



The CHIPS Act Creates a New, CFIUS-Like, Outbound Investment Review Process for the Semiconductor Industry

AUGUST 22, 2022

President Biden recently signed into law the CHIPS and Science Act of 2022 (the “CHIPS Act”), which, among other things, provides billions of dollars of federal financial assistance to semiconductor companies to construct, expand, and modernize semiconductor manufacturing facilities in the United States.

As we noted recently in a [related post](#), the CHIPS Act may impact both the domestic industry and the importation requirements in Section 337 investigations at the U.S. International Trade Commission (“ITC”).

Beyond its impact on ITC investigations, the CHIPS Act will make it more difficult for semiconductor companies to invest in China. Any semiconductor company that receives federal financial assistance under the CHIPS Act must notify the Department of Commerce (“Commerce”) of any significant transactions involving the material expansion of semiconductor manufacturing capacity in China. After reviewing the transaction, Commerce can either approve, mitigate, or block the transaction. In other words, much like how the Committee on Foreign Investment in the United States (“CFIUS”) currently reviews inbound foreign direct investment for national security risks and approves, mitigates, or blocks transactions, semiconductor companies will now have to negotiate an outbound investment screening process whenever they want to make certain investments in semiconductor manufacturing in China.

How does the new outbound investment review process work?

A semiconductor company that receives federal financial assistance under the CHIPS Act will be required to enter into an agreement with the Secretary of Commerce specifying that for a 10-year period beginning on the date of the award, the company will not engage in any “significant transaction” involving the “material expansion of semiconductor manufacturing capacity in the People’s Republic of China.” This prohibition applies not only to the company that received financial assistance, but also to the company’s “affiliated group,” as defined under section 1504(a) of the Internal Revenue Code.

The CHIPS Act makes clear that semiconductor companies are not prohibited from making any and all investments in semiconductor manufacturing in China. The new law expressly states that the prohibition on material investments in China does not apply to: (i) expenditures for “existing facilities or equipment of a covered entity for manufacturing *legacy semiconductors*” and (ii) “significant transactions involving the material expansion of semiconductor

manufacturing capacity that produces *legacy semiconductors* and predominantly serves the market of a foreign country of concern” (emphasis added). The term “legacy semiconductors” means semiconductor technology that is of the 28 nanometer generation or older, or any additional semiconductor technology that is identified by the Secretary of Commerce, who is required to update the definition of “legacy semiconductors” every two years.

While the 10-year agreement remains in effect, a semiconductor company must notify Commerce of any planned significant transactions involving the material expansion of semiconductor manufacturing capacity in China. Commerce then has 90 days to review the transaction. If Commerce determines that a transaction is a breach of the 10-year agreement, the semiconductor company has 45 days to provide “tangible proof” that the transaction has ceased or been abandoned; otherwise, Commerce may “recover,” or claw back, the full amount of the federal financial assistance provided to the semiconductor company. If, during its review, Commerce determines that a company planning a significant transaction could take measures in connection with the transaction to mitigate any risk to national security, Commerce can negotiate, enter into, and enforce a mitigation agreement, or it can waive the recovery requirement (meaning that it can simply approve the transaction).

The CHIPS Act gives Commerce the authority to publish regulations implementing the statutory requirements for the new outbound investment screening process.

Is Commerce the only agency involved in this new outbound investment screening process?

No. The CHIPS Act gives Commerce the responsibility for carrying out the federal semiconductor incentives program, and Commerce is clearly the lead agency for reviewing outbound transactions, negotiating mitigation agreements, and publishing regulations. However, the new law requires Commerce to “consult” with the Department of Defense (“DoD”) and the Director of National Intelligence (“DNI”) on a range of issues. The statute is unclear on what form this consultation will take, or what will happen if Commerce disagrees with the input provided by the DoD and the DNI. Those issues will likely be fleshed out in future regulations.

Does the new outbound investment screening process apply only to China?

No. Although China is specifically mentioned by name in the statute, the new outbound investment screening process also applies to other “foreign countries of concern,” which is currently defined in the CHIPS Act to include North Korea, Iran, and Russia. However, given that those countries are heavily sanctioned, the CHIPS Act will likely have the greatest immediate impact on outbound investment to China, which is why China is the primary focus of this client alert.

The CHIPS Act gives Commerce (following consultation with other agencies) the ability to designate other countries as “foreign countries of concern” if those countries are “engaged in conduct that is detrimental to the national security or foreign policy of the United States.” Thus, the new outbound investment screening process may apply to additional countries in the future.

What does the new outbound investment screening process mean for semiconductor companies?

The CHIPS Act is clearly trying to force semiconductor companies to make a tradeoff: if they want federal financial assistance from the U.S. government, they will have to limit their investment in semiconductor manufacturing in China. Semiconductor companies eligible for federal financial assistance will have to decide whether the benefits of that assistance are worth the cost of reduced investment in China. If a semiconductor company accepts federal financial assistance under the CHIPS Act, the company will need to be careful before engaging in future transactions

in China. Specifically, the company will need to conduct due diligence to determine whether a potential transaction qualifies as a “significant transaction” involving the “material expansion of semiconductor manufacturing capacity in the People’s Republic of China,” or if the transaction falls within one of the exceptions for “legacy semiconductors.” When necessary, the company will need to submit a formal notice to Commerce regarding the planned transaction, and the company will need to be prepared to consult with Commerce about any national security risks arising from the transaction and whether those risks can be mitigated effectively. Finally, semiconductor companies will need to be prepared to negotiate, enter into, and monitor compliance with any mitigation agreement required by Commerce.

To be clear, the CHIPS Act does not prohibit all significant transactions involving the material expansion of semiconductor manufacturing capacity in China. Rather, the law creates what amounts to a presumption against such investments, but it gives semiconductor companies the opportunity to persuade Commerce that a particular transaction will not give rise to a national security risk or that such risk can be mitigated effectively. This process will likely be similar to the current CFIUS process for foreign direct investment in the United States, except that for CFIUS transactions, the burden is on the government to establish that a national security risk will arise from a transaction, whereas for outbound investments in the semiconductor manufacturing industry in China, the burden will be on semiconductor companies and their counsel to prove that a particular investment is harmless.

What happens next?

The CHIPS Act leaves lots of questions to be answered about the new outbound investment screening process. What are the exact terms of the 10-year agreements? What is the process for submitting notice of a “significant transaction” to Commerce? What must be included in the notice? Will Commerce provide more guidance on the definitions of “significant transaction,” “material expansion,” “foreign country of concern,” and “legacy semiconductors”?

We expect Commerce to publish regulations (or at least some type of less formal guidance) in short order, and we will provide updates on any developments as they occur. In the meantime, if you have any questions about the CHIPS Act in general, or the new outbound investment screening process for the semiconductor industry in particular, please contact the authors or your Winston relationship attorney.

Winston’s Semiconductor Industry Experience

Winston & Strawn boasts a cross-disciplined team of attorneys with significant experience assisting clients in the semiconductors and materials science industry. Our semiconductors group helps our clients to navigate various intellectual property, securities, international trade, CFIUS, and antitrust issues, including those involving alleged conspiracies to unreasonably restrain trade, illegal imports, alleged anticompetitive licensing schemes, FRAND violations, and monopolization claims. We have worked to get punitive consumer class actions dismissed, Section 337 investigations settled, and high-profile claims by competitors and licensees dismissed. In his prior role as the Deputy Assistant Secretary for Investment Security at Treasury, one of our key international trade partners oversaw several CFIUS reviews of high-profile semiconductor company transactions. Our firm includes over 20 attorneys with technical degrees in life sciences and high-tech (including industrial and systems engineering, electrical engineering, and computer engineering) sectors, and attorneys with previous experience working for leading semiconductor companies, allowing us to truly understand the technology involved in this field. We also have extensive experience overseas, with a particularly strong presence in Asia, often allowing us to pursue a comprehensive legal strategy across jurisdictions to help our clients achieve their business goals.

The CHIPS Act – How We Can Help

With the passing of the CHIPS Act, our firm can further assist semiconductor industry clients with their regulatory obligations. Our highly skilled team can guide clients on ways to structure transactions to stay compliant within the

guidelines of the CHIPS Act. Utilizing our significant experience engaging with Commerce, we can respond to Commerce's requests for notice and comment on proposed regulations, communicate with Commerce about proposed transactions, and submit filings. Finally, if mitigation is required, our team can negotiate mitigation agreements that minimize the risk to our clients' company operations.

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