

Alert | Antitrust Litigation & Competition Regulation



May 2021

The European Commission's Proposal for Regulating Foreign Subsidies Control

1. Introduction

On 5 May 2021, the European Commission (the Commission) **proposed a regulation** to tackle foreign subsidies causing distortions in the European Union's internal market (the Proposal).

The Commission is concerned that subsidies granted by non-EU countries may cause distortions in the internal market and undermine the level playing field within the EU, especially when they are used to finance participation in public procurement tenders or acquisitions of undertakings. According to the Commission, whereas public support granted by EU Member States is subject to State aid rules, the current competition, trade, and public procurement rules do not address distortions caused by foreign subsidies. Therefore, undertakings benefitting from third-party subsidies enjoy a competitive advantage over those that cannot receive the same.

To address this regulatory gap, following a public consultation launched in June 2020,¹ the Commission has proposed the adoption of a three-tiered investigative tool consisting of the following components:

- a general “*ex officio*” power for the Commission to review any market situation;

¹ *White paper on levelling the playing field as regards foreign subsidies* (COM(2020) 253 final).

- a notification-based tool for concentrations exceeding certain thresholds;
- a notification-based tool for bids in public procurement whose value exceeds EUR 250 million.

If adopted, the Proposal would significantly increase the regulatory burden on companies backed by non-EU States that are active in the EU internal market.

As to M&A transactions, a foreign-State-backed undertaking will have to assess whether a given deal is subject to notification under various sets of rules (i.e., under the proposed regime, EU, and national merger control rules and national Foreign Direct Investment control procedures) and, if necessary, engage in multiple review procedures before different authorities.

Moreover, as better explained below, the introduction of a foreign subsidy control regime might impact the duration of public procurement procedures and ultimately, in order to prevent delays, induce contracting authorities to award contracts to companies that did not receive foreign financial contributions.

2. General provisions

2.1 The notion of “foreign subsidy”

The definition of “foreign subsidy” closely reflects the notion of “subsidy” provided under the World Trade Organization’s Subsidy and Countervailing Measures Agreement as well as the notion of State aid under Article 107 TFEU (Treaty on the Functioning of the European Union).

Under the Proposal, a foreign subsidy is defined as a financial contribution granted by a third party, which contribution confers a benefit to an undertaking engaging in an economic activity in the internal market and which is limited, in law or in fact, to an individual undertaking or industry or to several undertakings or industries.

Similarly to State aid rules, the notion of “financial contribution” is very broad in that it encompasses the transfer of funds or liabilities in any form (e.g., capital injections, loans, guarantees, fiscal incentives), the foregoing of revenue that would otherwise have been due (e.g., tax exemptions or deductions), and the provision or purchase of goods or services.²

Financial contributions fall within the Proposal’s scope both if they are provided by the central government or governmental authorities and if they are granted by public or private entities whose conduct can be attributed to the third country, taking into account, among other things, the characteristics of the entity and the role of the foreign government in the economy of the state where the recipient is active.

2.2 The notion of “distortions on the internal market”

A foreign subsidy is deemed to cause a distortion on the internal market if it “is liable to improve the competitive position of the recipient in the internal market and where, in doing so, it actually or potentially negatively affects competition on the internal market.” The existence of the distortion is assessed on the basis of a set of indicators, which include the amount and nature of the subsidy, the

² Therefore, export subsidies also are covered. As stressed in Recital 12 of the proposal “*subsidies in the form of export financing may be a cause of particular concern because of their distortive effects. This is not the case if such financing is provided in line with the OECD Arrangement on officially supported export credit*”.

conditions attached to the subsidy, and the specific circumstances surrounding the undertaking and markets concerned.

The Proposal provides for a sort of *de minimis* exemption setting forth that subsidies whose amount is below EUR 5 million over three consecutive fiscal years are unlikely to distort the internal market.

Certain categories of subsidies are deemed “most likely to distort the internal market”; thus, it appears that a detailed evaluation is not required for this category. Subsidies “at risk” include public support to ailing undertakings (unless a credible restructuring plan exists), unlimited guarantees, subsidies directly aimed at supporting a concentration or a participation to a tender.

The Commission is required to balance the negative effects on the internal market of a foreign subsidy with the positive ones on the development of the relevant activity. The same balancing exercise must be carried out when deciding whether to impose redressive measures.

The above-mentioned provisions are familiar to State aid practitioners. However, the Proposal lacks details on how the Commission should carry out the balancing exercise.

In light of the principle of non-discrimination, EU companies backed by third-party countries should receive the same treatment as companies benefitting from the public support of EU Member States. Therefore, the analysis of foreign subsidy ought to be based on the same criteria and standards applicable to the compatibility assessment of measures falling within the notion of aid. In other words, it is arguable that a foreign subsidy having structure and effects analogous to a measure deemed compatible aid should not be qualified as distortive.

In any case, to avoid uncertainty, the Commission should issue clear guidance on the relevant criteria for the evaluation.

2.3 Commitments and redressive measures

The Commission can impose redressive measures to remedy distortions to the internal market. Additionally, the undertaking concerned may offer commitments to remedy the distortion or to repay the subsidy to the third-party grantor, applying an appropriate interest rate.

A broad range of measures is available for the Commission to remedy the distortion. For instance, potential commitments or redressive measures include access obligations, reduction of capacity or market presence, divestments, and dissolution of a concentration.

These categories of remedies generally reflect those imposed by the Commission in the context of antitrust and merger investigations.

3. The three-tiered investigation tool

3.1 The general “*ex officio*” review of foreign subsidies

The Proposal confers to the Commission extensive powers to investigate any distortive foreign subsidies, including concentrations and public procurement bids falling below the relevant thresholds. The Commission may initiate an investigation *ex officio*, e.g., following an examination of information from

any source. It appears that the Commission will not be bound to consider all complaints received, contrary to what happens in the field of State aid.³

The Proposal also contemplates the opening of a market inquiry on an entire sector if there is a reasonable suspicion that subsidies to that sector distort the internal market. Information obtained during the sector inquiry may be used against individual undertakings in investigations under the framework of the Proposal.

Under the Proposal, the Commission is entitled to exercise investigative powers similar to those conferred by EU competition and State aid law rules. Specifically, the Commission may seek all necessary information either by requesting it or by conducting inspections on company premises inside and outside the EU.⁴ Given the voluminous case law on the boundaries to the authority's investigative powers, *mutatis mutandis* will likely apply to such inquiries and inspections of non-EU undertakings.

Interestingly, if a foreign State or undertaking fails to cooperate, the Commission may render a decision based on the facts available. In addition, fines may be imposed on the undertaking concerned if it provides incorrect, incomplete, or misleading information or refuses to submit to inspections.⁵

Following a preliminary review, the Commission may either initiate an in-depth investigation or close the review process and inform the undertaking concerned. Under the Proposal, the Commission is also entitled to impose interim measures if there is a serious risk of substantial and irreparable damage to competition on the internal market.

As mentioned above, if the Commission finds that the foreign subsidy distorts the internal market, it will be entitled to impose redressive measures or make binding commitments offered by the undertaking concerned. Such powers are subject to a limitation period of 10 years, starting on the day when a foreign subsidy is granted.

In case of an undertaking's failure to comply with the interim measures, commitments, or redressive measures, the Commission may impose fines up to 10% of the undertaking's aggregate worldwide turnover and periodic payments up to 5% of the global average daily turnover for each day of non-compliance.⁶

3.2 The notification-based tool for concentrations

Under the Proposal, the Commission must be notified of concentrations if the following conditions are met:

1. the concentration involves a change of control on a lasting basis arising out of an acquisition, merger, or establishment of a full-function joint venture. Control is defined as the "possibility to exercise a decisive influence" as set forth under Regulation (EC) n. 139/2004 (EU Merger Regulation);

³ Pursuant to Article 12(1) of Regulation (EU) 2015/1569, the Commission shall "*examine without undue delay*" any complaint submitted by any interested party in accordance with Article 24(2) of the same Regulation (i.e., any complaint providing a specific set of mandatory information).

⁴ If the inspection must be conducted in the territory of a non-EU country, the prior consent of the undertaking and the government of the country concerned is required.

⁵ Fines shall not exceed 1% of the aggregate turnover of the infringer in the preceding business year, and periodic penalties shall not exceed 5% of the average daily turnover of the undertaking concerned.

⁶ These are the same caps to fines set out under articles 23(2) and 24 of Regulation (EC) n. 1/2003.

2. the acquired undertaking, at least one of the merging undertakings, the joint venture, or one of its parent companies is established in the EU and has an aggregate EU turnover of at least EUR 500 million;
3. the undertakings concerned received from third countries an aggregate financial contribution of more than EUR 50 million in the three calendar years prior to notification.

The last threshold is met even if the contributions provided by different third countries jointly (but not individually) exceed EUR 50 million. It seems that – for jurisdictional purposes – the Commission will look at the value of the financial contribution received by the undertaking concerned, regardless of its qualification as “foreign subsidy”; only in the course of the review will it be assessed whether such contributions amount to “foreign subsidy.”

The proposal confers the Commission the power to request a prior notification of any concentration falling below the aforesaid thresholds at any time prior to its implementation if there is a suspicion that the undertaking concerned has benefitted from foreign subsidies in the three preceding years. Additionally, transactions that do not meet the thresholds may be investigated under the “*ex officio*” general tool described above.⁷

The notification procedure is similar to the one set out under the EU Merger Regulation. The regime provides for a bar on closing, meaning that transactions may not be consummated before clearance (although limited exceptions are provided for public bids). Exceptions to such suspension obligations are granted in exceptional circumstances.

The timeline is analogous to the one provided by the EU Merger Regulation. The phase 1 review has a 25-working-day duration from the date of notification; if, upon expiration of phase 1, the Commission opens an in-depth investigation, phase 2 will have a maximum duration of 90 working days (which can be extended for an additional 15 working days if commitments are offered). Said terms may be suspended if the undertakings concerned fail to submit complete information. The Commission will have the same investigative powers outlined under para. 3.1 above (e.g., conduct inspections, request information).

Following a phase 2 investigation, the Commission may issue the following decisions: (i) a no objection decision; (ii) a decision with commitments; (iii) a decision to prohibit the concentration if the subsidy distorts the internal market. If a concentration subsequently found to distort the internal market has been implemented before clearance, the Commission can order its dissolution.

The Commission may impose (a) penalties on companies providing incorrect or incomplete information (up to 1% of aggregate turnover); (b) fines up to 10% of the aggregate turnover on undertakings that fail to inform the Commission of a notifiable concentration or that implemented the same before clearance.

The interactions between such tool and the current merger control rules are not clear yet. For instance, it is not explicit whether a transaction that is notifiable under both regimes will be reviewed by the same case team and will be notified by means of a single form containing information required for both reviews (this would be a sensible solution to avoid delays and duplication of activities).

The new tool would apply to foreign financial contributions granted in the three years prior to the date of the Proposal’s application; however, those concentrations for which, before the date of the Proposal’s

⁷ Conversely, the Proposal does not provide for a referral mechanism analogous to the one set forth under Article 22 of the EU Merger Regulation. This is likely because Member States’ authorities are not empowered to review foreign subsidies under the Proposal.

application, the agreement was concluded, the public bid was announced, or a controlling interest was acquired are not included.

If the Proposal is adopted, the Commission should issue some implementing measures to address the practical aspects of the new regime (such as the structure of the form) and its interplay with the EU and national merger control rules.⁸

3.3 The notification-based tool for public procurement bids

Finally, the Proposal introduces a notification-based tool applicable to public procurement procedures having an estimated value of EUR 250 million or more. Public procurement is defined by reference to other EU legislation. The Proposal would apply only to procurement procedures initiated after its effective date.

The Proposal would cover foreign financial contributions granted in the three years prior to the start of application. The Proposal does not set forth any minimum thresholds of foreign subsidy: thus, all foreign financial contributions need to be notified.

Under the Proposal, undertakings submitting a bid or requesting to participate in a tender procedure must either notify the contracting authority of all foreign financial contributions received in the three years preceding that notification or confirm in a declaration that they did not receive any foreign financial contributions in the last three years. Contracts may not be awarded to companies that fail to provide said information.

The contracting authority shall transmit the notification to the Commission, which has to review it within 60 days of receipt. The Commission may decide to open an in-depth investigation, which has to be closed no later than 200 days after it received the notification. The Commission has investigative powers analogous to those described above.

Upon completion of the investigation, the Commission may either issue a no-objection decision or impose commitments. If commitments are not offered or are insufficient to remedy the distortion, the Commission will prohibit the award of the contract. The Commission may impose fines if the undertakings concerned fail to notify or supply incorrect, incomplete, or misleading information.

In principle, the evaluation of tenders continues pending the procedure before the Commission. However, the contract may not be awarded before the expiration of the preliminary review term (60 days from the receipt of the notification). The contract shall not be awarded to the notifying undertakings unless the time limits for the completion of the review (200-day term) have expired or the Commission has decided that the subsidy does not distort the internal market.

A contract may be awarded to the notifying undertaking before expiration of the time limits or issuance of a decision only if the latter has submitted the most economically advantageous tender.

⁸ Under the Proposal, the Commission can adopt implementing acts on various matters, including the form, content, and procedural details of notifications of concentrations.

4. Key takeaways and next steps

The Proposal removes the differentiation of treatment between undertakings that can benefit from foreign subsidies and those that do not receive similar financial contributions (or only have access to public support by Member States, which support is subject to EU State aid rules).

On the other hand, the Proposal, if adopted, will significantly increase the regulatory burden on undertakings that wish to invest in the internal market and that receive support from non-EU States.

Companies involved in M&A transactions may have to simultaneously deal with multiple review procedures, since a filing might be required under EU and national merger control rules, national Foreign Direct Investment regimes and, of course, pursuant to the Proposal. The interplay between the envisaged regime and the existing procedures remains unclear; thus, guidance from the Commission will be required.

The Proposal might also impact the duration of public procurement procedures, given the need to wait for the outcome of the Commission's review. In addition, contracting authorities might be induced not to award contracts to companies under foreign subsidy investigation in order to avoid delays in the procurement procedure. This would put companies backed by third-party States in a disadvantageous position.

Finally, companies backed by non-EU countries should carefully monitor the financial contributions they receive (for instance, self-assessing whether the contributions qualify as "foreign subsidy"). Indeed, considering that the Commission will take into account financial contributions received over the preceding three years, companies receiving support today might, at a later stage, face limitations to their ability to invest in the EU. This will be a complex assessment requiring the assistance of experienced practitioners (both lawyers and economists).

The Proposal will be **open for feedback for eight weeks**. The European Parliament and the Council will discuss the Proposal within the framework of ordinary legislative procedure.

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