

The European Commission published last week its draft [Regulation](#) on distortive foreign subsidies. The Regulation largely follows the recommendations of its June 2020 [White Paper](#).

The Regulation, once adopted, will subject some companies that have received subsidies to new requirements including an obligation to notify the European Commission before they acquire a target that is active in the EU, and an obligation to disclose that they have received a subsidy when they participate in EU tenders. The proposed new regime will, however, rely on established EU concepts and enforcement powers well known to EU competition/antitrust practitioners.

This client alert provides a brief description of, and some practical thoughts in relation to, this likely soon-to-be-adopted Regulation.

Notion of a “Distortive Foreign Subsidy”

- A foreign subsidy is defined as “a financial contribution which 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.”¹ The term “economic activity” has been defined in previous decisions as “any activity consisting in offering goods and services on a market.”
- The notion of foreign subsidy will cover **financial** contributions granted indifferently by foreign public and private entities² of different forms, including:
 - The transfer of funds or liabilities³
 - The foregoing of revenue that is otherwise due
 - The provision of goods or services, or the purchase of goods and services
- As regards the notion of “distortion”, the Regulation distinguishes between:
 - **Per se problematic** subsidies, including subsidies to firms in difficulty, unlimited guarantees and subsidies that directly facilitate a concentration or enable an advantageous tender.⁴

- **Unproblematic** subsidies, the amount of which has not exceeded €5 million in the last three fiscal years.⁵
- Subsidies requiring a **case-by-case analysis** to demonstrate that it is “liable to [unduly] improve the competitive condition of the undertakings concerned on the internal market” based on an assessment of the following indicators: amount, nature, purpose and conditions of the subsidy, as well as economic conditions of the market concerned.⁶
- Note that any finding of a “distortive effect” will be subject to a balancing test between “the negative effects of a foreign subsidy in terms of distortion on the internal market with positive effects on the development of the relevant economic activity.”⁷ Such positive effects could include, for example, environmental considerations.⁸
- The Regulation does not target any particular:
 - **Sector** (although the European Commission does refer to the semiconductor, aluminium and steel sectors as particularly “affected by foreign subsidies”).⁹
 - **Country**, as it will apply equally to subsidies granted by all non-EU countries that have a distortive effect on the Single Market. That said, in its Impact Assessment Report, the European Commission has identified China as the largest provider of subsidies among the EU’s five main trading partners.¹⁰

In million Euros	2017	2018
China	380,132.7	520,012.9
USA	14,932.8	17,008.4
UK	919.7	888.1
Russia	3,959.52	3,803.94
Switzerland	515.0	697.4

- The receipt by a foreign government of a subsidy meeting the above criteria could either make the recipients subject to one or both requirements listed below and/or trigger an *ex officio* investigation by the European Commission. Note that these requirements and proceedings complement (but do not replace) EU rules and proceedings on antitrust, merger control, state aid and public procurement, as well as WTO rules on subsidies.

1 Article 2(1) of the Draft Regulation.

2 Provided the actions of these private entities can be attributed to a third country.

3 For example, capital injections, grants, loans, loan guarantees, fiscal incentives, setting off of operating losses, compensation for financial burdens imposed by public authorities, debt forgiveness, debt to equity swaps or rescheduling.

4 Article 4.

5 Article 3(2).

6 Article 3(1).

7 Article 5(1).

8 See p58 of the Impact Assessment Report.

9 Impact Assessment Report, pp90-94.

10 Impact Assessment Report, p27.

New Requirements for Foreign Subsidy Beneficiaries

- The Regulation would introduce two new (additional) requirements:
 - **Mandatory pre-completion filing** to the European Commission for transactions meeting the following conditions:
 - Qualify as “concentration” within, broadly speaking, the meaning of the EU Merger Regulation (i.e. merger, acquisition of sole or joint control and/or JV creation)
 - Meet the following thresholds: (1) the target’s EU revenue exceeds €500 million, and (2) the buyer(s) received a foreign subsidy above €50 million in the last three years
 - By way of illustration, the European Commission described the acquisitions of Pirelli by ChemChina in 2018 and of Vossloh Locomotives by China-based CRRC as acquisitions distorted by foreign subsidies¹¹

The waiting periods essentially replicate EU merger control,¹² the idea behind this being that companies will notify the merger and the foreign subsidy at the same time. This raises the question whether indeed a separate procedure is required or whether this requirement should not be simply included as a new section in the EU filing forms (the Form CO and the Short Form CO).

- **Mandatory pre-bid disclosure to the Contracting Authority** of any subsidy for any public procurement above €250 million.

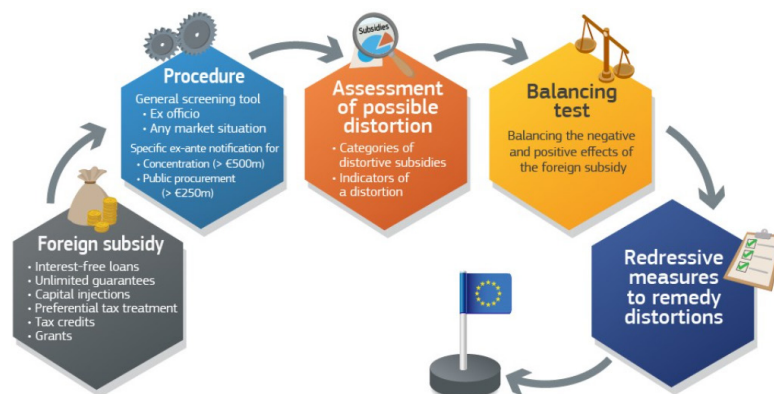
The Contracting Authority will then transfer the disclosure notification to the European Commission, which will have to take a final decision no later than 200 days after receiving the notification (safe exceptions). Note that pending the European Commission’s review, the evaluation of tenders may continue, but the contract may, in principle, not be awarded to the notifying party.

Ex Officio Review and Market Investigation

- In addition to the above requirements, the Regulation will introduce:
 - An *ex officio* review mechanism to investigate any foreign subsidy likely to distort the internal market. The European Commission can rely on “any source” that opens the possibility of investigations triggered by complaint of third parties.¹³ In the press release accompanying the proposal, the European Commission explains that this power could be used to investigate “greenfield investments or concentrations and procurements below the thresholds”
 - A general market investigation tool, which will enable the European Commission to investigate a particular sector, a type of economic activity and/or the use of certain subsidy instruments.¹⁴

Classic Enforcement Powers

- The Regulation provides for a number of classic investigative and disclosure powers:
 - **Information requests.**¹⁵
 - **Dawn raids.**¹⁶ Inspections outside of the EU are limited to cases where the companies and the government of the third country agree (which seems difficult to imagine happening in practice other than in exceptional circumstances).
 - **Interim measures.**¹⁷ It remains to be seen, however, how the European Commission uses the instrument, given it has been sparsely used by the European Commission in antitrust/competition matters.
 - **Fines** for not complying with any of the investigative and/or discovery measures (para 9) and requirements (para 7) listed above. In particular, Article 25(3) provides for “gun jumping” fines, i.e. fines for implementing a concentration prior to obtaining the approval of the European Commission on the foreign subsidy aspects of that transaction.¹⁸



Source: The European Commission

¹¹ Impact Assessment Report, pp12-14.

¹² See Article 23. The regime seems to include a “pre-notification” phase, as the waiting periods will start only once the European Commission receives the “complete” notification. The waiting periods are then as follows: 25 working days for the preliminary review, prolonged by 90 working days if the European Commission initiates an “in-depth” investigation (extendable by 15 working days if the parties offer commitment to remedy the distortion of the internal market). The Regulation also provides for exemptions (Article 23(2)), derogations (Article 23(3)) and interruptive measures (Article 23(4)).

¹³ Article 7.

¹⁴ Article 34.

¹⁵ Article 11.

¹⁶ Articles 12 and 13.

¹⁷ Article 10.

¹⁸ These fines can be up to 10% of the company’s global turnover.

- If a market distortion is found and no commitments are offered or available to address such distortion, the European Commission has a range of redressive measures, including structural or behavioural measures:
 - Offering access under fair and non-discriminatory (FRAND) conditions to an infrastructure that was acquired or supported by the distortive foreign subsidies
 - Reducing capacity or market presence
 - Refraining from certain investments
 - Licensing on FRAND terms of assets acquired or developed with the help of foreign subsidies
 - Publication of results of research and development
 - Divestment of certain assets
 - Requiring the undertakings concerned to dissolve the concentration
 - Repayment of the foreign subsidy, including an appropriate interest rate
- These measures may be accompanied with reporting and transparency requirements to be defined.

Retroactive Aspects

- The Regulation will apply to foreign subsidies granted prior to its entry into force:
 - 10 years before its entry into force for *ex officio* review¹⁹
 - Three years before its entry into force for merger and public procedures notification²⁰
- Any adverse decision adopted by the European Commission on that retroactive basis will, no doubt, be hardly fought before the European courts. However, these provisions provide a strong incentive to beneficiaries of foreign subsidies to assess the impact on any recent subsidies they received.

¹⁹ Article 47(1).

²⁰ Article 47(2).

Next Steps

The European Parliament and the Council will now discuss the European Commission's proposal in an ordinary legislative procedure with a view to adopting a final text of the Regulation. The Regulation will be directly applicable across the EU once the European Commission adopts all relevant implementing acts – including the form, content and procedural details of all notification forms.

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