

The EU Foreign Subsidies Regulation Beds Down: 10 Enforcement Trends

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The EU's Foreign Subsidies Regulation (FSR) allows the European Commission (EC) to investigate and remedy subsidies received from non-European countries that distort the EU internal market. As the FSR marks its inaugural year of application, this briefing reports on key trends emerging from the initial deployment of the tool. For a more detailed summary of the legislation, see our 17 July 2023 client alert "[EU Foreign Subsidies Regulation Goes Live: Key Implications for M&A Transactions](#)".

- The FSR empowers the EC to address distortions in the internal market through a review of notified large transactions and public procurement procedures, as well as through investigations launched on its own initiative. The regime entered into force in June 2023 and the notification obligations started to apply in October 2023.
- The opening period of the FSR has been lively: It has seen a high number of notifications, the withdrawal of tenders from public procurement procedures following EC intervention, clarifications of the substantive test, the launch of four in-depth investigations and two *ex officio* cases, one of which involved dawn raids, and the first formal (conditional clearance) decision.
- The EC's growing enforcement of the FSR reinforces the importance for businesses operating in the EU of considering the application of the regime to commercial activities as early as possible, in particular businesses active in sectors or geographies that fall within the EU's strategic priorities.

1. The EC has received considerably more notifications than it expected

The EC has been scaling up its resources to manage an increasing volume of work under the FSR, largely stemming from a high number of notifications. By the end of September 2024, the EC said it had entered into pre-notification discussions in more than 120 M&A cases, 91 of which were formally notified, far exceeding the EC's initial prediction of 33 M&A notifications per year. The count for procurement in the same period reportedly reached 1,108 submissions relating to 213 tenders, which dwarfs the EC's initial estimate of 36 tender notifications per year.

Notably, although the EC is not required to publish details of FSR notifications or its case closures in the preliminary review phase, the authority recently decided to increase transparency regarding its caseload by publishing details of individual notifications on its website from 14 October 2024.

2. The EC conducts wide-ranging reviews

The concept of a "foreign" (non-EU) financial contribution (FFC) is extremely broad. It includes various direct or indirect contributions from non-EU governments or any public or private entity attributable to a non-EU country.

The EC reported in a [February 2024 policy brief](#) that the most common type of FFC assessed relates to the sources of financing of the notified transaction, followed by state guarantees, direct grants for specific projects and tax benefits. While the EC has not released a similar publication covering its procurement casework, the three in-depth procurement reviews to date demonstrate interest in a wide-range of FFCs, including government grants, tax refunds and fiscal incentives.

EC staff are prepared to probe notifying parties with wide-ranging questions and several requests for information during pre-notification talks in order to assess the presence and

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extent of any potentially distortive foreign subsidies. The EC scrutinises aspects such as the purchaser's financing arrangements and the relationship between the purchase price (or bid) and the value of the target (or contract put out to tender).

3. The process imposes a significant burden on private equity firms

The EC reported that approximately one third of the M&A notifications received in the first 100 days involved an investment fund as a notifying party. The FSR imposes a particular burden on private equity firms and other financial sponsors investing in the EU, which will need to make a detailed assessment of FFCs both at the level of the fund and across portfolio companies.

The EC also typically asks detailed questions about any investments in an acquiring fund from third-country limited partners (*e.g.*, a sovereign wealth fund). These investments may fall into the "most likely to distort" category of foreign subsidies on the basis that their purpose is generally to provide resources which are used by the funds to make the acquisitions. Investment funds are therefore expected to report any such investments in the notification together with an explanation of whether they have been made on market terms.

4. The EC has broad discretion

Substantive EC guidance on the distortive effects of foreign subsidies is not expected until mid-January 2026. In the meantime, the EC's [July 2024 Staff Working Document](#) (SWD) sets out a helpful preliminary framework for the EC's assessment. The preliminary clarifications are not binding and will be developed through decisional practice and rulings from the EU courts. For now, there remains some uncertainty over the way in which the EC will apply its substantive assessment.

- **Analysis for M&A versus public tenders.** For M&A transactions, the EC can examine distortions in the acquisition process and/or post-transaction in relation to the merged entity's activities. Conversely, public procurement investigations are restricted to the bidding process in question and evaluate whether the tender is unduly advantageous and linked to the foreign subsidy.
- **Distortion test.** A foreign subsidy will be found to distort the EU internal market where there is a link between the foreign subsidy and the beneficiary's EU activities, and if the foreign subsidy actually or potentially negatively affects competition in the internal market. The "most likely to distort" foreign subsidies falling under Article 5 of the FSR will generally be presumed to distort the market, whereas the EC will assess the distortive effects of non-Article 5 foreign subsidies on a

case-by-case basis. The SWD underscores the broad margin of discretion afforded to the EC in carrying out its substantive assessment: The EC ultimately decides which factors it will apply in the case in question.

- **Balancing test.** Should the EC conclude that there are foreign subsidies which distort the internal market, it will go on to assess whether the distortion can be outweighed by positive effects. The EC states in its SWD that it has not yet gathered enough experience in the application of the balancing test, and does not therefore offer much practical guidance on this aspect beyond noting that the negative effects of the most likely distortive Article 5 subsidies are "less likely" to be outweighed by positive effects.

5. The EC is prepared to initiate in-depth reviews if it has concerns

The EC may initiate an in-depth investigation following a preliminary review if it has concerns that foreign subsidies are present that may distort the EU internal market. The EC has launched four in-depth investigations to date in relation to notifications under the regime.

The first, launched just four months after the FSR notification obligations came into force, in February 2024, concerned a bid by a Chinese state-owned train manufacturer in a public procurement process for the provision of electric trains and related services in Bulgaria. Amongst other things, the EC pointed to potential subsidies received by the bidder that were five times larger than the value of its tender, and a bid that was "substantially lower" than the offer of the only other competitor.

In April 2024, the EC launched two further investigations into tenders submitted by Chinese bidders in a public procurement process for the design, construction and operation of a solar power project in Romania. The EC's concerns included potential subsidies received by both bidders that were "significantly higher" than the value of the contract put out to tender.

In all three of these procurement cases, the bidders voluntarily withdrew their tenders and the EC therefore terminated its investigations without needing to take a final decision.

The EC launched its first in-depth review into an M&A transaction in June 2024. The investigation concerned the acquisition by Emirates Telecommunications Group Company PJSC (known as e&), a state-controlled telecommunications operator based in the United Arab Emirates (UAE), of parts of PPF Telecom Group B.V. (PPF), a European telecommunications operator. The EC cleared the transaction subject to remedies, as explained in the next section.

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6. Behavioural remedies may resolve concerns

The EC's first formal decision under the FSR was handed down at the end of September 2024, following the conclusion of an in-depth review of the e&/PPF transaction. (The FSR does not contemplate the adoption of a formal decision following a preliminary review.) This marks an important milestone in the enforcement of the FSR and provides a welcome first look into how the EC will handle problematic foreign subsidies in the context of a transaction. The EC's full decision, when published, will provide further clarity on its practical application of the tool.

Putting into practice the two-limbed test of assessing potential distortions both in the acquisition process and post-acquisition — discussed above — the [EC's press](#) release set out its view that:

- Subsidies granted by the UAE would have artificially improved the capacity of the merged entity to finance its activities in the EU and enabled it to take greater risks than its competitors. The subsidies involved an unlimited state guarantee to e& in the form of an exemption from bankruptcy law as well as funding granted to e&'s controlling sovereign wealth fund. An unlimited guarantee is one of the “categories of foreign subsidies most likely to distort the internal market” under Article 5 of the FSR.
- No distortion was identified in relation to the acquisition process on the basis that e& was the only bidder and had sufficient resources of its own for the acquisition, and because the consideration paid reflected the target's market value.

The EC approved the transaction subject to behavioural remedies. The remedies package consisted of:

- i. The removal of the state guarantee.
- ii. A prohibition of any financing from the purchaser and its controlling sovereign wealth fund to the target's activities in the EU (subject to certain exceptions) and a requirement that transactions between those companies take place at market terms.
- iii. A requirement that the purchaser informs the EC of future acquisitions even if they are not notifiable under the FSR. The commitments are valid for 10 years and can be extended.

This decision signals one possible path to clearance for state-backed purchasers which are prepared to ringfence the target's EU business activities from potentially distortive funding for at least 10 years, as well as UAE purchasers with similar state guarantees.

Encouragingly, and in contrast to the majority of remedies accepted under the parallel EU merger regulation (EUMR), the remedies do not include any structural elements. Another noteworthy aspect of the case is that the EC's decision was

delivered two and a half months before the statutory deadline (although pre-notification talks extended almost a year before the five-month formal review, as this was only the 11th case file under the FSR). This is in contrast to the EC's approach under the EUMR, where the large majority of deadlines in in-depth investigations are extended.

7. *Ex-officio* investigations highlight the broader risks for businesses

The EC has already launched two FSR investigations on its own initiative. The preliminary reviews in both cases are ongoing and, unlike the procedure following a notification, there is no fixed timeline for *ex officio* investigations. These investigations show an assertive approach by the EC in tackling perceived distortive subsidies and highlight the risks for businesses outside of large transactions and public procurement procedures.

The EC launched its first own-initiative investigation in April 2024 in relation to potential foreign subsidies affecting competition in the EU's wind power sector, focusing on Chinese wind turbine suppliers to wind farms in various member states. The EC initiated its second investigation two weeks later by carrying out its first-ever dawn raids under the FSR, targeting the Chinese security scanner company Nuctech at its premises in two member states.

8. Strategic sectors are prioritised

The EC's initial enforcement practice to date signals a focus on sectors that are relevant to the strategic objectives and policies of the EU. The EC has opened *ex officio* or in-depth investigations into the clean energy, security technology, infrastructure including transportation, and telecommunications sectors. These focus areas reflect the EU's policy objectives of the green and digital transition as well as security concerns.

9. The EC has shown heightened interest in Chinese businesses

While the FSR was designed to be country-agnostic, it is notable that the majority of the public investigations to date have targeted Chinese companies. This geographic focus reflects the EC's wider concerns about subsidized investments from Chinese businesses undercutting European competitors, and has led to increased geopolitical tensions between the EU and China.

Nonetheless, the first known FSR approval of a transaction involving a Chinese purchaser came at the start of October 2024 following a preliminary review (Haier Smart Home/Carrier's commercial refrigeration businesses), signalling that not all Chinese investments in the EU are seen as problematic. Also,

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the recently concluded in-depth M&A investigation involving a UAE-based purchaser demonstrates that the EC is ready to investigate potential subsidies granted by any non-EU country under the FSR.

10. The FSR is not a barrier in most cases

According to the EC, the FSR has not — to date — added significant complexity to M&A and public procurement processes.

For M&A transactions, once notified, the FSR investigation can usually run in parallel to any merger control and foreign direct investment processes. The single in-depth referral in the first year is in line with expectations that only a small number of M&A notifications will be found to involve distortive foreign subsidies. Furthermore, the EC's pragmatic approach to finding a path to clearance in the e&/PPF transaction shows that parties willing to cooperate with the case team can achieve a timely resolution even in cases where the EC identifies distortive state contributions. It remains to be seen, though, whether the process will be as smooth for future transactions.

The EC's approach in procurement cases is less clear, because the three in-depth procurement referrals were closed without a final decision. These cases do, however, highlight the importance of providing complete information because the EC may open an

in-depth investigation if it does not receive sufficient information initially to rule out its concerns. The bidder in the electric trains tender did not list any reportable FFCs in its initial notification, and the bidders in the solar power project tender failed to show that they would not benefit from cross-subsidization.

Looking Ahead

It now falls to the newly constituted EC to decide how to deploy the tool over the next five years. EC President Ursula von der Leyen, who was elected for a second mandate, has proposed a set of new commissioners, who are expected to be in place later this year.

President von der Leyen has asked the incoming EC to “vigorously” enforce the FSR, and senior EC officials have said that they plan to “invest more” in ex-officio investigations to enable the EC to focus its resources on the most distortive practices. Enforcement is expected to be guided by the recent report on the future of European competitiveness by Mario Draghi, commissioned by President von der Leyen, which highlights how the tool can support the EU's broader strategy to integrate decarbonisation with competitiveness by continuing to focus on areas such as cleantech and transport. The Draghi report also emphasises the need for adequate resources for the EC to effectively apply the FSR, which means that the EC is likely to continue to expand its team.

Professional Support Lawyer **Elizabeth Malik** contributed to this article