



## BRUSSELS À JOUR

## Foreign Subsidies Regulation: a Year of Mandatory Notifications in Review

Markus Röhrig, Christoph Wilken und Christian Dankerl report on the latest developments from the European capital of competition law.

Since mid-October 2023, certain M&A transactions and participations in public procurement proceedings must be notified to the European Commission (“Commission”) under the Foreign Subsidies Regulation (Regulation (EU) 2022/2560, “FSR”). This past year was a busy year for the Commission, for FSR lawyers and, most importantly, for companies falling within the scope of application of the FSR. The FSR has been criticized by many, not only for the burden it puts on transactions and public procurements, but also for its very broad scope.

The first year of mandatory notifications has provided some clarity on the application of the FSR, although much remains uncertain. The past year has also highlighted some enforcement trends and key developments. Below, we are providing some insights on these.

### Unexpected high number of cases and resources allocated by the Commission to the application of the FSR

Initially, the Commission expected an annual case load of around 30 notified concentrations, 36 notified bids in public procurement proceedings and around 30-45 ex officio cases. The actual number of notified cases greatly exceeded these expectations. Since the application of the filing obligations in mid-October 2023, the Commission has received a low three-digit number of merger notifications and more than 1.000 notifications relating to more than 200 public procurement proceedings. It is no surprise that the Commission has used its ex officio powers sparsely.

To deal with this case load, the European Commission’s Directorate-General for Competition (DG COMP) and its Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (DG GROW) have ramped up their internal resources for dealing with FSR cases over the last year. In the Commission’s proposal for the FSR, it expected that 145



FTEs would be required to effectively achieve the objectives, but early reports suggested that the Commission struggled to dedicate staff to the FSR. Initially, FSR merger cases were handled by a subdivision of DG COMP's unit responsible for international relations. Over time, the Commission dedicated more staff to FSR and eventually established an own directorate ("K"), headed by Karl Soukup who is also acting Deputy Director-General in charge of State Aid, with three units solely handling FSR cases. We expect the Commission to continue bolstering its capabilities as the recent "Draghi Report" (The Future of European Competitiveness, September 2024) emphasized the need for adequate resources to ensure an efficient application of the FSR.

Practice has shown that the Commission tries to be efficient when dealing with unproblematic FSR cases by streamlining and swiftly concluding the pre-notification discussions. In general, pre-notification discussions lasting longer than two to three months are caused by missing information provided by the parties rather than by a bottleneck on the Commission's end.

### **Bits and pieces that provide guidance and clarity on the application of the FSR**

From the outset, the Commission's application of the FSR was heavily criticized for its lack of transparency. Indeed, under the FSR, the Commission is not required to issue and publish clearance decisions in Phase 1 proceedings, but only decisions concluding in-depth Phase 2 investigations as well as decisions to enter Phase 2 proceedings.

During 2024, the Commission on several occasions provided further guidance and clarifications. In February, the Commission issued a policy brief on the first 100 days of the notification obligations, outlining some trends that became apparent during that period. On the substantive side, the Commission has published on 26 July 2024 a Staff Working Document on the FSR, which discusses two core elements of the FSR to further clarify the Commission's assessment process. Firstly, the document describes situations in which the Commission considers a foreign subsidy to distort competition in the internal market and secondly, it describes how the Commission considers the balance between the beneficial effects of a foreign subsidy on the internal market and the distortion caused by it.

In a recent push for more transparency, DG COMP has decided to publish information on notified cases since 14 October 2024 in the case search on its website lists all merger notifications received. This at least gives third parties the opportunity to voice their views on notified transactions.

Yet, uncertainty remains. Despite the Staff Working Document, it is still not clear how exactly the Commission assesses a potential distortion of the internal market caused by a foreign subsidy. From the Commission's first phase 2 merger decision it became apparent that the Commission applies a broad understanding of what may amount to a potential distortion. While Art. 19 FSR states that the "*assessment shall be limited to the concentration concerned*", the Commission not only assessed whether the foreign subsidies allowed the acquirer to submit an unduly high bid in the acquisition process, but also whether the foreign subsidies could impact the market behaviour post-transaction. In contrast, the Commission's assessment of a potential distortion in a public procurement investigation



is limited to the bidding process in question and whether the recipient of a foreign subsidy was able to submit an unduly advantageous bid.

Further clarification on the application of the FSR can be taken from the General Court's first judgment on an FSR case dated 12 August 2024. In this judgment the court confirmed the Commission's investigation powers in relation to an inspection against subsidiaries of a Chinese company located in the EU, which opened the door for an extraterritorial application of the FSR. The court ruled that Commission is entitled to request information stored outside the EU to assess whether their conduct infringes EU law and is likely to distort the internal market. This investigative power is justified by the necessity for effective investigations and the ability to hold non-EU companies liable for distortions of the internal market.

The "Draghi Report" further opened the door for an additional defence for companies that have received financial contributions from non-EU states that could distort the internal market. According to the report, interventions may not be warranted if European companies have fallen behind to a degree that intervening against foreign subsidies would result in deadweight costs on the European economy and, ultimately, detrimental effects for consumers.

### **The Commission's first Phase 2 decision – Behavioural remedies to eliminate a threatened distortion**

The Commission's first phase 2 merger decision – its conditional approval of the acquisition of PPF Telecom Group B.V. by Emirates Telecommunications Group Company PSJC (e&) on 24 September 2024 – was awaited with high expectation. While the non-confidential version of the decision has not been published yet, based on information that is available on the case from the Commission's press release and its decision to enter phase 2, it did not disappoint these expectations.

The Commission was concerned that the foreign subsidies granted to e& in the form of unlimited guarantees from the United Arab Emirates (UAE) and a loan from UAE-controlled banks may have distorted competition in the internal market. The Commission did, however, not limit its assessment to the acquisition process itself (as the wording of Art. 19 FSR would suggest) but found that the guarantees and the loan would have enhanced the merged entity's ability to (unduly) finance its activities in the EU, increasing its risk aversion, while ultimately encouraging infrastructure investment or spectrum purchases that other companies without financial state support would not consider.

Securing the clearance came at a cost for e&. The Commission approved the acquisition subject to a 10-year behavioural remedies package. It entails commitments to remove the state guarantee and to refrain from financing the target's European businesses, except for some non-EU related operations and instances where emergency funding is required. The commitment package further includes the obligation to conduct any commercial agreements between e& and PPF at market terms, and e& must inform the Commission of any transactions of significant value prior to their completion, even if they are not notifiable under the FSR.



Although we do not yet know the full details of the decision, the Commission has addressed some key points:

- Foreign subsidies have no actual or negative effect on the acquisition process if the company is the only potential purchaser, already having sufficient resources to carry out the acquisition.
- The Commission's assessment is not limited to the acquisition process: unlimited guarantees may have effects on the merged entity's post-transaction market behaviour that could distort the internal market. The Commission seems to have a wide discretion when assessing whether foreign subsidies could have such effects.
- Long-term behavioural remedies are acceptable to the Commission if it is certain that the foreign subsidies cannot be used for unduly market behaviour post-transaction. This was a somewhat unexpected approach as the behavioural remedies relate to a potential future market conduct that the Commission could investigate by using its ex officio powers.

The Commission accepting the behavioural remedy package could be used as a blueprint to obtain FSR clearance by state-supported acquirers, provided that they are willing to ringfence the EU operations of the target post-transaction.

### **Enforcement priorities?**

Commission officials were very diligent in stating that the FSR is both industry and country agnostic and has not been designed as a tool to specifically target Chinese subsidies. However, China has played a key role not only in the Commission's approach leading up to the FSR – case studies featured Chinese companies as subsidized acquirers of businesses located in the EU – but also in the cases over the past year.

In February 2024, the Commission launched its first in-depth investigation under its public procurement tool related to a bid by a Chinese manufacturer of rail vehicles in a Bulgarian public tender. Two months later, the Commission launched two further in-depth investigations in the photovoltaic sector. Both investigations related to bids by Chinese suppliers. In these three cases the Chinese bidders withdrew their bids before the Commission was able to conclude its investigations.

Commission officials have suggested to focus the use of bloc's power to launch ex officio investigations on those cases where there appears to be credible evidence of a significant market impact caused by a potential distortion. This focus also seems to lie on Chinese companies as two ex officio investigations related to Chinese suppliers (one supplier of wind turbines and the other a supplier of security equipment in which case the Commission dawn raided the premises of EU subsidiaries in two Member States).

However, the Commission's Phase 1 merger clearance under the FSR of Haier Smart Home's acquisition of Carrier's Commercial Refrigeration business from the beginning of October demonstrates that not all Chinese-backed investments raise concerns.

The Commission's geographical focus has led to tensions in the international trade relations to China. The China Chamber of Commerce to the EU (CCCEU) has repeatedly expressed its dissatisfaction with the application of the FSR, inter alia by referring to the FSR as



“a new tool of economic coercion to interfere with the reasonable and lawful economic operations of Chinese enterprises in the EU.” Recently, Chinese lobbying groups urged the Chinese government to take the necessary countermeasures and warned EU exporters to expect retaliatory measures if the Commission continues its course of action against Chinese companies.

In terms of industry focus, the Commission’s investigations unsurprisingly related to sectors of strategic importance to the objectives and policies of the EU, with cases in the transportation, green energy and security equipment and telecommunications industries.

The Commission’s focus is likely to remain on China, while companies from other countries with no or less stringent state aid control regimes may also come increasingly under investigation, as evidenced by the first in-depth merger investigation into foreign subsidies attributable to UAE. Additionally, based on recently publicly announced complaints, European companies seem more willingly to raise concerns about state-baked non-EU investors and bidders, which may affect the geographic and industry focus of the Commission.

**Outlook**

It can be expected that the Commission will double down on its ex officio investigation and call-in powers. With the designated new Commissioner’s hearing in the European Parliament and the US elections in early November 2024 (and the next US administration’s foreign trade policies), the coming month is loaded with political developments that may influence the FSR enforcement activities of the Commission. Additionally, re-elected President von der Leyen’s in her mission statement instructs the new Commissioner in charge of competition to vigorously enforce the FSR, and senior Commission representatives stated that the Commission intends to conduct more ex officio investigations. This is in line with the outlook provided in the “Draghi Report” on how to apply the FSR to ensure the future of European competitiveness. What this means in practical terms remains to be seen once the dust has settled.

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