# Foreign Subsidies Regulation: Mergers and public procurement procedures involving companies subsidised by non-EU countries

**EU REGULATION ON FOREIGN SUBSIDIES DISTORTING THE INTERNAL MARKET**



## Executive Summary

- The notification requirements for certain corporate mergers and acquisitions and participation in major procurement procedures under the "Regulation on foreign subsidies distorting the internal market" (Foreign Subsidies Regulation – FSR) come into force from 12 October 2023.
- The European Union passed the Foreign Subsidies Regulation to prevent subsidies from countries outside the EU (foreign subsidies) from undermining the European Single Market.
- The most important legal instruments introduced by the FSR are
  (1) an obligation to notify the European Commission of relevant mergers and acquisitions (referred to by the Regulation collectively as "concentrations") if companies subsidised by a non-EU government are involved,
  (2) the obligation for companies receiving subsidies from non-EU countries to notify the Commission prior to participating in high-volume public procurement procedures and
  (3) granting the Commission the power to start investigations on its own initiative.
- The FSR will be another cornerstone of competition law in a globalised EU economy. The Regulation combines aspects of antitrust, public procurement and state aid law and draws on their regulatory mechanisms.


The European Single Market is an attractive economic area for companies from other countries and needs to be open to trade and investment. However, it also needs to offer a level playing field for all market players.

This kind of level playing field cannot be achieved if the European Commission and the Member States only allow subsidies within the limits of European state aid law while companies from non-EU countries are freely able to use government subsidies to acquire companies or to gain advantages in public procurement procedures in the EU and increase their chances of securing such contracts.

The Foreign Subsidies Regulation[1] together with its Implementing Regulation[2] are intended to remedy this situation.

The Commission's Executive Vice-President Valdis Dombrovskis described the high expectations regarding the FSR as follows: *"The Foreign Subsidies Regulation will help us to protect the integrity of the Single Market, our most precious economic asset. For EU companies, this is a game changer as it will create fairer rules of engagement so they can compete on an equal footing with foreign competitors."*

## I. Objectives and background

State aid law, anti-trust law and public procurement law contain the most important regulations protecting competition in the Single Market. They are designed to ensure that all market players are able to compete on an equal footing.

However, there was previously a regulatory gap in terms of protecting this competition from subsidies from non-EU countries, as state aid law simply does not cover foreign subsidies. This led to the following consequences:

- In the case of corporate transactions, it previously did not matter if these were (partially) financed by non-EU state subsidies.
- In major procurement procedures, contracting authorities had no means of taking action against tenderers who could afford to engage in price wars thanks to non-EU subsidies.

The FSR and its Implementing Regulation are about to change this. The Regulation contains the main obligations for companies and the Commission's powers, while the Implementing Regulation regulates the details of the procedures envisaged by the FSR, including forms, deadlines, handling of documents, and the inspection of files, etc.

## II. Foreign subsidies and distortion of the Single Market – key concepts

### 1. Foreign subsidy (Art. 3 FSR)

The new regulation hinges on the concept of a "foreign subsidy". The term is defined very broadly. As a rule of thumb, anything that would be considered a benefit under EU law in the sense of aid under Art.107(1) TFEU if the subsidy were provided by a Member State is considered a foreign subsidy if it is provided by a third (non-EU) country. In the words of the FSR:

A **foreign subsidy** is a financial contribution which confers a benefit on an undertaking engaging in an economic activity in the internal market and which is limited, in law or in fact, to one or more undertakings or industries (Art. 3(1) FSR).

Pursuant to Art. 3(2) sentence 1, a financial contribution can be:

- Capital injections and grants
- Loans and loan guarantees
- Fiscal incentives
- Setting off of operating losses
- Compensation for other financial burdens
- Debt forgiveness
- Foregoing of revenue (for example, tax exemptions)

[1] Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market, Official Journal L 330/1, 23 December 2022.
[2] Commission Implementing Regulation (EU) 2023/1441 of 10 July 2023 on detailed arrangements for the conduct of proceedings by the Commission pursuant to Regulation (EU) 2022/2560 of the European Parliament and of the Council on foreign subsidies distorting the internal market, Official Journal L 177/1, 12 July 2023.

- Provision of goods or services
- Purchase of goods or services
- Other benefits received by an entity without adequate remuneration.

A financial contribution is deemed to be **foreign** if it is granted directly or indirectly by a third country. This includes not only the central government and public authorities, but also foreign public entities whose actions can be attributed to the third country. This is assessed taking into account the characteristics of the entity, the legal and economic environment prevailing in the state in which the entity operates, including the government's role in the economy. Finally, funds received from private entities are also deemed foreign subsidies if the actions of such private entities can be attributed to the third country taking into account all relevant circumstances (Art. 3(2) FSR).

### 2. Distortions in the internal market

If there is a foreign subsidy, this is only relevant for concentrations or procurement procedures if it distorts the internal market (Art. 10, Art. 11 FSR).

A foreign subsidy distorts the internal market if it can improve the competitive position of the subsidised undertaking and, in doing so, negatively affect competition in the internal market. The criteria for this assessment are the amount of the foreign subsidy, its nature, the situation of the subsidised undertaking, the evolution of economic activity on the internal market, as well as the subsidy's purpose and use (Art. 4(1) FSR). According to Art. 4(2) FSR, it is presumed that a foreign subsidy not exceeding EUR 4 million over three years is unlikely to lead to distortions in the internal market. Furthermore, a foreign subsidy is not considered to distort competition if it does not exceed the amount of de minimis aid – currently EUR 200,000 over three financial years.

Art. 5 FSR contains the legal presumption in reverse: Subsidies are most likely to distort the internal market if, among other things:

- they are granted to an ailing undertaking,
- they take the form of unlimited guarantees,
- they directly facilitate a concentration (merger); or
- they enable an undertaking to submit an unjustifiably low tender.

## II. Distortion in the internal market caused by foreign subsidies in concentrations (Art. 19 et seq. FSR)

The new rules are intended to discourage concentrations that are based on subsidies from third countries and therefore distort the internal market. However, the rules apply only if the concentrations are economically significant:

### 1. Concentrations

Concentrations arise where a change in the control of an undertaking on a lasting basis results from either a merger of two or more previously independent undertakings or the acquisition of control of the whole or parts of one or more other undertakings (Art. 20(1) FSR). The same applies to the creation of joint ventures (Art. 20(2) FSR). In substance, the FSR thus establishes a special and additional merger control system.

### 2. Notification thresholds

Art. 20(3) FSR provides for two notification thresholds for "notifiable concentrations". These are determined firstly by the aggregate turnover and secondly by the amount of the financial contributions from third countries. Specifically, notifiable concentrations are deemed to arise where

- the undertakings concerned or the joint venture are established in the European Union and generate an aggregate annual turnover in the EU of at least EUR 500 million, and
- the following undertakings receive financial contributions of more than EUR 50 million from third countries: in the case of an acquisition, the acquirer or the acquired undertaking, (2) in the case of a merger, the merging undertakings, or (3) in the case of a joint venture, the undertakings creating the joint venture or the joint venture itself. This only applies to financial contributions granted in the three years prior to

the signing of the contract, the publication of the takeover bid or the acquisition of control.

There are detailed regulations for both the acquisition of control and the calculation of aggregate annual turnover. The basic rules, which are subject to many details, can be summarised as follows:

- Just as in antitrust law, control is established by rights, contracts or any other means which confer the possibility of exercising decisive influence over the activities of an undertaking (Art. 20(5) FSR),
- Aggregate turnover comprises all turnover achieved by the undertakings concerned in the preceding financial year (Art. 22 FSR).

### 3. Legal consequences

The first legal consequence for notifiable concentrations is obvious: Concentrations must be notified to the Commission prior to their implementation (Art. 21(1) FSR). The undertakings must then wait until the Commission makes a decision ("standstill obligation").

The legal consequences of notifying the Commission or failing to do so are much more interesting:

Per Art. 24(1) FSR, notification of a concentration sets off time limits during which the merger or acquisition may not be implemented to give the Commission time to review the matter. If the Commission receives a complete notification, this period is only 25 days (Art. 24(1), point (a) FSR).

However, it is foreseeable that it will be virtually impossible to file complete notifications if the Commission takes more than 25 days for its review. Similar to the notification procedure for state aid, the Commission will always find further information to request, which will extend the review period. The Commission therefore encourages companies – similar to the notification procedure for state aid – to contact the Commission beforehand in order to clarify certain points before any review period even starts. Companies affected by the regulation should definitely take advantage of this offer.

It should be noted that the Commission also has another option to extend its review deadlines and intensify the review procedure. In accordance with Art. 24(1)(b) FSR, the Commission may decide – before the expiry of 25 days – to conduct an **in-depth investigation**, which extends the review period to 90 days. The only substantive requirement for the in-depth investigation is that "the Commission, based on the preliminary review, has sufficient indications that an undertaking has been granted a foreign subsidy that distorts the internal market".

The Commission shall conclude the in-depth investigation (see Art. 11 FSR on implementation) in accordance with Art. 25(3) FSR,

- either with a decision with commitments;
- a no objection decision; or
- a decision prohibiting a concentration.

The **decision with commitments** according to Art. 11(3) FSR is a compromise: On the one hand, the Commission finds that the foreign subsidy distorts the internal market. On the other, the undertaking under investigation offers certain commitments to remedy the distortion. The Commission can require subsidised undertakings to reduce their market presence or to divest assets. Among other things, it can also order companies to refrain from certain investments or to repay the foreign subsidy with interest (Art. 7(4) FSR). The Commission can then declare these commitments to be mandatory and the concentration can be implemented.

The **no objection decision** is adopted in the form of an implementing act as per Art. 11(4) FSR. The Commission issues this act if its preliminary assessment of a distortive foreign subsidy is not confirmed or if a distortion in the internal market is outweighed by positive effects of the concentration. Art. 6 FSR contains guidelines on how to conduct this "balancing test" between positive effects and the distortion in the internal market.

A **decision prohibiting a concentration** from the Commission prohibits the concentration altogether. If such a decision is issued and becomes final, the merger or acquisition cannot go ahead.

Failure to notify the Commission of a concentration that would have required notification or proceeding with the transaction before receiving approval constitute violations of the notification obligation or the prohibition on implementing a concentration before receiving approval as per Art. 24(1) FSR. The prohibition on implementing a concentration is likely to be considered a statutory prohibition according to German standards, just like the prohibition on Member States putting proposed measures into effect in the area of state aid law according to Art. 108(3) sentence 3 TFEU. Therefore, implementing a concentration without notifying the Commission or before the Commission's review is complete will likely render it ineffective under German law under Section 134 of the German Civil Code (BGB).

In addition to this civil sanction, the FSR also protects the notification obligation and the implementation ban by imposing fines and periodic penalty payments. Both can be imposed by the Commission according to Art. 26 and 17 FSR. If incorrect information is provided in the notification, fines can amount to up to 1% of the aggregate turnover of the undertaking concerned in the preceding financial year. If a notifiable concentration is implemented without notification, the fine may amount to up to 10% of the aggregate turnover achieved in the preceding financial year.

### III. Public procurement procedures (Art. 27 et seq. FSR)

Foreign subsidies can also distort competition in procurement procedures for services by contracting authorities and contracting entities in certain sectors. The Regulation targets foreign subsidies that enable an economic operator – a tenderer – to submit an unduly advantageous tender. This is to be assessed on a case-by-case basis for the procurement procedure in question (Art. 27 FSR).

Companies participating in public procurement procedures must notify the contracting authority of foreign subsidies if these exceed the following thresholds (Art. 29(1), 28(1) and (2) FSR):

- The estimated contract value is equal to or greater than EUR 250 million.
- In addition, the participating company or certain of its affiliates have received foreign subsidies equal to or greater than EUR 4 million (in the three years prior to notification, Art. 27 sentence 3 FSR, Art. 28(1)(b) FSR).
- If the procurement is divided into lots, the threshold for the lots the company is bidding on has a total value equal to or greater than EUR 125 million.

If the tenderer has received foreign subsidies but there is no notification obligation (because the subsidies are under the threshold), the tenderer must declare this vis-à-vis the contracting authority. In this case, the tenderer must also list all foreign subsidies received (Art. 29(1) sentence 2 FSR). The contracting authority must then forward declarations or notifications to the Commission (Art. 29(2) FSR).

In a two-stage procurement procedure with a prequalification competition, the tenderer must submit the notification or a declaration that no notification is necessary twice: first with the request to participate and then with the final tender (Art. 29(1) sentence 4 FSR).

This will obviously raise many questions. For example: Assessing the contract value is the responsibility of the contracting authority (cf. Section 3 of the German Regulation on the Award of Public Contracts (VgV)). While the contract notice form provides a field for the contract value, this is not a mandatory field. Does this mean tenderers could argue that they did not notify the Commission because their estimate of the contract value on the basis of

which they submitted their tender was lower than the actual contract value?
If the contracting authority forwards the notification to the Commission, it will review the notification. If the notification is incomplete despite a subsequent request for further information, the Commission shall adopt a decision requesting that the contracting authority reject the tender (Art. 29 (4) FSR).

If the notification is complete, the Commission will review its content. This review consists of the preliminary review and, if required, the in-depth investigation. Assuming that a complete notification has been submitted, the Commission has to observe certain deadlines – in the case of the preliminary review, between 20 and 30 days (Art. 30(2) FSR). The Commission has up to 110 days to issue a decision in the event of an in-depth investigation (Art. 30(5) FSR).

The in-depth investigation can lead to – as in the case of merger control – a decision with commitments requiring the tenderer to remedy the distortion on the internal market. However, it may also lead to a “decision to prohibit the award of the contract”. Such a decision forces the contracting authority to reject the tender of the tenderer in question.

This poses certain challenges for contracting authorities who may have such companies receiving foreign subsidies as tenderers in their procurement procedures. These include not only how to handle their obligations under the FSR, but also the considerable delays to procurement procedures caused by such tenderers due to the corresponding notification obligations and review by the Commission. In this context, Art. 32(1) FSR makes certain concessions to contracting authorities and their time constraints by allowing all procedural steps in the procurement procedure to continue with the exception of the award of the contract. However, it is already foreseeable that expiring binding periods or changing calculation bases during the Commission’s review will force contracting authorities to use as many of the options provided by public procurement law as possible to prevent their procedures from failing. The ideal outcome for contracting authorities would be that another tenderer, who is not subject to notification due to the receipt of foreign subsidies, ultimately submits the most economical bid. Then the whole process of notification, review and expiry of deadlines with the Commission can be avoided.

## IV. “Ex officio” reviews by the Commission (Art. 9 et seq. FSR)

As described above, Commission reviews are mainly initiated by notifications in the context of concentration control or by contracting authorities during public procurement procedures. The Commission is also entitled to initiate “ex officio” reviews. It may on its own initiative examine information “from any source” regarding alleged foreign subsidies distorting the internal market. This is no different from the examination of alleged unlawful aid on the basis of information “from whatever source” (see Art. 12 of Regulation (EU) 2015/1589[3]). It is also already possible to predict which source of information will play the biggest role in practice: companies trying to prevent concentrations involving competitors receiving foreign subsidies. The situation is different for public procurement procedures, as the Commission’s ex officio review is limited to contracts that have already been awarded, and Art. 9 (2) FSR also stipulates that such reviews may not result in the cancellation of the decision awarding a contract or in a termination of a contract. The critical question for competitors is then likely to be whether they discover during the procurement procedure that tenderers who have received foreign subsidies are involved and whether the contracting authority in question is handling this correctly. If this is not the case, they should be able to seek recourse via the Public Procurement Tribunal. This is because the rules to prevent contract awards being unduly influenced by foreign subsidies are not only intended to protect the internal market in general, but are also likely to be classified as bidder-protective under German law (Section 160 (2) of the German Act against Restraints on Competition)), which allows tenderers to file an

[3] Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union, Official Journal of the European Union L 248, 24 September 2015.

application to the Public Procurement Tribunal if these rules are violated.

### V. Procedure

As described above, the FSR consists of substantive regulations that define the application, obligations and requirements for approvals, refusals and sanctions. In addition, the new regulation contains procedural rules determining the interaction between the undertakings concerned and the Commission and, in the case of public procurement procedures, between the contracting authorities, the tenderers concerned and the Commission. These rules concern, for example

- requirements for the transmission of information to the Commission (Art. 3 et seq. of the Implementing Regulation) including the use of forms,
- details of the Commission's investigation procedures (Art. 8 et seq. of the Implementing Regulation),
- time limits and procedures for commitments (Art. 13 et seq. of the Implementing Regulation),
- the handling and protection of information as well as file access (Art. 18 et seq. of the Implementing Regulation) and
- (general) rules on time limits and the handling of documents (Art. 21 et seq. of the Implementing Regulation).

### VI. Conclusion

The FSR protects the European Single Market and competition from the effects of state subsidies from non-EU countries. This protection was long overdue.

In the case of companies that have received foreign subsidies, however, this also means that the FSR now applies in addition to existing antitrust and public procurement law. It is unlikely that anyone will have any concerns about the content of the regulation. Those who are used to dealing with antitrust and/or public procurement law are well positioned. Anyone who is also familiar with the procedures of state aid law – especially notification and investigation procedures – will also have no trouble with all the procedural steps contained in the FSR or dealing with the Commission.

That being said, FSR checks will take up valuable time in transactions and procurement procedures. Despite all the time limits in place, the speed at which reviews actually proceed and decisions and legal certainty are achieved will depend on two factors:

- Firstly, the Commission must be sufficiently staffed to even have the capacity to process these reviews quickly. The length of current notification procedures in the area of state aid and the strain on the Commission in its core field of competition law raise justified doubts as to whether this will work.

- Secondly, companies involved in a concentration, tenderers that have received foreign subsidies or contracting authorities who find such companies are present in their tendering market should familiarise themselves with these new rules and focus on providing complete information as quickly as possible in all of the Commission's procedural steps, ideally eliminating the need for, or at least reducing the number of, follow-up questions (these are already familiar from the ("pre-)notification procedures for state aid").

Outlook: The new legal field "FSR" will continue to gain momentum after the notification obligations come into force on 12 October 2023.

- The Commission has announced an initial clarification on the concepts of internal market distortion and the balancing test for 12 July 2024.
- In addition, the Commission will publish supplementary guidelines by 12 January 2026 at the latest (Art. 46 FSR).

There will also be evolving case practice. Our advice: All public and private market players need to stay on the ball if companies from non-EU countries that maintain close links with their governments and state funds play an important and active role in their market environment within the Single Market.

**Dr Arne Gniechwitz**
Lawyer
Hamburg
arne.gniechwitz@gsk.de

**Heiko Maas**
Lawyer
Berlin
heiko.maas@gsk.de

GSK STOCKMANN



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**GSK Stockmann**
Rechtsanwälte Steuerberater Partnerschaftsgesellschaft mbB

**BERLIN**
Mohrenstrasse 42
10117 Berlin
T +49 30 203907 - 0
F +49 30 203907 - 44
berlin@gsk.de

**HEIDELBERG**
Mittermaierstrasse 31
69115 Heidelberg
T +49 6221 4566 - 0
F +49 6221 4566 - 44
heidelberg@gsk.de

**FRANKFURT/M.**
Bockenheimer Landstr. 24
60323 Frankfurt am Main
T +49 69 710003 - 0
F +49 69 710003 - 144
frankfurt@gsk.de

**MUNICH**
Karl-Scharnagl-Ring 8
80539 Munich
T +49 89 288174 - 0
F +49 89 288174 - 44
muenchen@gsk.de

**HAMBURG**
Neuer Wall 69
20354 Hamburg
T +49 40 369703-0
F +49 40 369703-44
hamburg@gsk.de

**LUXEMBOURG**
GSK Stockmann SA
44, Avenue John F. Kennedy
L - 1855 Luxembourg
T +352 271802 - 00
F +352 271802 - 11
luxembourg@gsk-lux.com

**LONDON**
GSK Stockmann International
Rechtsanwaltsgesellschaft mbH,
London branch
Queens House, 8-9 Queen Street
London EC4N 1SP
United Kingdom
T +44 20 4512687-0
london@gsk-uk.com

Registered office: Munich
Munich Local Court
HRB 281930
Managing directors:
Dr Mark Butt, Andreas Dimmling

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