US TREASURY'S COINS ACT PROPOSAL WOULD BROADEN AI INVESTMENT PROHIBITIONS AND EXPAND BIOTECHNOLOGY AND QUANTUM RESTRICTIONS

Date: 3 November 2026

US Policy and Regulatory Alert

By: Guillermo S. Christensen, Thoreau A. Bartmann, Yuki Sako, Sanjeev Bhasker, Lucy Mani, Myeong S. Park

On 22 October 2026, the US Department of the Treasury (Treasury) issued a Notice of Proposed Rulemaking (NPRM) to implement the Comprehensive Outbound Investment National Security Act of 2025 (COINS Act) and expand the Outbound Investment Security Program (OISP). The NPRM would extend the OISP to additional countries and technologies, including hypersonic systems and biotechnology, and would expand the existing quantum restrictions to reach associated software and algorithms as well as specified sensing and networking applications. The most consequential change concerns artificial intelligence (AI), which the NPRM now labels “super intelligence” (SI) in line with Executive Order 14434. Despite the nomenclature, the proposal is not limited to frontier systems: Under the NPRM, covered national security transactions by US persons involving covered foreign persons that develop any SI system would be prohibited, with no notification-only category, regardless of the capability threshold of the SI systems. Many AI investments that are permissible today would become prohibited outright under the NPRM. The NPRM would also prohibit covered national security transactions involving specified biotechnology activities, potentially restricting US investment in much of China's pharmaceutical and life sciences tools industries. The NPRM also would revise and expand several key concepts and definitions, such as covered national security transactions and covered foreign persons.

For asset managers and investors, the exceptions for publicly traded securities and US Securities and Exchange Commission (SEC)-registered fund shares would remain substantively unchanged, but the proposal would eliminate the business development company exception, extend the “knowingly directing” prohibition to notifiable transactions, and require meaningful updates to outbound investment policies and procedures built around the current rules. Because the exceptions for publicly traded securities would remain available, the NPRM's expanded prohibitions would fall most heavily on private, venture, and pre-initial public offering (pre-IPO) investments and on investments that carry governance rights. The NPRM's proposed modifications relating to limited partner (LP) investments in connection with the covered national security transaction definition or the exception for LP investments would impose an increased and expanded compliance burden on LPs.

Comments on the NPRM are due 7 December 2026.

©2005-2026 K&L Gates LLP. All Rights Reserved.

BACKGROUND

The OISP, established by Executive Order 14105 of August 2023, took effect on 2 January 2025. It prohibits certain investments and requires notification of certain other investments by US persons involving businesses connected to China, Hong Kong, or Macau that engage in specified semiconductor, quantum information technology, or AI activities.[1] Congress enacted the COINS Act on 18 December 2025 as part of the Fiscal Year 2026 National Defense Authorization Act. The act codified the OISP framework in Title VIII of the Defense Production Act and added high-performance computing and supercomputing and hypersonic systems to its statutory coverage. The statute calls for final implementing regulations within 450 days of enactment or by 13 March 2027. The NPRM, published in the Federal Register on 26 October 2026 (91 Fed. Reg. 67396), would set out those regulations as a new, stand-alone 31 C.F.R. Part 851. The existing regulations at 31 C.F.R. Part 850 would continue to apply until the new regulations take effect, and the new regulations would not apply retroactively.

EXPANDED TECHNOLOGY COVERAGE

AI/SI

The NPRM would significantly expand the restrictions applicable to AI. Following Executive Order 14434 of 29 September 2026, which directs agencies to use “super intelligence” and “SI” in place of “artificial intelligence” and “AI,” the NPRM refers to AI systems as SI systems. The definition of “SI” would reach systems that generate content or make predictions or decisions, as well as applications, agentic tools, and AI-enabled robotics and other autonomous systems that use such systems. “Develop” would reach work conducted through affiliates and high-level oversight, direction, or strategic planning, so a parent or holding company that directs an affiliate's SI work could itself be treated as a developer. Work that enhances or extends the capability of a third-party SI system may count as development, while strictly internal, noncommercial use of an off-the-shelf system would not constitute development solely on that basis. As a result, the prohibition could reach most companies in countries of concern that build AI-enabled products, whether on their own models or on third-party models. Current rules distinguish notifiable from prohibited AI investments using intended uses and computing thresholds, and they leave investments in other AI developers outside the program. The NPRM would prohibit covered national security transactions involving developers of any SI system without a notification-only tier, computing threshold, or military end-use test. Notably, the COINS Act does not compel this result. While the statute authorizes Treasury to set technical parameters for both notifiable and prohibited AI technology, Treasury has elected to treat all SI development as prohibited, a choice that is likely to draw substantial comment.

Biotechnology

Treasury would also use its discretionary authority to classify biotechnology, a sector not specifically named by the COINS Act, as prohibited technology, with no notification-only tier. The NPRM would cover certain biological systems used to produce specified agents, toxins, materials, pharmaceutical compounds, and biofuels, as well as brain-computer interfaces, export-controlled biomanufacturing equipment, sequencing technology, certain laboratory instruments, bioinformatics tools, and laboratory automation. Pharmaceutical compounds would include small molecules, vaccines, cell and gene therapies, and monoclonal antibodies. As drafted, the biotechnology category could reach a large share of China's pharmaceutical and life sciences tools industries.

©2005-2026 K&L Gates LLP. All Rights Reserved.

However, the NPRM should not be read as a blanket prohibition on licensing pharmaceutical products from Chinese counterparties. Treasury indicates that licensing, consulting, and procurement contracts generally fall outside the program, while co-development, co-marketing, and other collaboration arrangements require structure-specific analysis, particularly where they include equity, equity-like financing, or a joint venture.

Semiconductors

For semiconductors, the NPRM would expand prohibited activities to include high-bandwidth memory with bandwidth density exceeding 2 gigabytes per second per square millimeter, radiation-hardened integrated circuits, photonic integrated circuits, and advanced packaging of integrated circuits, while retaining notification for certain other design, fabrication, and packaging activities. For high-performance computing, the NPRM would retain the existing supercomputer prohibition and require notification for development or production of certain high-bandwidth, low-latency interconnects. Quantum prohibitions would extend to critical quantum-computer components, associated software and algorithms, and specified sensing and networking applications.

Hypersonic Systems

For hypersonic systems, defined as vehicles or weapon delivery systems capable of sustained flight at Mach 5 or greater, prohibited technologies would include the systems themselves, propulsion systems and fuels, specified materials, testing facilities, and digital twin and digital thread technologies. Certain sensors, control equipment, software, and materials capable of use in hypersonic systems would require notifications. The proposed category is not limited to military applications and could reach civilian systems meeting the relevant technical criteria.

TRANSACTIONS SUBJECT TO THE PROPOSED RULE

Expanded List of Countries

Consistent with the COINS Act's statutory list, the NPRM would expand the countries of concern beyond China, Hong Kong, and Macau to include Cuba, Iran, North Korea, and Russia. Because existing sanctions already foreclose most US investments in those four countries, China and Hong Kong likely remain the program's principal practical focus. The statutory list also refers to the Bolivarian Republic of Venezuela (Venezuela) under the former regime of Nicolás Maduro Moros, but not under the current leadership of Delcy Rodriguez. Treasury indicates that the Maduro government no longer exists and that Venezuela therefore does not meet the proposed “country of concern” definition, although the proposal could still apply to certain investments in Venezuelan entities.

Expanded Definition of “Covered Foreign Person”

Whether an investment target is a “covered foreign person” would depend on whether it engages in a covered technology and on its country ties, ownership or control, and, in certain cases, relationship to other covered foreign persons. The NPRM would reach certain entities whose management or policies are subject to direction or control through contractual or other arrangements, making ownership percentages alone an insufficient basis for assessing country-of-concern ties. The NPRM would retain a test capturing entities outside a country of concern that hold equity, a board seat, or contractual control in a covered foreign person and derive more than 50% of their revenue, net income, capital expenditures, or operating expenses from such persons.

©2005-2026 K&L Gates LLP. All Rights Reserved.

Additionally, the NPRM would define an entity's principal place of business to include both its headquarters and the location of its main business activities, so a company headquartered in the United States but with its main business activities in China could be treated as a covered foreign person. An entity could also have more than one principal place of business. For a pooled investment fund, the analysis would look to where the general partner or equivalent primarily directs, controls, or coordinates the fund's activities.

Expanded List of Covered National Security Transactions

The NPRM would cover a broad range of direct and indirect investments (each, a covered national security transaction), including equity and contingent equity investments, debt financing with equity-like rights, joint ventures, greenfield and expansion investments, and LP investments in non-US funds that the US person knows are likely to invest in covered foreign persons. Compared to the existing rule, the NPRM also covers (i) transactions structured through intermediaries or other arrangements that obscure a US person's role, as well as (ii) a US person knowingly directing a transaction by a non-US person that would be prohibited or notifiable if undertaken by a US person. Notably, extending the knowingly directing prohibition to notifiable transactions is significant for US advisers and portfolio managers who serve on investment committees or otherwise participate in investment decisions of non-US funds.

Under the NPRM, LP investments in a pooled investment fund that the US person LP knows at the time of the commitment likely will invest in a “covered foreign person” (changed from a “person of a country of concern” under the OISP) that is in the covered sectors would be covered national security transactions.[2] In consideration of the knowledge standard framework retained under the NPRM, this change would suggest that LPs may be required to conduct deeper diligence regarding the fund's portfolio investments, i.e., not only the locations and jurisdictions of the portfolio companies but also whether any portfolio companies are subject to the direction or control of a person of a country of concern.

Expanded Knowledge Standard

The existing knowledge standard, which calls for a reasonable and diligent inquiry, would continue to apply, with two additions: (i) Treasury would also consider whether the US person took account of information Treasury provided before closing, and (ii) a controlled foreign entity's knowledge would bear on whether its US parent has complied. Under the current rules, a transaction involving notifiable technology is prohibited where the covered foreign person appears on certain US government lists, such as the Entity List or the Specially Designated Nationals and Blocked Persons List. The NPRM would extend this treatment to cases where an affiliate or subsidiary is listed on such lists and also add the Department of War's section 1260H list and the Office of Management and Budget's BIOSECURE Act list.

EXCEPTED TRANSACTIONS

The NPRM would retain exceptions, substantively unchanged from the existing rules, for investments in publicly traded securities and securities issued by SEC-registered investment companies, as well as qualifying LP investments in non-US pooled funds. The existing exception for business development companies would not be carried forward, although Treasury invites comments on restoring it. Shares of listed business development companies would remain covered by the publicly traded securities exception, but investments in nontraded and private business development companies would lose their exception. Treasury also has not proposed an

©2005-2026 K&L Gates LLP. All Rights Reserved.

exception for investments in non-US regulated funds, such as UCITS funds, although the COINS Act would permit one.

The proposal also introduces a US$50,000 de minimis exception, aggregated over the preceding 12 months, but only for otherwise notifiable transactions, not prohibited transactions. Other exceptions would address qualifying buyouts of all covered foreign person interests in entities or assets outside countries of concern, certain intracompany transfers, transactions made under binding capital commitments entered into before the new rules take effect (which would remain subject to the OISP), and specified secondary and ancillary financial activities, such as bank lending, underwriting, custody, and prime brokerage. The NPRM would also exclude ordinary or administrative business transactions, a term Treasury has not yet defined. Treasury's accompanying FAQs indicate that technology licensing, consulting, and procurement contracts are generally outside the program, subject to the transaction-structure qualifications discussed under “Expanded Technology Coverage” above.

The exception for secondary and ancillary financial activities should not be confused with a general exemption for secondary purchases of fund interests. Secondary acquisitions may remain covered despite an investor's limited access to portfolio-level diligence. Separately, Treasury's preamble to the NPRM suggests that an investment in a fund with existing covered holdings may constitute an indirect covered investment independently of the specific provision governing LP investments. This interpretation is not expressly set out in the NPRM's proposed regulatory text and warrants clarification.

LP Investments

The LP investment exception would continue to apply if committed capital does not exceed US$2 million or if the LP obtains a binding contractual assurance that its capital will not fund any transaction that would be a covered national security transaction if undertaken by a US person. The NPRM clarifies that (i) for notifiable transactions, an LP would be excepted from the notification requirement if it obtains a binding contractual assurance covering notifiable transactions; and (ii) for prohibited transactions, an LP would not be in violation if it obtains a binding contractual assurance covering prohibited transactions even if the fund uses its capital for a prohibited transaction contrary to the assurance. Under the NPRM, LPs seeking to rely on the LP investment exception would need to request contractual assurances specifically for both notifiable and prohibited transactions.

Derivatives

The NPRM would broaden the exception for derivatives of excepted securities and allow derivatives that confer a right to acquire equity or assets of a covered foreign person. Treasury asks whether this change would create a loophole, so advisers using options, warrants, or similar instruments on listed securities of covered foreign person issuers should not assume the broader exception will survive in the final rule.

As under the OISP, these exceptions would not apply where the US person receives governance rights beyond standard minority shareholder protections.

ENFORCEMENT AND PROCESS

Covered national security transactions involving prohibited technologies would generally be prohibited, and those involving notifiable technologies would require notice to Treasury within 30 days.

Penalties

©2005-2026 K&L Gates LLP. All Rights Reserved.

The NPRM would strengthen Treasury's enforcement tools. Violations would be subject to civil penalties up to the maximum permitted under the International Emergency Economic Powers Act (the NPRM would not provide for criminal penalties), and Treasury could compel divestment of a prohibited transaction. Voluntary self-disclosure would remain a mitigating factor, but a disclosure would need to propose mitigation of any resulting harm, such as divestment or voluntary disgorgement of profits.

Notification Requirements

Notifications would require more extensive information, and records, including diligence materials, would need to be retained for 10 years. The NPRM would also create a confidential channel through which any person could submit information indicating that a foreign person is a covered foreign person.

Nonbinding Feedback

In addition, a person with a direct financial interest in a transaction could request nonbinding feedback from Treasury on whether the transaction would be prohibited, in the form of either anonymized public guidance or confidential feedback. Treasury would not be required to respond, and any feedback would neither authorize the transaction nor provide an enforcement safe harbor. US persons could continue to request a national interest exemption from the prohibition.

OPPORTUNITY TO COMMENT

Treasury requests comments supported by empirical data or transaction examples wherever possible. For SI, Treasury seeks comments on, among other topics, the proposed prohibition on SI development, the SI definition, and potential alternative approaches to address national security concerns. For biotechnology, Treasury seeks comment on whether coverage should be tied to particular biological systems or equipment, whether biofuels should exclude ethanol, and whether coverage of pharmaceutical compounds and listed equipment should focus on advanced or frontier technologies.

Treasury also seeks comment on whether to extend the definition of “parent” to certain sub-advisers and general managers of non-US funds, several proposed exceptions (including whether to restore the business development company exception), national interest exemptions, a potential public database of covered foreign persons, and its cost estimates. Other issues that companies may wish to address in comments include the treatment of mixed licensing and co-development arrangements, secondary fund acquisitions, the absence of an exception for non-US regulated funds, investments in funds with existing covered portfolios, and the feasibility of obtaining sufficient information to conduct diligence on indirect investments. Companies considering comments should assess which of these issues are most relevant to their operations or investments and, where possible, support their comments with specific examples or data.

Comments are due 7 December 2026 and may be submitted through regulations.gov under Docket No. TREAS-DO-2026-0595.

KEY TAKEAWAYS

Although the NPRM is not final, the COINS Act calls for final regulations by 13 March 2027; that deadline should not be confused with the final regulations' effective date. Transactions now under negotiation may close after the

©2005-2026 K&L Gates LLP. All Rights Reserved.

new rules take effect. Companies should assess pipeline transactions, including investments to be funded from uncalled capital commitments, against both Part 850 and the proposed Part 851, taking account of any applicable exception for pre-effective-date binding capital commitments. Companies should also expect a transition period in which compliance procedures must address both regimes. In the meantime, companies should update diligence questionnaires, representations, and warranties to address the proposed SI definition, biotechnology, hypersonic systems, high-performance computing, the new countries of concern, and the expanded list-based prohibitions. List screening alone would not establish that a target falls outside the program. Companies should document diligence concerning the target's activities, country ties, ownership and control, and relevant affiliates and subsidiaries.

IMPLICATIONS FOR ASSET MANAGERS AND LPS

Funds Investing in Public Markets

For registered funds and separately managed accounts that invest primarily in listed securities, the direct impact of the NPRM is likely modest because the publicly traded securities exception would carry forward. The expanded prohibited categories, however, would make that exception more important. Advisers should confirm that their procedures identify transactions that fall outside the exception, including private placements, pre-IPO and cornerstone or anchor investments, PIPE transactions, and any investment accompanied by board, observer, or other governance rights beyond standard minority shareholder protections.

Funds Focusing on Private Investments

Sponsors of private funds and US advisers to non-US funds face the most significant changes. The expanded SI and biotechnology prohibitions would reach a substantial share of venture and growth investment opportunities in China.

Treasury is also considering extending the definition of “parent” to certain sub-advisers, which could make non-US funds controlled foreign entities of their US sub-advisers.

Advisers that adopted outbound investment policies under the OISP should plan to update them before the new rules take effect. Treasury has indicated that it would likely reissue its existing guidance under the new rules if adopted, but until it does, advisers relying on the previously issued FAQs should note that the guidance was issued under the prior regulations.

LP Investors

The expanded covered technologies and concepts of covered foreign person and covered national security transaction under the NPRM would result in significant and meaningful changes for LPs. The OISP was an issue for technology-focused funds. Under the NPRM, a wide range of investment funds would likely be within the scope of covered technologies. Even if portfolio companies are located in jurisdictions outside China or another country of concern, LP investments may nevertheless be covered if the companies are subject to the direction or control of a person of a country of concern. In addition, LPs should be prepared to update their standard side-letter requests relating to the binding contractual assurance if relying on the LP investment exception.

©2005-2026 K&L Gates LLP. All Rights Reserved.

Please contact our International Trade, Investment Controls, and National Security practice group, our Policy and Regulatory practice, or our Asset Management and Investment Funds practice if you would like assistance assessing the NPRM's potential impact or preparing comments for Treasury.

FOOTNOTES

[1] For additional background, see our prior alert, *US Treasury Department Moves Closer to Implementing Outbound Investment Restrictions Through Latest Proposed Regulations* (26 June 2024).

[2] It is worth mentioning that the Treasury staff noted in the preamble to the OISP that: "the Treasury Department understands that it may not be practicable for a *U.S. person* LP to *know* the specific investment target entity or entities of a pooled investment fund even following a 'reasonable and diligent inquiry' at the time of its LP investment. However, it is the Treasury Department's understanding that it may be possible for such LP to know, through a 'reasonable and diligent inquiry,' the country and general sector in which the pooled investment fund is likely to invest." Provisions Pertaining to U.S. Investments in Certain National Security Technologies and Products in Countries of Concern, 89 Fed. Reg. 90398, 90420 (Nov. 15, 2024).

KEY CONTACTS



GUILLERMO S. CHRISTENSEN
PARTNER

WASHINGTON, DC
+1.202.778.9095
GUILLERMO.CHRISTENSEN@KLGATES.COM



THOREAU A. BARTMANN
PARTNER

WASHINGTON, DC
+1.202.778.9301
THOREAU.BARTMANN@KLGATES.COM



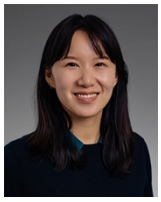
YUKI SAKO
OF COUNSEL

WASHINGTON, DC, TOKYO
+1.202.778.9061
YUKI.SAKO@KLGATES.COM



SANJEEV BHASKER
PARTNER

WASHINGTON, DC, MIAMI, CHARLOTTE
+1.202.778.9260
SANJEEV.BHASKER@KLGATES.COM



LUCY MANI
ASSOCIATE

SEATTLE
+1.206.370.7837
LUCY.MANI@KLGATES.COM

©2005-2026 K&L Gates LLP. All Rights Reserved.

This publication/newsletter is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer. Any views expressed herein are those of the author(s) and not necessarily those of the law firm's clients.

©2005-2026 K&L Gates LLP. All Rights Reserved.