

Competition & Regulation Briefing

EU Foreign Subsidies Regulation: M&A and Public Tender Impacts – Are You Ready?

With the new EU Foreign Subsidies Regulation (“**FSR**”) now fully in force, M&A transactions and public procurement processes above certain prescribed thresholds are now mandatorily notifiable to the European Commission since 12 October 2023. While the EC has had a ‘call in’ power to review potentially distortive non-EU subsidies since the FSR regime went live on 12 July 2023, identifying the existence of such mandatory approval requirements will further increase the compliance burden on companies moving forward.

The new FSR regime is part of the EU’s broader industrial policy agenda, and represents a tougher stance against perceived unfair competition from outside the bloc. While the EC’s State aid regime has long ensured oversight over subsidies given by EU Member States, the EC has lacked the same power in respect of subsidies granted by non-EU governments. The new FSR regime closes that gap by giving the EC a review power, as well as a power to block or impose commitments when it identifies potentially distortive subsidies at play.

The implications for both EU and non-EU companies in receipt of non-EU financial contributions and subsidies granted by non-EU government bodies or public or private entities attributable to non-EU governments are significant. At a minimum, new internal data collection processes will need to be implemented to capture all non-EU financial contributions received to ensure compliance.

This Briefing provides an overview of the key elements of the new FSR regime, and what companies can do to get ready and ensure they are compliant.

FSR Regime Fully in Force

The new regulatory regime established under the FSR and administered by the EC came into force on 12 July 2023. Since then, the EC has had a ‘call in’ power to initiate ex-officio investigations into potentially distortive non-EU subsidies, including in respect of M&A transactions and public procurement initiated after that date.

Since 12 October 2023, larger-scale M&A transactions and high-value public contracts that meet the relevant thresholds will also need to be notified to the EC. This includes all M&A transactions that have been signed on or after 12 July but not completed by 12 October 2023, and public contracts announced on or after 12 July but not awarded by 12 October 2023.

Mandatory Notification Thresholds

M&A transactions

In relation to M&A transactions, parties will need to notify the EC to obtain pre-closing approval where the following cumulative thresholds are met:

1. **Turnover threshold:** one of the target company, one of the merging parties, or the joint venture (“JV”) is established in the EU and has EU-wide turnover of at least €500 million in the last completed financial year; and
2. **Non-EU financial contribution threshold:** the undertakings involved in the transaction (ie, the acquiring company and the target, the merging entities, or the JV and its parent companies) have received combined aggregate financial contributions of more than €50 million within the three year period prior to the agreement.

The transaction itself needs to involve an acquisition of ‘control’ (ie, ‘decisive influence’ or the power to approve or block strategic commercial decision-making) over the target business or the establishment of a ‘full-function’ JV (ie, a JV that will operate independently and autonomously on the market).

These mirror the same concepts as under the EU Merger Regulation (“EUMR”).

Importantly, the concept of a non-EU ‘financial contribution’ is defined broadly, and notably, below the threshold of a non-EU ‘subsidy’ which confers a benefit on an undertaking(s). Thus, the concept of a non-EU ‘financial contribution’ covers any direct or indirect financial contribution made by governments of, or any public or private entity attributable to, a non-EU country, and including:

- i. The transfer of funds or liabilities such as capital injections, grants, loans, loan guarantees, fiscal incentives, the 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, such as tax exemptions or the granting of special or exclusive rights without adequate remuneration; or
- iii. The provision of goods or services or the purchase of goods or services (even at market value).

While the turnover threshold is set relatively high, the financial contribution threshold is set a much lower level. The broad concept of ‘financial contributions’ is also cast widely to catch a broad set of arrangements with non-EU governments. Accordingly, if the turnover threshold is met, the prospect of the non-EU financial contribution threshold would generally be expected to be higher (but will depend on the parties and sectors involved, amongst others).

Potential mandatory FSR approvals will now be a standard element of the regulatory due diligence analysis, alongside merger control and foreign investment screening requirements.

See **Figure 1** below regarding the M&A filing analysis.

Public Procurement

In relation to public procurement processes, tenderers participating in a public procurement procedure, are required to notify the contracting authority or contracting entity of all foreign financial contributions where:

1. **Contract value threshold:** the estimated value of the public procurement (or framework agreement) is at least €250 million (and, where the contract is divided into lots, the aggregate value of each lot is €125 million); and
2. **Non-EU financial contribution threshold:** the company (including its subsidiary companies without commercial autonomy, holding companies, and, if applicable, main subcontractors and suppliers involved in the same tender in the public procurement procedure) was granted aggregate financial contributions in the 3 years prior to notification of at least €4 million per non-EU country.

The notification obligation also applies to the main subcontractors and suppliers if the economic share of their contribution exceeds 20% of the estimated contract value.

As referenced above, the tenderer is required to notify the contracting authority or contracting entity of all foreign financial contributions where the above thresholds are met. The contracting authority or contracting entity is then required to transfer the notification to the European Commission for review.

Where the contract value is above the threshold, but the non-EU financial contributions received are below threshold, the tenderer is still required to submit a declaration to the contracting authority or contracting entity setting out all non-EU financial contributions received and why the non-EU financial contribution threshold is not met.

Tenderers therefore need to be aware of the potential impact of mandatory notification or declaration obligations arising from non-EU financial contributions received.

See **Figure 2** below regarding the public procurement filing analysis.

Residual 'Call In' Power

The EC has also had a general 'call in' power to initiate *ex-officio* investigations into potentially distortive non-EU subsidies, including in the context of M&A transactions and procurement processes initiated after that date and also including those below the mandatory notification thresholds. This power has been effective since the regime came into force on 12 July 2023.

The EC may exercise this power based on information from all sources including information from Member States and third party complaints.

In evaluating whether to exercise this power, it is likely that the EC will have regard to the considerations set out in the FSR as to when a financial contribution or subsidy is likely to distort the internal market. These considerations include the amount of the foreign subsidy; the nature of the foreign subsidy; the situation of the undertaking, including its size and the markets or sectors concerned; the level and evolution of economic activity of the undertaking on the internal market; and the purpose and conditions attached to the foreign subsidy as well as its use on the internal market.

The EC can exercise its 'call in' power in relation to any M&A transaction involving a potentially distortive subsidy that was granted in the five years prior to 12 July 2023 (ie, since 12 July 2018) and which potentially distorts the EU market after 12 July 2023. In the context of a public procurement process, the 'call in' power can be exercised in relation to any potentially distortive subsidiary that was granted in the three years prior to 12 July 2023 (ie, since 12 July 2020).

While the circumstances in which the EC will exercise its 'call in' power are as yet unclear, the possibility of a 'call in', even where mandatory approvals are not required, will create further risk for companies in receipt of non-EU subsidies.

Figure 1: FSR Filing Analysis - M&A transactions

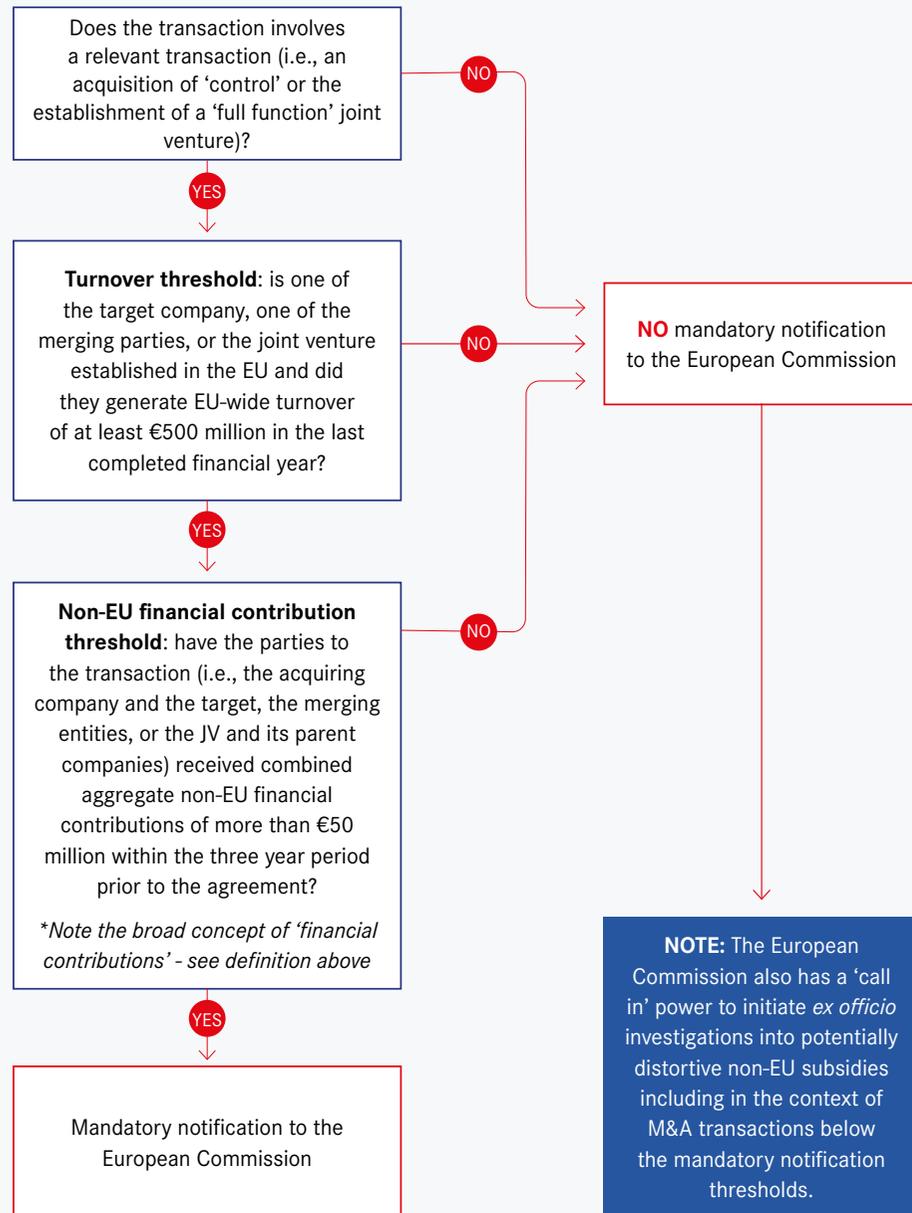
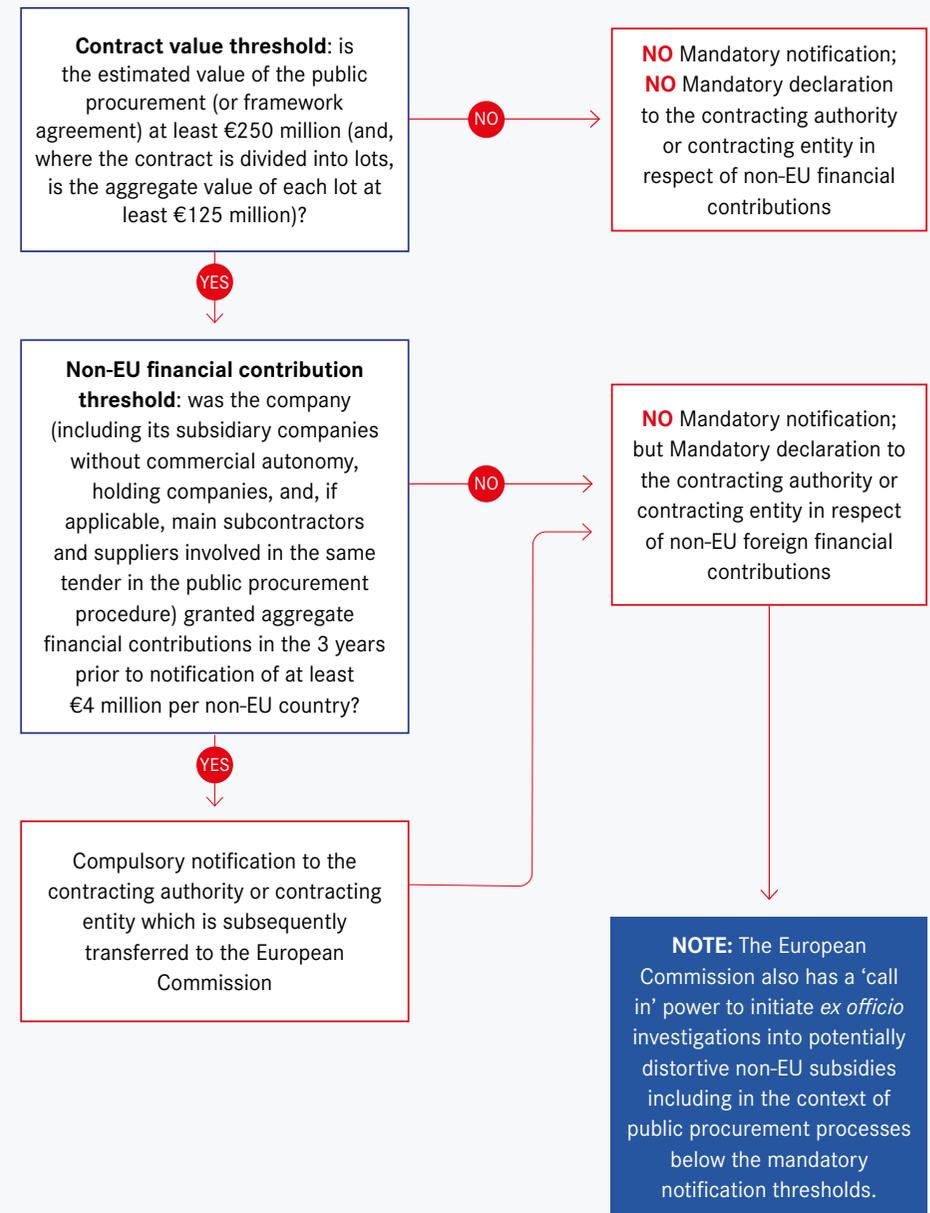


Figure 2: FSR Filing Analysis - Public Procurement



Disclosure Obligations

The EC adopted the final Implementing Regulation to the FSR on 10 July 2023. In particular, the Implementing Regulation includes the final notification forms setting out the exact disclosure requirements in respect of notifiable transactions and public contracts.

The most controversial of these disclosure requirements has been the extent of information parties need to disclose in respect of non-EU financial contributions received, noting the broad definition as outlined above.

In the final notification forms, companies need to disclose:

- Detailed information and documentation on all non-EU financial contributions granted to the notifying parties over the past 3 years that are considered most likely to distort the internal market as set out in the FSR (ie, those granted to ailing undertakings; unlimited guarantees; export financing measures that are not in line with the OECD Arrangement on officially supported export credits; those directly facilitating a concentration; and those enabling an undertaking to submit an unduly advantageous tender on the basis of which the undertaking could be awarded the relevant contract) and of an individual amount of at least €1 million; and
- An overview of all other non-EU financial contributions granted to the notifying parties over the past 3 years, of an individual amount of at least €1 million and in relation only to those countries that have granted to the parties to the transaction at least €45 million over the 3 years before the concentration, excluding certain ordinary course transactions and financial contributions within the same investment funds. (The aggregate country threshold is lower at €4 million in respect of public contracts.)

The disclosure requirements are significantly reduced relative to the initial EC draft proposals. The EC significantly reduced the scope of the financial contributions for which detailed

information and documentation is required, as set out above. The *de minimis* thresholds have also been increased (ie, from €200,000 to €1 million) and a number of additional exemptions have been introduced which narrow the scope further.

Waivers from disclosure requirements may also be granted where information may not be reasonably available, or where information is not considered necessary for examination of the case. How the EC's future waiver practice will evolve remains to be seen.

Clearance Timelines & Outcomes

M&A transactions

The FSR clearance timelines are similar to those under the EUMR. This involves an initial pre-notification process and a Phase 1 review of 25 working days. In the event the EC has substantive concerns, the EC may open a Phase 2 review, which will last up to 90 working days and is extendable by 15 working days if the parties offer remedies. Notably, in contrast to the EUMR process, the FSR regime does not allow remedies to be offered during the Phase 1 review.

Where the EC calls in a transaction for review, the transaction is subject to the usual review process and clearance timelines, as outlined above.

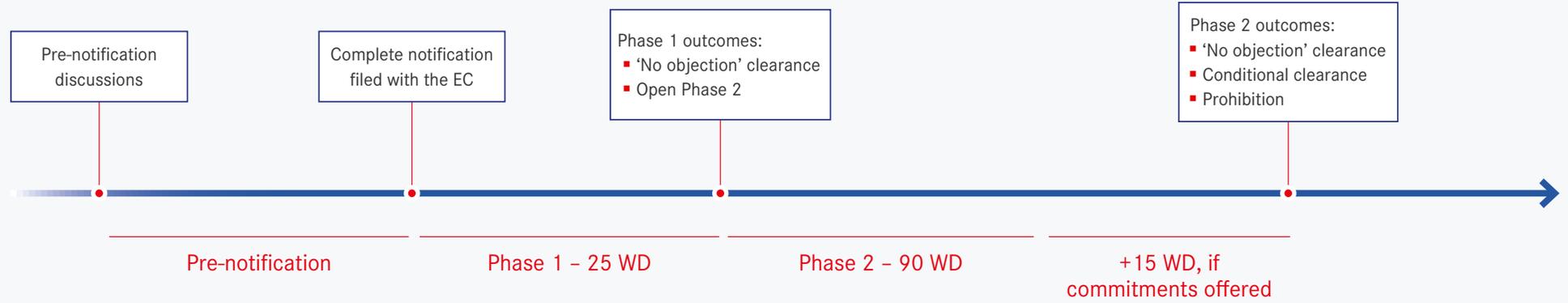
Public Procurement

The EC's review process and timeline are intended to run parallel to the public procurement procedure, although in practice the FSR review, if instigated, may extend beyond the normal timings of a procurement procedure. There is an initial Phase 1 review of 20 working days (which may be extendable by 10 working days). If the EC has initial concerns, the Phase 2 review extends the timeline by another 110 working days (extendable by 20 working days). Similar to the M&A process, any commitments can only be offered at Phase 2.

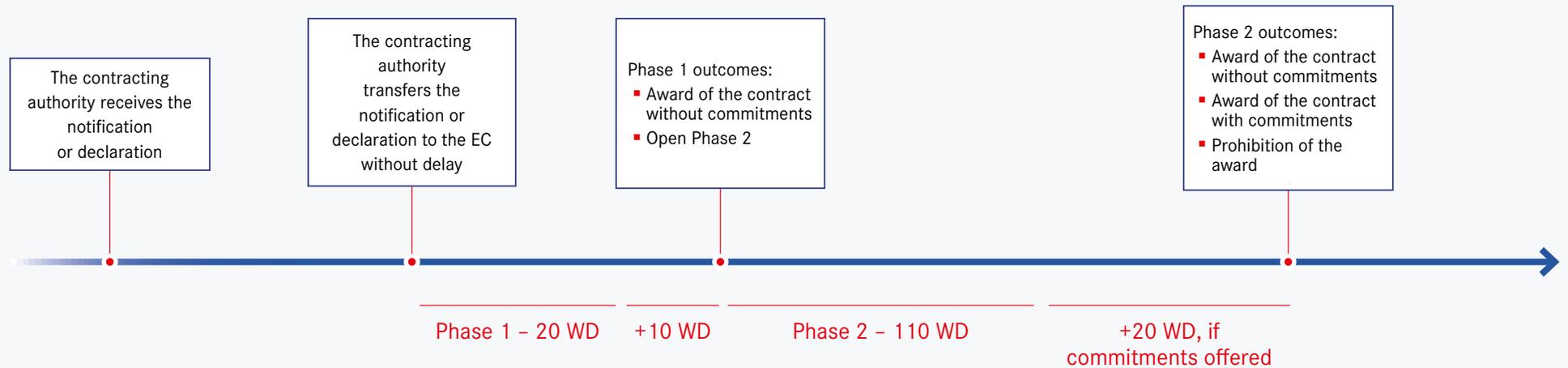
See **Figure 3** below which sets out the clearance timelines in the context of M&A and public procurement approvals.

Figure 3: Clearance Timelines

M&A transactions



Public Procurement



Substantive Assessment

The EC will assess whether non-EU financial contributions received constitute subsidies that may distort the EU internal market. The assessment ultimately involves a balancing test between the competitive advantage conferred by any distortion caused by the subsidy, and any positive effects for the relevant subsidised economic activity, as well as broader policy considerations.

Under the FSR, the following categories of foreign subsidies are apparent which is relevant in the context of the EC's substantive assessment:

- No distortive effects – A financial contribution is considered to have no distortive effects where (1) the total amount is less than €200,000 per country over three years; or (2) where it relates to compensation for harm caused by natural disasters or exceptional occurrences.
- Unlikely distortive effects – A financial contribution is unlikely to have distortive effects where the total amount is less than €4 million over three years.
- Most likely distortive effects – A financial contribution is most likely to have distortive effects where (1) it is granted to an ailing undertaking; (2) it takes the form of an unlimited guarantee(s); (3) it takes the form of an export financing measure that is not in line with the OECD Arrangement on officially supported export credits; (4) it directly facilitates the transaction; and / or (5) it enables an undertaking to submit an unduly advantageous tender on the basis of which the undertaking could be awarded the relevant contract.

Where the EC takes the view that a non-EU subsidy has an actual or potential distortive effect on the EU market, it may impose redressive measures. A non-exhaustive list of potential redressive measures is set out in the FSR which includes access to infrastructure on fair, reasonable and non-discriminatory (“FRAND”) terms; reduction of capacity or market presence; refraining from certain investments; licensing of assets on FRAND terms; publication of R&D results; divestment of assets; adaption of corporate governance structures; the repayment of the foreign subsidy (including interest); and the notification of future transactions.

Other Powers

The EC is vested with a broad range of investigative and enforcement powers under the FSR, including:

- The EC will have broad powers of inspection and to compel the provision of information. This includes on-site inspections on premises both within the EU and outside the EU (provided the relevant third country government has been notified and not objected).
- The EC power to impose fines of up to 10% of worldwide turnover for a failure to submit a mandatory notification in respect of a M&A transaction or a procurement process above the prescribed thresholds. The EC will also have a power to impose fines of up to 1% of worldwide turnover for failure to reply to a formal information request or to supply false or misleading information. Similarly, the EC will have a power to impose a fine of up to 10% of worldwide turnover where a party does not comply with any redressive measures imposed.

Getting Ready: Tracking Non-EU Financial Contributions

Tracking financial contributions received from non-EU countries will place a huge burden on companies. Doing so will however be necessary, both to assess whether mandatory approvals are needed in the context of M&A transactions or public procurement processes or whether there is a risk of a ‘call in’ by the EC and to satisfy information disclosure requirements if approvals are needed.

New internal data collection processes in respect of all non-EU financial contributions received across the organisation will be needed to ensure that approval requirements are properly identified and information disclosure requirements can practically be met when it comes to actual notification processes.

Putting such processes in place is likely to be a significant undertaking, although the extent of the mapping exercise will naturally vary depending on the size of the organisation in

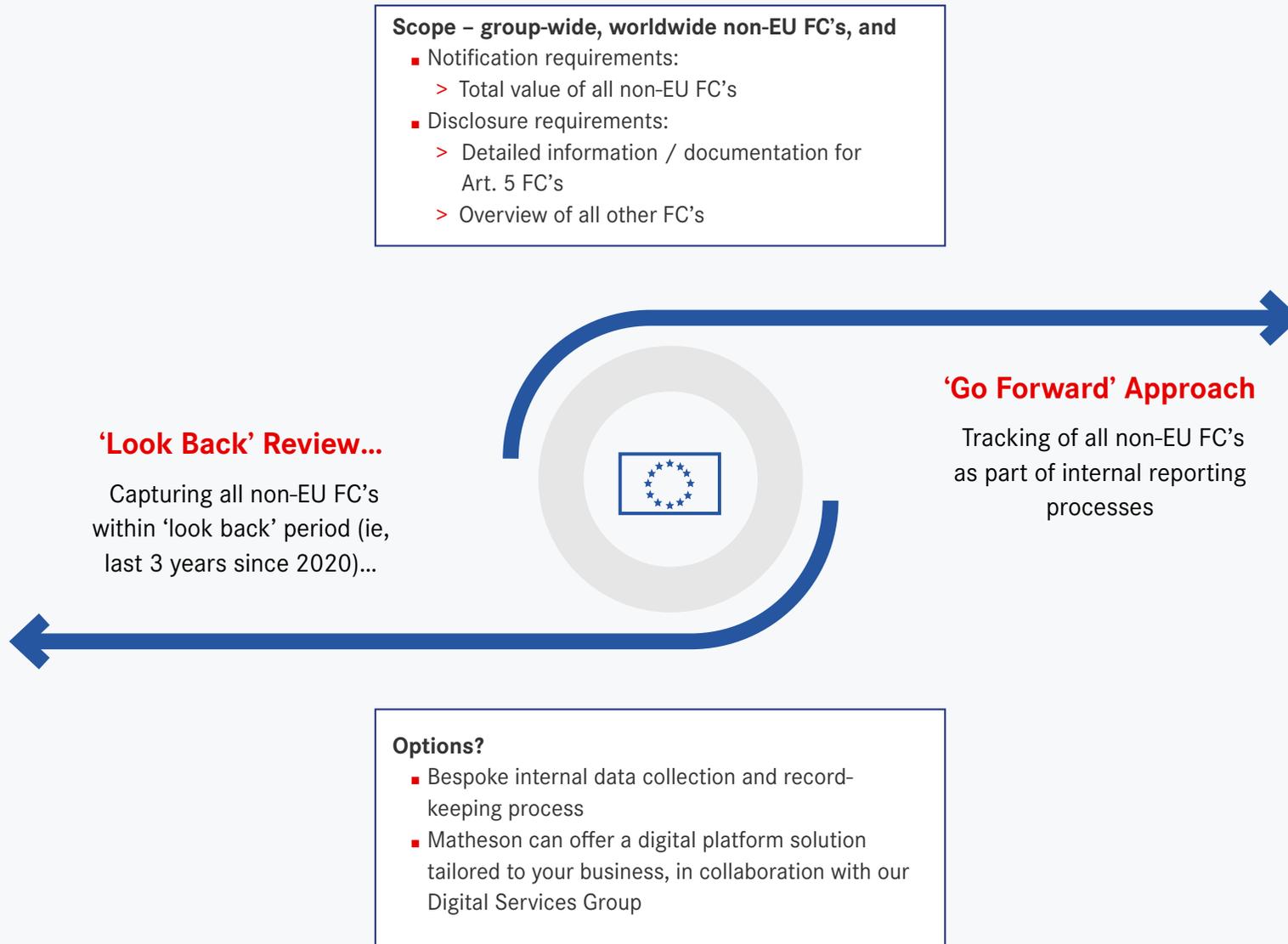
question. For example, larger multi-national organisations will likely need a process that ensures the systematic collection of information on all non-EU financial contributions received and a consistent approach across all global locations.

Additional compliance measures will also need to be considered. In the M&A context, standard due diligence questions will need to be raised to identify approval requirements or ‘call in’ risks. In the public procurement context, additional compliance checklists and obligations in respect of non-EU subsidies may need to impose on due diligence processes or consortia participation.

Figure 4 below provides an overview of the data collection process.

Matheson's Competition and Regulation group stands ready to guide affected parties on their obligations under the new regime and the type of data collection processes that may be considered, including digital solutions in collaboration with our market-leading Digital Services Group.

Figure 4 – Tracking Non-EU Financial Contributions (“FCs”)



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