LEGAL UPDATES

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Biden Administration Issues Executive Order to Restrict U.S. Investment in Chinese Technology Sectors

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Last week, President Biden issued an Executive Order outlining the long-anticipated proposed restrictions on outbound U.S. investments in entities located in China or otherwise subject to China's jurisdiction. The Executive Order would establish a new national security program to be implemented by the U.S. Department of the Treasury, and according to the Biden administration, the program would target "countries of concern" that seek to develop sensitive or advanced technologies and products critical for military, intelligence, surveillance, or cyber-enabled capabilities. The Treasury Department has already established a website for this outbound investment program, which provides copies of a press release and a fact sheet discussing the proposed restrictions in further detail.

Importantly, the Executive Order does not implement any regulations, nor does it contain any draft regulations. Instead, the Treasury Department has used the authority provided under the Executive Order to issue an Advance Notice of Proposed Rulemaking (ANPRM) which outlines the intended scope of the program and starts a 45-day comment period in which the Treasury Department will seek feedback from the public on the restrictions. The Treasury is expected to issue its proposed draft regulations sometime next year.

The ANPRM generally envisions implementing regulations which will outright prohibit persons subject to U.S. jurisdiction from making certain extremely sensitive investments related to China and then require them to provide prior notification to Treasury before making other less sensitive investments related to China. Key aspects of the ANPRM include (but are not limited to):

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The proposed restrictions and reporting requirements will cover any **"countries of concern"** as identified by the president. Thus far, the only designated "country of concern" is China, which also includes the Special Administrative Regions of Hong Kong and Macau.

The ANPRM proposes to target U.S. investments in companies subject to China's jurisdiction which are engaged in activities related to the following advanced technologies and products:

> **(i) Semiconductors and microelectronics.** Proposed **prohibited investments** would include investments in entities engaged in the development of electronic design automation software or semiconductor manufacturing equipment; the design, fabrication, or packaging of advanced integrated circuits which meet or exceed certain performance capabilities; and the installation or sale of supercomputers. Proposed **notification requirements** would cover investments in entities engaged in the design, fabrication, and packaging of integrated circuits with performance capabilities below the investment prohibition threshold.
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> **(ii) Quantum information technologies.** Proposed **prohibited investments** would include investments in entities engaged in the production of quantum computers and certain related cooling components; the development of certain quantum sensing platforms to be exclusively used for military end uses, government intelligence, or mass-surveillance; and the development of a quantum network or communication system designed to be exclusively used for secure communications. Treasury stated it is not currently considering a separate **notification requirement** for this category.
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> **(iii) Artificial intelligence systems.** Proposed **prohibited investments** would include investments in entities engaged in the development of software that incorporates an AI system and is designed to be either "exclusively used" (the Treasury Department indicated that the term "primarily used" is also under consideration) for military, government intelligence, or mass-surveillance end uses. Proposed **notification requirements** would cover investments in entities engaged in the development of software that incorporates an AI system and is designed to be either "exclusively used" (or possibly "primarily used") for certain uses related to cybersecurity, robotic controls, surreptitious listening, non-cooperative location tracking, or facial recognition.

The ANPRM anticipates the prohibitions and/or notification requirements will apply to U.S. investments in companies that are engaged in the above activities and that are **legally organized and/or headquartered in China or owned by Chinese citizens or the Chinese government, in addition to companies located *outside* of China that are at least 50%**

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owned, individually or in the aggregate, directly or indirectly, by Chinese citizens, Chinese parent companies, or the Chinese government.

The ANPRM also proposes prohibiting or requiring notice for certain transactions, including **greenfield investments** in certain industries in China. From a practical standpoint, this could restrict certain companies from forming subsidiaries in China if they do business in any of the industries subject to the ANPRM's prohibitions or notice requirements.

The ANPRM technically only applies to **U.S. persons**, which it defines as any U.S. citizen, lawful permanent resident, entity organized under U.S. law (including foreign branches), and any person in the U.S. However, Treasury is considering imposing requirements which could effectively extend the ANPRM's restrictions to subsidiaries legally organized outside the U.S. by prohibiting U.S. persons from "directing" any action by a non-U.S. person that would violate the ANPRM's restrictions if performed by a U.S. person. The ANPRM also contemplates requiring U.S. persons to take appropriate action to cause foreign-organized subsidiaries under their control to comply with its restrictions.

When the Treasury Department does eventually enact implementing regulations under the Executive Order and the ANPRM, it does not appear that the Treasury Department will seek to retroactively impose those regulations' prohibitions and notification requirements on transactions conducted before the forthcoming regulations' eventual effective date. However, once the Treasury Department does implement these regulations, the ANPRM explicitly states that Treasury is "not considering granting retroactive waivers or exemptions (i.e., waivers or exemptions after a prohibited transaction has been completed)." Therefore, once the new rules take effect, companies will need to **avoid prohibited transactions** and **proactively disclose reportable transactions** to avoid violating the new rules.

Comments to the ANPRM must be submitted within **45 days** after the ANPRM is published in the Federal Register. The ANPRM was published on August 14, 2023, and therefore comments must be received by **September 28, 2023**, to be considered. If you are interested in submitting a comment, please reach out to HB's export controls and economic sanctions team or your HB contact for additional guidance.

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The ANPRM's prohibitions appear to apply to a very narrow segment of industries and therefore may only impact a very small number of U.S. investors (if any). However, even if their transactions will not implicate any of the ANPRM's prohibitions or notice requirements, persons subject to U.S. jurisdiction and seeking to invest in China should be aware that various other existing U.S. laws and regulations could still severely restrict their ability to invest in China. For example, export controls imposed under the U.S. International Traffic in Arms Regulations (ITAR) and U.S. Export Administration Regulations (EAR) will potentially restrict any exports of U.S. origin "technical data" or "technology" to China made in connection with otherwise permissible foreign investments. If Chinese companies do receive U.S. origin software or technology in connection with any U.S. investment, then products manufactured in China through the use of such software or technology could become subject to the EAR's export controls pursuant to the EAR's existing foreign-produced direct product rules. Additionally, sanctions imposed by the U.S. Treasury Department's Office of Foreign Assets Control (OFAC) will prohibit U.S. persons from purchasing any publicly traded securities issued by certain companies listed on the Non-SDN Chinese Military Industrial Complex List.

Contact us

Husch Blackwell's Export Controls and Economic Sanctions Team will be closely monitoring the Treasury Department's implementation of these forthcoming outbound investment regulations. If you have questions regarding the Executive Order or the ANPRM, please contact Cortney Morgan, Grant Leach, Emily Mikes, Eric Dama, or your Husch Blackwell attorney.

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