

Foreign Subsidies Regulation – ready, set, go

14 December 2022

On 28 November 2022, the Council has finally approved the regulation on foreign subsidies distorting the internal market (*Foreign Subsidies Regulation - FSR*). The FSR was adopted with only minor changes to the provisional agreement of the European Parliament and the Council of 11 July 2022. It will enter into force 20 days after its publication in the EU's Official Journal, so likely still this year. Most of the new rules will be directly applicable after 6 months, but the new notification requirements for M&A transactions and public procurement procedures will apply 9 months after entry into force of the FSR, i.e. around the start of Q4 2023.

The FSR will give the EU Commission new powers to investigate and counteract market-distorting subsidies granted by non-EU governments to companies set to acquire EU businesses or take part in public procurement procedures in the EU. It will introduce another layer of regulatory scrutiny, which companies operating in the EU internal market need to have on their radar from now on.

BLOMSTEIN has monitored the genesis of the FSR from the Commission's initial White Paper to the final text (see BLOMSTEIN [briefing of September 2020](#), [briefing of May 2021](#), and [briefing of July 2022](#)). This briefing summarizes the main provisions of the final text of the FSR.

Scope of the FSR

A foreign subsidy is a financial contribution from a non-EU government which gives a company active in the EU a certain benefit, which is "selective", i.e. limited to one or more undertakings or industries. This includes non-EU subsidies to private and public EU-undertakings and financial contributions coming from private entities attributed to third countries. While the FSR targets subsidised non-EU investors and state-owned undertakings from state-controlled economies, the new rules equally apply to companies established in the EU.

Examples of financial contributions include among others interest-free loans, below-cost financing, unlimited guarantees, capital injections, preferential tax treatment and tax credits – but also supply contracts with foreign public counterparties.

The three FSR pillars

The FSR introduces three new tools to enable the Commission to effectively investigate distortive foreign subsidies, namely two notification-based tools to investigate concentrations and bids in public procurement procedures as well as an ex-officio tool to investigate all other market situations.

Notification obligation for concentrations

Concentrations will trigger an ex-ante notification obligation if two cumulative thresholds are met:

- The aggregate turnover of at least one of the merging undertakings, the acquired undertaking or the joint venture established in the EU exceeds EUR 500 m in the EU; and
- all undertakings involved in the concentration were granted combined aggregate foreign financial contributions of more than EUR 50 m in the three financial years preceding the deal.

The Commission has estimated that approx. “only” 40-50 transactions per annum trigger the relevant turnover threshold, and that only a fraction of these will also meet the second limb and thus require notification under the FSR. However, the broad notion of foreign financial contribution will make it difficult to filter, with a sufficient degree of legal certainty, those cases that meet the turnover threshold but do not require notification and review on the basis that the foreign financial contribution does not exceed EUR 50m.

Where a notification is required, the concentration cannot be completed until approved by the Commission (so-called **standstill obligation**). While the review periods provided for in the FSR follow the timelines under the EU Merger Regulation (**EUMR**), the review procedures under the FSR and EUMR will be completely independent. If the Commission finds that a subsidy from a third country distorts the internal market, it can request the parties to remedy the distortion or otherwise block a concentration.

Notification obligation for bids in public procurement procedures

Regarding bids in public procurement procedures, the notification-based tool applies where

- the estimated contract value is equal to or exceeds EUR 250 m; and
- the bidder, its group or main subcontractors/suppliers were granted a financial contribution of at least EUR 4 m per third country.

In case of procurement by lots, in addition to the above, the value of the lot or the aggregate value of all the lots to which the tenderer applies must be equal to or greater than EUR 125 m.

Where a notification is required, the bidder concerned cannot be awarded the contract until cleared by the Commission. If the Commission finds that the bidder has benefited from subsidies from third countries that distort competition, it can prohibit the award of a contract to a particular bidder.

Ex-officio tool

The ex-officio tool enables the Commission to investigate any market situation, including concentrations and procurements below the thresholds, when it suspects that a distorting foreign subsidy may be involved. The Commission will be able to start investigations on its own initiative and may request ad-hoc notifications. In this context, it may ask companies to provide relevant information and conduct on-site inspections. In cases where it is not possible to collect all necessary information, e.g. from companies based outside the EU, the Commission may decide the case on the basis of the facts available to it.

Two-step investigation procedure

To assess whether a foreign subsidy has a distortive effect on the internal market, the FSR foresees a two-step investigation procedure. As a first step, the assessment involves a preliminary review and as a second step, if there are indications of the existence of a distortive foreign subsidy, an in-depth investigation.

First step – preliminary review

As a first step, the Commission assesses whether a foreign subsidy may be distortive. For this purpose, the FSR provides for a number of categories and indicators ranked by likelihood of distortive effect.

- The categories of subsidies which are **most likely** to be distortive include among others (i) subsidies to an ailing company without restructuring plan, (ii) unlimited guarantees for debts or liabilities of the undertaking, (iii) export financing measures not in line with the OECD Arrangement on Officially Supported Export Credits, (iv) subsidies directly facilitating an acquisition, and (v) subsidies facilitating the submission of an unduly advantageous tender.
- A foreign subsidy is **unlikely** to distort the internal market if its total amount does not exceed EUR 4 m over any consecutive period of three financial years.
- A foreign subsidy **does not distort** the internal market (i) if its total amount does not exceed the amount of a de minimis aid over any consecutive period of three

financial years (current de minimis amount: EUR 200 000 per single undertaking over any period of three fiscal years or resp. EUR 100 000 for road freight transport for hire or reward), or (ii) if it is aimed at making good the damage caused by natural disasters or exceptional occurrences.

In all other cases, the Commission will **consider certain indicators**, such as, among others (i) the amount of the subsidy, (ii) the nature of the subsidy, (iii) the purpose and conditions attached to the subsidy, (iv) the situation of the company, including its size and the markets or sectors concerned, and (v) the level and evolution of economic activity of the company.

Second step – In-depth investigation (balancing test)

As a second step, the Commission, where warranted, considers the market-distorting effects of foreign subsidies and balances these against potential wider benefits (so-called **balancing test**). Positive effects shall also include broader positive effects related to relevant EU policy objectives. The EU State aid compatibility test and case practice is expected to serve as a benchmark for the balancing test under the FSR.

Since the concrete application of the balancing test, in particular the definition of positive and negative effects, is still rather unclear, the Commission has already committed to provide initial clarifications on the assessment of distortion and the application of the balancing test no later than 12 months after the entry into force of the FSR. In addition, it will publish Guidelines on the application of the FSR by the end of three years after the entry into force of the FSR.

Redressive measures and commitments

Where, in the Commission's view, the negative effects prevail, the Commission may impose redressive measures or accept commitments from the companies concerned that remedy the distortion.

Redressive measures or commitments may consist, inter alia, of the following, (i) offering access to an infrastructure acquired or supported by the subsidy, (ii) reducing capacity or market presence, (iii) refraining from certain investments, (iv) licensing on fair, reasonable and non-discriminatory terms of assets acquired or developed with the help of foreign subsidies, (v) publishing results of research and development, (vi) divesting certain assets, (vii) requiring undertakings to dissolve the concentration, (viii) repaying a subsidy or (ix) requiring the undertakings concerned to adapt their governance structure.

Penalties in case of non-cooperation

Non-compliance with the obligations under the FSR carries significant fines. During the investigation phase, the Commission may impose fines and periodic penalty payments

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where an undertaking intentionally or negligently supplies (i) incorrect, incomplete, or misleading information, (ii) does not supply information within the prescribed time limit, or (iii) refuses to submit to an inspection.

Higher fines may be imposed in case of non-compliance with the notification obligations. These include:

- fines up to 1% of the aggregate turnover in the preceding financial year in case of (intentional or negligent) supply of incorrect or misleading information in a notification of a notifiable concentration, and
- fines up to 10% of the aggregate turnover in the preceding financial year in case of failure to notify (i) a concentration subject to a filing obligation under the FSR or (ii) foreign financial contributions in accordance with a public procurement procedure.

Outlook

The final text of the FSR contains a number of new legal terms that lead to significant legal uncertainty not only for foreign investors but also for EU companies that have dealings with non-EU governments. Although the Commission has committed to provide initial clarifications on the application of the FSR, including on the balancing test, within 12 months after its entry into force, the FSR will significantly add to the regulatory burden and will make deal timing predictions more difficult. To increase deal certainty, significant experience in dealing with parallel reviews and familiarity with State aid rules and national FDI regimes now is key. Foreign and EU-investors will need to allocate more time and attention to identify any applicable regulatory pre-closing requirements.

BLOMSTEIN is monitoring further developments closely and will keep you informed. This summary of the final rules is only the first briefing in a series of briefings that will focus on the specific tools under the FSR, the definition of a financial contribution, the relationship to the WTO Agreement on Subsidies and Countervailing Measures (ASCM) and general pitfalls to be aware of. For questions regarding the potential impact of the FSR on your company or your industry in relation to pending or future transactions, please contact [Max Klasse](#) and [Jasmin Mayerl](#) and for questions regarding the impact on public procurement, please contact [Pascal Friton](#) and [Ramona Ader](#).