

## EU's Foreign Subsidies Check for Public Procurement Tenders Goes Live

August 7, 2023

The [Foreign Subsidies Regulation](#) (FSR), the European Union's new screening tool for third-country subsidies, introduces a novel and additional layer of scrutiny in public procurement. Companies that take part in sizeable public tenders in EU Member States need to account for the provision of significant information and the involvement of potentially time-consuming review processes in their bid strategy.

From 12 July 2023, the European Commission (EC) has the power to *ex officio* investigate potentially distortive subsidies granted by third countries. The FSR takes full effect on 12 October 2023, when participation in certain public tenders must be notified, reviewed and cleared before the relevant contracts can be awarded.

The FSR establishes mandatory notification requirements, backed by standstill obligations, and compliance is subject to potentially severe financial penalties. Notwithstanding the fact that the final [Implementing Regulation \(FSR-IR\)](#) streamlined the requirements of notification – consistent with overwhelming consultation feedback – the reporting burden on firms remains significant. Compliance with the FSR should therefore form an early and integral part of planning for participation in public procurement tenders.

### What is the purpose of the new system?

The goal of the FSR is to 'level the playing field' with respect to unfair advantages that third- country (non-EU) government subsidies may cause in the context of public tenders. The need to address foreign subsidies distorting the EU internal market is considered especially salient in public procurement procedures given the economic significance of tenders in the internal market, as well as the fact that public contracts are financed by taxpayer funds.

Before adoption of the FSR, the EU regulatory framework allowed only for the control over State aid granted by EU Member States. In particular, a contracting authority may reject a tender offer on the basis that the offer is abnormally low because the bidder had obtained illegal State aid. The FSR aims to address competitive distortions caused within the EU's internal market by foreign subsidy schemes that facilitate submission of bids that are unduly advantageous. That is a tall order and uncharted waters: Not only will the EC need to appraise the impact of foreign government subsidies in the context of a complex and disrupted global economic climate, the EC for the first time is granted direct powers to intervene in public procurement procedures held within Member States.

The FSR supplements – and will be applied in parallel to – the EU's existing regulatory toolbox for EU rules on State aid and public procurement. The FSR also includes specific rules for subsidy screening in M&A deals (see our [our M&A-related July 2023 client alert](#))

### What is in scope for review?

The FSR requires a notification if the following two thresholds are satisfied:

- The estimated value of the public procurement or framework agreement exceeds 250 million euros (net of value-added tax) or, where divided into lots, the aggregate value of the lots that the bidder applied for exceeds 125 million euros.
- The bidder (and relevant affiliates) and, where applicable, its main subcontractors and suppliers in the tender offer, was awarded aggregate financial contributions in the three years prior that exceeded 4 million euros.

If no notifiable financial contributions have been granted in the past three years, tenderers must submit a declaration to that effect. Nevertheless, the EC can request notification even if the thresholds are not satisfied to review whether a party benefitted from foreign subsidies. Lastly, similarly to the M&A procedure, the EC also may launch an ex officio investigation over a tender that has already been awarded.

Should a bidder fail to submit a notification when one is required, the EC may impose fines on bidders of up to 10% of their aggregate turnover in the preceding financial year.

## **What needs to be notified?**

A designated notification form (Form FS-PP) specifies the information to be provided about the tender, the third-country financial contributions and their possible positive effects. Business documents are also required to explain the rationale of the financial contribution. Notification is made in the first instance to the relevant contracting authority, which then transmits the notification to the EC.

Bidders are required to give detailed information for certain foreign financial contributions which are considered the 'most likely distortive'. These include:

- Subsidies provided to a bidder that is likely to go out of business in the short or medium term without the subsidy.
- Unlimited guarantees for the debts or liabilities of the bidder.
- Export financing measures not in line with the Organisation for Economic Co-operation and Development (OECD) Arrangement on Officially Supported Export Credits.
- A subsidy enabling a bidder to submit an unduly advantageous tender.

Whilst in practice the incidence of bidders being in receipt of such subsidies may be limited such that no or little detail needs to be provided, bidders are still expected to provide an overview of all other foreign financial contributions equal to or exceeding one million euros received in the preceding three years. Given the broad notion of 'foreign financial contribution' which would include measures such as direct grants, tax advantages, loans, etc. received globally, this will be a particularly onerous obligation for bidders and their sub-contractors when competing in large European procurements. As such, corporates who regularly participate in large European procurements will need to ensure that they put in place sophisticated systems capturing this information, as well as imposing clear information obligations on parties with whom they may subcontract or partner.

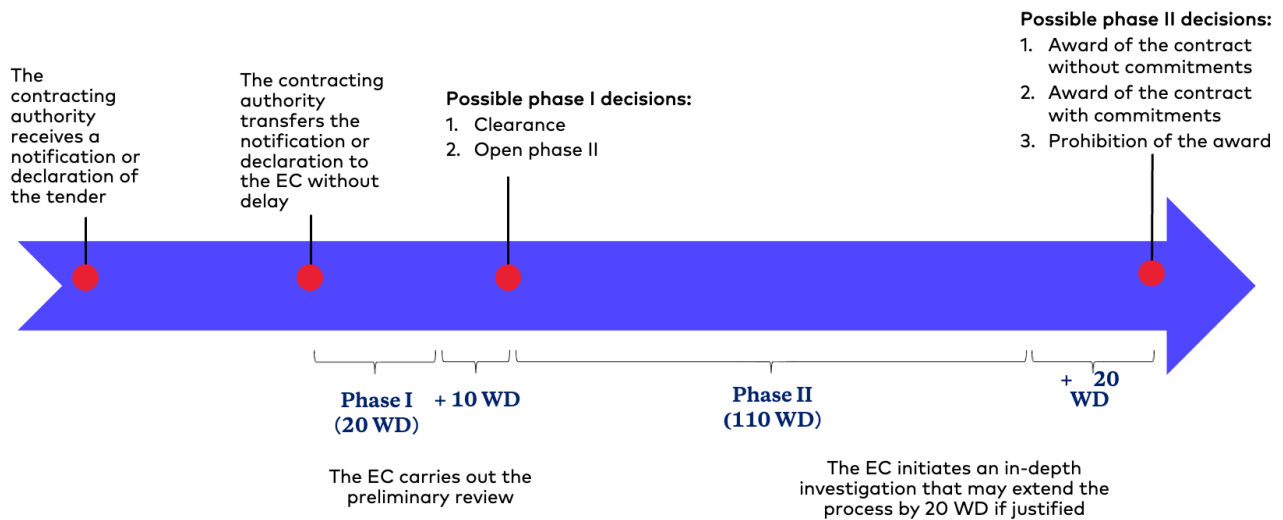
Even for tender offers that do not qualify for review, bidders must sign a declaration that the notification thresholds were not satisfied. Requests to participate in a tender process may be rejected if a bidder has not provided an FSR notification, or declaration, as part of the documentation.

## **What does the EC's review involve?**

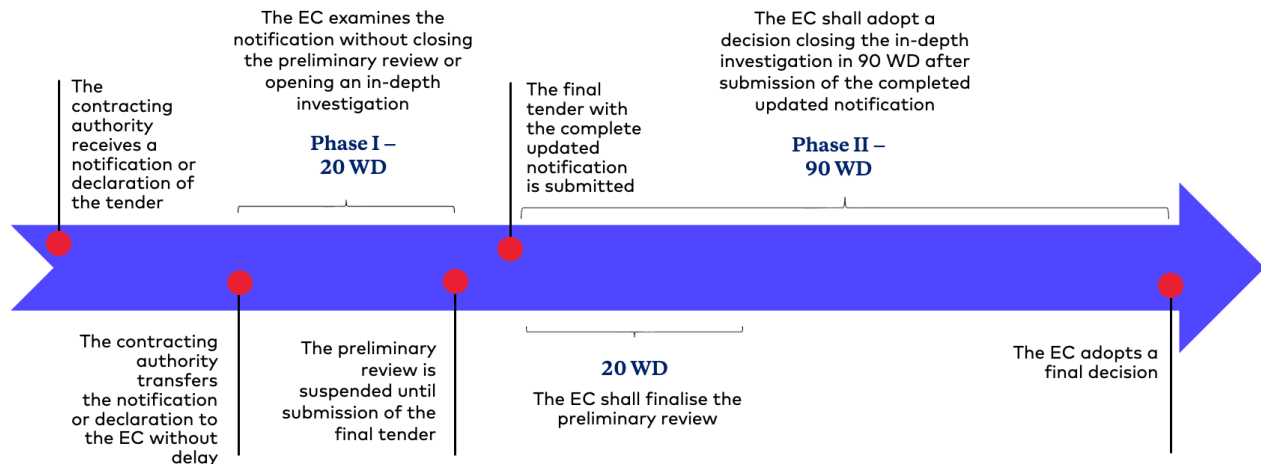
If a tender proposal satisfies the thresholds, the contracting authority must not award the contract to the relevant bidder unless and until the EC grants its approval.

The EC's review process and timeline are intended to run parallel to the public procurement procedure, although in practice the FSR

review, if instigated, may extend beyond the normal timings of a procurement procedure. An initial phase of 20 – 30 working days may be followed by a phase II review that can last up to 130 working days. Similar to the M&A process, any commitments are formally addressed only in phase II.



In a multistage procedure, the timeline changes, as the notification or declaration shall be submitted twice, first with the request to participate and then as an updated notification or declaration with the submitted tender or final tender.



The practical impact is that not only will contracting authorities have to make accommodation for potential delays to their procurement procedure, but also they may have little control over these events. Bidders should therefore anticipate longer tender procedures in large procurements. Procurement processes also are likely to commence much earlier and significantly before the expiry of existing contracts, with the impact that the term of certain public contracts may be extended beyond current typical contract durations.

### When is a third-country subsidy problematic – and is there a fix?

As mentioned, the jurisdictional and notification requirements reference third-country financial contributions. But the actual review concerns 'subsidies', meaning financial contributions by a third country that – directly or indirectly – confer benefits on a party

conducting business in the EU and are selective in the sense that they are limited as to the number of beneficiaries or industries. This is a broad notion.

A foreign subsidy is deemed to be distortive of the EU's internal market if it 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'.

This assessment depends on several factors, including the subsidy's amount, nature, purpose and any conditions attached to it. The following rules of thumb can be discerned:

No distortive effects	<ul style="list-style-type: none"><li>• The total amount is less than 200,000 euros per country over three years.</li><li>• Compensation for harm caused by natural disasters or exceptional occurrences.</li></ul>
Unlikely distortive effects	<ul style="list-style-type: none"><li>• The total amount is less than 4 million euros over three years.</li></ul>
Most likely distortive effects	<ul style="list-style-type: none"><li>• Subsidy to an ailing firm, absent a credible restructuring plan.</li><li>• Unlimited guarantees for debts or liabilities.</li><li>• Subsidy directly facilitating a concentration.</li><li>• Export financing measures.</li><li>• Subsidy enabling submission of an unduly advantageous public tender.</li></ul>

Naturally, factors pertaining to the beneficiary's situation also are important, including the competitive landscape of the markets, the sectors involved, and the nature and degree of the beneficiary's presence in the EU.

The assessment ultimately involves a balancing test between, on the one hand, the competitive advantage conferred by any distortion caused by the subsidy and, on the other hand, any positive effects for the relevant subsidized economic activity, as well as broader policy considerations. It is unclear how, in practice, the EC will conduct this assessment and how involved the relevant contracting authority will be.

The parties may propose remedies to address any actual or potential distortions arising from foreign subsidies, but formal offers may only be put forward during an in-depth review. Any remedies should be tailored to the harm and may, for instance, involve:

- Foreign subsidy repayment.
- Corporate governance commitments.
- Access or licensing commitments.
- Capacity or market presence reductions.
- Investment restraints.
- Divestment commitments.

## **Takeaways for bidders, subcontractors and suppliers**

The FSR adds complexity to the public procurement procedure. Companies that intend to take part in public bids should note that:

- The FSR applies to public procurement procedures taking place after 12 July 2023, and notifications are required for those that will take place after 12 October 2023, if jurisdictional thresholds are satisfied.
- For bidders participating in large European procurements, bidders will need to have compiled a detailed assessment of the subsidies they have received globally. Bidders are recommended to:
  - Assess their involvement in upcoming EU tenders and identify if the pipeline will involve qualifying tenders.
  - Conduct a mapping exercise of all potential subsidies received across the organization. This is likely to be a significant undertaking, and it is recommended to put in place a system for tracking the receipt of foreign subsidies and develop a detailed database to capture the necessary information. An equivalent assessment will need to be undertaken for subcontractors and bidding partners.
  - To the extent there is an existing contract with a contracting authority which may soon be expiring, or it is known that a tender is about to commence, clarify with the relevant contracting authority the impact of the FSR requirements on proposed tender timings.
  - Consider any additional compliance checklists and obligations that consortia participation – or other institutions overseeing participation in public procurement procedures – might impose in relation to foreign subsidies.
- The FSR will affect companies who rely on supply chains or consortia bidding arrangements in public procurement. Given that the EC's ability to screen extends to subcontractors, bidders who rely on bidding partners and subcontractors are likely to be more selective in their choice of partners. As a result, companies that often act as subcontractors can expect more extensive due diligence from contractual partners.
- Contracting authorities whose tenders may fall within the scope of the FSR will need to balance the requirements of the FSR with achieving their procurement objectives. This is likely to impact tender processes. For example, it is to be expected that contracting authorities may look to be more selective in reducing the bidder pool when down-selecting in multistage procurements, and bidders should anticipate enhanced requirements to provide greater transparency of pricing components in their financial models and pricing offers.
- In addition to exploiting the remedies and challenge routes prescribed under the EU's procurement directives, it can be expected that disgruntled bidders also could look to use the FSR as an alternative basis of challenge to contract awards. This is likely to extend the duration of legal challenges and may result in delays to contract awards.

For further information on the new regime and how it could impact your business, please do not hesitate to contact the authors listed below.

*Cooley trainee Athina Gaki contributed to this alert.*

## **Notes**

1. A multistage procedure is a restricted tender procedure, a competitive tender procedure with negotiation, a negotiated tender procedure without prior publication, a competitive dialogue or an innovation partnership.

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## Key Contacts

Megan Browdie Washington, DC	mbrowdie@cooley.com +1 202 728 7104
Caroline Hobson London	chobson@cooley.com +44 20 7556 4522
Alexander Israel Brussels	aisrael@cooley.com +32 2 486 7520
Jonas Koponen Brussels	jkoponen@cooley.com +32 2 486 7545
Stella Sarma Brussels	ssarma@cooley.com +32 2 486 7533

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