

The FSR Will Soon Apply: What Companies Need to Know

The EU's new regime for tackling foreign subsidies will kick in on 12 July 2023.

On 10 July 2023, the European Commission (Commission) published the final text of the Implementing Regulation (Final IR) on proceedings pursuant to the Foreign Subsidies Regulation (FSR). The Final IR is the last legal instrument to be adopted before the FSR takes effect on 12 July 2023. The FSR empowers the Commission to investigate and remedy subsidies received from non-EU States that distort competition in the EU internal market. For companies, the FSR adds a further layer of regulatory scrutiny on top of existing merger control and foreign direct investment rules.

From 12 October 2023, companies that have received financial contributions from non-EU States will need to file notifications for M&A deals and public tenders above certain thresholds to the Commission or national authorities pursuant to the FSR. Deals signed on or after 12 July 2023, but that do not close by 12 October 2023, will need to be notified as well. From 12 July 2023, the Commission will have the power to investigate suspected distortive subsidies on its own initiative and request ad hoc notifications for M&A deals and public tenders falling below the relevant thresholds.

The Final IR sets out the procedural requirements for notifications under the FSR and attaches forms to use in each case (Annex 1 for M&A, Annex 2 for public tenders). Significant changes to the final text show that the Commission took on board much of the industry feedback provided in the public consultation on the draft Implementing Regulation published on 6 February 2023. These changes meaningfully reduce the administrative burden on companies of FSR compliance.

Final Implementing Regulation — What's New?

The notification thresholds applicable to M&A deals and public tenders under the FSR remain unchanged. However, the Final IR increases the thresholds and exemptions that apply when determining which financial contributions are reportable in a notification and clarifies the level of disclosure required. Below are six key takeaways for companies.

1. Unchanged notification thresholds for M&A deals and public tenders

M&A deals: Acquisitions, mergers, and joint ventures will require notification under the FSR when two thresholds are met:

- at least one of the merging firms, target, or joint venture is established in the EU and has EU turnover of at least €500 million; and

- the acquirer and target, merging parties, or joint venture and its parents have received aggregate financial contributions of more than €50 million in the previous three years.

Public tenders: A public tender with an EU-based authority will require notification under the FSR when two thresholds are met:

- the estimated contract value is €250 million or more; and
- the “economic operator” (i.e., bidder plus main subcontractors and main suppliers) received aggregate financial contributions of €4 million or more per third country in the last three years.

For both M&A and public tenders, all financial contributions received must be taken into account when determining whether the second threshold in the notification test is met (underlined above). However, the Final IR limits the types of contribution that must be reported and the level of disclosure required.

Key reporting thresholds, exemptions, and disclosure requirements in the Final IR are summarised below. These apply to both M&A and public tender notifications, unless otherwise indicated.

2. Higher reporting thresholds for all types of financial contribution

The Final IR increases the thresholds for reportable financial contributions in notifications of M&A deals and public tenders under the FSR based on the type of contribution received.

- Contributions amounting to less than €1 million are not reportable.
- Contributions falling into one of the categories considered “most likely to distort” competition in the EU must be reported if the individual amount of the contribution is or exceeds €1 million.
- All other types of contribution must be reported if the aggregate amount received is or exceeds the following thresholds: (i) for M&A deals, €45 million per third country in the three years prior to signing of the transaction agreement or announcement of the public bid; and (ii) for public tenders, €4 million per third country in the three years prior to notification.

The €1 million reporting threshold applies to five specified categories of “most likely distortive” subsidy: (i) aid to ailing firms; (ii) unlimited guarantees for debts or liabilities; (iii) export financing not in line with OECD rules; (iv) subsidies directly facilitating a concentration; and (v) subsidies enabling a firm to submit an “unduly advantageous” bid in a public tender. The Final IR confirms that financial contributions to cover operating costs are not a stand-alone category of “most likely distortive” subsidy.

3. Disclosure requirements tailored based on contribution type

The level of information required in the notification form differs depending on the type of financial contribution. In particular, contributions that are considered “most likely distortive” are subject to more onerous disclosure obligations than other, less problematic types of financial contribution.

- *For “most likely distortive” contributions*, detailed information is needed for each individual contribution above €1 million (e.g., amount and type, granting authority, purpose and economic rationale, and any conditions attached), along with supporting documentation.
- *For all other types of contribution*, companies need only to provide information at an aggregate level (e.g., the types of contribution received for each third country where the aggregate reporting

threshold is met, and the estimated total amount of contributions received per third country, expressed in broad ranges (e.g., €45 million–€100 million, €100 million–€500 million, etc.). However, no supporting documentation is required.

The Commission has the power to request more detailed information on all types of financial contribution, including those not falling into the categories of “most likely distortive” subsidy, on a case-by-case basis.

4. New exemptions for certain non-problematic contributions

Financial contributions that do not fall into one of the categories of “most likely distortive” subsidy do not need to be reported or described in M&A or public tender notifications where they relate to:

- certain general tax measures and relief (e.g., deferrals of payment, tax amnesties) — however, selective measures aimed at a specific firm, type of company, or sector need to be reported; or
- the supply or purchase of goods or services (except financial services) at market terms in the ordinary course of business (e.g., in a competitive, transparent, non-discriminatory tender).

These “exempt” contributions do not count towards (i) the aggregate amount threshold above which financial contributions are reportable (e.g., in calculating whether a company meets the €45 million threshold (M&A) or €4 million threshold (public tender) per third country in the last three years) or (ii) the aggregate amount that is reportable once the relevant threshold has been reached. However, financial contributions that are considered “most likely to distort” competition, and which amount to €1 million or more, will be taken into account when determining whether these aggregate reporting thresholds are met.

5. Special disclosure regime for investment funds

Investment funds are subject to a more limited disclosure regime when engaging in M&A. Only financial contributions received by the fund involved in the transaction and its controlled portfolio companies are reportable in the notification. Contributions granted to other funds managed by the same investment firm (or by portfolio companies controlled by those funds), but with a majority of different investors, do not need to be reported and will not be taken into account when calculating the aggregate amounts. This more limited disclosure regime is available only to investment funds that meet the following conditions:

- the fund controlling the acquirer is subject to the EU’s Alternative Investment Fund Managers Directive (or equivalent third-country prudential, organisational, and conduct rules); and
- there are no or only limited economic or commercial transactions between the fund that controls the acquirer and other funds managed by the same investment firm (or their controlled portfolio companies), including sales of assets, ownership in companies, loans, credit lines, or guarantees.

Notably, the special disclosure regime for investment funds does not apply to any categories of contribution considered “most likely distortive”. In this case, contributions received by *any* fund managed by the same investment firm are reportable, provided the individual amount is €1 million or more.

6. Information on non-notifiable contributions required in public tender “declarations”

When a public tender meets the contract value threshold (€250 million) but not the financial contribution threshold (€4 million per third country in the last three years), bidders are required to submit (i) a “declaration”, stating that they did not receive any notifiable financial contributions and (ii) a list of all non-notifiable financial contributions received in the last three years, subject to two qualifications:

- contributions amounting to less than €1 million but more than €200,000 in the last three years can be listed in aggregate form, with a brief description of the types of contribution received (e.g., direct grant, tax advantage, etc.) per third country, but without indicating their values; and
- contributions amounting to less than or equal to €200,000 per third country in the last three years do not need to be listed or described in the declaration at all.

Financial contributions equal to or more than €1 million in the last three years need to be listed and described individually in the declaration, per third country, also indicating the amount of the contribution.

Notably, the standard reporting exemptions for general tax measures and for the supply and purchase of goods and services on market terms applicable to notifications do not apply to declarations.

Implications for Companies

The Final IR represents a significant improvement to what was widely criticised as an unworkable and unduly onerous regime. Indeed, industry associations and in-house lawyers have welcomed the Final IR as creating a more manageable system.

That being said, compliance with the FSR will not simply be a box-ticking exercise, and ongoing attention from companies' legal and compliance organisations will be required. Importantly, the pared-down reporting obligations in the Final IR do not lessen the need for companies to monitor financial contributions to determine whether notification and reporting thresholds are met. Accordingly, companies will need to establish robust internal systems to identify and record foreign financial contributions.

With the text of the Implementing Regulation now final and the FSR about to take effect, companies should focus on preparing for notifications in Q3 of this year. Notably, transactions that sign on or after 12 July 2023 but have not closed by 12 October 2023 will be notifiable. Helpfully, the Commission has signaled that it is open to start pre-notification discussions with companies from 12 July 2023, preferably on the basis of a draft notification. Companies that already have notifiable deals or public tenders in the pipeline should use this opportunity to clarify, and ideally reduce, the information that will be required.

For acquirers, the impact of the FSR on deal risk and timing should also be factored in to transaction planning and negotiation of deal documents. As with merger control, the risk of investigation under the FSR will need to be allocated through the usual contractual provisions (e.g., conditions precedent, effort obligations and cooperation clauses, long stop date, and representations and warranties). Due diligence of the target will also need to include a review of reportable financial contributions (in particular, potentially distortive subsidies) received in the past three years, which could affect regulatory risk.

For M&A requiring approvals under multiple regulatory regimes (FSR, merger control, and foreign direct investment review), a coordinated legal strategy for all approvals will now be more important than ever.

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