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The EU Foreign Subsidies Regulation

New Filing Obligations in M&A Transactions

SUMMARY

The EU Foreign Subsidies Regulation (“FSR”) entered into force on 12 July 2023. The FSR allows the European Commission (“Commission”) to take action against potentially distortive subsidies granted by countries outside the European Union (“EU”) to companies active in the EU.

In the M&A context, the FSR establishes a pre-closing suspensory filing regime for acquisitions of “control” of targets with at least EUR 500 million in EU turnover, and where the parties to the transaction received in aggregate more than EUR 50 million in “financial contributions” from non-EU countries. The FSR also confers extensive powers on the Commission to investigate on its own initiative EU market distortion caused by non-EU subsidies in all market sectors (e.g., following a complaint).

The filing obligation applies from 12 October 2023. However, reportable transactions signed on or after 12 July 2023 which have not closed before 12 October 2023 are subject to the filing obligation.

Parties subject to the filing obligation will need to disclose information to the Commission relating to “financial contributions” they have received. Financial contributions include a very broad range of support measures provided by state bodies (or by private entities at the direction of a state) from outside the EU.

The Commission is particularly interested in financial contributions that (i) confer a benefit on their recipient (if the support measure could not have been obtained under normal market conditions) and (ii) are selective (limited in law or in fact to one company, certain companies or industries). Financial contributions that meet these tests are considered to be “subsidies” under the FSR.

Following the filing of a notification, the Commission has 25 working days to clear the transaction. If it opens an in-depth investigation, it has a further 90 working days to unconditionally clear the transaction, clear the transaction subject to commitments to alleviate the effects of the subsidy or prohibit the transaction.

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The FSR requires parties to M&A transactions to determine whether they have received non-EU subsidies that meet the filing thresholds. This is likely to be a burdensome exercise, although the FSR imposes relatively less extensive requirements on investment funds.

I. BACKGROUND

Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market (“FSR”) was adopted on 14 December 2022 to prevent distortions of competition caused by subsidies granted by countries outside the European Union (“EU”) to companies active in the EU.

The FSR (i) establishes a pre-closing suspensory filing obligation for certain M&A transactions involving parties that received financial contributions from non-EU countries above a specified threshold; (ii) confers extensive powers on the European Commission (“Commission”) to investigate and remedy distortions of competition caused by foreign subsidies in all market sectors; and (iii) establishes a filing obligation in certain public procurement contract awards. The Commission will act as a “one-stop shop” to review transactions falling within the scope of the FSR (*i.e.*, no parallel filings at EU Member State level).

On 10 July 2023, the Commission adopted Regulation (EU) 2023/1441 on detailed arrangements for the conduct of proceedings by the Commission pursuant to the Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market (“FSR Implementing Regulation”). The FSR Implementing Regulation specifies the information required in filings under the FSR and sets out procedural rules for the conduct of FSR investigations.

The FSR applies from 12 July 2023. However, the filing obligation for relevant transactions will apply only from 12 October 2023.

II. FILING OBLIGATION IN M&A TRANSACTIONS

When will filing be required?

The filing obligation applies from 12 October 2023. However, relevant transactions signed on or after 12 July 2023 which have not closed before 12 October 2023 are subject to the filing obligation. Companies meeting the relevant thresholds (set out below) will have to file an FSR notification (Form FS-CO) with the Commission.

Which transactions need to be filed?

Filing is required in transactions involving:

1. A change of “control” on a lasting basis resulting from acquisitions (acquisitions of sole or joint control), mergers,¹ or the creation of “full function” joint ventures (the same as in the EU merger control regime); and
2. The target (in an acquisition), merging party (in a merger), or full function joint venture is “established in the EU” (e.g., has a subsidiary, branch, or other stable arrangements in the EU); and
3. The following quantitative thresholds are met:
 - a. **Relevant party turnover:** the target (but not the seller), one of the merging parties, or the “full function” joint venture (as the case may be) has at least EUR 500 million of turnover in the EU; and
 - b. **Financial contributions:** the parties to the transaction received combined aggregate “financial contributions” from non-EU countries of more than EUR 50 million in the three years preceding signing of the transaction agreements (or announcement of the bid in the case of public bids).

In addition, certain transactions involving a change of control of a target, merging party, or full function joint venture established in the EU which do not meet these thresholds may be “called-in” for investigation by the Commission if it considers that the transaction involves distortive foreign subsidies.

The concept of “financial contributions”

Financial contributions include a very broad range of support measures provided by non-EU countries, including the transfer of funds, capital injections, grants, loans, guarantees, fiscal incentives, tax exemptions, debt forgiveness, granting of exclusive rights without adequate consideration, provision of goods and services to a non-EU country or the purchase of goods and services from a non-EU country (including at market prices).

The concept of “foreign subsidies”

A foreign subsidy is a financial contribution which:

1. Is provided by a non-EU country to a company active in the EU; and
2. Confers a benefit on its recipient (not obtained under market conditions); and
3. Is limited in law or in fact to one or more companies or industries: specificity/selectivity (*i.e.*, the support measure only applies to a certain company(ies)/industry(ies)).

¹ In this context “merger” means a combination of two or more entities into one entity.

Filing process, substantive test and review periods

Parties must file prior to closing and following signing or, in the case of a public bid, announcement of the bid (filing can be based on a good faith intention to conclude an agreement, e.g., MoU). A suspensory obligation applies during the review period: parties must not close the transaction prior to Commission clearance, except in public bids or series of on-market transactions in securities resulting in the acquisition of control from various sellers, provided that the acquirer (i) files an FSR notification without delay and (ii) does not exercise the voting rights attaching to the relevant securities unless the Commission has granted a derogation from this obligation.

The filing process starts with pre-notification discussions with the Commission, in which the parties prepare and, essentially negotiate, the Form FS-CO filing with the Commission. Timing of pre-notification may vary depending on the complexity of the transaction and presence of foreign subsidiaries (pre-notification will last, at a minimum, several weeks). Once the parties formally file the notification, the Commission has 25 working days to clear the transaction or to proceed to an in-depth investigation. The Commission proceeds to an in-depth investigation where it has sufficient indications of there being distortive foreign subsidies and the parties have not offered a suitable remedy.

A distortion arises when a foreign subsidy improves, or may improve, the competitive position of its recipient in the EU internal market, and it actually or potentially negatively affects competition in the EU internal market.

Under Article 5(1) of the FSR, certain foreign subsidies are presumed to be most likely to distort the EU internal market, such as subsidies granted to ailing firms, unlimited guarantees for debts and liabilities, export financing measure not in line with the OECD arrangement on officially supported export credits, and subsidies directly facilitating a relevant transaction (so-called “*Article 5 Financial Contributions*”).

The Commission has 90 working days from opening the in-depth investigation (subject to certain extensions) to adopt one of the following decisions:

1. Unconditional clearance;
2. Clearance subject to commitments (which may be the divestment of subsidised assets, repayment of foreign subsidies, changes to governance structures, assumption of reporting obligations, or refraining from pursuing certain investments in the EU); and
3. Prohibition of the transaction.

Failure to file, closing prior to obtaining clearance, circumventing or attempt to circumvent the filing obligation, and providing incorrect, incomplete or misleading information to the Commission may lead to fines and daily fixed-sum penalties.

III. INFORMATION REQUIRED BY FORM FS-CO

Form FS-CO specifies the information that notifying party(ies) need to provide to the Commission in FSR filings. In mergers and acquisitions of joint control, the notifying parties are the merging parties or the acquirers of joint control. In acquisitions of sole control, the acquirer is the notifying party.

The Form FS-CO requires the following information (i) description of the transaction, (ii) information on the parties (ownership and structure of control pre/post-transaction), (iii) turnover information for the relevant parties and (iv) information on certain financial contributions and relating supporting documentation.

Information required for Article 5 Financial Contributions

Form FS-CO requires extensive information and supporting documentation for each potential Article 5 Financial Contribution equalling or exceeding EUR 1 million received by each of the parties to the transaction in the three years prior to signing, announcement of the public bid or the acquisition of a controlling interest (this includes financial contributions granted to the acquirer and the target).

Information required for other financial contributions

For all other financial contributions – those that do not constitute Article 5 Financial Contributions – the notifying party needs to provide only an overview of (i) financial contributions equal to or in excess of EUR 1 million that the notifying party has received in the three years prior to signing, announcement of the public bid or the acquisition of a controlling interest and (ii) only in relation to non-EU countries that have granted financial contributions to the notifying party of at least EUR 45 million during the three years prior to signing of the transaction (or announcement of the public bid or the acquisition of the controlling interest).

A number of financial contributions do not need to be reported, including the provision/purchase of goods/services (except financial services) at market terms in the ordinary course of business, and financial contributions below the individual amount of EUR 1 million.

In the case of acquisitions of control by investment funds (or by an entity controlled by an investment fund), the notifying party will not need to provide information on financial contributions granted to other investment funds (and their portfolio companies) managed by the same investment company but with a majority of different investors measured according to their entitlement to profit (such as limited partners), provided that (i) the fund which controls the acquiring entity is subject to the EU Alternative Investment Fund Manager Directive or to an equivalent third country legislation and (ii) the economic and commercial transactions – such as sale of assets, loans, credit lines, guarantees – between the fund which controls the acquiring entity and other investment funds (and portfolio companies controlled by these funds) managed by the same investment company are non-existent or limited.

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Importantly, all financial contributions (Article 5 Financial Contributions and other types of financial contributions) received by the parties in the three years prior to signing (or announcement of the public bid or the acquisition of a controlling interest) must be taken into account for determining whether the EUR 50 million filing threshold is met.

IV. CONCLUSION – CONSIDERATIONS FOR THE FUTURE

The FSR filing obligation imposes substantial requirements on parties to M&A transactions with respect to financial contributions granted by non-EU countries to companies active in the EU. The relevant information is not typically readily available or collated within companies. Therefore, companies will need to keep track of financial contributions received from non-EU countries.

In addition, the FRS adds a further layer of *ex ante* regulation of M&A transactions to the already increasingly complex regulatory landscape resulting from antitrust and foreign investment laws.

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