THE EU'S FOREIGN SUBSIDIES REGULATION – NOTIFICATIONS & PRACTICAL CONSIDERATIONS FOR CONCENTRATION FILINGS

editorial

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The European Union's Foreign Subsidies Regulation (**FSR**), applicable since 12 July 2023, introduces a new regime aimed at combating actual and potential distortions of competition within the EU internal market caused by foreign subsidies. The FSR aims to ensure a level playing field, closing the regulatory gap between foreign subsidies (which were previously unaddressed) and subsidies granted by Member States (which are subject to EU State aid rules).

The FSR, which empowers the European Commission to investigate potential distortive foreign subsidies, distinguishes between two main categories of procedures which require an *ex ante* notification:

- **public procurement procedures**, i.e. relevant award procedures for the conclusion of a supply, works, service or concession contract;
- **concentrations**, i.e. mergers and acquisitions (M&A) operations, including the creation of a joint venture, resulting in a change of control on a lasting basis.

This newsletter focuses on the notification obligation for M&A operations.

WHAT TRIGGERS THE FSR REQUIREMENT TO NOTIFY A CONCENTRATION?

For concentrations, a notification is required under FSR (and subject to standstill) when the following cumulative thresholds are met:

- The **EU turnover** of at least one of the merging undertakings, or the target, or the joint venture, amount to **EUR 500 million** or more;

  and

- **Foreign financial contributions (FFCs)** received in the last three years by the merging undertakings, the acquirer and the target, or the undertakings creating a joint venture and the joint venture, amount to **EUR 50 million** or more.

These contributions are considered on a group-wide basis. All contributions within the last three years preceding the conclusion of the agreement, counted from the date of entitlement (not of receipt), must be included to determine if the notification threshold is met, regardless of whether all details of these contributions must be reported (see below). In most instances, the FSR procedure will run parallel to a merger procedure in the context of EU merger control – although each procedure will be handled by a different case team.

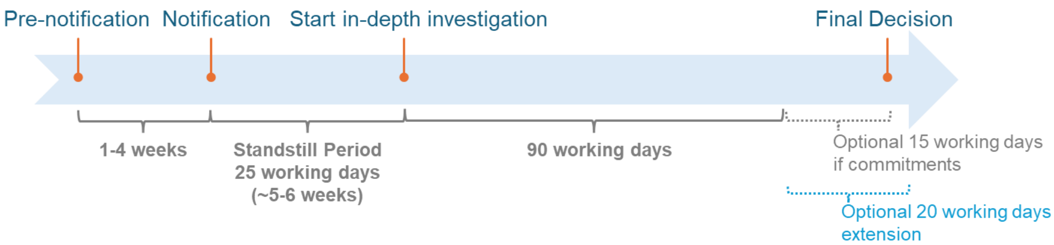
WHAT IS THE NOTIFICATION PROCESS AND SCHEDULE?

The European Commission encourages pre-notification discussions to ensure all necessary information is provided and avoid a declaration of incompleteness.

After submitting a complete notification, a **period of 25 working days** begins, during which the Commission conducts its preliminary assessment, and during which the notified concentration cannot be implemented.

For transactions that do not trigger specific issues, the expected schedule of clearance should approximately be in the range of 5 to 9 weeks, depending on the length of the pre-notification stage (see timeline below). Typically, the Commission clears the transaction by allowing the standstill period to expire without taking any action. The expected timeline is as follows:

For more problematic transactions giving rise to an in-depth investigation, the time required until a decision is issued can be up to 7 months[1]. After opening an in-depth investigation, the Commission has 90 working days to reach a decision, which can be extended by 15 working days if commitments are offered by the notifier. Additionally, the investigation period can be further extended (up to 20 working days) either upon request from the notifier, or by the Commission with the notifier's agreement. Moreover, the Commission has the power to suspend the procedure indefinitely ("stop the clock") if the notifier fails to deliver the complete information required. The expected timeline (without suspension) is as follows:



Diverging Merger and FSR timelines — The timelines for Phase 1 (25 days) and Phase 2 (90 days) investigations in merger control overlap in principle with the timeline of an FSR investigation. However, this does not necessarily mean that both procedures will progress at the same speed. A parallel track would depend on the simultaneous filing of both the merger and FSR notifications, which may be impractical and, in any case, unnecessary:

- Depending on the transaction, either procedures may raise specific questions and require a more thorough preparation and/or assessment.
- In complex merger cases, a prolonged pre-filing phase may be required, unlike for the FSR process.
- Even if filed simultaneously, the timelines for the reviews may diverge. For instance, if the case team clears the transaction in Phase 1 under merger control, it does not preclude the FSR case team from initiating an in-depth investigation.
- Where the Commission "stops the clock", under either the merger control or the FSR procedure, the timelines will further diverge.

In general, parties can and should expect divergences in the timeline between the merger control and FSR procedures as a baseline scenario. Given such a risk of divergences, parties should anticipate and prepare accordingly by determining which procedure is most likely to raise concerns or take longer and factoring this in transaction documentation.

[1] As of now, there has only been one FSR in-depth investigation (pending).

WHAT INFORMATION MUST BE NOTIFIED?

The notification form for a concentration must include the following information:

- **Basic information**: Description of the concentration, parties involved, type of concentration, rationale behind the concentration, and domains of activity of the parties;
- **Details on the concentration**: Structure of ownership and control, implementation of the concentration, target valuation, and sources of financing;
- Details on the **foreign financial contributions received** (see below on 'How to report foreign financial contributions?');
- **Impact on the internal market** : explaining whether (and how) the financial contribution may improve the competitive position in the internal market of the parties to the concentration;
- Information may also be provided to demonstrate possible positive effects on the development of the relevant subsidised economic activity on the internal market.

Addressing data collection challenges — Experience shows that companies may struggle to gather within a short timeframe up-to-date information concerning FFCs received. This difficulty often arises because such information is not typically maintained at the parent company level, especially when it must be collected from subsidiaries or joint ventures outside the EU.

To avoid difficulties during a projected transaction, **it is recommended to set up internal policies to ensure that information on FFCs is consistently collected and reported to the parent company**, with appropriate granularity (country, type and purpose of the of FFC, amount, date on which the FFC was granted, etc.). Records should be kept up to date.

HOW TO REPORT FOREIGN FINANCIAL CONTRIBUTIONS?

Broad scope of FFC reporting — The concept of FFC is very broad – it includes various financial contributions that can be granted through either public or private entities, provided they can be can be attributed to the third country. Companies should therefore be wary of gathering inaccurate information, which may in turn affect both the calculation of the threshold as well as the accuracy of the notification form.

To ensure that FSR thresholds are accurately calculated and all relevant FFCs are accounted for, it is recommended to develop appropriate guidelines (at Group level) to correctly identify and report FFCs.

Notification contents — The notification should include:

- **Details of the "most distortive" FFCs received of EUR 1 million or more**, including qualification, amounts, purpose, characteristics, whether they confer a benefit (non-market terms), and whether they are specific to a group of industries or undertakings.

  FFCs most likely to distort the internal market include:

  - Support to ailing undertakings
  - Unlimited guarantees for debts/liabilities
  - Certain export financing measures
  - Aid directly facilitating a concentration
  - Aid unduly enabling an unduly advantageous tender

  FFCs not exceeding EUR 4 million over three years are generally unlikely to be considered distortive.

- **An overview of other FFCs received of EUR 1 million or more**, grouped per country and type of contribution, and only for countries where **aggregate contributions in the preceding three years are EUR 45 million or more**.

  This overview includes the purpose of each FFC and the granting entities, along with the quantification in ranges of estimated aggregate FFCs from each third country in the preceding three years.

EXCEPTIONS AND DEROGATIONS

Notifiers are to make **a full and accurate disclosure** to the European Commission of the relevant facts for taking a decision on the notified concentration; but certain information may be omitted from the notification form.

This concerns in particular information that is not reasonably available to the parties or information that is not necessary for the Commission's examination of the case. In such cases, a waiver request should be submitted to the Commission and discussed with the case team in the course of pre-notification.

In addition, the notification form does not have to include information on:

- Deferrals of tax payments or social security contributions, tax amnesties which are generally applicable;
- Tax relief for double-taxation;
- Financial contributions granted to other investment funds managed by the same management company, provided they are AIFMD-regulated (or equivalent) and there is no commonality of investors across the funds;

- Arm's length provision/purchase of goods/services (except financial services) at market conditions, within the normal course of business;
- Contributions below an individual EUR 1 million amount.

Although such information may be omitted from the form, companies should still ensure that the collection of information is comprehensive, in case the Commission requests additional information in the course of the prenotification.

Fund exemption — Although there is an exemption for FFCs granted to other investment funds or their portfolio companies managed by the same AIFM, complexities remain for fund managers' compliance with FSR. In particular, this exemption is conditional on the majority of investors being different between the funds, which may not always be easily determined, especially with indirect investments through feeder vehicles. The FSR regime may also require data collection across other funds and portfolio companies. Therefore, it is advisable for investment funds and managers to pay particular attention to FSR compliance, and to establish protocols so as to ensure the relevant information is promptly reported and avoid delays during filing.

WHAT ARE THE RISKS AND SANCTIONS IN CASE OF NON-COMPLIANCE?

Failure to comply with the notification obligation or the standstill can result in sanctions of up to 10% of the aggregate turnover of the undertaking in the preceding financial year.

Incorrect or misleading information can result in fines of up to 1% of aggregate turnover and periodic penalty payments.

Alongside antitrust notification obligations and those related to the control of foreign investments, the control of M&A operations established by the FSR is a new constraint that foreign investors must now fully understand and take into consideration.

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