

e-Competitions

Antitrust Case Laws e-Bulletin

May 2021

The EU Commission issues its proposal to create wide-ranging powers to tackle non-EU subsidies which may distort competition in the Single Market

REGULATORY, EFFECT ON INTERSTATE TRADE, INVESTIGATIONS / INQUIRIES, MERGER NOTIFICATION, ALL BUSINESS SECTORS, EUROPEAN UNION, THRESHOLDS, REFORM, FOREIGN INVESTMENT, COMPETITION POLICY

EU Commission, *Proposal for a regulation of the European Parliament and of the Council on foreign subsidies distorting the internal market*, Draft regulation, COM(2021) 223 final, 5 May 2021

Alec J. Burnside | Dechert (Brussels)

Marjolein De Backer | Dechert (Brussels)

e-Competitions News Issue May 2021

On May 5 the European Commission issued its proposal to create wide-ranging powers to tackle non-European subsidies which may distort competition in Europe. The proposal introduces three different regimes:

- An ex officio investigation up to 10 years after the subsidy was received.
- A mandatory notification regime for M&A if one of the parties is established in the EU.
- A mandatory notification for companies bidding in certain public procurement procedures.

The proposal will now go into the legislative process which will no doubt spur significant debate since it reflects a growing protectionist sentiment in the EU—but may at the same time be seen as a threat to incoming foreign investment.

Key takeaways

- The proposed Regulation on foreign subsidies distorting the internal market will apply to companies doing business in the EU who have directly or indirectly benefited from any type of financial contribution from a non-European government. If the financial contribution did not exceed €5 million over a consecutive period of three years, the subsidy is presumed to be unproblematic.
- The proposal introduces three different regimes:

- **Ex officio review of foreign subsidies:** Companies doing business in the EU who have benefited from a non-European subsidy can be investigated for up to 10 years after the subsidy was received.
- **Acquisitions:** Companies who received foreign subsidies prior to making an acquisition will need to make a mandatory filing and await the outcome of the Commission's investigation before closing. Public bids and full-function joint ventures are also caught. Thresholds apply to limit the impact of this new regime: the target, the joint venture, or at least one of the acquiring undertakings must be established in the EU and generate an aggregate EU turnover of at least €500 million; and the parties to the concentration must have received an aggregate financial contribution in the three calendar years prior to the notification of more than €50 million. The Commission also has authority to request a notification of concentrations falling below these thresholds when it suspects that the parties benefited from foreign subsidies in the three prior years. The Commission must do so before the deal has closed [7].
- **Public procurement procedures:** Companies bidding in a public procurement procedure with a value of at least €250 million will have to submit a notification if the bidder received a financial contribution from a non-EU government during the last three years. If that is not the case, companies must so confirm in a declaration. Failure to submit a declaration or a notification will lead to the exclusion of the bidder from the tender procedure. In the same way as for concentrations, the Commission has the authority to request a notification in all cases where it suspects that a company has benefitted from foreign subsidies in the three years prior to the submission of the tender or request to participate in the public procurement procedure.
- The Commission will be empowered to investigate whether financial support provided by a non-EU government constitutes a foreign subsidy and distorts the EU market. The Member States will not have concurrent powers.
- The new powers do not replace but complement existing rules – at EU, national and WTO level. Notably the proposed Regulation gives the Commission the ability to extend rules on subsidies granted by EU governments to support from non-European governments, thereby giving teeth to WTO agreements.
- The proposal will now go into the legislative process, with the final text to be agreed between the Commission, European Parliament and Council of Ministers. The proposal will no doubt spur significant debate since it reflects a growing protectionist sentiment in the EU; but it may at the same time be seen as a threat to incoming foreign investment. These concerns led the Commission to significantly raise the thresholds compared to last year's White Paper, in particular for M&A activity. Nevertheless the proposal may well undergo further changes in the legislative process ahead and is unlikely to be adopted before the end of 2022.

The perceived regulatory gap

Since 2019 there has been a growing concern that the openness of the European market has left European businesses vulnerable to takeover by companies benefiting from foreign government support, and equally competition from such companies. There are international instruments, such as the WTO Agreement on Subsidies and Countervailing Measures, which address this to a certain extent, but these are seen as insufficient. The same is true of existing EU regulations or national laws on merger control, FDI screening, state aid and public procurement.

In June 2020 the Commission issued a White Paper with an analysis of the situation and proposed avenues for action. This consultation exercise has not led to any fundamental change in approach other than increasing the thresholds for the Regulation to apply, seeking to strike the right balance between fair competition versus the

openness of the European market to foreign players. Vice-President Vestager stressed during her press conference that EU Member States grant many subsidies to their national companies; but these are monitored, unlike foreign subsidies. It is this gap that the proposal addresses.

Definition of a foreign subsidy

The definition of a “foreign subsidy” incorporates many elements of EU state aid law which governs subsidies granted by Member States. EU law takes an extensive approach. In particular, a foreign subsidy is one satisfying these tests:

- any financial contribution: capital injections, loans, preferential tax treatment; or the provision of goods or services, or the purchase of goods or services, on preferential terms;
- granted by a government, governmental authorities at any level, or public or private entities whose actions can be attributed to the non-EU country;
- which confers a benefit on the recipient: this is determined on the basis of the usual practice of private investors in similar circumstances; and one limited (in law or in fact) to an individual company or industry or to a group of companies or industries (“selectivity”).

If the subsidies did not exceed €5 million over three consecutive years, they are deemed to be unproblematic. This is a higher threshold than the de minimis test applicable to European subsidies (€200 000) which was proposed in last year’s White Paper.

Distortion of the European market and balance of interests test

A foreign subsidy is deemed to distort the internal market if it is liable to improve the competitive position of the beneficiary in the European market and this has actual or potential effects on competition in the European market.

Some types of foreign subsidies are, according to the proposal, likely to distort the European market: foreign subsidies granted to ailing undertakings, unlimited guarantees for debts or liabilities, a foreign subsidy directly facilitating a concentration, or a foreign subsidy enabling a company to submit an unduly advantageous tender. All other types of subsidies will be assessed on a case-by-case basis taking into account, inter alia, the following criteria: amount of the subsidy, nature of the subsidy, situation of the company and the markets concerned (based on the White Paper, e.g. level of excess capacity, level of concentration, level of maturity), level of activity of the beneficiary in Europe, and the purpose and conditions attached to the foreign subsidy as well as its use in the European market.

The actual or potential distortion caused by the foreign subsidies will, where necessary, be balanced against positive effects on the relevant economic activity. This is narrower than the “European interest” test proposed in the White Paper which allowed broader European interests to counterbalance the distortions, i.e. the positive impact within the EU or on a public policy interest recognized by the EU such as employment, environmental protection, digital transformation, security or public order.

Three forms of control

The proposal creates three different disciplines to address the distortions caused by foreign subsidies. A given subsidy may come to be assessed more than once, e.g. if first notified as part of a concentration or procurement exercise, and then later relevant again in other circumstances.

1. **Ex officio review of foreign subsidies:** a general power to address – ex post – foreign subsidies that cause distortions in the EU. The Commission will have 10 years to intervene from the grant of the subsidy. The limitation period will be interrupted and restarted by any action taken by the Commission in relation to the foreign subsidy. The Commission expects to review 30-45 cases a year on this basis, including cases which do not fall within the thresholds for the concentrations and public procurement regimes.
2. **Concentrations:** an ex ante regime introducing a mandatory advance notification for acquirers who benefited from financial contributions from non-EU countries in the three calendar years prior to a transaction. The regime will apply to acquisitions of control in the sense of the EU Merger Regulation when (1) the target, the joint venture, or at least one of the acquiring undertakings is established in the EU and one of them generates an aggregate EU turnover of at least €500 million, and (2) the parties to the transaction received from non-European countries an aggregate financial contribution in the three calendar years prior to the notification of more than €50 million. The proposal also includes a catch-all provision which allows the Commission to request a notification of transactions not meeting these thresholds but where the Commission suspects that the parties benefited from foreign subsidies in the three years prior to the concentration. The Commission must do so prior to the completion of the transaction. If companies fail to notify, the Commission will be able to call in the transaction and will not be bound by the procedural timelines. It may impose fines on the parties of up to 10% of their aggregate turnover in the preceding business year, where they failed to notify. The Commission estimates that around 30 companies per year will be affected by the regime covering concentrations.
3. **Public procurement procedures:** an ex ante regime introducing a mandatory notification for firms participating in a public tender with a value of €250 million or more, and where the bidder benefited from foreign subsidies during the three years prior to the notification. If no such subsidies were received, the bidder must submit a declaration to that effect. Failure to submit a notification or declaration will lead to exclusion from the bidding process. In the same way as for concentrations, the Commission has the possibility to request a notification in all cases where it suspects that a company has benefitted from foreign subsidies in the three years prior to the submission of the tender or the request to participate in the public procurement procedure. Notifications of foreign subsidies will not suspend the public procurement procedures; but the contracting authority will not be allowed to award the contract to a company under investigation. If companies fail to notify, the Commission may impose fines of up to 10% of their aggregate turnover in the preceding business year.

The proposal also allows the Commission to conduct market investigations into certain sectors, economic activities or subsidy instruments if there is a particular concern with any of these. But the Regulation will apply to companies in all sectors and subsidies received from any non-European country.

Procedure

In all three cases the investigation will start with a first phase preliminary review to examine whether there is a foreign subsidy that may distort the EU market. If there is no concern at the end of the preliminary review, the Commission will close its investigation with no intervention and acquisitions or public tenders can then proceed.

If, however, there is evidence that the foreign subsidy may distort the functioning of the European market, the Commission will open an in-depth investigation. At that time the Commission will publish a notice in the Official Journal of the European Union inviting comments from third parties. It will also summarize its findings in a decision

to the parties involved. The second phase investigation will be closed by adopting corrective measures or commitments, or a no-objections decision. Parties will have been given the opportunity to comment on the Commission's concerns before a decision is taken and the Commission will be advised by a Committee composed of representatives of Member States.

As regards concentrations, the Phase 1 and Phase 2 timetable is similar to that of EU merger investigations (25 working days and 90 working days respectively which can be extended and suspended). For public procurement cases the Commission has 60 days for the phase 1 review which extends to 200 days if a phase 2 investigation is opened. The Commission will publish a non-confidential version of its phase 2 decisions.

In all cases the Commission will be able to compel companies to provide information requested from them, and will also be empowered to request information from other market participants as well as the non-EU government in question. It will also be able to carry out inspections at EU locations - as well as in non-European countries, although subject to approval from the relevant government. If companies do not provide information in a timely way, or provide incomplete, incorrect or misleading information, or do not cooperate, the Commission will be able to impose fines and periodic penalties. Despite these powers, the Commission recognizes that it may be challenging to gather the necessary information and it is therefore empowered, in the absence of cooperation, to take a decision on the basis of the available facts.

Measures to redress or prevent the distortions caused by foreign subsidies

If the in-depth investigation confirms the Commission's concerns, it will be able to impose measures to redress or prevent the distortions in the EU market, or to accept commitments from the companies involved. The proposal provides the following examples: offering fair and non-discriminatory access to an infrastructure acquired or supported by the foreign subsidies; reducing capacity or market presence; refraining from certain investments; licensing on fair, reasonable and non-discriminatory terms of assets acquired or developed with the help of foreign subsidies; publication of results of R&D; divestment of certain assets; dissolving the concentration; repaying the foreign subsidy (plus interest).

Interim measures may be adopted during the procedure, where there are indications that a foreign subsidy distorts the European market and not intervening would create a serious risk of substantial and irreparable damage to competition in the European market. These conditions are similar to those for interim measures powers under EU competition law - which have rarely been applied due to the high thresholds set in decisional practice and court judgments, although the Commission imposed interim measures on Broadcom in 2019 during an abuse of dominance investigation.

What's next?

The proposal will now be reviewed by the European Parliament and the Council of Ministers who will each issue an amended text and then seek to find a compromise together with the Commission. We would not expect such a compromise to be reached before the end of 2022 and - given the potential controversies around increasing the burden for inbound investments into the EU - the final text may undergo significant changes from the present proposal. The memorandum accompanying the proposal and the presentation by Vice President Vestager at the press conference reiterate though that the proposal has broad support from the Member States, the Council of Ministers and members of the European Parliament. Nevertheless, it would not be the first time that a Commission initiative in relation to foreign subsidies fails to proceed due to opposition by large Member States. The Commission's proposed International Procurement Instrument, for example, suggested that Europe may block

non-European companies from participating in European tenders if their home country is a state which applies discriminatory rules to foreign companies. This proposal did not proceed, according to reports, because of the opposition of at least one larger Member State.

The current proposal foresees that, once adopted, the Regulation will enter into force 20 days after its publication in the Official Journal and will apply in full six months later. The Regulation's ex officio regime would apply retroactively to foreign subsidies granted in the ten years prior to that date, while the public procurement regime would apply to subsidies granted in the three years prior to the date of application but not to public procurement procedures initiated before that date. The Regulation will not affect concentrations implemented before the date of application.

The three proposed instruments will increase the administrative burden for companies doing business in the EU. They complement the existing EU legislative framework and do not replace any existing instruments. Foreign – and European – companies benefiting from “foreign” subsidies may, in particular in the case of transactions, need to file entirely separate notifications under the EU Merger Regulation, national FDI laws, and the newly proposed “foreign” subsidies instrument. These will each address different aspects of a given transaction, be investigated by different officials, and could require rather different commitments or remedies. Questions of coordination between different procedures are unlikely to be addressed in any Implementing Regulation the Commission may adopt in relation to procedures, but at a certain stage guidelines may be needed.

[1] *Although the procedure and timelines are similar to those of the European Merger Regulation, this will be a separate notification which is also distinct from FDI filing obligations.*