FAMILIAR TOOLS IN FOREIGN SETTINGS: PRACTICAL CONSIDERATIONS FOR COMPLYING WITH THE NEW FOREIGN SUBSIDIES REGULATION

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By Nicole Robins & Francisco Couto

The introduction of the Foreign Subsidies Regulation ("FSR") aims to address an existing regulatory gap in ensuring a level playing field in the internal market. The FSR will have far-reaching consequences for companies operating in the EU, particularly those that are planning mergers or acquisitions or engaging in large public tenders. The European Commission has highlighted that, "in substance," the FSR will be similar to state aid control. Therefore, drawing on insights from assessments in the state aid context, this article discusses the economic tools that could be used to assess whether a financial contribution from a third country confers a benefit on an undertaking. If a financial contribution is found to constitute a foreign subsidy, the Commission has indicated that an assessment of the likely distortions to competition caused by the foreign subsidy will be particularly important. In the context of the assessment of concentrations and public procurement procedures, this is likely to require relatively new theories of harm to be examined. This article therefore also discusses, from an economics perspective, how the assessment of the distortions to competition could be carried out in practice, and the possible interactions with the EU Merger Regulation (the "EUMR").

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I. INTRODUCTION

The European Commission's Foreign Subsidies Regulation ("FSR") entered into force on January 12, 2023. This new instrument gives the Commission the authority to assess the existence, and impact, of foreign subsidies provided by public entities outside the EU to companies operating within the EU. The instrument is designed to address a gap in the existing toolkit of EU state aid control, the World Trade Organization's anti-subsidy rules, and the monitoring of foreign direct investments.

Under the FSR, the Commission will be able to investigate whether distortive foreign subsidies exist in the following situations.

- **Merger control**: Companies involved in a concentration, where one or both parties have a turnover in the EU in excess of €500m, will have to notify the Commission of individual financial contributions received from third countries over the last three years, if the total amount of the financial contribution received by one of the parties exceeds €50m.[2]
- **Public procurement**: As part of the tender process for projects with an estimated value of at least €250m, the bidder and the main sub-contractors will need to disclose any financial contributions received from third countries, if the amount of the financial contributions exceeds €4m from any third country over the previous three years.[3]
- ***Ex officio* investigations**: The Commission will have the power to start investigations into specific instruments or companies where it suspects that foreign subsidies may have distortive effects on the EU market, or require ad hoc notifications for mergers or public procurement procedures below the above thresholds.[4]

The Commission can also start market investigations into certain sectors, economic activities or subsidy instruments, the findings of which may be used to support its assessment of foreign subsidies in the context of the three procedures outlined above.[5]

As of July 12, 2023, the Commission can start *ex officio* and market investigations, with the notification requirements for public procurements and concentrations applying as of October 12, 2023.[6]

The FSR is a far-reaching tool that aims to preserve a level playing field in the Single Market by limiting the potentially distortive impact of foreign subsidies on competition. However, the legislation also recognizes that not all foreign subsidies are detrimental to the Single Market, and that they can help to achieve the EU's economic and policy objectives.

If, however, the Commission deems that the foreign subsidy will cause significant distortions in the EU, it can impose behavioral or structural measures, including requirements on the beneficiary to divest certain assets. The remedies could also include the repayment of the foreign subsidy (with interest).

In light of its broad scope, the FSR is likely to have a considerable impact on large companies operating in the EU, particularly those with significant operations in countries where governments play a prominent role in the economy. In the recent responses to the Commission's Draft Implementing Regulation, which sets out the notification forms that companies would need to complete for mergers and public procurements, stakeholders have highlighted the substantial burden that the FSR places on both EU and non-EU companies. In particular, significant concerns have been raised about the reporting obligations of the FSR and that the FSR will have a "*chilling effect*" on foreign companies operating in the EU.[7]

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2 A financial contribution is defined as:"*(a) the transfer of funds or liabilities, such as capital injections, grants, loans, loan guarantees, fiscal incentives, the setting off of operating losses, compensation for financial burdens imposed by public authorities, debt forgiveness, debt to equity swaps or rescheduling; (b) the foregoing of revenue that is otherwise due, such as tax exemptions or the granting of special or exclusive rights without adequate remuneration; or (c) the provision of goods or services or the purchase of goods or services.*" See European Commission (2022), "Regulation (EU) 2022/2560 of the European Parliament and of the Council of December 14, 2022 on foreign subsidies distorting the internal market," December 14, 2022, *Official Journal of the European Union*, Articles 3 and 20. In the remainder of this article, we subsequently refer to this as the FSR.

3 Article 28 of the FSR.

4 Chapter 2 and Article 9 of the FSR.

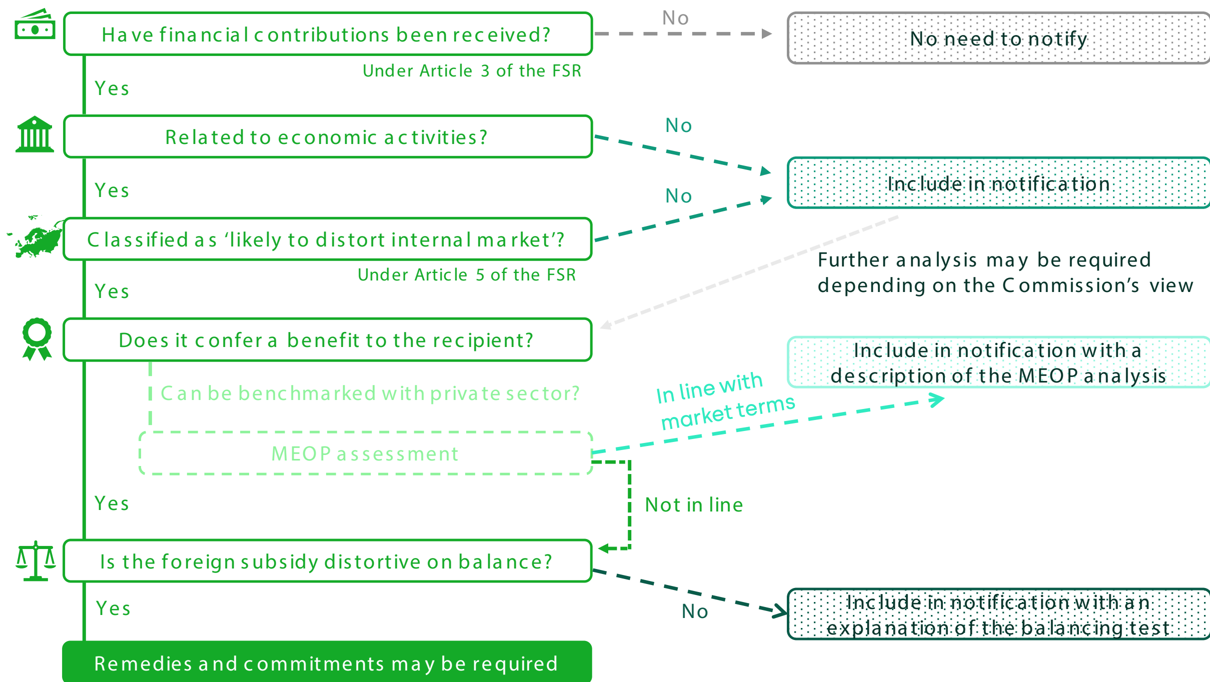
5 Chapter 5 of the FSR. Article 36 of the FSR states: "*Where the information available to the Commission substantiates a reasonable suspicion that foreign subsidies in a particular sector, for a particular type of economic activity or based on a particular subsidy instrument may distort the internal market, the Commission may conduct a market investigation into the particular sector, the particular type of economic activity or into the use of the subsidy instrument concerned.*"

6 Article 54 of the FSR.

7 Pronina, L. (2023), "EU Subsidies Rule Would Hurt Global Firms, Business Groups Warn," *Bloomberg*, 4 April; and Mackrael, K. (2023), "Intel, Raytheon, Other Big Companies Push Back on EU Subsidy Rules," *The Wall Street Journal*, March 28, 2023.

Figure 1 illustrates the different steps, from an economics perspective, that could be followed by companies engaging in large concentrations and public procurement procedures in the EU to assess any financial contributions that they might have received from third countries, in order to determine the appropriate course of action.

Figure 1: Illustration of the Steps to Assess Financial Contributions



Note: The figure provides a stylized representation from an economics perspective.
Source: Oxera, based on the FSR and the Draft Implementing Regulation.

While the Commission has highlighted that guidance on concepts that are key to the application of the FSR can be provided only over time with decisional practice, it has indicated that the application of the FSR will, "*in substance*," be similar to state aid control.[8] Therefore, in this article, drawing on insights from state aid cases, we explain the potential role for economic and financial analysis in helping to ensure compliance with the FSR. We first discuss how it could be determined whether financial contributions confer a benefit (and therefore fulfil one of the main criteria for the existence of a foreign subsidy). Secondly, as the Commission has suggested that the assessment of the impact of foreign subsidies on competition will be particularly important,[9] we set out how this assessment could be undertaken from an economics perspective.

II. DOES A FINANCIAL CONTRIBUTION CONFER A BENEFIT ON AN UNDERTAKING?

The Commission has adopted a wide definition of a financial contribution, which includes the transfer of funds (e.g. capital injections, loans), the "*foregoing of revenue*" (e.g. tax exemptions or the granting of special or exclusive rights), and the provision or purchase of goods and services.[10]

In light of its broad definition, companies could face challenges in determining whether certain measures should be classified as a financial contribution, particularly in relation to the "*foregoing of revenue*," which is considered a financial contribution only if the remuneration is not "*adequate*."[11] In order to assess whether a tax reduction or exemption received by, for example, an entity of a multinational constitutes a financial contribution, an analysis of whether the transfer pricing arrangements between the relevant entities of the multinational are on an

8 See Mlex (2023), "EU's foreign subsidies instrument must be fair and go after the 'big fish,' Vestager says," March 6, 2023; and the Commission's comments at a seminar on the FSR on February 2, 2023, available at: https://www.oxera.com/insights/events/seminar-on-the-foreign-subsidies-regulation/ (subsequently referred to as the "February 2, 2023 FSR seminar").

9 See the Commission's comments at the February 2, 2023 FSR seminar.

10 Article 3 of the FSR.

11 *Ibid.*

arm's-length basis would be required. Similarly, the assessment of whether the remuneration of special or exclusive rights is "*adequate*" would, in principle, require analysis of a market-conforming level of remuneration.

If a financial contribution is found to confer a benefit on an undertaking, under certain circumstances it will be considered a foreign subsidy.[12] The Commission highlights that the assessment of whether a financial contribution confers a benefit will depend on whether the characteristics of a given financial contribution are consistent with "*normal market conditions*," based on benchmarks from the private sector.[13] If the terms and conditions of a financial instrument are in line with those that would be available in the private sector, it is unlikely that the instrument confers a benefit. This appears to be akin to the market economy operator principle ("MEOP") in the state aid context.[14]

As companies will be required to identify which financial contributions confer a benefit, the onus will be on companies themselves to assess the contributions that fall under the categories that the Commission has identified as being potentially problematic, which include:[15]

- Support to an ailing undertaking in the absence of a comprehensive restructuring plan;
- Unlimited guarantees;
- Export financing measures;
- Support that directly facilitates a concentration;
- Support that enables an undertaking to bid for a tender with unduly advantageous conditions.
- While some financial contributions are likely to confer a benefit (e.g. unlimited guarantees), whether other instruments, such as loans or equity injections, confer a benefit is likely to need to be assessed. This could be undertaken using similar techniques to those that are used in the state aid context to apply the MEOP. However, the assessment in the FSR context could be more challenging, particularly if the financial contributions are provided by public entities from countries with less developed or transparent capital markets.

In the following sub-sections, we discuss how one could analyze whether financial instruments, such as loans and equity injections, confer a benefit. Such an assessment could be prioritized for those large financial contributions that are shown to, or are suspected to, have directly funded an acquisition or influenced a company's bid in a public tender.

A. Loans

A loan is likely to confer a benefit on an undertaking if it is provided on terms and conditions that are more favorable than the company would be able to obtain from private lenders.

If the terms and conditions of a loan provided by a third country, such as the interest rate, are in line with the company's existing commercial loans from privately owned lenders, this provides evidence that the loan does not confer a benefit.[16] Such direct benchmarking is possible if the characteristics of the loan from the third country (including the principal amount, currency, duration, level of collateral and seniority) are sufficiently comparable to those of its existing commercial loans.

However, such benchmarking may not always be possible as companies may not have an extensive portfolio of loans (or bonds), and therefore it might prove difficult to identify sufficiently comparable instruments.[17] In such cases, the terms and conditions of the loan from the third country could be compared with debt instruments from other similar companies. Such external benchmarking can be particularly useful during periods of

12 Article 3 of the FSR states that a "*foreign subsidy shall be deemed to exist where a third country provides, directly or indirectly, a financial contribution which confers a benefit on an undertaking engaging in an economic activity in the internal market and which is limited, in law or in fact, to one or more undertakings or industries." Ibid.*

13 According to the Commission, "*[a] financial contribution should be considered to confer a benefit on an undertaking if it could not have been obtained under normal market conditions. The existence of a benefit should be determined on the basis of comparative benchmarks, such as the investment practice of private investors, financing rates obtainable on the market, a comparable tax treatment, or the adequate remuneration for a given good or service. If no directly comparable benchmarks are available, existing benchmarks could be adjusted or alternative benchmarks could be established based on generally accepted assessment methods.*" European Commission (2022), op. cit., December 14, para. 13.

14 See the Commission's comments at the February 2, 2023 FSR seminar.

15 See Article 5 of the FSR.

16 Information regarding a company's existing commercial loans (and bonds) can normally be obtained from its financial statements and/or management accounts. In addition, financial data providers such as Bloomberg or Refinitiv Eikon will usually report this information.

17 For example, if a loan provided by a third country is unsecured (i.e. the company is not required to pledge collateral in case of default), it should, all else being equal, have a lower credit rating.

interest rate volatility, which may render comparisons with older instruments from the same company less reliable. However, it is important to ensure that the debt instruments that are considered are from private investors with similar characteristics to the loan provided by the third country.

Interest rates on debt instruments are influenced by country-specific and currency-specific dynamics. The interest rate on debt instruments reflects the risk-free rate (i.e. the rate that is free of default risk, which is usually proxied by yields on AAA rated government bonds), plus the additional premium required by investors for investing in risky corporate debt. In the context of the FSR, such an assessment may be challenging if the loan has been provided by a third country that does not have the AAA credit rating that is usually associated with a "risk-free" status, and where there may be limited examples of comparable debt issuance from private investors in the country. In such circumstances, the benchmarking could be based on transactions from other countries where the state may have a higher credit rating, with appropriate adjustments to reflect the additional remuneration required by investors for exposure to additional risk in the third country in question (so-called country risk).[18]

If a loan is denominated in the currency of a country with a fairly small capital market, there might be only a limited number of debt instruments in the same currency. Similarly, in countries where the state is significantly involved in the economy, the number of debt instruments issued by privately owned companies could be limited. In these circumstances, the analysis could instead be based on corporate bonds from larger capital markets, with appropriate adjustments to reflect the additional risk faced by investors in these markets. Therefore, while the context of the FSR may make such an analysis more complicated than in the state aid context (where benchmarks are more likely to be readily available), the economic toolkit could be used to apply the necessary adjustments to the available data to enable the benchmarking exercise.[19]

B. Equity Injections

In order to determine whether an equity injection confers a benefit, two questions need to be considered:

- What level of commercial return does the third country expect to obtain from providing the equity injection?
- Is the expected return sufficiently high such that a private investor operating in similar circumstances would be likely to undertake a similar investment?

If the commercial return expected by the third country is in line with, or higher than, that required by a profit-driven investor, the financial contribution is unlikely to confer a benefit. The return required by such an investor could be approximated based on the cost of equity for a similar company, which will depend on its risk exposure (with higher returns required for riskier investments) and the capital structure (as a higher share of debt financing will lead to greater risk for equity holders). The appropriate return could be estimated using the Capital Asset Pricing Model ("CAPM"), a well-established methodology that relates the expected return of an equity investment to its risk.[20] While it is not unusual for corporate finance practitioners to use the CAPM in countries with less developed capital markets, as with the assessment of the interest rate on debt instruments it is possible that investors may require an additional return for exposure to greater country risk.

In order to estimate the commercial return expected by the third country from the equity injection, it is necessary to forecast its expected cash flows. This will require an estimation of the value of the initial equity stake, any dividends expected over the period when the third country holds the equity stake, and the value of the equity when the third country expects to sell its stake. These estimates will then need to be "discounted" to their present value using the CAPM cost of equity. If the outcome from this discounting exercise (known as the net present value of an investment, or its risk-adjusted profitability) is positive, this indicates that a private sector investor would be likely to make the same equity investment in similar circumstances.

While data constraints may mean that the assessment would be more challenging in the context of the FSR than in the state aid context, as discussed above, it is possible that adjustments could be applied to the available benchmarks to tailor their applicability to the third country in question. Furthermore, a detailed assessment could be prioritized for the largest financial contributions, for which a MEOP-type defense might

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18 It is common practice for practitioners to include a measure of country risk in the estimate of the cost of debt to reflect exposure to the riskier credit profile of such governments.

19 If it can be established that the main terms and conditions of the loan provided by the third country are in line with market terms, for the largest debt instruments it might help to strengthen the evidence base by assessing whether, under a reasonable set of assumptions, the company expects to be able to service its obligations on the loan, based on reasonable cash flow projections.

20 Under the CAPM, the expected return on equity is calculated as the risk-free rate (as proxied by yields on government bonds with a AAA credit rating) plus the product of the equity risk premium and the equity beta of the company. The equity beta measures the systemic (i.e. undiversifiable) risk of the company, which is a function of the underlying risk of the company and its leverage (i.e. the extent of debt financing). The equity risk premium refers to the additional return that is required to invest in the equity market as opposed to a risk-free security.

be possible, and where there is evidence, or it might be suspected, that the financial contribution has directly affected a company's bid in the concentration or public tender. While the assessment may need to be undertaken separately for each financial contribution, there may also be instances where a company has received a number of financial contributions from a third country at a similar point in time. This might require the financial contributions to be assessed together in order to determine whether they confer a benefit in aggregate on the company in question.

III. BALANCING THE POSITIVE IMPACTS OF FOREIGN SUBSIDIES AGAINST THEIR DISTORTIONS

For those financial contributions that meet the definition of a foreign subsidy, the Commission will assess whether they create any distortions to competition in the Single Market, and particularly whether they provide an unfair advantage to a company vis-à-vis its competitors. The Commission may then balance any distortions against the potential positive effects of the foreign subsidy on the internal market.[21]

The FSR recognizes that foreign subsidies could have a beneficial effect on the economic objectives of the EU. As such, companies are required to articulate how foreign subsidies could play an important role in developing economic activities or achieving relevant policy objectives within the Single Market.[22] Examples provided by the FSR include "a high level of environmental protection and social standards, and the promotion of research and development."[23]

At this stage, it is uncertain how the Commission will assess the positive effects of foreign subsidies, as well as the threshold that it will adopt to determine what constitutes a distortion to competition. Indeed, the Commission has stated that the application of the balancing test, including how it will determine the existence of a distortion, will be "*by large, a matter of decisional practice.*"[24]

In contrast to the State aid framework, where it is usually presumed that aid will create distortions, there does not appear to be any such a priori presumption underpinning the FSR.[25] It is therefore possible that the assessment of the impact of a foreign subsidy on competition could be explored in more detail than in the state aid context. Indeed, Commissioner Vestager has highlighted that "*[t]he concept of a "distortion" is not defined in the Regulation, nor is it presumed, which means that distortions will have to be proved. This will certainly be at the core of the future enforcement […].*"[26]

The Commission highlights that the competitive distortions created by any foreign subsidy will be assessed on a case-by-case basis.[27] Such an assessment could be prioritized for those large foreign subsidies with characteristics that have been identified by the Commission as being more likely to distort competition, such as unlimited guarantees or subsidies granted to an undertaking in difficulty that is likely to exit the market in the short or medium term in the absence of the subsidy. However, in contrast to state aid control, where either an individual aid measure or a scheme covering a number of beneficiaries is being examined, in the context of the FSR it is possible that a company could have received a number of foreign subsidies.

Therefore, the analysis might need to be undertaken at an aggregate level by grouping together certain categories of subsidy. It will be important to examine the cumulative effects of foreign subsidies received by an undertaking at a similar point in time, as their combined impact may

21 Article 4 of the FSR states that "*[a] distortion in the internal market shall be deemed to exist where a foreign subsidy is liable to improve the competitive position of an undertaking in the internal market and where, in doing so, that foreign subsidy actually or potentially negatively affects competition in the internal market.*" Article 6 of the FSR goes on to state: "*[t]he Commission may, on the basis of information received, balance the negative effects of a foreign subsidy in terms of distortion in the internal market, according to Articles 4 and 5 against the positive effects on the development of the relevant subsidised economic activity on the internal market, while considering other positive effects of the foreign subsidy such as the broader positive effects in relation to the relevant policy objectives, in particular those of the Union.*"

22 Section 7 of the Draft Implementing Regulation for concentrations (section 5 in the case of public procurements) asks parties to "*list and substantiate any possible positive effects on the development of the relevant subsidised economic activity on the internal market. Please also list and substantiate any other positive effects of the foreign subsidy such as broader positive effects in relation to the relevant policy objectives, in particular those of the Union, and specify when and where those effects have or are expected to take place.*" See European Commission (2023), "Annex to the Commission Implementing Regulation (EU) …/… 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 single market."

23 Para. 21 of the FSR.

24 Mlex (2023), *op. cit.*, March 6, 2023.

25 See the Commission's comments at the February 2, 2023 FSR seminar.

26 Mlex (2023), *op. cit.*, March 6, 2023.

27 Para. 17 of the FSR.

differ from the effects arising from an individual foreign subsidy. At this stage, although the Commission has highlighted that certain indicators will be examined, such as the magnitude and nature of the foreign subsidy, it remains to be seen how the Commission will approach the assessment.[28]

While the level of detail at which the Commission may undertake the analysis remains to be seen, in the sub-sections below we present an economic framework that could be followed to assess the possible distortive effects of foreign subsidies, and we outline possible theories of harm that might need to be considered.

A. Possible Economic Framework to Assess the Distortive Effects of Foreign Subsidies

In the state aid context, the focus is on assessing the effect of a change in the beneficiary's behavior as a result of the aid received.[29] This requires the products and the relevant geographic market that might be affected by a change in the aid beneficiary's behavior, as well as the relevant competitors, to be identified. However, the relevant product and geographic markets are often not defined precisely.

In the context of the FSR, in contrast to state aid control, the competitive assessment is likely to focus on any distortions created by the foreign subsidies on concentrations or the public procurement process. In the context of concentrations, however, the Commission has indicated that it may also assess the wider implications of foreign subsidies on competition in the relevant markets.[30]

Therefore, building on the approach in state aid control, in order to assess the likely impact of foreign subsidies on competition, three steps could be followed:

- Identifying the main characteristics of the foreign subsidies and the market(s) that might be affected;
- Developing the hypotheses to be tested — i.e. the theories of harm — regarding the likely impact of the foreign subsidies on concentrations and the public procurement process, which would require a counterfactual scenario to be developed that sets out what would have been likely to occur in the absence of the subsidies;
- Assessing the actual impact of the foreign subsidies on competition relative to the counterfactual scenario.[31]

As set out below, the relevant theories of harm are likely to differ across concentrations and public procurement cases. As indicated by the Commission, in the context of the FSR, some of the theories of harm that might need to be examined might be "*relatively novel*."[32]

C. Concentrations

In cases of notified mergers, the FSR assessment will be conducted in parallel with the filing under the EU Merger Regulation ("EUMR"). While the focus of merger control tends to be on the effects of the proposed concentration on consumers (i.e. prices, quality, choice, and innovation), the assessment in the FSR context may more closely mirror state aid control by focusing on how the foreign subsidies affect the position of the beneficiary vis-à-vis its competitors.[33]

In relation to concentrations, foreign subsidies could support a prospective acquirer by enabling access to financing on more favorable terms. The relevant theories of harm will ultimately depend on the counterfactual scenario, which could include:

- Another competitor that does not receive any significant foreign subsidies purchases the target instead in those cases where there is a competitive bidding process;
- If there are no other potential buyers, and the prospective buyer cannot conduct the acquisition without the subsidies, the target company remains independent.

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28 Article 4 (1) of the FSR.

29 See European Commission (2009), "Common principles for an economic assessment of the compatibility of state aid under Article 87.3," para. 51, available at: https://ec.europa.eu/competition/state_aid/reform/economic_assessment_en.pdf.

30 See the Commission's comments at the February 2, 2023 FSR seminar.

31 In the state aid context, the impact of aid on competition is examined in more detail as part of *ex post* evaluations of aid schemes. In this context, for details regarding the economic framework, see Oxera (2017), "Ex post assessment of the impact of state aid on competition," prepared for European Commission, November, available at: https://ec.europa.eu/competition/publications/reports/kd0617275enn.pdf.

32 Crofts, L. (2023), "EU subsidy screening will see draft "implementing" rules next week," *Mlex*, February 2, 2023.

33 See the Commission's comments at the February 2, 2023 FSR seminar.

In the first case, where a prospective buyer that has not received a substantial amount of foreign subsidies would have acquired the company, the foreign subsidies significantly alter the outcome of the competitive process. However, it remains to be seen whether the Commission would consider that this represents a sufficient distortion to competition without assessing the other effects of this alternative outcome of the process, such as the differences in market shares of the main players under this outcome.

In the second case — where the target remains independent — potential theories of harm could relate to whether competition might be impeded as a result of the merger strengthening the beneficiary's market power and contributing towards, or raising, barriers to entry. In this scenario, there could be a significant overlap with the assessment under the EUMR, as the competition distortions relative to the counterfactual scenario will also depend on the nature of the merger — i.e. whether the merger is between companies operating at different levels of the supply chain (i.e. a vertical merger) or between companies operating in closely related markets (i.e. a conglomerate merger), or a combination of both.[34] It remains to be seen how the analysis and the conclusions of the assessment in the context of the FSR will interact with the EUMR assessment. For example, it is possible that the Commission might determine that the concentration is not sufficiently problematic from the perspective of the EUMR, while simultaneously concluding that foreign subsidies were instrumental in enabling the concentration, and that the concentration negatively affects competitors.

The assessment in the FSR context may be complicated due to the lack of transparency concerning foreign subsidies and the complexity of the commercial reality. For example, assume that a third country has provided funding that confers a benefit on a company, and this company is bidding to acquire an EU target. If the company benefiting from the foreign subsidies outbids competitors, its decision to purchase the company may be unrelated to the foreign subsidies that it has received. It might instead be due to its valuation of the target being significantly higher, as a result of significant synergies expected from the deal. If this is indeed the case, then any distortions to competition caused directly by the foreign subsidies should be more limited.

If, however, the company outbids competitors as a result of increased willingness to pay due to the foreign subsidies, this is more likely to distort competition. Therefore, as a result of the introduction of the FSR, there may be a need for more detailed due diligence by the bidder and the target. In particular, in cases where a company receiving foreign subsidies outbids competitors that have not received such subsidies, more detailed evidence might help to demonstrate that it is due to a significantly higher valuation (as a result of substantial expected synergies, for example), as opposed to increased willingness to pay due to the foreign subsidies (for example, by lowering the company's cost of capital).

D. Public Procurement

As the price, alongside quality and experience, are key components of any public tender, foreign subsidies can pose a risk to the Single Market if they give certain bidders an unfair advantage. In the context of public tenders, to assess the competitive effects of the foreign subsidies, it would be particularly important to identify the magnitude of the subsidies received by the bidder relative to the value of the tender. A foreign subsidy may help the beneficiary to bid at a lower price through means such as more favorable financing terms, and/or subsidized access to labor, raw materials (e.g. electricity) and technology from state-owned companies.

In this context, a possible counterfactual scenario is that the second-best bidder would have instead been awarded the project. Similar to the case with concentrations, it remains to be seen whether this would be sufficient for the Commission to conclude that the foreign subsidies have distorted competition, or whether other theories of harm, such as the impact on companies across the value chain associated with the second-highest bidder, would also need to be examined.[35]

IV. CONCLUSIONS

The FSR represents a major piece of legislation that provides the Commission with far-reaching tools to address a gap in its existing policy instruments. However, significant concerns have been raised by businesses both within and outside the EU that complying with the regulation will be complex and burdensome. While the Commission has clarified that it will only go after *"big fish,"* the Commission's priorities, particularly in relation to the use of the *ex officio* tool and market investigations, are unclear at this stage.[36]

34 It is typically considered that non-horizonal mergers are less likely to impede competition, as they do not entail the loss of direct competitors. See European Commission (2008), "Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings," *Official Journal of the European Union*, C 265/6, October 18, 2008, para. 12.

35 Users may also suffer if the firm that receives the foreign subsidies wins the project due to its cheaper bid despite the lower appraised quality.

36 Mlex (2023), op. cit., March 6, 2023.

As discussed in this article, from an economics perspective there appear to be significant parallels between the state aid framework and the FSR. However, at this stage a number of important questions are still to be addressed, such as how the Commission will assess what constitutes a significant distortion, and the type and magnitude of the positive effects that would be sufficient to outweigh any distortions. In the context of a concentration under the FSR, if the Commission deems that a foreign subsidy is distortive, and therefore requires remedies, it is not yet clear how these will be imposed, and how they would interact with any remedies required under the EUMR. These questions may only be answered in time and when guidance becomes available from the Commission.

In the meantime, it is advisable that companies that are planning mergers or acquisitions or engaging in large public procurement procedures in the EU assess whether they might have received any large financial contributions from third countries. For those large financial contributions, particularly those that fall within the Commission's "most distortive" categories, it would also be advisable to assess whether they were made on market terms. If, however, companies are aware that they have received or are receiving large "favorable" deals from third countries, it would be prudent to consider developing evidence regarding their potential positive effects on the EU market, and how these potential positive effects might outweigh any distortions to competition.

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