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The EU Anti-Subsidy Regulation Enters Trilogue Negotiations – New Obligations for Multinationals Coming into Focus

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Exactly one year after the European Commission (Commission) proposed the **Anti-Subsidy Regulation** (the Regulation) (discussed on KCLB already here and here), on May 5, 2022, EU legislators launched their "trilogue" negotiations to reach an agreement on the final text.

The Regulation is a global first. It combines elements of traditional merger control, EU State aid review and trade law. The Regulation gives the Commission sweeping new powers to investigate and combat distortions of competition caused by subsidies granted by non-EU countries, for example to State-owned enterprises (SOEs), who may use those subsidies to compete against EU companies that are subject to EU State aid rules.

Importantly, the Regulation creates mandatory new notification requirements for M&A transactions, the formation of joint ventures and public tenders. These requirements are based on a combination of the target's EU revenues and the parties' "financial contributions," a new global, group-wide metric. "Financial contributions" are defined broadly, including, for example, contracts with governments or entities whose actions are attributable to governments and calculated over a rolling three-year period (e.g., 2020-2022 for transactions notified in 2023).

Here, I review the key elements of the Regulation and the main changes proposed by the European Parliament and Council going into the trilogues. Although some of the proposed changes are significant, there are no obvious show-stoppers that seem likely to prevent an agreement by June 2022. The new regime thus seems to be on track for implementation by mid-2023.

"Financial contributions" vs "subsidies"

The Regulation distinguishes between three related concepts: "financial contributions," "foreign subsidies", and "distortions on the internal market." Importantly, the new mandatory reporting regimes for acquisitions, joint ventures and public tenders are triggered by receipt of financial contributions, not foreign subsidies.

More specifically,

- The Commission proposal defines financial contributions as "(i) the transfer of funds or liabilities, such as capital injections, grants, loans, loan guarantees, fiscal incentives, setting off

of operating losses, compensation for financial burdens imposed by public authorities, debt forgiveness, debt to equity swaps or rescheduling; (ii) the foregoing of revenue that is otherwise due; or (iii) the provision of goods or services or the purchase of goods and services," whether provided by government authorities or public or private entities whose actions can be attributed to a non-EU country. The Parliament and Council have proposed adding special or exclusive rights granted without adequate remuneration, though how the adequacy of remuneration would be measured is unclear.

- Under the Commission's proposal, a foreign subsidy arises where "a third country provides a financial contribution which confers a benefit to an undertaking engaging in an economic activity in the internal market and which is limited, in law or in fact, to an individual undertaking or industry or to several undertakings or industries." The Parliament and Council have not proposed to modify these concepts.
- A "distortion on the internal market" arises "where a foreign subsidy is liable to improve the competitive position of the undertaking concerned in the internal market and where, in doing so, it actually or potentially negatively affects competition on the internal market."

Whether there is a distortion on the internal market depends on factors such as the amount and nature of the subsidy, the situation of the beneficiary and the markets concerned, the beneficiary's economic activity in the EU, and the purpose and conditions attached to the subsidy. Foreign subsidies most likely to cause a distortion include subsidies granted to companies that would otherwise have been likely to go out of business (unless there is a viable restructuring plan including a significant own contribution by the beneficiary); unlimited guarantees for debts or liabilities; subsidies directly facilitating a concentration; and subsidies enabling submission of an unduly advantageous tender for a public contract.

The definition of financial contribution is deliberately very broad, enabling the Commission to review a large number of transactions. For example, many if not most multinationals provide or receive goods or services under public-sector contracts. Such contracts range from oil and gas leases, mining concessions, and defence-sector contracts worth hundreds of millions or even billions of euros (and often subject to confidentiality requirements) to ordinary course contracts with publicly owned water or electric utilities and health insurance providers. The Parliament has proposed excluding contracts awarded pursuant to "competitive, transparent, non-discriminatory and unconditional tender procedures," but Commission officials have objected to the subjective nature of these criteria.

Importantly, the Regulation does not allow multinationals to exclude *de minimis* financial contributions (except under a proposed Council amendment to notification requirements in connection with public tenders). This contrasts with the approach to "foreign subsidies," which are considered unlikely to distort competition in the EU below certain thresholds (€5 million, in the Commission's proposal).

As a result, both acquirer and target groups will need to identify and quantify the financial contributions they receive from the first euro on a global, group-wide basis. Given the administrative burden for multinationals to identify and quantify large numbers of financial contributions that would be presumed non-distorting even if they qualified as foreign subsidies, it would make sense – and significantly reduce the Regulation's burden – to allow multinationals to exclude *de minimis* financial contributions from the thresholds and reporting requirements.

M&A transactions and joint ventures

The Regulation will create a new, mandatory ex-ante notification system for mergers, acquisitions and joint ventures that will sit alongside the EU Merger Regulation (EUMR), as well as foreign direct investment screening regimes. The notification process and timetable closely resemble the EUMR process, with an initial 25 working day review period, followed by an in-depth 90 working day review period, starting from the date of formal notification. Notified transactions cannot be closed while the review is pending.

Preparatory documents published by the Commission highlighted concerns over non-EU companies using subsidies to overbid for EU businesses, crowding out potential EU buyers in competitive acquisitions. The Regulation is not limited to this scenario, however, the proposal provides little or no guidance on the type or degree of harm the Commission must show to prohibit or impose conditions on a notifiable transaction.

Under the Commission's proposal, the notification requirement would apply to acquisitions where the target's EU turnover is at least €500 million, double the €250 million basic threshold under the EUMR. The Parliament has proposed lowering the €500 million threshold to €400 million, while the Council has proposed raising it to €600 million. If the revenue threshold is met, an acquirer would be required to notify the Commission if the buyer and the target together received an aggregate financial contribution from non-EU countries of at least €50 million in the prior three years. Neither the Parliament nor the Council proposed changes to the €50 million financial contribution threshold.

Unlike the EUMR (and contrary to recommended best practices of the International Competition Network), there is no requirement for two or more parties to meet thresholds for a notification to be triggered. Indeed, given the broad definition of financial contribution, if a target meets the EU revenue threshold, it will likely meet both thresholds all by itself.

Similar to the EUMR, so-called "full-function" joint ventures may be caught by the Regulation. Under the Commission proposal, notification would be required if any party had an EU turnover of at least €500 million and all parties together received financial contributions of at least €50 million in the prior three years. This threshold would catch many joint ventures with no connection to the EU, much as the EUMR catches many non-EEA joint ventures. The Council and Parliament versions both apply a revenue threshold to the joint venture itself, eliminating the need to notify joint ventures with no EU nexus. However, the Commission may resist this change since greenfield joint ventures would not be caught regardless of the size of their parent company groups or the foreign subsidies they receive. Still, the introduction of an EU nexus requirement for joint ventures would reduce the volume of required notifications.

Should the Commission find that a foreign subsidy distorts the internal market following an in-depth investigation, it could either accept commitments to effectively remedy the distortion, or prohibit the transaction. The Commission will also have remedial powers – including ordering a transaction to be unwound — when it finds that a notifiable transaction has already been implemented and distorts the EU internal market.

With the possible exception of a foreign subsidy directly facilitating a proposed acquisition (which the Commission could require a proposed acquirer to reject or reimburse), the appropriate remedy for a distortion will often be unclear. What would be the remedy, for instance, if the Commission

concludes that long-standing subsidies under public-sector contracts raise a bidder's general profitability, enabling it to pay more for a target than EU bidders? What if the subsidized acquirer is the only bidder, or all potential acquirers are subsidized? These and many other questions are likely to arise as the Regulation is implemented.

EU public procurement procedures

The Regulation will also supplement existing EU public procurement rules by requiring bidders in significant tenders to notify the contracting authority of any financial contribution they have received in the preceding three years. The objective is to catch foreign subsidies "that cause or risk causing a distortion in a public procurement procedure [by enabling] an undertaking to submit a tender that is unduly advantageous in relation to the works, supplies or services concerned," thereby putting non-subsidized bidders at an unfair disadvantage. As with the new M&A/joint venture notification process, the Regulation gives the Commission exclusive authority to review the distortive effect of financial contributions in public procurement procedures.

A bidder subject to a notification requirement must provide information about its own financial contributions and those of its main suppliers and subcontractors. Responding to a key business concern, however, the Parliament and Council amendments provide that notifying bidders will not have liability for information on financial contributions received by suppliers and subcontractors.

Upon receipt of a notification, the contracting authority must transfer the file to the Commission, which will determine whether foreign subsidies distort the bid. The Commission can also require notification where it suspects that a participant in a public procurement process has benefitted from foreign subsidies in the previous three years.

Key issues to be debated in the trilogues include the value threshold triggering the notification requirement for public procurement contracts – the Commission proposed €250 million – and the timeframe for Commission review. The Parliament and Council both agree that the Commission's proposed timelines (60 days for a preliminary review and 200 for an in-depth review) should be shortened.

Apart from the administrative burden and delay involved in notifications, the new requirements will create challenges for bidders, such as the need to provide information on the activities of suppliers and sub-contractors, who may be competitors. The risk of triggering a notification requirement may become a factor in the selection of bidding consortia, potentially leading to the selection of less qualified or cost-effective suppliers and subcontractors.

***Ex officio* review of foreign subsidies**

The Regulation empowers the Commission to conduct *ex officio* reviews of alleged distortive foreign subsidies. The Commission's reviews will be divided into two phases, a preliminary review to assess whether a financial contribution constitutes a foreign subsidy that appears likely to distort the EU internal market, followed by an in-depth review when needed.

For this purpose, the Commission will have powers, familiar from its antitrust toolkit, to impose

interim measures, issue requests for information, conduct inspections both inside and (with the relevant company's and government's consent) outside the EU, take action against non-cooperation and impose fines and periodic penalty payments. In the event of non-cooperation, the Commission will be entitled to take decisions "on the basis of facts available," a standard familiar from EU trade law investigations.

Where the Commission finds that a foreign subsidy distorts the internal market, the Commission may impose redressive measures or, if the company concerned offers satisfactory commitments, adopt a decision making those commitments binding.

Balancing test

In each of the Regulation's three modules – M&A/joint venture notification requirements, public tender notification requirements and *ex officio* powers – if the Commission finds a risk of distortion of competition, it will also determine whether positive effects outweigh the distortion. If so, no action to prevent or remedy the distortion will be required.

According to the Commission's proposal, positive impacts that could be taken into account include creating jobs, achieving climate neutrality and protecting the environment, digital transformation, security, public order and public safety and resilience. The Parliament and Council have both called for greater guidance on the application of the balancing test, which is analogous to – but less precise than – the assessment of efficiencies under the EUMR or Article 101(3) TFEU.

Notably, the Parliament and Council have both called for cognizable positive effects to be limited to effects in the EU. However, Commission officials have stated that World Trade Organization obligations require them to consider positive effects in relevant non-EU countries (contrary to the Commission's traditional assessment of efficiencies in antitrust markets).

Key takeaways

The Parliament's and Council's amendments to the Commission proposal seem unlikely to delay adoption for long. Where their approaches diverge, as with the EU revenue-based notification thresholds, the differences seem marginal and susceptible to compromise. The Parliament and Council both agree on some amendments to mitigate the Regulation's burden on business, such as requiring an EU nexus for notifiable joint ventures and shortening the Commission's review of public procurement notifications, although the Commission may push back in the trilogue discussions.

The Regulation draws on familiar EU competition law tools but combines and re-purposes them unprecedentedly. Absent clear standards in the Regulation itself or EU or international precedents, the Commission will be ploughing new ground. In determining whether a financial contribution constitutes a foreign subsidy, the Commission can draw on decades of State aid precedents. But proving causal links between subsidies granted outside the EU and distortions in the EU will be a new challenge, as will designing remedies.

As it applies its *ex officio* powers, the Commission will likely target non-EU SOEs believed to

enjoy significant subsidies. The Commission will be able to choose its targets and develop experience at its own pace. Under the mandatory merger and public procurement notification regimes, however, neither the Commission nor multinationals will have that luxury. The Commission will no doubt draw on EUMR precedents for guidelines, notification forms, and procedures. Notifications are likely to be complex, as multinationals will need to disclose hundreds, if not thousands, of financial contributions and provide the information needed to determine which, if any, qualify as foreign subsidies and potentially distort competition in the EU while navigating legal and contractual confidentiality requirements applicable to those financial contributions.

The burden of the new monitoring and compliance procedures required to identify and quantify financial contributions from 2020 will vary from firm to firm. However, such procedures will need to be carefully designed in cooperation with EU and local counsel familiar with the different arrangements prevalent in global markets and how these arrangements will be viewed from an EU law perspective. In many cases, designing and implementing new procedures will take many months. Perhaps ironically, the new Regulation's burden will fall most heavily on EU-based multinationals who are most likely to meet the notification thresholds.

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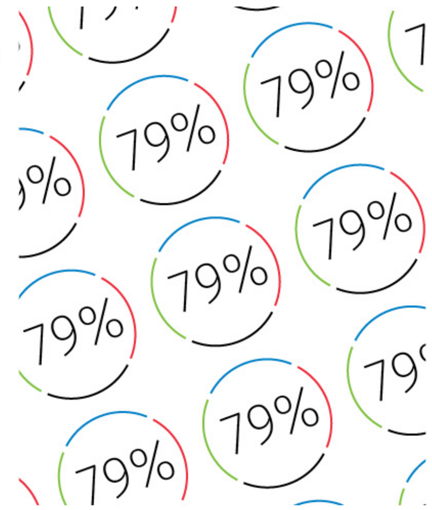

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This entry was posted on Tuesday, May 10th, 2022 at 2:45 pm and is filed under European Union, Foreign subsidies, Merger control, State aid, State owned enterprise (SOE), Subsidies, Trade Law
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