

# Kluwer Competition Law Blog

## The EU Adopts the Long-Awaited Foreign Subsidies Regulation

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On 28 November 2022, the EU adopted the Foreign Subsidies Regulation, giving the European Commission powers to intervene to tackle foreign subsidies distorting competition in the EU internal market. The FSR, due to apply by mid-2023, will have a major impact on companies that engage in M&A and public tenders in the EU, and which have received financial contributions from non-EU countries. Deal execution will be more complex and public awards more uncertain.

Companies now have six months to get ready for the entry into force of the FSR, in particular, to map financial contributions received from non-EU countries, or identify situations where they suffer from unfairly subsidised competition, as the case may be.

### In a nutshell

On 28 November 2022, the Council of the European Union **adopted** the Foreign Subsidies Regulation (“**FSR**”), aimed at preventing foreign subsidies from distorting competition in the internal market. This was the last legislative step following the European Parliament’s adoption of the FSR on 10 November 2022 (see our [alert](#) on the European Commission’s proposal of 5 May 2021).

The purpose of the FSR is to address the distortions to the EU’s internal market caused by subsidies granted by non-EU countries (“*foreign subsidies*“) to companies active in the EU. According to the Commission, the FSR closes an important enforcement gap in its toolbox, as these foreign subsidies have so far been escaping its control, unlike the subsidies given by EU Member States, which are subject to stringent EU State aid rules.

Under the FSR, the Commission has the exclusive competence to investigate and assess if the businesses operating in the EU have been backed by foreign subsidies, and whether these distort competition in the internal market. In case of distortion, the Commission has wide-ranging powers to impose redressive measures, block deals / public awards and even dissolve concentrations already concluded.

The FSR is expected to be published in the Official Journal in January 2023 and will enter into force 20 days after that. It will only apply six months after its entry into force. The notification

obligation for M&A deals and public tenders will apply nine months after its entry into force. An implementing regulation is expected to be adopted before summer 2023 (and after a public consultation, which will take place in the coming months).

## Target

The FSR targets all companies that are active in the EU and have received any form of direct or indirect financial contribution from a non-EU country (“*foreign financial contributions*”), and in particular, those that engage in M&A transactions or public tenders in the EU. Financial contributions are defined very broadly and include, *inter alia*:

- **Any transfer of State funds:** such as capital injections, grants, fiscal incentives, loans, guarantees, contracts given below-market terms, debt to equity swaps or rescheduling, etc.; and
- **Any foregoing of State revenue:** such as tax exemptions or granting of special/exclusive rights without adequate remuneration.

The financial contributions may come from the central government, but also any public or private entity whose actions can be attributed to a third country. As things stand, all financial contributions will count, regardless of their size, or whether they qualify as “foreign subsidies” or have an EU nexus.

The FSR applies to private and public companies, including Sovereign Funds. It catches not only foreign companies operating in the EU but also EU-based multinational companies that have received foreign financial contributions.

## Impact

Unlike with Foreign Direct Investment (“**FDI**”) rules, which have remained within the competence of EU Member States, the Commission will be the sole enforcer of the FSR. According to the FSR impact assessment, the Commission envisages in total 145 full-time employees in the FSR task force at DG Competition (under the Directorate for International Relations). In practice, however, we expect that the Commission will start with 40 to 50 officials in mid-2023.

The FSR vests the Commission with far-reaching investigative powers under two regimes—the *ex-ante* mandatory filing regime and the *ex officio* investigation regime.

### *Filing obligation for M&A deals*

Akin to merger control proceedings, if the below thresholds are met, the FSR imposes mandatory *ex-ante* filing and standstill obligations for companies engaging in concentrations.

- **Turnover threshold:** At least one of the merging companies (in case of a full merger), the target (in case of acquisition) or the JV is established in the EU and generates an aggregate EU-wide turnover of at least €500 million in the previous financial year; and

- **Foreign financial contributions:** The parties to the transaction have received combined foreign financial contributions exceeding €50 million in the three years prior to the conclusion of the agreement, the announcement of the bid, or the acquisition.

The FSR review deadlines are aligned with merger proceedings, to allow the two notifications to run in parallel. Phase I review will be 25 working days, while Phase II is 90 working days, extendable by 15 working days, in case of remedies. The FSR foresees the possibility for companies to hold pre-notification talks with the Commission, in particular, to receive guidance on whether the thresholds for notification are met. More details on the process and the form will be available in the implementing regulation.

#### *Filing obligation for public tenders*

The FSR also poses mandatory *ex-ante* filing obligations for companies engaging in public tenders in the EU, if:

- **Contract value:** The contract value is equal to or above €250 million; and in cases where the tender is divided into lots, the aggregate value of the lots applied for is equal to or above €125 million; and
- **Foreign financial contributions:** The bidding party (including its subsidiaries and/or holding) and its main subcontractors (or suppliers) receive aggregated foreign financial contributions equal to or above €4 million in the past three years prior to the notification. Bidding parties falling under €4 million are still under an obligation to submit a declaration confirming that they are under the filing threshold.

The FSR's preliminary review will last 20 working days, extendable only by ten working days, while the in-depth review should not last more than 110 working days from complete notification, extendable only once by 20 working days in exceptional cases.

#### *Filing obligation for M&A deals / public tenders below the thresholds, if the Commission requests*

Under the FSR, the Commission may also request parties to M&A deals/public tenders that are below the above filing thresholds to still notify their transactions/public tender prior to their implementation/award, if the Commission considers that these transactions are backed by distortive foreign subsidies.

#### *Ex officio investigation of the Commission*

The FRS grants powers to the Commission to investigate *ex officio* all potentially distortive foreign subsidies on its own initiative (or following information received by Member States, or a complainant), including, but not limited to, M&A deals and public tenders that have already been concluded (although the Commission cannot cancel a public award, but can order a break-up of M&A deal). The procedure includes a preliminary review followed by in-depth if necessary; there is no legal deadline for the Commission to complete its *ex officio* investigations, although it must

strive to complete them in 18 months. The Commission can investigate foreign subsidies up to ten years from the date when they were given.

## Procedure

Under both investigative regimes (*ex-ante* and *ex officio*), the FSR review follows a two-tier structure:

- **Preliminary review** (akin to Phase I for merger control) to check if there are sufficient indications that a company has been granted a foreign subsidy that distorts the internal market. If no sufficient indications are established, the investigation will be closed with a no objection decision (which, if the decisions are aligned with the State aid procedure, does not need to be reasoned); and
- **In-depth investigation** (akin to Phase II for merger control) in case there are sufficient indications that a company has been granted a foreign subsidy that distorts the internal market.

Following an in-depth investigation, the Commission can adopt: (i) a no objection decision; (ii) a commitments / redressive measure decision; or (iii) a decision prohibiting a concentration or the award of the contract.

The redressive measures and commitments can be *structural* (such as an acquisition ban, divestment of assets or reduction of capacity or market presence), or *behavioural* (such as offering access or licencing at FRAND conditions to an infrastructure, publicising R&D results, repaying of the foreign subsidy with an interest rate or making adaptations in the governance structure).

The Commission has extensive investigative powers, including powers to request information and conduct dawn raids in the EU and verification visits outside the EU. If the parties breach the standstill obligation or fail to notify a notifiable transaction, the Commission may impose a fine of up to 10% of their aggregate turnover in the preceding financial year. Where a company supplies incorrect, incomplete or misleading information, it may be subject to fines of up to 1% of global turnover and periodic penalty payments of up to 5% of the average daily aggregate turnover for each working day of delay.

## Focus of review

The focus of the FSR's review will be on whether the foreign financial contributions granted to companies active in the EU constitute foreign subsidies that distort the EU internal market. In order to determine that, the Commission will need to show that the financial contributions confer a competitive advantage on the company active in the EU and is specific to one or more company or industries. Once the Commission determines an existence of a subsidy, it will assess if the subsidy (i) has distortive effects on the internal market, and (ii) whether this distortion can be counterbalanced by positive effects.

In general, a subsidy would be considered distortive if it could improve the business's competitive position in the EU and in doing so, negatively affects competition on the internal market. To ease the Commission's review, the FSR includes a few legal presumptions to determine the existence of

distortion or lack thereof:

- *Subsidies likely to be distortive*: (i) supporting failing business (without a long-term plan to restructure); (ii) unlimited guarantees; (iii) facilitating a concentration; (iv) an export financing measure that is not in line with the OECD Arrangement on officially supported export credits; and (v) enabling a company to submit an unduly advantageous tender;
- *Subsidies unlikely to be distortive*: if lower than €4 million in the past three years; or if aimed at repairing damage caused by natural disasters or exceptional circumstances; and
- *Non-distortive subsidies (de minimis)*: below €200,000 per the third country in the previous three years.

If there is a distortion, the Commission will conduct a balancing test before deciding whether to block the deal/award, impose redressive measures or accept commitments. In this regard, the Commission will take into account the positive effects of the subsidy on either the development of the subsidised economic activity on the internal market or to support a broader EU policy objective, such as environmental protection and social standards, and the promotion of R&D.

### Takeaways and action items

- **Brace for more filings and Commission powers affecting deal execution.** The FSR creates a new filing obligation for companies engaging in certain concentrations in the EU. Companies contemplating M&A deals should thus envisage an FSR review, in addition to merger control and FDI reviews. Deal documentation will have to be adapted accordingly, and deal timing may be affected (until there has been enough practice, there will be considerable uncertainty about how long pre-notification discussions may run). We expect an increased number of complaints to be filed with the Commission during and after the notification of the M&A deals. Bear in mind that the Commission also has powers to request notification of non-notifiable transactions and investigate implemented deals (and issue break-up orders).
- **New uncertainty in public tenders:** whether a company is receiving foreign subsidies or competing with companies that do, the FSR will add a new dimension to public tender competition. Companies may be disqualified from public tenders if they do not report their foreign financial contributions or if they benefit from distortive subsidies. They may also be requested to offer far-reaching and tough commitments if they want to be awarded a tender. We expect an increased number of complaints to be filed with the Commission during and after awards. Bear in mind that even awarded contracts can lead to *ex-post* intervention by the Commission, for example, to impose redressive measures.
- **Get the data ready.** Companies receiving foreign financial contributions should systemically collect information concerning any financial contributions they receive on a group-wide basis and regardless of whether they constitute foreign subsidies (as this is for the Commission to assess). This information is not only necessary to assess if an M&A deal / public tender is notifiable but also in case the Commission decides to ask the company to notify their transaction (even though it is below the filing thresholds) or in case of an *ex officio* investigation (for example, in case of a complaint from competing bidders). Given the broad definition of foreign financial contributions under the FSR, the data collection is likely to be burdensome. Any notification obligation will require information on foreign financial contributions going back three calendar years back as part of the review process, *i.e.* mid-2020. It is advisable not to wait until the obligation to notify arises. It may also be useful to already consider if these financial

contributions were made on market terms, *i.e.* can be obtained under normal market conditions.

- **Participate in the consultation.** The Commission is due to publish shortly for consultation a set of guidelines and implementing acts concerning the application of the FSR. The Commission is actively encouraging interested parties to come forward and express their views.

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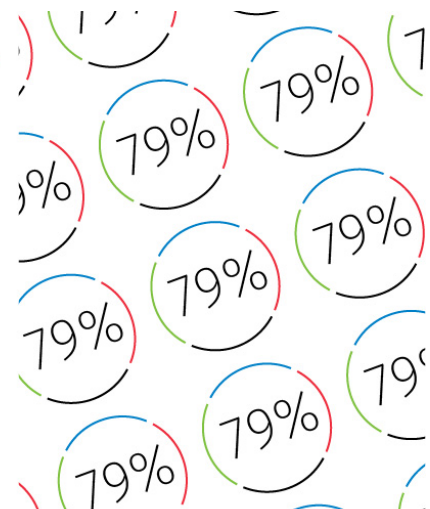
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