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DZP legal and tax alerts

Foreign subsidies and public procurement

Entry into force of foreign subsidies regulation

On 12 January 2023, the new Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market ("**Regulation 2022/2560**") came into force. Regulation 2022/2560 is directly applicable in all Member State of the European Union and covers all companies operating in the EU internal market, including those applying for public contracts.

Start of application of Regulation 2022/2560

Regulation 2022/2560 applies from 12 July 2023. From this date, the European Commission will be able to initiate proceedings ex officio to review foreign subsidies in terms of the distortions they cause in the internal market. The requirement for undertakings to notify such subsidies in the context of concentrations and public procurement will, however, arise on 12 October 2023. In the context of public procurement procedures, Regulation 2022/2560 will only apply to procedures initiated after 12 July 2023.

Foreign subsidies and public procurement

Regulation 2022/2560 applies to all economic activities in the internal market that are undertaken by undertakings benefiting from foreign subsidies.

The concept of foreign subsidies is broadly defined as financial contributions made by a third (non-EU) country that may benefit a particular undertaking or industry while distorting competition in the internal market. It is indicated only by way of example that such contributions may be capital injections, grants, loans, loan guarantees, debt forgiveness, tax exemptions, the granting of special or exclusive rights without adequate remuneration and the provision or purchase of goods and services.

Regulation 2022/2560 places particular emphasis on concentration transactions and public procurement procedures :

To ensure a level playing field throughout the internal market and consistency in the application of this Regulation, the Commission is the sole authority competent to apply this Regulation. The Commission should have the power to examine any foreign subsidy, to the extent it is in the scope of this Regulation, in

any sector of the economy on its own initiative, relying thereby on information from all available sources. To ensure effective control, in the specific case of large concentrations (mergers and acquisitions) and public procurement procedures above certain thresholds, the Commission should have the power to review foreign subsidies based on a prior notification by the undertaking to the Commission.

(preamble to Regulation 2022/2560)

In the case of public procurement, an economic operator's obligation to notify a financial contribution will arise if:

- 1) the estimated value of that public procurement or framework agreement net of VAT or a specific procurement under the dynamic purchasing system is at least EUR 250 million; and
- 2) the economic operator was granted aggregate financial contributions in the three years prior to notification of at least EUR 4 million per third country.

Financial contributions should include those received by both the economic operator and its subsidiaries without commercial autonomy, holding companies, and main subcontractors and suppliers. Under the Regulation, a subcontractor or supplier is deemed to be main where they ensure key elements of the contract and in any case where the economic share of their contribution exceeds 20 % of the value of the submitted tender.

Selected exclusions

Contracts awarded pursuant to Article 346 of the TFEU are excluded from the application of Regulation 2022/2560.

For contracts in the field of defence and security awarded under Directive 2009/81/EC, the European Commission may only initiate a foreign subsidy review procedure ex officio.

Moreover, a foreign subsidy will not distort the internal market if it is aimed at making good the damage caused by natural disasters or exceptional occurrences.

Proceedings before the European Commission

Regulation 2022/2560 introduces two types of foreign subsidy proceedings. First, the European Commission will always be able to initiate proceedings ex officio by requiring an undertaking to submit an ad hoc notification to that effect (irrespective of whether the contract is covered by or excluded from the Directives – except in cases covered by Article 346 of the TFEU). Second, as part of any public procurement procedure where the value exceeds the thresholds set, undertakings will be required, together with their tender, to notify the European Commission of all subsidies received.

Regulation 2022/2560 provides for two types of document that undertakings will have to submit:

- 1) a declaration of all foreign financial contributions received if their value does not exceed EUR 4 million, or
- 2) notification of all financial contributions if they are equal to or exceed the thresholds in Regulation 2022/2560.

The notification requirement will apply not only to individual economic operators, but also to a group of economic operators (consortium) and to the main subcontractors and suppliers known at the declaration/notification stage (documents will be submitted on their behalf by the consortium leader/economic operator).

Upon receipt of the documents, the Commission will carry out the relevant proceedings in which it will be able to (1) request the necessary information from the economic operator, (2) interview a natural or legal person and (3) carry out an inspection within or outside the EU. The Commission may also impose fines and penalty payments on economic operators that do not comply with Regulation 2022/2560 .

Proceedings will comprise two stages :

- 1) The first stage – preliminary review – to obtain all the information required for the Commission to assess whether the investigated financial contribution constitutes a foreign subsidy, may take up to 20 business days (possible extension of 10 days).
- 2) The second stage – in-depth investigation – involving a further assessment of the foreign subsidy through the measures available at the initial review stage, may take another 110 business days (possible extension of 20 days).

In total, therefore, proceedings may take 160 business days from the economic operator submitting the notification to the Commission issuing a decision.

Proceedings before the EC will end with one of three types of decision:

- 1) **Decision with commitments**, which will be issued where the EC finds that a foreign subsidy distorts competition and the economic operator offers commitments which the EC deems appropriate and sufficient to fully and effectively remedy the distortion (e.g. a commitment to reduce capacity or market presence, refrain from certain investments, make research, production or essential infrastructure available, divest certain assets or repay the subsidy).
- 2) **Decision prohibiting the award of the contract**, which will be issued where the economic operator does not offer commitments or the Commission considers that the commitments are neither appropriate nor sufficient to fully and effectively remedy the distortion .
- 3) **No objection decision**, which will be issued where the preliminary assessment as set out in the decision to initiate the in-depth investigation is not confirmed or a distortion in the internal market is outweighed by positive effects.

Pending the Commission's decision, the Contracting Authority will be able to take all actions in the procurement procedure apart from awarding the contract (signing the contract). The Commission's decision to prohibit the award of the contract will result in the rejection of the economic operator's tender and, if it was the most advantageous, in the Contracting Authority selecting the next best tender. In the case of the other two decisions, the Contracting Authority will be able to award the contract to such economic operators.

The decision taken by the Commission is of a one-off nature and will not be binding in future contract award procedures. Subsidies will be reviewed again each time.

Selected risks arising from Regulation 2022/2560

- 1) New rules that may significantly affect the course of the largest public procurement procedures in the EU (lack of experience in applying the new regulations)
- 2) Competence to assess whether the economic operator is the beneficiary of foreign subsidies distorting competition in the internal market has been delegated to an external body (the European Commission) – the contracting authority and the economic operators have limited influence on the course of the procedures laid down in Regulation 2022/2560

- 3) The broad and imprecise scope of the term "foreign subsidies" may give rise to interpretative doubts as to the scope of application of the obligations under Regulation 2022/2560 – the risk falls primarily on economic operators
- 4) The procedure to examine the impact of foreign subsidies on the internal market may be repeated several times for a given economic operator
- 5) Risk of a tender being rejected in a procedure, financial penalties or other commitments
- 6) Risks potentially extending beyond a public procurement procedure

Recommendation

We therefore recommend that entities operating in the area of public procurement in the EU analyse any financial contributions received by the undertaking from third countries over the past three years. The undertaking should include in its analysis not only the subsidies it has received, but also the financial contributions received by subsidiaries, holding companies, and main subcontractors and suppliers. We also recommend that procedures be developed to allow participation in EU procurement procedures in line with the new rules, including procedures to select consortium members, subcontractors and suppliers.

Who will my adviser be?



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