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CLIENT ALERT

EU Foreign Subsidies Regulation – draft Implementing Regulation published for consultation

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On 6 February 2023 the European Commission (***EC***) launched a consultation on its draft Implementing Regulation for the EU Foreign Subsidies Regulation (***FSR***). The draft Implementing Regulation provides details on the requirements of the notification form for qualifying M&A transactions, and on practical and procedural aspects related to the application of the FSR's M&A approval regime.

The EC acknowledges that it does not wish compliance with the FSR to be overly onerous, and has attempted to ease the burden on notifying parties in respect of the financial contributions to be disclosed, as well as introducing the potential for waivers of unnecessary information. Whether this will be sufficient in practice is unclear and will likely remain so until the EC has established a track record on its enforcement of the new rules.

Responses to the consultation are due by 6 March 2023.

Background

The FSR entered into force on 12 January 2023. Its aim is to close a perceived 'regulatory gap', whereby subsidies granted by EU Member States were subject to close scrutiny under the State aid rules while subsidies granted by non-EU

Member States went largely unchecked.[1] Amongst other things, the FSR introduced a new regime to apply from 12 October 2023, which will require prior EC approval for M&A transactions signed on or after 12 July 2023 if:

(1) either the target of an acquisition, at least one of the parties to a merger, or a joint venture company (as applicable) generates EU turnover of at least **€500 million**; and

(2) the parties in aggregate (i.e. any acquirer of control and the target; the merging parties; or the JV parents plus the JV itself) have received combined "financial contributions" of more than **€50 million** which qualify as "foreign subsidies" in the last three calendar years prior to the transaction.

Transactions will be approved if the foreign subsidy does not "negatively affect competition in the internal market". The FSR expressly identifies a foreign subsidy that directly "facilitates" a transaction as being one of those "most likely" to cause distortion.

If the EC considers that a financial contribution does distort the internal market, it is able to require far-reaching conditions (such as divestments, behavioural remedies or a repayment of the subsidy) or even to prohibit the transaction entirely in order to restore a "level playing field".

Purpose of the draft Implementing Regulation

The draft Implementing Regulation sets out the procedure for the notification and review of qualifying transactions under the FSR. In particular, the draft Implementing Regulation provides detailed rules on points such as:

(i) the information required by the notification form and the procedures for making the notification;

(ii) procedures for the submission of commitments;

(iii) deadlines and rules for the calculation of time limits;

(iv) other procedural aspects of the EC's investigation of suspected distortive foreign subsidies, such as the notifying parties' rights of defence and the procedure for access to the EC's case file; and

(v) the EC's investigatory powers when it investigates subsidies on its own initiative (i.e. in the absence of a notification).

An attempt to reduce the information burden

[1] See Willkie's client alert dated 6 December 2022, here.

The notification obligation in the FSR arises merely as a result of the existence of sufficient levels of "financial contribution", irrespective of whether or not the contribution confers a selective benefit on the recipient (in contrast with the "selective advantage" principle under EU State aid rules).

The FSR also applies a broad approach to financial contributions which might be defined as foreign subsidies (covering an extremely wide range of financial assistance/investments, from state-owned enterprises and sovereign wealth funds but also very possibly entities such as public pension schemes). This has raised concerns that the FSR would require notification of a large number of situations which are usually not distortive of competition, creating an unnecessary regulatory burden on benign transactions.

That said, the FSR itself acknowledges that compliance with the FSR should not become overly burdensome for businesses. And the draft Implementing Regulation introduces several measures intended to reduce the information burden on notifying parties by avoiding the reporting of less relevant financial contributions, including through the introduction of minimum thresholds, waiver requests and pre-notification discussions.

Minimum thresholds

First, the draft notification form annexed to the draft Implementing Regulation establishes minimum thresholds below which financial contributions do not need to be disclosed. Parties to an M&A transaction need only include details of contributions in their notification if:

(i) the individual amount of the contribution equals or exceeds **€200,000**; and

(ii) the total amount of contributions per third country and per year is **€4 million or more**.

While this may lead to fewer disclosures in a notification form, the nature of these combined thresholds means that internally monitoring all the financial contributions received may still be a complex exercise for businesses – and in particular for financial investors and asset managers, as the position will need to be assessed across all their funds and portfolio companies.

Waiver for the provision of information

Second, notifying parties may also request that the EC waives the obligation to provide certain information which is not necessary for the EC to carry out a substantive assessment of the notification, or where the information is not reasonably available to the notifying parties (e.g. because information on a target is not available in the context of a contested bid).

How useful this will be in practice will depend on how readily the EC will grant such waivers. However, in theory it would allow the EC to materially reduce the notification burden on certain categories of party (e.g. financial investors and asset managers), in particular as it becomes more experienced in applying the new regime.

Pre-notification discussions

Third, similar to the EC's existing merger control process, the EC encourages parties to engage in pre-notification discussions on the basis of a draft notification form. The EC expects that this pre-notification phase will greatly reduce the information burden on the notifying parties, and in practice such discussions will likely become effectively mandatory.

The fact that the waiver requests referred to above can be submitted – and presumably debated – in the context of such discussions may well increase their chances of acceptance. This opportunity for engagement with the EC prior to submitting the waiver request is therefore welcome.

That said, pre-notification discussions are a double-edged sword. The lack of formal guidance around the timing for such discussions means it is unclear how long such discussions will typically take before the formal review timetable can start. This might not be a problem if a transaction requires a parallel EC merger control filing and would be undergoing equivalent pre-notification discussions in that context as well. The spectre nonetheless remains that the FSR notification could become the last regulatory clearance, with an unclear overall timeline.

Conclusion

The draft Implementing Regulation provides helpful guidance on the requirements of the notification form for qualifying M&A transactions, and on practical and procedural aspects of the FSR's approval regime. Crucially, it appears to reflect a welcome intention to reduce the information burden on notifying parties under the new regime.

But how far these steps go in practice to achieve this goal is unclear. It is helpful for transactions with a parallel EC merger control filing that certain sections of the notification form can simply be repurposed for the FSR notification. However, the EC's introduction of thresholds for the disclosure of financial contributions will not materially reduce the compliance burden for financial investors and asset managers, who will still need to maintain a detailed record of all non-EU financial contributions received. It is also not clear to what extent the EC will be willing to use its waiver powers to relieve businesses of such obligations. Additional guidance on the circumstances in which the EC would be willing to waive information requirements would therefore be welcome.

The consultation on the draft Implementing Regulation provides interested parties with an opportunity to shape the EC's future approach to this important area of industrial policy. Responses to the consultation are due by 6 March 2023 – please get in touch with your usual Willkie contact if you would like to contribute to the debate, or if you would like to discuss ways to effectively monitor any financial contributions you may receive.

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