

Insights

FOREIGN SUBSIDIES UNDER THE EUROPEAN COMMISSION'S MICROSCOPE

STATE SUBSIDISED M&A BUYERS, PUBLIC PROCUREMENT BIDDERS TO BE REGULATED

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SUMMARY

The European Commission's June 2020 White Paper outlined its initial plans for a subsidies regime. The Commission has now developed these plans in its proposals for a new regulation. If approved, the regulation would establish three broad tools through which the Commission could regulate foreign subsidies within the EU - including the mandatory notification of certain M&A transactions and public procurement bids.

The debate surrounding companies active in the EU that receive foreign state subsidies has been unfolding for some time. Back in October 2020, [we highlighted](#) that the European Commission was planning to establish a new regulatory regime to control the impact of subsidies given by non-EU governments to companies doing business in Europe.

On 5 May 2021, the Commission took the next step towards making these plans a reality by publishing its proposals for a new regulation to regulate distortions to the internal market that could be caused by foreign subsidies. Speaking at the press conference announcing the long-anticipated foreign subsidies legislation, European Commissioner Margrethe Vestager stressed: "we want every company that operates in Europe no matter where it comes from to respect our house rules." Those "house rules" include the EU's State aid regime, which does not regulate subsidies given by non-EU states to companies active in the EU. This proposal would give the EU significant new watchdog powers to scrutinize, on foreign subsidies grounds, M&A deals, public procurement bids and the activities of companies receiving foreign aid active in the EU.

Data from the Commission's impact assessment that supported this proposal emphasises how much foreign investment enters the EU, and the number of subsidies that could have played a part in some of this investment:

- Foreign direct investments (FDI) within the EU totalled in excess of €7 trillion in 2019, approximately 25% of global FDI that year.
- There were 3,254 foreign acquisitions of at least 30% of the equity of European companies in 2019.
- The EU's five biggest trading partners (USA, China, Russia, UK and Switzerland) are known to have implemented 1,724 subsidy measures.

The proposed regulation would furnish the Commission with three broad tools to tackle third country subsidies that it considers harmful:

- a mandatory notification regime for acquisitions where the purchaser in an M&A transaction has received financial support from a non-EU state;
- a separate notification regime relating to bids in public procurement which include a financial contribution from a foreign government; and
- new powers to investigate any company that has received financial aid from a non-EU state that amounts to more than either €200,000 or €5 million over the previous three years, and potentially force it to sell off assets (the Commission has yet to decide which of these thresholds it would like to pursue).

These attempts to vet FDI on the basis of subsidies received from foreign governments makes the Commission an outlier amongst major economic powerhouses. The American Chamber of Commerce to the EU, which is generally supportive of the proposal and the Commission's efforts, has already commented that the proposed legislation must be balanced and proportionate rather than creating additional compliance requirements for those companies already complying - as this could deter legitimate foreign investment in Europe.

Evidently, the Commission aims to bolster EU companies against their non-EU competitors who benefit from the type of government assistance that is precluded under the EU's state aid rules. Its definition of foreign subsidies is far-reaching, capturing zero-interest loans, unlimited state guarantees, zero-tax agreements and dedicated state funding. Will this definition and the Commission's approach against foreign subsidies proceed in its current form? If the proposed regulation remains as is, companies will have to negotiate an additional layer of regulation for their European activities.

Two new notification regimes – M&A and public procurement

In June 2020, the Commission outlined its early plans for a subsidies regime in its White Paper. This included proposals to control the use of foreign subsidies to facilitate acquisitions of EU-based targets through a mandatory notification regime. The latest proposals are a development of the

Commission's intention to scrutinise deals involving foreign subsidies. The key aspects of the proposed regime are:

- M&A: acquisitions would have to be notified to the Commission where an EU target has EU revenues of at least €500 million, and the purchaser has received at least €50 million in subsidies from a non-EU state.
- Public procurement: for public procurement bids, the requirement to notify would be triggered where the estimated value of the procurement is at least €250 million.

In addition, the Commission would have power to "call-in" deals and bids below these thresholds when it suspects that a foreign subsidy might be involved.

Transactions that satisfy the notification thresholds would have to be notified before they are closed, and closing must be suspended until clearance is received from the Commission. Parties that fail to notify or that provide incorrect information could receive substantial fines.

The proposed notification regime is remarkably similar to the Commission's existing merger review process, with the notable - and significant - exception that the notification threshold for acquisitions does not include a global turnover threshold. Parties involved in transactions that are not notifiable to the Commission under the merger control rules could still find that they may need to submit an EU filing under this new regime.

Additional market investigation power to scrutinise foreign subsidies

Under the proposed regulation, the Commission would also have an additional power to examine foreign subsidies received by companies active within the EU. This power would be subject to a *de minimis* threshold below which foreign subsidies could not be presumed to be distortive. The Commission has proposed setting this threshold at either €200,000 or €5 million, with the lower figure reflecting the *de minimis* threshold under its state aid regime.

Where the Commission has established the existence of foreign aid that surpasses the *de minimis* threshold, it would look for "indicators" that determine whether - on balance - that subsidy has had a harmful effect. These indicators could include foreign aid that:

- covers a substantial part of a tender contract or transaction value;
- provides support to a company in financial distress;
- amounts to an export subsidy or unlimited guarantee;
- is especially large;

- is granted to a company that already enjoys a considerable market share in a sector with little competition.

The Commission's investigative powers would be similar to those it enjoys for its competition law investigations, which are substantial. They would include the ability to conduct dawn raids and issue requests for information. Fines could be imposed on companies that provide false information or otherwise fail to comply with the investigative procedure.

Once the Commission has established that a company has received distortive foreign aid, that company could be prohibited from buying an asset, forced to sell specific assets, made to repay the subsidy or required to comply with an array of behavioural measures.

What happens next?

These proposals will now wind their way through the EU's complex legislative system and we would not expect to see final legislation in force before 2023. If approved, they would be a significant addition to the Commission's arsenal for scrutinising transactions within the EU, alongside EU and national merger control and the FDI regimes. Companies active in M&A in the EU where the buyer receives state support as well as companies bidding for public procurement projects will need to consider carefully these new powers and procedures and build them into their planning and timing processes. This significant move by the EU to control subsidies provided abroad will present another regulatory hurdle for dealmakers and public contract bidders in the EU.

BCLP's Antitrust & Competition team has been engaging with the EU on these developments and monitoring the progress of these proposals. If you have any questions on the status of these proposals or how they may affect your business, or if you would like to engage with the EU during the legislative process, please don't hesitate to reach out to any member of the team.

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