

An introduction to the EU Foreign Subsidies Regulation

The Foreign Subsidies Regulation (EU) No 2022/2560 (FSR) entered into force on 12 January 2023 and became effective on 12 July 2023. It is designed to address distortions of the EU's internal market caused by foreign subsidies, with the aim of ensuring fair competition and a level playing field. There are two key aspects:

- **Mandatory notification regime** - the FSR creates a new mandatory notification regime for certain EU mergers, acquisitions, joint ventures and public tenders involving parties that have received financial contributions from non-EU countries. These deals must be cleared by the Commission before they can be implemented. The notification regime will be effective from 12 October 2023.
- **Power to carry out *ex officio* investigations** - the FSR gives the European Commission the power to investigate financial contributions from non-EU countries to businesses operating in the EU to assess whether they are foreign subsidies that distort the internal market. These new investigative powers came into force on 12 July 2023.

Who may be affected by the FSR?

Businesses which receive "financial contributions" in non-EU countries and which operate in the EU will need to be aware of the FSR and should collect data on any foreign financial contributions they receive.

Businesses planning to undertake M&A transactions or public tenders in the EU need to be aware of, and comply with, the mandatory notification regime.

Meaning of "financial contribution" and "foreign subsidy"

The FSR states that a foreign subsidy is deemed to exist where a third country provides, directly or indirectly, a financial contribution which confers a benefit on an undertaking engaging in an economic activity in the EU internal market. The benefit must be limited to one or more undertakings or industries.

The concept of a financial contribution is very broad, covering transfers of state funds (e.g. grants), foregoing of state revenue (e.g. tax exemptions), arrangements relating to liabilities (e.g. debt rescheduling) and the provision or purchase of goods or service to or from a non-EU government. Non-EU financial contributions can be made by a wide range of government bodies and public authorities, including local government. The definition also covers contributions from private companies whose actions are attributable to a non-EU government. All financial contributions count – there is no de minimis threshold. Businesses which are active in the EU and which have trading arrangements with non-EU government bodies, non-EU public authorities or private companies whose actions are



attributable to a non-EU country should be aware that those arrangements are likely to be considered as financial contributions.

Mandatory notification regime for EU M&A transactions

From 12 October 2023, businesses planning M&A deals in the EU which trigger the thresholds in the FSR (see below) will be required to notify the Commission. Notification should be made by the buyer (in the case of an acquisition of sole control), the merging parties, or the parties acquiring joint control of the whole or part of an undertaking. Once notification has been submitted, the parties will have to await approval from the Commission. There is an initial 25 working day review period followed by an in-depth 90 working day review period (with a possible extension by 15 working days if commitments are offered) from the date of formal notification.

Notification is also required for M&A transactions for which the agreement was concluded on or after 12 July 2023 but which have not yet been implemented on 12 October 2023.

There are two threshold tests:

- €500 million in EU-wide turnover in the previous financial year from at least one of the merging parties, the target or the joint venture established in the EU; and
- €50 million in combined foreign financial contributions received by the parties within the three years prior to the conclusion of the agreement, announcement of the bid, or the acquisition.

The FSR regime will need to be factored into the due diligence process on any M&A transaction where a target, merging party or joint venture vehicle is established in the EU. The parties will need to identify any financial contributions received from non-EU countries and whether the thresholds are crossed. If so, the parties will need to consider whether these financial contributions might be regarded as distortive foreign subsidies and therefore affect the likelihood of the transaction being cleared by the Commission. Buyers are also likely to require warranties in transaction documents.

Following a notified transaction, the Commission can issue a no-objection decision, a decision with commitments to resolve any concerns, or a decision prohibiting the transaction altogether.

Notification of tenders for government contracts

Businesses bidding for public contracts in the EU must notify all financial contributions received from non-EU countries where:

- the value of the contract is at least €250 million; and
- the bidder (including its group and main sub-contractors and suppliers) has received foreign financial contributions of at least €4 million in the last three years.

Where the contract value threshold is met, bidders that do not meet the second threshold must make a declaration to the effect that they are under the threshold and disclose the foreign financial contributions received.

What makes a foreign subsidy distortive?

The FSR states that a distortion in the internal market shall be deemed to exist where a foreign subsidy is liable to improve the competitive position of an undertaking in the internal market and where, in doing so, that foreign subsidy actually or potentially negatively affects competition in the internal market. There is a non-exhaustive list of categories most likely to distort the internal market:

- a subsidy supporting a failing business
- unlimited guarantees
- a subsidy directly facilitating a concentration
- export financing measures which are not in line with OECD rules
- a subsidy enabling a company to submit an unduly advantageous tender

Subsidies which are unlikely to be distortive include those lower than €4 million in the past three years, and those aimed at repairing damage caused by natural disasters or exceptional circumstances.

Subsidies which are not distortive are those which are below €200,000 per non-EU country in the previous three years.

Power to carry out *ex officio* investigations

The Commission has the power to initiate *ex officio* investigations into all potentially distortive foreign subsidies. The Commission will also have powers to investigate M&A deals and public tenders that are below the mandatory thresholds set out above, or which have been implemented without prior notification. The Commission will have around 150 full-time employees in an FSR task force.

After an in-depth *ex officio* investigation, the Commission can issue a non-objection decision, or a decision with commitments or redressive measures to resolve any distortion of competition.

Fines and periodic penalty payments

The Commission may impose fines or periodic penalty payments. For provision of incorrect, incomplete or misleading information, fines may be up to 1% of global turnover or periodic penalties of up to 5% of average daily turnover. Failure to notify an M&A transaction which is within scope may attract a fine of up to 10% of the undertaking's aggregate global turnover in the last financial year.

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