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Competition *FSR brief*

The Foreign Subsidies Regulation – 100 days since the start of the notification obligation for concentrations

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Introduction: a new regulatory framework

Regulation (EU) 2022/2560 of the European Parliament and the Council of 14 December 2022 on foreign subsidies distorting the internal market ("the Foreign Subsidies Regulation" or "FSR") started to apply on 12 July 2023. The FSR allows the European Commission to scrutinise subsidies granted by third countries to undertakings active in the internal market through different types of procedures: control of subsidies in concentrations and public procurement, *ex officio* investigations and wider (e.g., sectoral) market investigations[1].

As far as concentrations are concerned, the FSR introduces an obligation to notify transactions exceeding certain turnover and foreign financial contribution ("FFC") thresholds.[2] The purpose of the notification is to enable the Commission to assess whether a foreign subsidy in a concentration distorts the internal market.

This obligation to notify started to apply on 12 October 2023 and now, after 100 days, we take stock of the general trends observed in the first notified cases and focus on specific situations. Finally, this brief also provides clarifications with regard to the exceptions to the obligation to report certain FFCs which have been set out in the FSR Implementing Regulation.[3]

Overview of cases during the first 100 days

Snapshot of cases

100 days after the start of application of the notification obligation, the Commission services (DG Competition) have received case team allocation requests[4] and engaged in pre-notification talks with the notifying parties in 53 cases,[5] covering a large set of sectors, ranging from basic industries to fashion retail and high technologies. Out of those cases, 14 have been formally notified, of which 9 have been fully assessed. In one of those 53 cases, the notifying parties decided not to proceed with the transaction and therefore abandoned the case in pre-notification.

In a nutshell

The Foreign Subsidies Regulation started to apply on 12 July 2023 and the obligation to notify certain large concentrations kicked in on 12 October 2023.

The policy brief provides statistics on notifications in the first 100 days since the start of the notification obligation, as well as clarifications on some recurring issues that have arisen in the context of notifications received, including how to properly categorise foreign financial contributions, the level of detail required to report those identified as most likely to distort the internal market, as well as how to interpret some of the exceptions included in the notification form for concentrations.

[1] The FSR is jointly enforced by DG Competition and DG Internal Market, Industry, Entrepreneurship and SMEs. The latter, in line with its expertise, is responsible for the assessment of potential foreign subsidies that can distort public procurement procedures. On the other hand, DG Competition is responsible for the assessment of alleged foreign subsidies related to all other types of economic activities, including concentrations.

[2] In accordance with Article 20 FSR, a concentration needs to be notified if two cumulative thresholds are met – a turnover of more than EUR 500 million achieved by the target and more than EUR 50 million of FFCs received by the parties to the concentration in the three years prior to the conclusion of the transaction.

[3] Commission Implementing Regulation (EU) 2023/1441 of 10 July 2023 on detailed arrangements for the conduct of proceedings by the Commission pursuant to Regulation (EU) 2022/2560 of the European Parliament and of the Council on foreign subsidies distorting the internal market, OJ L 177, 12.7.2023, p. 1.

[4] A Case team allocation request (CTAR) is the initial document sent by notifying parties, who have identified that their transaction is notifiable under the FSR, requesting for the allocation of a dedicated team with whom they can engage in pre-notification discussions.

[5] Statistics related to the first 100 days of notification obligation, spanning from 12 October 2023 to 20 January 2024.

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Most cases brought for assessment under the concentration module of the FSR have also been subject to parallel assessment under Council Regulation (EC) 139/2004 of 20 January 2004 on the control of concentrations between undertakings ("EU Merger Regulation" or "EUMR") (42 out of 53 pre-notified cases so far). In several situations, the cases brought for assessment under the FSR have been subject to a national merger procedure (5 out of 53). In addition, roughly half of the FSR cases so far (26 out of 53) are or have also been subject to a foreign direct investment screening in one or several Member States.

In terms of the typology of concentrations, more than half of the cases (33 out of 53) involved a cross-border EU-non-EU transaction, 7 cases involved a cross-border transaction within the EU, 7 involved a cross-border transaction outside the EU, and 6 involved a transaction within the same EU Member State.

Another notable trend is the relatively large number of transactions that involve an investment fund as a notifying party – roughly one-third of all cases in which a case team allocation request has been received.

Preliminary assessment: publicity of cases and standstill obligation

In the first 100 days the Commission services have not identified in any case sufficient indications regarding the presence of a distortive foreign subsidy such as to warrant the opening of a second phase ("in-depth investigation"). This means that in the cases fully assessed (9 cases), DG Competition either did not identify foreign subsidies relevant to the concentration in accordance with Article 3 FSR or, if there were foreign subsidies relevant to the concentration, there were no sufficient indications that they would distort the internal market within the meaning of Articles 4, 5 and 19 FSR.

Unlike the EUMR, the FSR does not provide for the publication of notifications received or of the closing of investigations in the preliminary review phase. Indeed, this was a deliberate choice by the co-legislators, who were mindful that the publication of individual notifications under the FSR might lead to the disclosure of particularly sensitive information related to financial contributions granted by third countries to the parties and therefore found it necessary to adopt a more restrictive publicity regime than under the EUMR, unless an in-depth investigation is opened. In this regard, according to Article 10(4) FSR, where the Commission does not intend to open an in-depth investigation, it informs by administrative letter the notifying parties (as well as any Member State that has notified the Commission about a national procedure related to the same case) of the closure of the preliminary review. The procedure does not contemplate the adoption of a decision. It is only the lapsing of the standstill period of 25 working days after the formal notification that allows companies to implement the concentration.

The situation is different if the Commission decides to open an in-depth investigation. In such cases, the Commission must adopt a decision and, in accordance with Article 10(3) FSR, it will publish in the Official Journal of the European Union a summary notice with the main elements of that decision.

Most common types of FFCs assessed so far

The most common types of FFCs assessed in the first notifications relate to the sources of financing of the notified transactions. So far, those have included capital injections and equity contributions, but also loans obtained from financial institutions which could be considered as attributable to a third country. Other forms of FFCs frequently observed in the cases assessed so far include state guarantees, direct grants for specific projects, as well as tax benefits, notably for R&D expenses and investment projects.

When does the obligation to notify arise, what type of information to provide?

A notifiable concentration is deemed to arise where two cumulative conditions are met. First, either (i) one of the merging parties, (ii) the acquired undertaking or (iii) the joint venture is established in the Union[6] and generated an aggregate EU turnover of at least EUR 500 million in the last financial year. Second, the parties to the concentration were granted combined aggregate FFCs of more than EUR 50 million from third countries in the three years preceding the conclusion of the agreement.

Both the notification obligation and the information to be reported are based on FFCs, not on foreign subsidies. Indeed, FFCs and foreign subsidies are different concepts under the FSR: FFCs can be (i) any transfers of funds or liabilities, (ii) any foregoing of revenue or (iii) any provision or purchase of goods and services, provided by a third country through different levels of government, or by a foreign public entity or by a private entity whose actions can be attributed to the third country. In contrast, a foreign subsidy is a narrower concept which includes only FFCs which confer a benefit to their recipients and are limited to a certain undertaking or group of undertakings. That said, only the presence of FFCs, and not foreign subsidies, is relevant for notifying parties in determining their obligation to notify. Therefore, the fact that some or even all of the relevant FFCs have been provided on market terms and thus do not confer a benefit, or that they are generally available and are thus not limited in nature, is irrelevant to determine whether a concentration needs to be notified.

It is for notifying parties to assess whether they meet the conditions for notification. Upon receipt of the draft notification (the Form FS-CO), the Commission's services verify that the concentration is notifiable and that the parties have correctly reported the necessary information.

[6] 'Established in the Union' must be understood in accordance with the case law of the Court of Justice and includes the incorporation of a subsidiary in the Union, see footnote 7 of Form FS-CO.

In the first place, the proper qualification of the concentration as an acquisition, a merger or creation of a joint venture[7] is crucial for determining whether the notification thresholds are met. Indeed, the FSR thresholds apply to different companies, among those involved in a given transaction, depending on the nature of the concentration. For example, a transaction is inaccurately characterized as an acquisition of sole control instead of a merger, and thus only the turnover of the target has been considered to determine whether the turnover threshold of Article 20(3)(a) FSR is met. In that situation, if the turnover of the (incorrectly qualified) target is below EUR 500 million, but the other undertaking has a turnover exceeding that threshold, the merging parties, by implementing the transaction without prior notification, would violate the standstill obligation.

In the second place, the correct qualification of the concentration is also important in determining what type of FFCs needs to be reported for each party to the transaction. Generally, the notification should include the FFCs that may fall within Article 5(1)(a) to (d) FSR granted to *all* the parties to the transaction (i.e., notifying parties *and* the target or joint venture, as defined in recital 23 of the Introduction to the Form FS-CO). By contrast, FFCs not falling under Article 5 FSR should be included only if granted to the notifying parties.[8] An incorrect qualification of a concentration could thus turn out to lead to an incomplete notification, for example if an acquisition of joint control was incorrectly characterized as acquisition of sole control. A similar situation would also arise where a merger has been wrongly identified as an acquisition of sole control and FFCs not falling under Article 5 FSR have been reported only in relation to one of the merging entities.

Difference between notification threshold and reporting threshold for FFCs granted

The FSR sets out a *notification threshold* of EUR 50 million of FFCs granted to the parties to the transaction. At the same time, the Implementing Regulation, in its Instructions to provide information on FFCs not falling under Article 5 ("Instructions"), introduces a threshold of EUR 45 million of FFCs per third country to *report* FFCs granted to the notifying party.

A recurring question in discussions with notifying parties is which FFCs have to be considered for the notification threshold, on the one hand, and for the reporting threshold per country included in the Instructions, on the other hand.

All FFCs granted to the undertakings identified in Article 20(3)(b) FSR in the three years preceding the conclusion of the agreement, the announcement of the public bid or the acquisition of a controlling interest must be taken into account to determine whether the notification threshold set out in that provision is met. This also includes FFCs excluded from reporting in accordance with points 6 and 7 of the Instructions.[9]

By contrast, for the purpose of determining whether the reporting threshold of EUR 45 million per third country is met, the FFCs included in points 6 and 7 of the Instructions do not need to be taken into account.

The practice so far shows that in certain situations, the different calculation of the notification and reporting thresholds can lead to cases where the notifying parties have determined that they meet the notification threshold, but none of the received FFCs need to be reported. In these situations, notifying parties are expected to explain in the notification why the EUR 50 million notification threshold is met, setting out the reasons for not reporting any FFC. For example, this could be because no single foreign country has provided more than EUR 45 million in FFCs or because the FFCs received fall in one or several of the exceptions in points 6 of the Instructions. In the absence of such information provided in the notification, case teams need to request more information to make certain that the notification threshold has indeed been met, which could lead to delays in the review of the concentration.

Navigating the Form FS-CO: what financial contributions to report? and where?

An issue that arises frequently in pre-notification discussions is what type of FFCs should be reported in the notification and in which section.

FFCs are to be included in Section 5 of the Form FS-CO. But in which specific subsection and what information should be provided? The answer to this question depends on the type of FFC.

Categorising FFCs

According to the Form FS-CO, Sections 5.1 and 5.2 should contain detailed information about the FFCs that *may fall* into any of the categories of Article 5(1), points (a) to (d) FSR,[10] i.e., those which

[7] The concepts of "concentration", "merger", "joint venture" and "acquired undertaking" in Article 20 FSR are inspired from those used in the EUMR. General guidance on how these specific notions have previously been interpreted can be found in the Commission Consolidated Jurisdictional Notice.

[8] In situations where there is more than one notifying party to the transaction, the reporting of FFCs under Section 5.3 of the Form FS-CO should be done by providing a separate overview table for each notifying party (see notes below the table in the Instructions).

[9] The exceptions in point 6 refer to FFCs in the form of the provision or purchase of goods and services at market terms in the ordinary course of business, FFCs below EUR 1 million, certain tax and social security reductions of general application and some tax reliefs for the avoidance of double taxation. The exception in point 7 refers to the reporting of FFCs granted to investment funds involved in concentrations.

[10] Article 5(1)(e) FSR refers to the concept of unduly advantageous tender – a notion which is mostly relevant for the review of distortive foreign subsidies in the field of public procurement and as such is not relevant in the assessment in the context of notifications of large

are most likely to distort the internal market, whereas Section 5.3 will contain information, in a summarised form (in Table 1), about any other FFCs.[11] Importantly, as already mentioned, whether a FFC can be qualified as a foreign subsidy or not is irrelevant for it to be reported in the Form FS-CO, and therefore also to be categorised as potentially falling under Article 5 FSR. The decisive question for such categorisation is thus whether the FFC in question *would* fall under one of the categories of Article 5 FSR *were it to be qualified as a subsidy*. In fact, in Section 5.2.4 the parties can always explain why FFCs falling under article 5 do not qualify as subsidies.[12] In case of doubts about the correct qualification of a subsidy, the parties are encouraged to contact the case team during the pre-notification phase. In any case, the reporting of an FFC in Sections 5.1 and 5.2 rather than in Section 5.3 does not have any negative consequences: the reporting, as such, does not prejudge whether that FFC constitutes a subsidy – let alone whether it is distortive. It is a just a matter of correctly delineating the type of FFCs received.

The question of the categorisation of a certain FFC as potentially falling under Article 5 FSR also impacts the undertakings to be considered: information on FFCs which would *not* fall under this provision do *not* have to be provided in respect of targets or of joint ventures.

FFCs that may fall under Article 5 FSR: categories

The categorisation of certain FFCs within the different categories of Article 5(1) FSR is generally straightforward. This is the case, for instance, of unlimited guarantees (Article 5(1)(b) FSR). In the case of foreign subsidies to an ailing undertaking absent a restructuring plan (Article 5(1)(a) FSR), the qualification of an entity as "ailing" can easily be assessed with the questions included in sections 5.1.1.1 to 5.1.1.4 of the Form FS-CO. If the reply to any of those questions is positive, then the entity in question is likely to be considered "ailing". Importantly, this assessment should be done *by legal entity*, not by undertaking. In other words, if one of the legal entities to the group of the acquiring undertaking meets the conditions to be considered ailing, this should be disclosed in this section even if, overall, the group as such is not undergoing financial difficulties. In any case, the fact that one entity is considered ailing does not mean that the parties have to provide the detailed information required by Section 5.2 in relation to *all* FFCs granted to it, but only in relation to those, if any, "*that may have contributed to restore its long-term viability (including any temporary liquidity assistance designed to support that restoration of viability) or to keep that party afloat for the short time needed to work out a restructuring or liquidation plan*". At the same time, these FFCs will only fall under Article 5(1)(a) FSR if there is no restructuring plan capable of leading to the long-term viability of the entity, including a significant own contribution by the undertaking.

As to FFCs that may fall under the category of subsidies directly facilitating a concentration (Article 5(1)(d) FSR), the parties are expected to disclose all FFCs used to finance the acquisition or from which the transaction benefits. For instance, grants, loans or guarantees which are granted specifically for a given acquisition should be considered as directly facilitating it. But the intention of the granting third country to facilitate a specific transaction is not decisive. A grant, loan or guarantee which is conceded generally for acquisitions or which is used for, or facilitates a given transaction may also be considered as directly facilitating it, and therefore should be included.

As a result, FFCs granted by third countries as limited partner investments in an acquiring investment fund should in principle be reported under Sections 5.1 and 5.2, since the purpose of these investments is typically to provide resources which are used by the funds to make the acquisitions. This means that the notifying party will be expected to explain in the notification whether or not those investments have been made at market conditions (section 5.2.7 of the Form FS-CO). The key element to assess in these cases is whether the investments attributable to third countries have been made at the same conditions as the investments of other limited partners in the acquiring fund whose actions are not attributable to a third country (e.g., private investors). The notifying parties will also need to provide information as to the conditions attached to those investments (section 5.2.5), namely the rights that limited partners have in the funds (for instance, as regards decisions on investments) or in the governance of the acquired undertakings. That said, as indicated above, including this information does not have any implications for the purpose of characterizing the existence of a foreign subsidy. If the information provided shows that the investments by limited partners attributable to third countries do not confer any benefit to the acquiring fund or the target, their reporting under Sections 5.1. and 5.2. will not prejudge the assessment.

Exceptions to the reporting obligations: when and how to apply them? The case of acquisitions by investment funds

The feedback received by the Commission from notifying parties is that the reporting exceptions included in points 6 and 7 to the Instructions have considerably reduced the administrative burden for undertakings by comparison to the initial draft of the notification form which was published for public consultation at the beginning of 2023. Indeed, the Commission paid particular attention to the feedback received by stakeholders and, after careful consideration, included the mentioned exceptions for certain types of FFCs not falling under Article 5 FSR. Based on this feedback, the exception for FFCs in the form of contracts

concentrations but rather in the context of public procurement procedures.

[11] In all cases, FFCs in principle need to be reported to the extent that they exceed the reporting thresholds set out in the Form FS-CO.

[12] Such an explanation is in principle not required for the rest of FFCs, although the Commission can ask for it if it considers it is relevant for the assessment of the case.

concluded at market terms in the ordinary course of business has been particularly helpful in streamlining the reporting obligations.

One common question being raised in pre-notification discussions is the scope of the exceptions set out in points 6 and 7 of the Instructions.

General principles

As these are exceptions to the general rule – the obligation to report these FFCs in Table 1 – they are to be interpreted narrowly. By way of example, point 6 of the Instructions indicates that certain tax measures can benefit from an exception if they are of general application. The list of tax measures provided in point 6 is exhaustive, which means that other or similar tax measures cannot benefit from the exception only because the notifying parties consider that they are also of general application. Tax measures not listed in point 6(a) of the Instructions should be reported regardless of whether the notifying parties consider them to be of general or limited application.[13] In case of doubt as to whether a certain measure would fall under the categories listed in point 6(a), the parties should consult the case team.

If a given FFC is covered by an exception, it does not need to be included and described in Table 1. However, case teams may ask the parties to substantiate why certain measures fall under the exceptions and to disclose these FFCs, should that be necessary for the assessment of the transaction.[14]

When assessing whether a certain exception applies or not, parties should keep in mind a fundamental distinction between the exceptions of point 6 of the Instructions and those of point 7: in the former it is for the parties to self-assess whether the exception would apply to their specific situation (without prejudice to the possibility of case teams to ask questions about it, as indicated above). By contrast, in the case of the latter (acquisitions by investment funds), the parties need to invoke that the conditions for the exception are met and substantiate why.

The specific case of the exception applicable to transactions made by investment funds

In the case of investment companies that enter into the transaction through one or different funds, it is worth reminding what the general rule and the rationale of the exception are.

In normal circumstances, and just as is the case when applying the EUMR, an investment company usually controls the different funds it sets up, as the investment funds are merely investment vehicles. Investors, on the contrary, typically participate as limited partners and normally do not exercise control, either individually or collectively, over the companies in which the funds invest.[15] This means that the relevant undertaking for the purposes of the notification will usually be formed by the investment company and *all* the funds it manages, as well as all the portfolio companies controlled by those funds.

The Commission, however, acknowledges the specificities of investment fund structures, and for this reason, point 7 of the Instructions allows the parties to limit the information they provide, under Table 1, to the FFCs granted to the acquiring fund and the portfolio companies of this fund. FFCs granted to other funds and their portfolio companies will thus not be reported, provided that certain conditions are met. These cumulative conditions are designed to give comfort to the Commission that a possible cross-subsidisation from other funds (or their portfolio companies) to the acquiring fund (and in particular, to the merging entity) is unlikely or that there are mechanisms in place to minimise this risk.

The first of those conditions is that the investors in the non-acquiring funds, in terms of their entitlement to profit, must differ from the acquiring fund. The rationale of this condition is that in situations where there is no or limited commonality of interests between funds, the incentives for cross-subsidisation will be more limited. In practice, the parties must demonstrate that the totality of the acquiring fund's limited partners do not constitute a majority of the limited partners in any of the non-acquiring funds.

The second condition is that the acquiring funds are subject to Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers or to an equivalent third country legislation in terms of prudential, organisational and conduct rules, including requirements aimed to protect investors. There is no pre-established list of jurisdictions which are considered to meet this condition. It is for investment companies notifying a concentration to provide evidence that the legislation in question includes sufficient guarantees to prevent cross-subsidisation between funds (including their portfolio companies). In particular, the legislation should include provisions ensuring that the funds are managed in the best interest of their respective investors, thus preventing profit shifting from another fund to the acquiring fund via, for instance, corporate reorganisations or transactions which are not at market conditions. These provisions should include, in particular, assurances concerning an adequate monitoring of cash flows and adequate internal control mechanisms, appropriate procedures for safe keeping and independent valuation of the funds' assets, transparency requirements vis-à-vis competent authorities and investors, measures to prevent or minimise conflicts of interest, an

[13] See question included in the Q&A published by DG COMP on its website (Questions and Answers - European Commission (europa.eu)).

[14] Moreover, case teams can request more detailed information of the FFCs reported in Table 1 to better understand the nature and characteristics of the FFCs and their link with the transaction and with the internal market.

[15] See Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings, paragraph 15.

adequate risk management system, rules ensuring fair treatment of investors and provisions ensuring the active supervision of those funds by competent authorities. In this regard, it is for the notifying party to explain why it considers that it is subject to and complies with a certain third country legislation and why it considers that third country legislation to comply with the condition set out in point 7(a) of the Instructions (making reference to the relevant provisions of that law).[16]

Finally, the third condition is that economic and commercial transactions between the acquiring and the non-acquiring funds (or their respective portfolio companies) are non-existent or limited. For that purpose, the parties should disclose any such transactions which took place in the three years prior to the concentration. In theory, general partners and fund advisors should avoid transactions which may give rise to conflicts of interest. Transactions such as transfers of assets between funds may serve as vehicles for cross-subsidisation, thus giving rise to profit shifting between funds if, for instance, they have not been adequately valued. Therefore, if there have been any of these transactions in the past, the case team may request explanations as to whether there has been a competitive and transparent process for the valuation of the assets or what the rationale for such a transaction was. Whether the number of transactions is "limited" will be a case-by-case analysis that will depend on many different circumstances such as the nature and number of those transactions, their amounts and dates, the types of assets involved or the mechanisms put in place to avoid conflicts of interest.

Conclusion

100 days after the start of application of the notification obligation under the FSR, both the Commission and notifying parties are gaining experience on the new regulatory steps in the review of concentrations. Going forward, as of 1 March 2024, the review of concentrations under the FSR will be entrusted to the newly created Directorate K in DG Competition, created to ensure the proper enforcement of the FSR.

In terms of take-aways, as the practice on the first cases shows, in order for notifying parties to ensure a timely and smooth assessment of their transactions, special attention should be paid to the quality and completeness of the reported information. This includes, most notably, the correct identification of reportable FFCs, the proper delineation of FFCs that may fall within the categories considered most likely to be distortive, as well as a circumscribed interpretation of the application of the exceptions in points 6 and 7 of the Instructions. In case of doubts and in order to prevent delays in the process, the parties can contact the case team as soon as practically possible.

DG COMP has also published a Q&A with clarifications and practical information related to procedural, implementation and practical application of the FSR, which are updated from time to time to reflect the answers to the most recurring questions of relevance for stakeholders

[16] The possibility to benefit from the exception referred to in point 7 of the Instructions is strictly limited to the specific case and to the specific purpose laid down in the exception, i.e. to prevent a possible cross-subsidisation, and in no way can be understood as expressing any position of the Commission as regards the equivalence of third country rules within the meaning of Directive 2011/61/EU on Alternative Investment Fund Managers.