contingent equity interest in a person that the U.S. person knows at the time of the acquisition is a covered foreign person;
2. Provision of a loan or similar debt financing arrangement to a person that the U.S. person knows at the time of the provision is a covered foreign person, where such debt financing affords or will afford the U.S. person an interest in profits of the covered foreign person, the right to appoint members of the board of directors (or equivalent) of the covered foreign person, or other comparable financial or governance rights characteristic of an equity investment but not typical of a loan;

    i. Treasury has clarified that obtaining convertible debt in an entity a U.S. person knows is a covered foreign person is a covered transaction. SeeFAQ II.2. In addition, the conversion of that contingent interest into an equity interest could trigger another covered transaction.

3. Conversion of a contingent equity interest into an equity interest in a person that the U.S. person knows at the time of the conversion is a covered foreign person, where the contingent equity interest was acquired by the U.S. person on or after January 2, 2025;

4. Acquisition, leasing, or other development of operations, land, property, or other assets in a country of concern that the U.S. person knows at the time of such acquisition, leasing, or other development will result in, or that the U.S. person plans to result in:

    i. The establishment of a covered foreign person; or
    ii. The engagement of a person of a country of concern in a covered activity;

    Treasury has stated that "[i]ndicators relevant to what the U.S. person 'plans' include, for example, correspondence with the investment target or relevant government, business plans, board presentations, and presentations to potential investors."

5. Entrance into a joint venture, wherever located, that is formed with a person of a country of concern, and that the subject U.S. person knows at the time of entrance into the joint venture that the joint venture will engage, or plans to engage, in a covered activity; or

6. Acquisition of a limited partner or equivalent interest in a venture capital fund, private equity fund, fund of funds, or other pooled investment fund (in each case where the fund is not a U.S. person) that a U.S. person knows at the time of the acquisition likely will invest in a person of a country of concern that is in the semiconductors and microelectronics, quantum information technologies, or artificial intelligence sectors, and such fund undertakes a transaction that would be a covered transaction if undertaken by a U.S. person.

    i. As an example, Treasury has noted that a statement in a fund's prospectus that it will invest in AI technology advancements in China is sufficient to give a U.S. person investor reason to know and thus, knowledge, that the fund was likely to invest in a country of concern in one of the sectors covered by the Outbound Investment Program and thus an actual investment by the fund would be a covered transaction. See FAQ II.2.

As an example of an indirect covered transaction, Treasury provided the example of a U.S. person purchasing shares in a special purpose vehicle established to acquire an equity interest in a covered foreign person. Upon actual acquisition of the equity interest, a covered transaction has occurred because the U.S. person has used an intermediary to engage in a transaction that would be a covered transaction if the U.S. person engaged in it directly. See FAQ II.2.

VII. Excepted Transactions

The Outbound Investment Program lists a set of transactions by U.S. persons that are exempt, and would not be considered prohibited or notifiable including:

1. Any transaction related to the conduct of the official business of the United States Government by employees, grantees, or contractors thereof;

2. Investment in any publicly traded security, with "security" as defined in section 3(a)(10) of the Securities Exchange Act of 1934, as amended, at 15 U.S.C. 78c(a)(10);

3. Investment in a security issued by any "investment company" as defined in section 3(a)(1) of the Investment Company Act of 1940, as amended, at 15 U.S.C. 80a-3(a)(1), that is registered with the U.S. Securities and Exchange Commission, such as index funds, mutual funds, or exchange traded funds;

4. Investment in any company that has elected to be regulated or is regulated as a business development company pursuant to Section 54 of the Investment Company Act of 1940, as amended, at 15.U.S. 80a-53;

5. Investment made as a limited partner or equivalent in a venture capital fund, private equity fund, fund of funds, or other pooled investment fund where the limited partner or equivalent's committed capital is not more than $2,000,000, aggregated across any investment and co-investment vehicles of the fund; or the limited partner or equivalent has secured a binding contractual assurance that its capital in the fund will not be used to engage in a transaction that would be a prohibited transaction or notifiable transaction, as applicable, if engaged in by a U.S. person;

6. Investment in a derivative, so long as such derivative does not confer the right to acquire equity, any rights associated with equity, or any assets in or of a covered foreign person;

7. The acquisition by a U.S. person of equity or other interests in an entity held by one or more persons of a country of concern, provided that the U.S. person is acquiring all equity or other interests in such entity held by all persons of a country of concern and, following such acquisition, the entity does not constitute a covered foreign person;

8. A transaction made after January 2, 2025, pursuant to a binding, uncalled capital commitment entered into before January 2, 2025 (note that any other transaction completed on or after January 2, 2025, may be subject to the Outbound Investment Program even if the agreement underlying the transaction was entered into prior to this date);

9. The acquisition of a voting interest in a covered foreign person by a U.S. person upon default or other condition involving a loan or a similar financing arrangement, where the loan was made by a syndicate of banks in a loan participation where the U.S. person lender(s) in the syndicate: cannot on its own initiate any action vis-à-vis the debtor; and is not the syndication agent;

10. The receipt of employment compensation by an individual in the form of an award of equity or the grant of an option to purchase equity in a covered foreign person, or the exercise of such option;

11. Transaction with a person of another country that has been designated by the Secretary of Treasury as having sufficient outbound investment controls. To date, no country has been so designated.

12. Covered transactions that are exempt pursuant to a national security exemption granted by the Secretary of the Treasury on a case-by-case basis. The national security exemption is discussed further in section VIII below.

It is important to note that in any case, an investment is not an excepted transaction if it affords the U.S. person rights beyond standard minority shareholder protections with respect to the covered foreign person.

VIII. National Interest Exemption

The Secretary of the Treasury, in consultation with the Secretary of Commerce, the Secretary of State, and the heads of other relevant agencies, as appropriate, may determine that a covered transaction is in the national interest of the United States and therefore exempt such transaction from the applicable provisions of the Outbound Investment Program.

Any determination that a national interest exemption is warranted will be based on a consideration of the totality of the relevant facts and circumstances, but Treasury has highlighted in recent guidance the following considerations:

- The transaction's effect on critical U.S. supply chain or critical infrastructure needs;
- Domestic production needs in the United States for projected national defense requirements;
- The United States' technological leadership globally in areas affecting U.S. national security; and
- The impact on U.S. national security from prohibiting a given transaction.

The Treasury Department expects that exemptions based on national interest will be granted only in exceptional circumstances. Before requesting a national security exemption, the relevant U.S. person undertaking a transaction has an obligation to determine whether the given transaction is prohibited, permissible but subject to notification, or not covered by the Outbound Investment Program because either it is an excepted transaction or does not otherwise meet the Outbound Investment Program's definition of a "covered transaction". Once the relevant U.S. person determines that such transaction is prohibited, they can proceed to submit a national security exemption.

IX. Submission Process

U.S. persons submitting notifications must do so electronically via the Treasury Department's Outbound Notification System. Treasury has stated that the submitter will receive an acknowledgement of receipt of the notification, but that submitters should not expect that there will be any further outreach from Treasury, although it is possible some submitters will receive questions or document requests from Treasury in response to the notification.

Those requesting a national interest exemption should do so as far in advance as possible by submitting a letter and supporting documentation to the email address specified on the Treasury Department's Outbound Investment Security Program website. Treasury has indicated that submissions should include, among other information:

- A description of the U.S. person or controlled foreign entity seeking the request, including ultimate beneficial owner;
- A brief description of the commercial rationale for the transaction;
- A brief description of why the U.S. person has determined the transaction would be a covered transaction;
- The anticipated timing of the transaction;
- The estimated total transaction value and a description of the consideration for the transaction;
- Information about the covered foreign person, including a post-transaction organizational chart and explanation of why the entity is a covered foreign person;
- Identification and description of the covered activity or activities undertaken by the covered foreign person that would make the transaction a notifiable transaction or prohibited transaction, as well as a brief description of the known end use(s) and end user(s) of the covered foreign person's technology, products, or services;
- Description of the U.S. person's or controlled foreign entity's existing commercial relationship with the covered foreign person, if applicable; and
- The requesting party's views regarding the transaction's potential impact on the national interest of the United States, the existing or contemplated measures by the U.S. person or the controlled foreign entity to mitigate national security risks related to the transaction, and any other considerations the requesting party assesses may be relevant, such as the financial impact to the U.S. economy should the transaction not receive an exemption.

X. Enforcement and Penalties

Failure to comply with the provisions of the Outbound Investment Program may result in civil and/or criminal penalties in the event of a willful violation. In the event of a violation, the Treasury Department is authorized to impose civil penalties and refer criminal violations to the Attorney General. The maximum civil penalty for violations is the greater of $377,700 (adjusted annually for inflation) or twice the value of the transaction that constitutes the violation as specified under the International Emergency Economic Powers Act ("IEEPA"). Additionally, the Secretary of the Treasury has the authority to nullify, void, or require divestment of any prohibited transaction. In the event of criminal penalties, violators could face up to 20 years of imprisonment and a fine of up to $1 million.

The Outbound Investment Program also allows U.S. persons to submit voluntary self-disclosures to the Treasury Department if they believe they have engaged in conduct that may violate the rule. When determining the appropriate response to a violation, the Treasury Department will consider the submission and the timeliness of the voluntary disclosure. Although a voluntary self-disclosure does not guarantee reduced penalties, the Treasury Department will review such disclosures on a case-by-case basis.

XI. Recommendations

U.S. businesses should implement robust compliance programs to align with the Outbound Investment Program. These measures should include training and an investment approval review process to ensure no investment is directed to a covered person involved in a covered transaction.

Additionally, U.S. businesses must ensure that their foreign subsidiaries comply with the Outbound Investment Program's requirements. While the Outbound Investment Program does not directly target foreign entities, those entities with U.S. employees should also establish new investment review procedures and decision-making processes to ensure their U.S. employees remain in compliance with the rule's requirements.

U.S. investors should add representations and warranties from the relevant transaction counterparty to investment agreements covering information relevant to the Outbound Investment Program, such as the investment target or counterparty's activities, ownership, and investments.

U.S. investors should enhance due diligence activities in order to determine if the target is a covered foreign person, whether any entity the target has an interest in is a covered foreign person (and, if so, if it contributes to the target's overall finances in a manner that results in the target itself becoming a covered foreign person). Treasury has indicated that U.S. persons are "expected to use, among other resources, available public and commercial databases to attempt to identify relevant information or verify relevant information provided by an investment target." See FAQ V.4.