Comments of the
Semiconductor Industry Association

On

The Notice of Proposed Rulemaking Entitled
"Provisions Pertaining to U.S. Investments in Certain National Security Technologies and Products in Countries of Concern"

89 Fed. Reg. 55846 (July 5, 2024)
RIN 1505-AC82
Docket ID TREAS_FRDOC_0001–0461

August 4, 2024

The Semiconductor Industry Association ("SIA") submits these comments in response to the request from the Office of Investment Security within the Department of the Treasury ("Treasury") in the above-captioned notice. The Notice of Proposed Rulemaking ("NPRM") seeks public comment on various topics related to the implementation of the Executive Order 14105 of August 9, 2023, "Addressing United States Investment in Certain National Security Technologies and Products in Countries of Concern" (the "Order"). The Order declared a national emergency using the International Emergency Economic Powers Act to address the threat to the United States posed by the advancement by countries of concern in sensitive technologies and products.

Part I contains introductory and background comments about SIA and semiconductors. Part II contains general comments about the new program and related requests for Treasury to consider. Part III contains responses to relevant issues for stakeholder comment that are set forth in the NPRM.

Part I – Introduction and Background

SIA has been the voice of the U.S. semiconductor industry for over 45 years. SIA member companies represent more than 99% of the U.S. semiconductor industry by revenue and nearly two-thirds of non-U.S. firms, and are engaged in the research, design, and manufacture of semiconductors. The U.S. is the global leader in the semiconductor industry, and continued U.S. leadership in semiconductor technology drives economic strength, national security, and global competitiveness. More information about SIA and the semiconductor industry is available at www.semiconductors.org.

Semiconductors are complex products critical to the functioning of everyday consumer electronics, communications, and computing devices in the automotive, industrial, financial, medical, retail, and many other sectors of the economy. They are also critical components for future technologies, such as artificial intelligence ("AI"), quantum computing, and 5G/6G telecommunications. Few industries, if any, have a supply chain and development ecosystem as complex, geographically widespread, and interdependent as the semiconductor industry.

Domestically, maintaining a strong U.S. semiconductor research, design, manufacturing, and supplier base is both an economic security and a national security imperative. As stated in both the House and Senate versions of the 2021 National Defense Authorization Act: *"The leadership of the United States in semiconductor technology and innovation is critical to the economic growth and national security of the United States."*[1] Given how important the economic vitality and competitiveness of the U.S. semiconductor industry is to national security, as a general matter, it is critical to ensure that any outbound investment regulatory regime is narrowly tailored and designed to achieve specific, clearly articulated national security objectives.

SIA has long supported policies that safeguard national security without unduly harming commercial innovation, manufacturing, employment, and continued American leadership in critical technologies. While SIA recognizes that appropriate measures designed to address risks from outbound investment may be necessary to fill gaps in existing legal authorities and complement policy tools like export controls and inbound investment review, it is imperative that such measures be coordinated in both scope and timing with measures implemented by allied and partner governments.

As explained in SIA's September 2023 comments,[2] China is the single largest sales market for semiconductor firms, accounting for more than a third of U.S. chip revenue, as well as the largest market for semiconductor manufacturing equipment sales. China also remains an important link in global semiconductor supply chains, comprising around 20% of front-end and nearly 40% of back-end semiconductor production capacity. We respectfully request that Treasury ensure that final rules will allow U.S. chip firms to compete on a level-playing field and access key global markets, which is critical to promote the long-term strength of the U.S. semiconductor industry and its ability to out-innovate global competitors, thereby strengthening U.S. national security over the long term.

In addition, with the revenue needed to maintain U.S. technology leadership impacted by U.S. government restrictions, we strongly encourage the U.S. government to actively pursue proactive trade and economic policies aimed at opening and expanding market access for semiconductors in third countries – namely to grow the addressable market

---

[1] H.R. 6395 § 1824(b) and S. 4049 § 1098(b).
[2] Comments of the Semiconductor Industry Association (SIA) on "Provisions Pertaining to U.S. Investments in Certain National Security Technologies and Products in Countries of Concern, 88 Fed. Reg. 54961 (Aug. 14, 2023). September 28, 2023. (*Available at* https://www.semiconductors.org/wp-content/uploads/2024/07/SIA-Comments-on-Treasury-Outbound-ANPRM.pdf)

outside of China. We likewise urge the U.S. government to address trade barriers that impact our companies' ability to operate their complex global supply chains and ultimately sell their semiconductor products in foreign markets.

SIA and our members are increasingly concerned about the unilateral nature of this proposed rule, along with many other economic and national security motivated actions the U.S. government is taking, which directly impact our member companies' ability to compete on a level playing field globally.

Finally, SIA and our member companies recognize the need to protect national security and believe maintaining a healthy U.S. semiconductor industry is an essential component to achieving that goal. To that end, SIA has long been a partner of the U.S. government in providing support and feedback regarding economic security policies, particularly with respect to semiconductors. SIA appreciates the opportunity to provide its comments, questions, and requests.

Part II – General Comments

Comment II.A: Foreign entities are already replacing U.S. financing and technological expertise in countries of concern, even before the program is implemented. Uncoordinated, unilateral U.S. outbound investment restrictions will lead to divergent or incompatible national approaches and decrease the global competitiveness of U.S. semiconductor firms, which undermines national security.

Given that U.S. and allied-headquartered companies directly compete in high-tech industries such as semiconductors, it is in the United States' strategic interest that partner governments implement outbound investment regimes with similar scope and effect as what is contemplated in the NPRM. If not, U.S. semiconductor companies likely will confront several new challenging realities. First, U.S. chip companies will be at a significant competitive disadvantage vis-à-vis foreign competitors, while the targeted sectors in countries of concern might not be adversely affected and will continue to have access to sensitive technologies and the "intangible benefits" described in the NPRM.

Second, U.S. semiconductor companies will be forced to cede their market share to foreign competitors, while investors from other countries may even be incentivized to forge partnerships within the targeted sectors in countries of concern in the absence of U.S. investment activity. These impacts will ultimately undermine the national security objectives of the NPRM's notification and prohibition requirements and erode U.S. leadership and strategic advantage in critical technology sectors like semiconductors, and other strategic industries that rely on semiconductors. Accordingly, the outbound investment regime could have the opposite effect of its intended policy objective.

U.S. foreign direct investment and venture capital transactions in China have already declined over the past several years, down nearly 52% from 2022 to 2023, and this trend is expected to continue.[3] In contrast, after a decline from 2018-2021, European outbound investments in China grew by 92.2% in 2022, according to foreign direct investment (FDI) data from China's Ministry of Commerce (MOFCOM).[4]

Much of this investment activity is happening in important semiconductor end markets and applications, such as the automotive sector and AI. For example, a leading European automaker announced plans to boost investment in its Chinese joint venture to nearly $2 billion in March 2024, and pledged to use more local components for its vehicles.[5] The same automaker has also established another joint venture with a Chinese auto tech startup, which is focused on rolling out automated driving technology powered by the Chinese firm's AI processors.[6] Separately, another automaker invested an additional $2.76 billion in China.[7] At the same time, China's Ministry of Industry and Information Technology is developing national standards for chips used in the automotive sector, and the Chinese government has issued directives to Chinese companies to design out U.S. and Western chips.[8] European investments in Chinese AI companies have also grown since 2017.[9] For example, a European company set up a dedicated fund in China to invest in advanced technology companies, including companies designated on the Entity List issued by the Department of Commerce's Bureau of Industry and Security (BIS).[10]

The NPRM states, "the Department of the Treasury, along with the Departments of State and Commerce, will continue to work with partners and allies as they explore addressing the national security concerns posed by certain outbound investments." To that end, while we acknowledge the U.S. government's well-meaning efforts to engage with U.S. allies and partners, and appreciate that such engagement is a complex and

[3] S&P Global, US-backed funding rounds in China fall to lowest in a decade. June 6, 2024. (*Available at* https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/us-backed-funding-rounds-in-china-fall-to-lowest-in-a-decade-81822765)
[4] http://www.mofcom.gov.cn/article/syxwfb/202301/20230103379768.shtml
[5] *Reuters*, Volkswagen Group China plans to boost investment in majority-controlled JV. March 12, 2024. (*Available at* https://www.reuters.com/business/autos-transportation/chinas-jianghuai-automobile-volkswagen-china-boost-investment-jv-2024-03-12/)
[6] TechNode, VW's JV to hire 300 workers with Horizon Robotics. December 11, 2023. (*Available at* https://technode.com/2023/12/11/volkswagens-china-jv-with-horizon-robotics-to-hire-300-workers/)
[7] *Reuters*, BMW to invest a further $2.76 billion in key market China. April 26, 2024. (*Available at* https://www.reuters.com/business/autos-transportation/bmw-invest-276-billion-chinese-production-site-2024-04-26/)
[8] Chamber of Commerce in China, China Accelerates Development of Automotive Chip Standards. January 15, 2024. (*Available at* https://shanghai.bencham.org/news/china-accelerates-development-automotive-chip-standards); *Nikkei Asia*, Top China chipmakers SMIC and CXMT push to scrap foreign inputs. May 21, 2024. (*Available at* https://asia.nikkei.com/Business/Tech/Semiconductors/Top-China-chipmakers-SMIC-and-CXMT-push-to-scrap-foreign-inputs)
[9] Mercator Institute for China Studies, AI entanglements: Balancing risks and rewards of European-Chinese collaboration. November 16, 2023. (*Available at* https://merics.org/en/report/ai-entanglements-balancing-risks-and-rewards-european-chinese-collaboration)
[10] Pandaily, Cambricon SingGo Secures Investment From Bosch. September 23, 2022. (*Available at* https://pandaily.com/cambricon-singgo-secures-investment-from-bosch/)

ongoing diplomatic process, the results of these efforts so far fall well short of multilateral alignment.

As it stands, SIA observes that major semiconductor producing countries and allies with significant commercial ties with "certain countries of concern" do not appear anywhere close to establishing their own regimes to regulate outbound investment. For example, while investment security is clearly a topic of discussion in multilateral forums such as the U.S.-EU Trade and Technology Council[11], the European Union ("EU") remains in an exploratory phase with respect to both assessing risks and taking action. In fact, in a policy paper issued earlier this year,[12] the European Commission ("EC") made clear that it will pursue a "gradual step-by-step approach" with respect to outbound investment; only after a yearlong "monitoring" period that ends in late 2025 will the EC even be in a position to "assess" the risks linked to outbound investment transactions. That same document also made clear that, after the monitoring and assessment phases, should the EC and EU Member States ultimately determine that a policy response is "necessary," the EC will first seek to address any identified risks through existing instruments, such as export controls and foreign direct investment screening mechanisms, before designing any new policy mechanism specific to outbound investment.

Other important allies and major semiconductor producing countries appear to be even less further along in their assessment of risks related to outbound investment, let alone pursue regulatory action. SIA observes that references to outbound investment are notably absent from the joint statements of recent economic security dialogues with key allies, such as Japan and Korea, including at the Leaders level.[13]

These comparisons underscore that, even in the most optimistic scenario, U.S. companies will face restrictions for a significant period of time while companies headquartered in these allied countries will be largely unencumbered and free to pursue business transactions in countries of concern. This will lead to further economic integration and commercial ties with countries of concern that will complicate those governments' efforts to establish regimes similar to the proposed rules under the NPRM down the road.

---

[11] European Commission, Joint Statement EU-US Trade and Technology Council of 4-5 April 2024 in Leuven, Belgium. April 5, 2024. (*Available at* https://ec.europa.eu/commission/presscorner/detail/en/statement_24_1828)

[12] European Commission, White Paper on Outbound Investments, January 24, 2024. (Available at https://circabc.europa.eu/ui/group/aac710a0-4eb3-493e-a12a-e988b442a72a/library/51124c0d-58d8-4cd9-8a22-4779f6647899/details?download=true)

[13] Department of the Treasury, Japan-Republic of Korea-United States Trilateral Ministerial Joint Press Statement. April 17, 2024. https://home.treasury.gov/news/press-releases/jy2264; White House, United States-Japan Joint Leaders' Statement, April 10, 2024, (*Available at* https://www.whitehouse.gov/briefing-room/statements-releases/2024/04/10/united-states-japan-joint-leaders-statement/)

Further, the NPRM does not concretely incentivize other countries to establish their own outbound investment security regimes. While the NPRM provides for the potential application of the term *excepted transaction* for certain transactions involving persons of third countries – it appears that this mechanism is intended to operate as an incentive for countries to put in place their own regimes by providing for a carve out – it is unclear precisely how such an exception would apply.

Although not yet developed, one potential mechanism for such an *excepted transaction* carve out could be permitting U.S. investments into entities organized in those countries, even if they are *covered foreign persons* as a result of satisfying the criteria in § 850.209(b) (e.g., receiving more than 50% of their revenue from covered foreign persons). However, it is unclear if Treasury has gathered relevant data to determine the total number of companies in third countries that would potentially benefit from such an exception. It is likely that any such exception would only apply to a small number of companies in any given country, which may not sufficiently incentivize third countries to take action. In addition, should Treasury opt to consider "other factors" (e.g., export controls to protect sensitive technologies and products) when choosing to designate a country, the country could gain the benefit of the incentive without having to establish its own outbound regime.

This is somewhat in contrast to the incentive in the Foreign Investment Risk Review Modernization Act of 2018 ("FIRRMA"). FIRRMA allows countries that take certain actions (including have their own process to analyze foreign investments for national security risks) to be candidates for selection as an "excepted foreign state," meaning that *all* investments from qualifying entities in those countries are carved out entirely from CFIUS's mandatory filing programs. Accordingly, the incentive provided under FIRRMA appears to represent a clearer benefit for a third country to establish an inbound regime as compared to the proposed rule in connection with the outbound regime *and* is more clearly tailored to motivating third countries to establish the same type of underlying regime.

We are concerned that the U.S. government's plan to proceed with regulatory action in the absence of similar regimes in other countries will place the U.S. semiconductor industry at a structural and strategic disadvantage vis-à-vis its global competitors, creating an opportunity for chip companies in countries of concern to gain market share, both domestically and globally. SIA member companies are already experiencing these competitive pressures in key end markets, such as the automotive sector. In the longer term, however, SIA sees a number of risks if the U.S. continually moves forward with restrictive actions absent a critical mass of partners willing to take similar actions on similar timeframes. Chief among these risks is the likelihood that the interest among and between the U.S. and its allies will diverge rather than converge over time. Countries of concern will inevitably exploit and enhance these differences.

The longer there is misalignment between U.S. approaches to outbound investment and other economic security tools – both in scope and timing – and those of allied and partner governments, the greater the risk that foreign adversary governments will deploy tools and measures to “divide and conquer,” shifting the decision calculus of allied and partner governments and potentially making them less willing or able to align with U.S. policy approaches.

We have previously voiced similar concerns[14] about the negative impacts of unilateral export control actions to U.S. companies that produce chips as well as chip-making equipment. We continue to see a similar risk of U.S. unilateral actions leading to divergence, rather than convergence, with allied and partner governments with respect to outbound investment restrictions.

Comment II.B: The NPRM significantly broadens the scope of *covered transaction* from the ANPRM by including expansions of existing operations or joint ventures and imposing an “intent” standard.

Including expansions of existing operations or joint ventures within the definition of *covered transaction* represents a significant broadening of the program’s scope relative to the ANPRM. The breadth of activities encompassed within the definition of *notifiable transactions* (i.e., designing, fabricating, or packaging of any integrated circuit (“IC”) that is not covered by the *prohibited transaction* definition), suggests that Treasury likely must be apprised of potentially any and all semiconductor transactions in a country of concern. Additionally, the NPRM adopts an “intent” standard in connection with greenfield or brownfield investments and joint ventures. In doing so, Treasury seeks to cover activities in which the *U.S. person* intends to bring about through the establishment of a *covered foreign person* or a *person of a country of concern*’s engagement in a new *covered activity*. The rationale for this intent standard, according to the NPRM, is that a *U.S. person* may not *know* at the time of the transaction that the entity will engage in a *covered activity*, yet Treasury seeks to capture transactions that are likely to convey intangible benefits. For many early-stage companies, their intended

[14] Comments of the Semiconductor Industry Association (SIA) on “Additional Export Controls: Certain Advanced Computing and Semiconductor Manufacturing Items; Supercomputer and Semiconductor End Use; Entity List Modification,” (87 Fed. Reg. 62186 (October 13, 2022)). January 10, 2023. (*Available at* https://www.semiconductors.org/wp-content/uploads/2024/07/SIA-Comments-to-BIS-on-October-2022-IFR.pdf); Comments of the Semiconductor Industry Association (SIA) on “Implementation of Additional Export Controls: Certain Advanced Computing Items Supercomputer and Semiconductor End Use; Updates and Corrections,” (88 Fed. Reg. 73458 (Oct. 25, 2023)). January 17, 2024. (*Available at* https://www.semiconductors.org/wp-content/uploads/2024/07/SIA-Comments-to-BIS-on-Advanced-Computing-IFR.pdf); Comments of the Semiconductor Industry Association on “Export Controls on Semiconductor Manufacturing Items,” (88 Fed. Reg. 73424 (October 25, 2023)). January 17, 2024. (*Available at* https://www.semiconductors.org/wp-content/uploads/2024/07/SIA-Comments-to-BIS-on-Semiconductor-Manufacturing-IFR.pdf); Comments of the Semiconductor Industry Association on “Implementation of Additional Export Controls: Certain Advanced Computing Items; Supercomputer and Semiconductor End Use; Updates and Corrections; and Export Controls on Semiconductor Manufacturing Items; Corrections and Clarifications,” (89 Fed. Reg. 23876 (April 4, 2024). April 29, 2024. (*Available at* https://www.semiconductors.org/wp-content/uploads/2024/04/SIA-Comments-on-Corrections-and-Clarifications-IFR.pdf)

products or services may ultimately not come to fruition or may evolve into something different. Prohibiting investment based on “intent” will likely have the unintended effect of chilling investment in early-stage companies (e.g., because a *U.S. person* might fear that Treasury will incorrectly interpret certain facts as satisfying the requisite intent standard), thereby diverting resources away from innovative and emerging companies and technologies. The “intent” standard also introduces the possibility of expansive interpretive applications. It is unclear from the NPRM whose intent is relevant and how “intent” is meant to be addressed or established. In addition, parties to one transaction may have differing “intent” for its outcome, resulting in ambiguity.

The definition of a *covered transaction* also now includes certain *U.S. person* investments in a foreign fund that might become *prohibited* or *notifiable transactions* based on the fund’s *subsequent* investments. For instance, Example 8 in the “Knowledge requirement for a covered transaction” of the NPRM provides a hypothetical situation whereby a *U.S. person* investing in a foreign fund, Company M, had reason to know (and is therefore deemed to have known) that Company M *was likely to invest* in a person of a country of concern in the semiconductors and microelectronics, quantum information technologies, or AI sectors. In the example, the *U.S. person’s* investment in Company M is only prohibited if Company M subsequently undertakes a transaction that would be a *covered transaction* if undertaken by a *U.S. person*.

This expansion of *covered transactions* has two key flaws. First, to ensure compliance with the outbound investment security regime, a *U.S. person* that invests in a foreign fund that is likely to invest in one of the three sectors must conduct routine and detailed post-closing diligence to determine whether the fund’s investments trigger a *notifiable transaction*. Such an ongoing obligation to regularly monitor the fund’s investments post-closing would be burdensome. Instead, the *U.S. person’s* obligation to conduct the requisite diligence and analysis in connection with its investment in the fund should cease once the U.S. person’s investment in the fund has closed. If the *U.S. person* considers a subsequent investment in the fund, it could still be obligated to re-run its diligence. Second, a *U.S. person’s* compliance would hinge on the *post-investment* actions of third parties, effectively deterring some *U.S. person* investments that ultimately might not fall within the scope of the outbound investment security regime. In the scenario described in the NPRM, the *U.S. person* is forced to decide whether it is “likely” that Company M will invest in persons of a country of concern engaged in one of these sectors, and, in many cases, the *U.S. person* likely will opt not to invest in Company M, even though Company M might never engage in a transaction that would be a *covered transaction* if undertaken by a U.S. person (i.e., Company M’s investments might never trigger a *notifiable* for the *U.S. person*). Accordingly, the NPRM’s overly broad standard will deter investments outside of the scope of the regime and is inconsistent with statements in the NPRM suggesting the U.S. government is in favor of “an open investment environment” and a narrowly tailored approach.

The broad scope of the regulations will also likely become unmanageable for U.S. semiconductor companies from a compliance perspective. For example, overly expansive notification requirements could create burdensome disclosure requirements for some companies. Indeed, such requirements could drive otherwise innovative companies to divert resources away from essential research and development and toward compliance.

Part III – Issues for Comment

Below, SIA provides comments on select questions posed by Treasury in Section IV of the NPRM.

1. Are there areas where the proposed rule is broader than necessary to address the national security concerns identified in the Outbound Order? Are there areas where it is narrower than necessary or contains loopholes? If so, where and what adjustments should be made?

SIA Comment: In certain cases, the scope of *covered activities* exceeds what is currently regulated under U.S. export controls. The NPRM targets all semiconductor electronic design automation (“EDA”) software for the design of ICs or advanced packaging, whereas corresponding export controls only exist for certain EDA software.

When the U.S. government identifies a discrete national security concern, restricting the transfer of items with export controls is prudent. Casting a wider net that entangles “enabling” technologies will only accelerate decoupling and “design-out” of U.S. technology in non- sensitive areas, thereby damaging the competitiveness of the U.S. semiconductor industry. For example, BIS, in cooperation with allies who are members of the Wassenaar Arrangement, has already subjected EDA software for gate-all-around field effect transistors (“GAAFET”) to national security controls. A successful outbound investment screening program should conform to, and should not exceed, these specific multilateral controls. Indeed, SIA provided comments in response to Item 29 of the ANPRM, in which we recommended that Treasury should harmonize definitions with the EAR, which would aid industry compliance efforts with these and other regulations. Our previous comments also provided detailed feedback on the definition for EDA.

2. How could the knowledge standard in the proposed rule be clarified? What, if any, alternatives should be considered? What other factors should be considered to assess whether a person conducted a reasonable and diligent inquiry?

The NPRM requires a *U.S. person* to file a notification within 30 days of obtaining “actual knowledge” of facts that would have made a prior transaction either notifiable or prohibited. However, the NPRM is not clear as to whether this responsibility to update Treasury only relates to circumstances in place at the time of the original transaction. The NPRM does not address the circumstance where a target company pivots into a different line of business that could be a *prohibited activity*. A target company may have plans to potentially engage in covered activities in the future, but the NPRM offers little to no guidance as to 1) how far into the future an investor must consider when assessing a target company's activities and 2) how mature those plans must be before the investment is brought within the scope of the rules. Would a *U.S. person* be required to divest its original investment if the due diligence conducted at the time of the investment met the NPRM requirements? The NPRM also does not provide a period of time during which a U.S. person is required to update their initial or subsequent filings with Treasury before responsibility for monitoring compliance ceases.

SIA recommends the NPRM be revised so that a *U.S. person* does not have an obligation to update a notification filing made in connection with a transaction until such *U.S. person* is considering a subsequent investment in the target company. The revision should also create 1) a clear exception from being forced to divest from an investment where a target company later pivots into a prohibited *covered activity*, but the notification filing (if required) otherwise satisfied the rules at the time of the investment and 2) offer a safe harbor for transactions for which thorough and documented due diligence was conducted, and with which Treasury is satisfied that the *U.S. person* <u>did not have knowledge</u> and undertook sufficient and proper due diligence.

3. What considerations should the Department of the Treasury take into account with respect to the ease or difficulty with which a *U.S. person* will be able to comply with the proposed rule, particularly with respect to ascertaining whether an investment target or relevant counterparty is a *person of a country of concern* and engaged in a *covered activity*?

<u>SIA Comment</u>: In determining whether to invest in a target company, the proposed rules require the *U.S. person* to conduct a "reasonable and diligent inquiry" to determine whether the target company is a *person of a country of concern*. By including "direct and <u>indirect</u>, individually and <u>in the aggregate</u>" in the definition, the diligence obligation put on the *U.S. person* is too broad and simply unworkable in many venture capital investments. The burden on *U.S. persons* in both time and money to gather direct and indirect ownership information on investors in a target company who hold less than 10% of the voting power or equity of a target company is extreme and will, among other things, place an undue burden on U.S. persons to conduct the requisite diligence to meet the definition. Importantly, this detailed level of diligence would be required in every venture capital investment. As drafted, a *U.S. person* must obtain information on all parties with a voting, board, or equity interest in the target company as well as the same details for any investors in those parties, until the *U.S. person* determines the ultimate owner of each such investor in the target company. Furthermore, the proposed rules require the *U.S. person* to gather this detailed ownership information on potentially hundreds of parties, and then <u>aggregate</u> their individual voting, board, or equity stakes

together (if they meet the criteria in § 850.221(a), (b) or (c)) to determine if they exceed 50% of voting or board power in the target company, and therefore render the target company a *person of a country of concern*. In venture capital investing, a target company might have 100 investors with de minimis ownership stakes. In addition, certain entities may be hesitant to disclose such detailed information on their ownership structure, especially further down the organization chain. Employees also often hold equity in a start-up company, as it is often a form of compensation for start-up companies. This outcome is burdensome and far beyond the scope of what should be required.

We recommend removing the aggregation of various unrelated parties' ownership stakes in the target company. The rule could require that affiliates are aggregated together for determining the affiliated group's ownership stake. The rules should also set a *de minimis* threshold and exclude small ownership investments in the target company below 10% of the outstanding voting power or equity (either individually or when aggregated with affiliates) in the target company. The *de minimis* threshold would also exclude most rank-and-file employees without any decision-making authority at the target company. Investors with a right to appoint a board member, regardless of their ownership stake, could be included.

The rules also require the *U.S. person* to conduct detailed diligence on "relevant counterparties," but the term is not defined, and guidance is not provided. In the investment context, does this include co-investors, the target company's stockholder, possible end-users of the target's product or services, or others? Would the investing *U.S. person* also be expected to gather details on the ultimate owner of each of these entities?

It would be unusual for a minority investor acquiring equity or debt in a start-up company to conduct diligence on any of those categories of "counterparty." In fact, it is often the case that an investor acquiring a minority stake does not know the identity of its co-investors or of the target company's stockholders until immediately prior to the closing of the investment, if at all. The expectation that *U.S. persons* will obtain detailed, complete responses from such third parties will negatively impact the ability of *U.S. persons* to participate in investment transactions in countries of concern because it will greatly slow down the timing of the transaction and chill the U.S. investing market as foreign persons refrain from inviting *U.S. persons* to participate. Requiring *U.S. persons* to conduct diligence on "relevant counterparties" may even have the unintended result of forcing *U.S. persons* to make larger investments in countries of concern so that these counterparties are incentivized to provide the request information.

Therefore, we request a definition of the term "relevant counterparty" and limit the required diligence to parties participating in the transaction. This enables the parties to the transaction to agree on reasonable representations and warranties addressing the areas of concern.

Further, the NPRM defines a "covered foreign person" to include any person (including a *U.S. person*) that directly or indirectly holds any voting interest, board seat, or equity interest in a *person of a country of concern* that is "engaged in" a *covered activity*. While the proposed rule identifies such "covered activities," (e.g., "fabricat[ing]" certain ICs), it offers no guidance or direction on what it actually means for a particular entity to "*engage in*" such covered activities. For example, has Treasury considered what it means for an entity to "engage in" the "fabricat[ion]" of ICs? U.S. businesses must determine whether, for example, the mere ownership of intellectual property ("IP") that may be related to a *covered activity* may constitute being "engaged in" a *covered activity*, or whether an entity that has a board of directors that directs the activities of a subsidiary that performs a *covered activity* would be considered "engaged in" a *covered activity*. This ambiguity creates serious implementation challenges for U.S. businesses trying to determine whether a transaction counterparty is a *covered foreign person*. As a practical matter, and to aid compliance with the regulations, we recommend that Treasury adopt a *de minimis* threshold for what constitutes being "engaged in" a *covered activity* for purposes of assessing whether an entity is a covered foreign person (*see* also SIA's response to Question 6 below regarding a *de minimis* threshold).

Similarly, the "covered foreign person definition" includes any person that attributes more than 50% revenue, net income, capital expenditure, or operating expenses to a *person of a country of concern* that is "engaged" in a *covered activity*, individually or in the aggregate with other such persons. The term "engaged" remains undefined in this prong of the definition, making the 50% rule significantly challenging to implement in practice, for reasons noted in the above paragraph.

In addition to adopting a formal definition for the term "engaged," SIA also recommends that Treasury revise the 50% rule to apply only if attributable to a single entity, rather than in the aggregate. The aggregation requirement creates a challenging diligence burden that would require U.S. companies to confirm that their transaction counterparties, including even U.S. counterparties, have aggregated the revenues or expenses of all applicable interests which may be allocated across tens or hundreds of different companies and equity positions that are not connected to each other (*see* also SIA's response to Question 12 below regarding proposed definitions).

4. Are there adjustments to the scope of *covered activities* identified in the definition of either *notifiable transaction* or *prohibited transaction* in the proposed rule (including addition(s), removal(s), or elaboration(s)) that should be made to help ensure that the definition addresses the national security concerns identified in the Outbound Order and discussed above while minimizing unintended consequences? If so, what are they?

<u>SIA Comment:</u> SIA notes it would be helpful to have *covered activities* (and related items) as defined in § 850.208 in the proposed rule tied more directly to export classifications or other technical methods for identifying certain categories of advanced technologies and products.

6. How do *U.S. persons* anticipate ascertaining the information necessary to comply with paragraph (a)(2) of the definition of *covered foreign person* at § 850.209? How, if at all, should this definition be adjusted for a situation in which no financial statement (audited or otherwise) is available for a covered foreign person?

SIA Comment: By declining to include either a *de minimis* threshold based on the financial significance of a *covered activity* or maintaining and updating a publicly available list of *covered foreign persons*, the NPRM has significantly increased the difficulty of ascertaining the information necessary to comply with paragraph (a)(2) of the definition of *covered foreign person* at § 850.209. Investors generally seek this type of information through due diligence requests, research, interviews, and other reasonable efforts but the lack of a direct relationship between the *U.S. person* and its target's subsidiaries in China will create sufficient challenges for the *U.S. person's* diligence. As a result, it will be difficult to determine with a high degree of certainty through diligence alone whether a target company possesses these types of ties.

Further, due to changes in the Chinese regulatory environment, certain information on Chinese parties is becoming harder to obtain, which will make it difficult for *U.S. persons* to comply with this section of the NPRM.

The language in § 850.209(b) of the proposed rule suggests that a determination about whether there is a covered foreign person under (a)(2) "*shall*" be made based on the most recent annual financial statement. Not every company will have annual financial statements. SIA notes that, although used in a different context, the Committee on Foreign Investment in the United States ("CFIUS") regulations regarding valuation of a business for purposes of determining CFIUS filing fees include the following language:

§ *800.1103(d): In determining fair market value, parties shall make a good faith estimate and generally may rely on the last valuation as presented in financial statements prepared in accordance with generally accepted accounting principles (GAAP) or other widely recognized accounting principles, such as the International Financial Reporting Standards, or the valuation of an independent appraiser; provided, however, that if no valuation has occurred within the prior two fiscal quarters, or if there have been significant changes to the fair market value since the last valuation, the parties shall make a good faith estimate at the time of filing the formal written notice, or, if the parties are filing after the completion of the transaction, the completion date of the transaction."*

SIA recommends that Treasury consider including language that states where no financial statements are available, the party *may* rely on information provided by independent appraisals or good faith estimates. As drafted, the proposed rule does not allow for a determination to be made pursuant to (a)(2) absent the existence of financial statements.

8. How, if at all, should the definition of *covered transaction* be modified with respect to the conversion of a contingent equity interest or convertible debt? What are the considerations as to the balance among minimizing compliance costs, avoiding over- or under-inclusiveness, while maintaining U.S. Government visibility into the instances of conversion?

SIA Comment: The NPRM provides that the provision of debt financing that affords or will afford a *U.S. person* the right to "make management decisions" on behalf of a covered foreign person would fall under the definition of a *covered transaction*. However, the intended scope of "make management decisions" is unclear. Does Treasury intend to include market standard debt covenants to be covered as management decisions? Debt covenants are conditions or restrictions that lenders often place on borrowers in a debt financing transaction (e.g., borrower must keep insurance or borrower cannot take on more debt or sell certain assets etc.). Given the NPRM's lack of clarity on this point, SIA recommends two options to Treasury: 1) expressly carve-out standard debt covenants from the definition of a *covered transaction* or 2) clarify the types of activities Treasury would consider as "making management decisions."

Additionally, are stock options and restricted stock units granted to employees of a *covered foreign person* covered by the definition of contingent equity interest? SIA recommends that these should not be included, as they do not improve U.S. government visibility into instances of conversion.

12. The proposed definition of *person of a country of concern* (in § 850.221(d)) and the proposed definition of *covered foreign person* (in § 850.209(a)(2)) could include a *U.S. person* entity. What considerations should the Department of the Treasury take into account with respect to an entity qualifying as a *U.S. person* and also as a *covered foreign person* or *person of a country of concern*? What are the instances in, and what is the frequency with which, this may occur?

SIA Comment: Further clarification is needed to ensure that *U.S. persons* are not improperly determined to be a *covered foreign person.* For example, in a scenario where a *U.S. person* owns an entity in a *country of concern* that is engaged in "covered national security technologies and products," would that U.S. owned foreign entity and *U.S. person* each be considered a *covered foreign person?* Would the 50% rule described in the NPRM also be applicable to any such analysis of *U.S. person* ownership? SIA recommends that Treasury consider the development of a test based on percentage ownership or control, for example, that would exempt a *U.S. person* from being a *covered foreign person*.

14. What are the considerations for *U.S. person* due diligence related to the specified end uses and computing thresholds in the different alternatives for an *AI system* in the definitions of *notifiable transaction* and *prohibited transaction*? How would a *U.S. person* investor determine the computational threshold levels

of any *AI system* of an investment target or relevant counterparty? What are the considerations with respect to making such determinations related to an entity of a *country of concern* specifically?

SIA Comment: Requiring the *U.S. person* to determine a *covered foreign person's* "intended" end use or end users asks the *U.S. person* to determine the intent of one or more third parties. This expectation is ambiguous and subjective and could lead to confusion between activities that are notifiable versus prohibited.

In the early-stage start-up environment, it is very difficult to ascertain an intended end use for the product or system. Indeed, the target company may not know or different individuals within the company may differ in their views. For example, if diligence materials for an AI image recognition technology refer to possible applications in smart infrastructure and congestion pricing, is that evidence of "intent" to develop mass surveillance capabilities? Further, is the "intent" that it be used exclusively in mass surveillance (and therefore prohibited) or not exclusively (and therefore notifiable)? Requiring the *U.S. person* to determine a foreign entity's intent, and if such transaction is prohibited, notifiable or neither as a result, will only chill the U.S. investment climate in certain sectors in China while simultaneously undercutting the U.S. government's goal of learning more about U.S. investment in these areas.

Rather than requiring a *U.S. person* to make a subjective determination of the "intent" of a third party, we suggest scoping the rules to require fact-based, technical criteria when determining whether, for example, a semiconductor activity falls into a notifiable or prohibited *covered activity*. The same should apply for any other potentially notifiable or prohibited *covered activity*.

17. How should the Department of the Treasury ensure the regulations remain responsive to changes in the sectors identified in the Outbound Order (i.e., the semiconductors and microelectronics, quantum information technologies, and artificial intelligence sectors)?

SIA Comment: The NRPM incorporates in its interpretation of *AI system* the definitions for "artificial intelligence" and "AI system" from Executive Order 14110, "Safe, Secure, and Trustworthy Development and Use of Artificial Intelligence" which was issued by President Biden on October 30, 2023 (the "AI Order"), after the ANPRM was published. Specifically, *AI system* is now defined to include not only the primary AI system itself, but also "any data system, software, hardware, application, tool, or utility that operates in whole or in part using" the AI system. While there may be a policy basis for implementing this broad definition in the context of the AI Order – which is focused on safety and security standards for AI and its wide-ranging applications – there is no clear reason or basis for the use of the definition in the context of the NPRM, particularly as such definition would have the effect of capturing not only entities directly engaged in developing AI but also any other entity that merely integrates such AI into their own technology. This is particularly the case as companies today are operating within the context of a fast-changing market landscape that has incentivized technology firms to purport to be "AI-driven" and/or adopt various AI functionalities without the capacity or intent to develop the underlying AI themselves. To minimize ambiguity regarding the scope of entities that could be covered and to ensure that the program is administrable, Treasury should remove prong (b) from the definition of *AI system*.

18. How, if at all, could the prohibition on *knowingly directing* a transaction be modified to best address national security concerns identified in the Outbound Order and discussed above while maximizing clarity and minimizing adverse impacts on *U.S. persons*, including their employment at foreign companies? What, if any, alternatives should be considered?

<u>SIA Comment:</u> As drafted, § 850.303 ("*Knowingly directing an otherwise prohibited transaction")* of the NPRM can be further clarified. Specifically, the final rule should make clear that a *U.S. person*, officer, director, or senior advisor, or a *U.S. person* who otherwise possesses senior-level authority at a non-U.S. person entity, should not be considered as *knowingly directing* a transaction undertaken by a non-U.S. person solely due to the *U.S. person's* title or authority. Instead, SIA recommends that Treasury clarify in the final rule that a *U.S. person* must actually exercise their authority to direct, order, decide upon, or approve a transaction to be considered as *knowingly directing* it. Further, the provision of third-party services, such as banking and routine administrative work by a *U.S. person* who lacks substantial involvement in investment decision making, should also be exempted in the final rule.

19. What is the practical utility of a recusal carveout from the prohibition on *knowingly directing* a transaction? What stage(s) of an investment should the recusal carveout from the prohibition on *knowingly directing* apply to (for example, should it apply to negotiating and decision-making related to an investment, management and oversight of the investment after the *completion date*, or something else), and why? In what ways could the recusal carveout's clarity or usefulness be enhanced?

<u>SIA Comment</u>: SIA is generally supportive of a recusal carveout from the prohibition on *knowingly directing* a transaction. To enhance the clarity and usefulness of the carveout, Treasury should make clear at which stage of a transaction a *U.S. person* is deemed to "make or substantially participate in decisions on behalf of a non-U.S. person, and exercises that authority to direct, order, decide upon or approve transaction." To the extent that the term *knowingly directing* is intended to capture (even absent a *U.S. person's* "exercise" of authority to "direct, order, decide upon, or approve a transaction") negotiating and decision-making related to an investment and management and oversight of the investment after the *completion date*, the recusal carveout should apply to those activities, too. This would likely allow *U.S. persons* who serve on the management committee at foreign funds to recuse themselves from *knowingly directing covered transactions* without adversely impacting their employment.

However, SIA reiterates to Treasury the importance of the final rule accommodating situations where investments made by a *U.S. person* would enable U.S. entities to establish leverage or control and retain visibility into the operation of a *covered foreign person* and/or the technological ecosystem of any *country of concern* (see also SIA comment to Question 24 regarding national interest exemption).

21. Are there categories of transactions that should be added to, or removed from, the definition of *excepted transaction* in light of the national security concerns identified in the Outbound Order? If so, what are they and why? What potential consequences should the Department of the Treasury consider in limiting the applicability of the definition of *excepted transaction* to a transaction made pursuant to a binding, uncalled capital commitment entered into before August 9, 2023?

SIA Comment: As previously stated in SIA's comments on the ANPRM, we believe that university-to-university research collaborations, company-to-university research collaborations, and intellectual property licensing arrangements and the sale of goods and services should be explicitly added to the definition of *excepted transaction*. While the preamble to the NPRM suggests that such activities do not meet the definition of a *covered transaction*, additional clarity would help prevent potential unintended consequences (e.g., encourage robust R&D investments and collaboration/support for the innovation ecosystem – including acceleration of pathways to commercialization).

The NPRM adopts terms such as "develop" "produce" "fabricate" and "design" in the definitions of *prohibited transaction* (§ 850.224) and *notifiable transaction* (§ 850.217) to describe activities that would be covered under the proposed rule. While some of these terms are further defined (e.g., "develop" at § 850.211; "produce" at § 850.223) the term "design" is not defined. It is therefore not clear whether, for example, an entity that is not itself engaged in a *covered activity* would nonetheless be viewed as engaging in a *covered activity* if it sells a product to a *covered foreign person* and provides further customer support to such covered person, including for example, support for integration of the product. Within the semiconductor industry, the provision of such customer support would not be understood to constitute the "design," "development," "production," or "fabrication" of a product. SIA recommends Treasury clarify that the definition of covered activities would not extend to the provision of customer support in connection with the sale of a product to a *covered foreign person* as part of an arms-length commercial transaction. Without clarification, the NPRM risks unintentionally expanding the definition of *covered foreign persons* to include even entities that are providing incidental support to covered activities. Without such clarification, this would be fundamentally inconsistent with the intent of the Order and introduce significant business uncertainty by capturing a broad swath of administrative business relationships and commercial commitments that are unrelated to investment activity.

SIA recommends a revision to § 850.501(b) (i.e., *exception for when U.S. person purchases all of the interests of a person of a country of concern in a covered activity)*.

Specifically, this section should be amended so that the *U.S. person* <u>is not required</u> to purchase <u>all of the interests</u> of persons of a *country of concern* but sufficient that such *persons of a country of concern* constitute, in the aggregate, a minority of interest stakeholders. What is the risk of a *person of a country of concern* holding minority interests such that the target company would no longer be considered a *covered foreign person*? For example, a similar transaction with an entity in which a person of a *country of concern* already holds a minority interest would not be a *covered transaction* and § 850.209(a)(2) seemingly already captures the risk of entities that are not themselves a *covered foreign person* but do have "significant financial connections" with a *covered foreign person*.

Lastly, there also appears to be risk that parties to transactions *signed* after the date of the Order but *closed* after the effective date of the regulations will inadvertently violate the regulations if an exception is not added. SIA recommends that Treasury include exception language in the NPRM to eliminate this uncertainty and ensure that this subset of transactions does not run afoul of the prohibited or notifiable requirements within the regulations.

22. Which of the two proposed alternatives for the exception for LP investments in the definition of *excepted transaction* best addresses national security concerns while minimizing disruptive effects? Should either approach and corresponding threshold for exception be adjusted, and if so, why and how? What consequences could result from basing an exception on either of the proposed thresholds? What are the considerations related to compliance by *U.S. persons*? Where available, please support your answer with data about the type, aggregate number, or total dollar equivalent amount of investments that would be excepted under each of the two proposed alternatives.

<u>SIA Comment:</u> As Treasury noted in the NPRM, a *de minimis* dollar threshold would establish a bright line test that would reduce the already high compliance burden. However, the proposed threshold of $1 million would, as a practical matter, result in more limited partner investments being *covered transactions*. If Treasury wishes to adopt Alternative 2, SIA recommends it should proceed only with a much higher threshold such as $20 million or more or a percentage of total fund size that reflects commercial realities.

23. What adjustments, if any, should be made to the proposed rule to clarify the coverage with respect to a greenfield investment, brownfield investment, or joint venture that is a *covered transaction* versus an intracompany transaction to support ongoing operations or other activities in a *country of concern* that is an *excepted transaction*?

<u>SIA Comment</u>: SIA proposes including a definition or additional guidance related to the breadth of the term "joint venture." As drafted, it is unclear in the NPRM the exact scope of activities that will be captured as a joint venture (e.g., contractual arrangements).

The Federal Bar Association ("FBA") notes some of the most common terms used to describe different forms of joint venture associations include consortiums, joint ventures, unincorporated joint ventures, partnerships, limited partnerships, teaming arrangement, corporations, and limited liability companies, among others. Further complicating this concept defining a joint venture, according to the FBA, is "whether the entity is 'populated (generally meaning it has its own employees and/or assets with the entity) or 'unpopulated' (generally meaning it will not have any employees or assets and must rely on the parent or an affiliate or third party to carry out the actual work). In fact, all of the different joint venture forms and their associated definitions give rise to ***significant confusion*** [emphasis added] in defining the term."[15] Treasury could clarify, for example, that only joint ventures that result in the establishment of a new legal entity are captured under the regulations. The lack of clarity within the NPRM will likely result in confusion, including transaction parties' ascertaining whether a transaction involves a joint venture. Further, the lack of clarity may also result in ordinary business transactions such as joint marketing or R&D agreements that do not provide the kind of intangible benefit about which Treasury is concerned, being subsumed under the otherwise broad term of "joint venture."

SIA commends Treasury for exempting from the regulations certain intracompany transactions between a *U.S. person* parent and its subsidiary to support ongoing operations (or other activities that are not covered activities as defined in § 850.208). As drafted, however, transaction parties could interpret the NPRM's exception language as only available if a subsidiary in a *country of concern* is a *direct* subsidiary of a *U.S. person* parent. U.S. companies, however, are likely not operating with a direct subsidiary in a *country of concern* (i.e., U.S. parent with a direct subsidiary in a *country of concern*). The subsidiary in a *country of concern* is more likely owned through one or more intermediate level companies.

SIA offers for Treasury's consideration the below clarifying language for the definition of "controlled foreign entity" under § 850.206(b)(1).

- (1) Where the relationship between an entity and another entity is that of **U.S. ultimate** parent and **its direct or indirect foreign** subsidiary, the holdings of voting interest or voting power of the board, as applicable, of a subsidiary shall be fully attributed to the **U.S. ultimate** parent.

SIA further recommends Treasury revise the NPRM so the exception for intracompany transactions applies not only to *covered transactions* between a U.S. parent and its controlled foreign entity, as discussed above, but also between a *U.S. person* and any of its affiliates (i.e., any person that controls, is controlled by, or is under common control with the *U.S. person*). The intracompany transaction exception also should apply

[15] James A. Van Horn, *The Federal Lawyer, A Brief Look into Joint Ventures in Pursuit of Government Contracts*, October 2012. (*Available at* https://www.fedbar.org/wp-content/uploads/2012/10/feature6-octnov2012-pdf-1.pdf)

to a transaction involving affiliates that are *knowingly directed* by a *U.S. person* or undertaken by a controlled foreign entity of a *U.S. person*.

In a departure from the ANPRM, the NPRM includes "brownfield investments" within the definition of *covered transactions*. Specifically, the NPRM states that a *covered transaction* includes the "[a]quisition, leasing, or other development of operations, land, property, or other assets in a *country of concern*" if it results in "the engagement of a person of a *country of concern* in a *covered activity* where it was not previously engaged in such *covered activity* (in the case of a business pivot.)" This language as drafted is ambiguous and will create significant business uncertainty if it is adopted as proposed.

Specifically, it is unclear at what juncture a person is considered as engaging in a new *covered activity* in which it previously was not engaged. Based on the NPRM's current language, businesses would face uncertainty not knowing whether, for example, the design of a next generation IC – even if such IC is of the same kind already being designed by business – would be considered as engaging in a "new" *covered activity* such that a notice obligation could be required. SIA recognizes Treasury's suggestion in the NPRM that the purpose of the language in § 850.210(a)(4)(ii) is to capture "business pivots," but the "business pivot" language itself is not defined, left unexplained in the proposed rule, and not an understood concept in other areas of law.

Further compounding the ambiguity is the exception to the *covered transaction* definition in § 850.501(c), which suggests that an intracompany transaction that "supports ongoing operations" would not be a *covered transaction*, but simultaneously notes that brownfield investments would be outside the scope of this exception. SIA member companies, and other U.S. businesses, are thus faced with an impossible task: businesses must somehow determine, with no guidance, at what juncture the support of "ongoing operations" for existing covered activities already being undertaken by a controlled foreign entity would trigger the NPRM's restrictions related to brownfield investments. As currently drafted, a U.S. company looking to ensure compliance with the proposed rule may have to adopt the position that it cannot provide any ongoing support to its controlled foreign subsidiary, where such subsidiary is a *covered foreign person* that is engaged in a *covered activity*, on the basis that Treasury could view such ongoing support as a "brownfield investment" where there is an advancement (technical or otherwise) in the company's efforts or successes with respect to that *covered activity*. SIA asks Treasury to clarify the intended scope of *covered transactions* under § 850.210(a)(4) given the considerable impact the ambiguity of this language may have on U.S. businesses' development and operations, including for brownfield investments but also greenfield investments and joint ventures.

The lack of clarity and outstanding questions within the NPRM, as highlighted above and in other sections of these comments, offers Treasury an opportunity to assist industry in its interpretation of any final rule. Currently, the NPRM lacks any mechanism for industry to obtain from Treasury non-binding guidance with respect to the final rule.

The burden of interpreting the NPRM falls on U.S. investors and their counsel. As a result, it likely would be helpful – even if for the first few years of compliance – for Treasury to permit companies to submit a fact pattern related to an investment and solicit guidance in applying the rules to a particular situation. This is not an uncommon tool for the U.S. government to provide the public. For example, the U.S. Securities and Exchange Commission (SEC) provides this type of resource in the form of no-action letters as well as compliance and interpretive guidance posted to the SEC website.

24. What is the value to stakeholders of including a national interest exemption for *notifiable transactions*, *prohibited transactions*, or both? Under what circumstance might a *U.S. person* request a national interest exemption in general? Specifically with respect to a *notifiable transaction*, under what circumstance might a *U.S. person* request a national interest exemption from the notification requirement, while still needing to provide information about the proposed transaction in the course of seeking the exemption?

<u>SIA Comment</u>: SIA is supportive of the national interest exemption outlined in the NPRM for both *notifiable transactions* and *prohibited transactions*. It is important that Treasury establish a process to accommodate unforeseen and extenuating circumstances, as well as situations where investments made by a *U.S. person* would enable U.S. entities to establish leverage or control and retain visibility into the operation of a *covered foreign person*.

If a *U.S. person* concludes that an investment activity would result in a benefit far outweighing the risk, it might consider requesting a national interest exemption, but the proposed rules do not include specific criteria that must be met in submitting a request. For example, consider a *U.S. person* that has existing business collaborations with *covered foreign persons* engaged in covered activities and derives considerable revenues from them. Such activities are not prohibited or restricted by existing rules. The *U.S. person* wants to make a small investment in such eco-system partner, for the following benefits: (i) having eyes and ears in the development of the industry/eco-system; (ii) enhancing revenues by influencing the partner/eco-system; and/or (iii) having a goal of buyout (if certain conditions are met).

The national interest exemption process considered by Treasury would benefit from a few revisions. First, the national interest exemption should follow clear timelines by which an entity would provide the required information, Treasury would need to request supplementary information, and Treasury would be required to decide. Second, the national interest exemption process should also outline an appeals process and timeline. Third, Treasury should make public when a transaction is provided a national interest exemption to help inform the regulated community of certain criteria that meet national interest requirements.

25. What specific information should the Department of the Treasury require from a *U.S. person* seeking a national interest exemption in order to evaluate the

transaction's potential impact on the national interest of the United States and to substantiate the basis for requesting an exemption from the prohibition or notification requirement?

<u>SIA Comment:</u> SIA recommends Treasury consider factors related to preserving human life, environmental concerns, and/or extreme financial loss to a *U.S. person* that would have commercial impacts beyond the one company (e.g., impacting a critical supply chain). Treasury should also consider some of the bases for which the U.S. government has granted exceptions in other areas of national security while still continuing to deny resources to malicious actors or countries of concern. For example, in the export control and sanctions compliance regimes, a party can submit a license for an otherwise *prohibited transaction* if there is a strong reason that the transaction is needed to protect the environment or human life, among other factors. The decision to grant a license is left to the respective agency based on the information submitted by a party. In doing so, the appropriate federal agency may weigh all factors in its decision to either grant or deny a license exception.

For example, Treasury in December 2022 implemented historic humanitarian sanctions exceptions following the adoption of United Nation's Security Council Resolution (UNSCR) 2664.[16] According to a Treasury press release, the U.S. co-led the development of UNSCR 2664, which implements a carveout from the asset freeze provisions of UN sanctions programs.[17] To implement this new policy across U.S. sanctions programs, Treasury's Office of Foreign Assets Control issued or amended general licenses (GL) to ease the delivery of humanitarian aid and ensure a baseline of authorizations for the provision of humanitarian support across many sanctions programs. The GLs issued or amended provide authorization in several categories, including the official business of certain international organizations such as the International Red Cross, certain humanitarian transactions in support of nongovernmental organizations' activities, and the provision of commodities such as medical devices, as well as replacement parts and components and software updates for medical devices, for personal, non-commercial use.

In addition to the areas highlighted in § 850.502(b) of the "National Interest Exception," Treasury likely would also benefit from receiving relevant information about the *U.S. person's* interactions with the *covered foreign person* and about any mitigation of potential threats from the *covered foreign person*. For example, whether the *U.S. person* approached the *covered foreign person* first; what qualifies the counterparty as a *covered foreign person*; is the *covered foreign person's* access to technology limited contractually or geographically in some way; and/or has the *covered foreign person* signed an end-use certificate or other certificate restricting their dissemination of

[16] United Nations, Adopting Resolution 2664 (2022), Security Council Approves Humanitarian Exemption to Asset Freeze Measures Imposed by United Nations Sanctions Regimes. December 9, 2022. (*Available at* https://press.un.org/en/2022/sc15134.doc.htm)
[17] Department of the Treasury, Treasury Implements Historic Humanitarian Sanctions Exceptions. December 20, 2022. (*Available at* https://home.treasury.gov/news/press-releases/jy1175)

information acquired through the transaction. These considerations are relevant in the national security and export control spaces and would likely help inform Treasury's determination of whether a *covered transaction* is in the national interest of the U.S. and therefore exempt from the regulations.

* * *

Thank you for the opportunity to provide these comments and we look forward to continued engagement with Treasury during the rulemaking process. If you have any additional questions or would like to discuss these comments further, please contact SIA via awoolf@semiconductors.org.

Uploaded to www.regulations.gov. TREAS-DO-2024-0012-0001

Courtesy copy sent to: Meena.Sharma@treasury.gov