

Mandatory disclosures in relation to foreign subsidies distorting the EU market (EU FSR) and its impact on Middle East businesses

March 2024



In brief

Starting from 12 July 2023, with filing requirements applicable since 12 October 2023, the Foreign Subsidies Regulation (“**FSR**”) introduces mandatory notification requirements for companies who receive foreign subsidies from non-EU countries and carry out certain economic activities on the internal European Union (“**EU**”) market.

The FSR scope and application is broad and brings into its scope EU and non-EU companies who receive or have received governmental support from non-EU governments. Middle East businesses carrying out certain economic activities in the EU market must assess their readiness to comply with FSR, particularly where they have received (or are expected to receive) a foreign (non-EU) subsidy.

In detail

Background

The EU recognizes merits for both European and non-European businesses to enable a strong internal market. However, when a business (either domestic or foreign) receives subsidies from non-EU governments which, in turn, will be used during a tender process or to carry out an economic activity on the EU market, this could undermine the level playing field that may distort the internal EU market.

On the basis foreign subsidies are not currently subject to the EU State Aid rules¹, which provide for limitations and notification obligations in relation to subsidies that the public administrations of EU Member States intend to grant to businesses located in the EU, the EU identified the need to complement the EU State Aid rules and its instruments with a new tool that will address distortions caused by foreign subsidies.

In order to address these EU internal market potential disadvantages arising from foreign subsidies, the EU adopted the Regulation (EU) 2022/2560 on foreign subsidies distorting the internal market (commonly known as “**EU FSR**”). The EU FSR entered into force on 12 January 2023 with an effective implementation on 12 July 2023.

The EU FSR effectively extends the EU State Aid rules outside the EU - by introducing notification requirements in relation to specific economic activities carried out by businesses on the internal EU market - and grants the EU Commission powers of intervention to prevent and/or correct distortions caused by foreign subsidies used by businesses on the EU internal market.

What is the EU FSR and who is expected to be in scope?

The EU FSR introduces disclosure requirements for businesses operating in the EU market who receive foreign subsidies from non-EU countries. The EU FSR objective is to address distortions caused by foreign subsidies in the EU internal market by giving the EU Commission powers to review public procurement procedures and M&A activities and to carry out ex officio investigations. In the widest sense of interpretation, the EU FSR applies to foreign subsidies granted to businesses engaging in an economic activity in the EU market. This means the EU FSR applies to any business, either EU based or non-EU based, carrying out an economic activity on the EU internal market.

An economic activity, according to the EU FSR, consists (mainly) of mergers and acquisitions and joint ventures (“**Concentrations**”) and Public Procurement Procedures (“**PPP**”). Whilst an economic activity may (predominantly) consist of Concentrations and PPP, it may also include all other market situations (in-scope activities).

¹ Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union

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What is the EU FSR scope of application? (cont'd)

According to the EU FSR, a foreign subsidy shall be deemed to exist where a non-EU country provides, directly or indirectly, a financial contribution which confers a benefit to a business engaging in an economic activity in the internal EU market and which is limited, in law or in fact, to one or more business or industries ("**Foreign Subsidy**").

On this basis, Foreign Financial Contributions ("**FFC**") are identified as potential distortions to the EU internal market, and therefore, a compliance requirement arises under certain criteria.

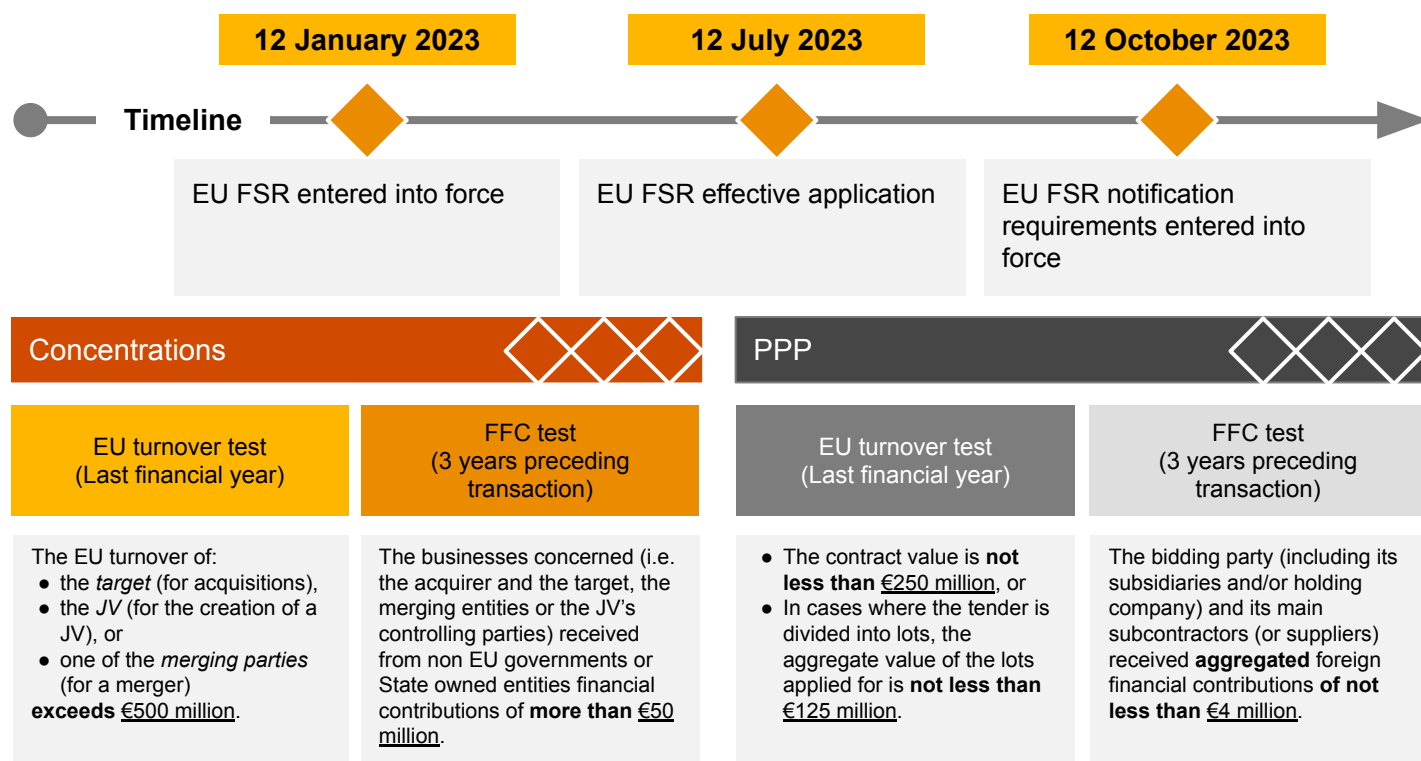
With exception to limited categories (e.g. purchases of goods/services at market terms, general, non-sector specific tax amnesty or holidays, specifically excluded categories (e.g., R&D credits)), a FFC includes, but is not limited to, subsidies of any kind (guarantees; exclusive rights without proper remuneration; grants), financial assistance (such as loans, financing, and repayable advances; risk capital instruments; equity intervention; and debt write-offs) and tax advantages (such as 'green' tax credits provided by the US Inflation Reduction Act; credits utilized under the OECD's Pillar Two global minimum tax initiative; local property tax rebates; and export-related provisions such as the US FDII regime).

Middle East businesses, direct or indirectly, carrying out an economic activity in the EU internal market by means of Concentration and/or PPP must assess to what extent they are impacted.

Timeline, penalties and related compliance obligations

Starting from 12 October 2023, businesses conducting economic activities in the EU market which, in turn, are in-scope of its application should submit a notification to the EU Commission. Businesses are expected to report detailed data generally looking back three years according to the EU Commission's formats and transmission channels.

The following diagram is a non-exhaustive simplistic representation of the potential notification triggers according to the EU FSR for Concentrations and PPP:



In relation to all other market situations, the EU FSR introduces ex officio investigations. In this regard, the EU FSR grants the EU Commission comprehensive ex officio powers of investigation for other market situations, if it suspects that a distortive foreign subsidy may be involved. The EU Commission can also request ad-hoc notifications for smaller concentrations and public procurement procedures if it suspects the existence of distortive foreign subsidies.



Investigation powers, redressive measures and penalties

Where an in-scope business does not comply with the notification requirements set out by the EU FSR, the EU Commission can, by decision, impose fines or periodic penalty payments in case of non-compliance. These fines may, depending on the type of infringement, amount to up to 10% of worldwide turnover. Financial penalties may also attract reputational risk and exposure to litigation.

Non-compliant businesses also need to be aware of the EU Commission's decisions and redressive measures under the EU FSR. For example, the EU Commission may, but not limited to, take forward any of the following actions:

- Offering access to infrastructure and equipment that were acquired or supported by the foreign subsidies,
- Reducing capacity or market presence (restriction on commercial activity),
- Refraining from certain investments, the divestment of certain assets,
- Requiring the undertakings to dissolve the merger concerned,
- Prohibit the award of contracts in PPP, or
- The repayment of the foreign subsidy.

The EU Commission will also be able to review the transaction as if it had been notified, with the possibility of prohibiting it. The procedure to investigate foreign subsidies will consist of:

- a preliminary review; and
- in-depth investigation (if there are sufficient indications of the existence of a foreign subsidy distorting the Single Market);

The EU Commission is able to look at subsidies granted 5 years prior to the start of application of the FSR when these subsidies distort the Single Market after the start of application.

EU FSR implications on businesses in the Middle East

On the basis the EU FSR brings into its scope both EU and non-EU businesses, Middle East businesses carrying (or expected to carry) out activities in the EU internal market either via Concentrations or PPP should immediately commence assessment activities targeted to identify the EU FSR potential impact.

Next steps

Businesses will need to assess the impact of EU FSR, particularly given the potential complications around this matter (e.g, impact assessment, historic data requirements identification, governance oversight, disclosure / notification requirements, etc.), and stakeholders likely to be involved involved.

1. Identify whether your business could potentially be in scope of EU FSR;
2. Where your business is (potentially) found within the EU FSR scope, conduct an impact assessment and (historic) data readiness level and availability; and
3. Prepare your business for the relevant notification requirements.

Your business can also consider the following activities to address the potential EU FSR impact:

1. Recording of financial within the group,
2. Review of all merger and acquisition projects,
3. Assessment of notification requirements for PPP, and
4. Notification procedures and / or ex officio review(s) monitoring.

The takeaway

Business carrying out activities on the EU internal market should take note and immediately implement the necessary actions to comply with the EU FSR requirements. A prompt action will allow businesses to avoid (potential) business disruptions and comply with notification requirements on a timely manner, particularly around public tenders.

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Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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