

**FOREIGN MERGER SUBSIDY DISCLOSURE ACT
Adding National Security and Trade Policy to the HSR Merger Review
Process**

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The Consolidated Appropriations Act for 2023 included a bill—the Foreign Merger Subsidy Disclosure Act (“FMSDA”)²—that adds a foreign subsidy reporting requirement to premerger notifications filed under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (“HSR Act”).³ The FMSDA is a potentially significant departure from modern U.S. antitrust enforcement policy, which heretofore has left trade policy and foreign investment issues to be addressed in other spheres.

Although there may be circumstances in which state ownership or financial support could impact competition analysis, the FMSDA appears to have been motivated more by strategic trade and security concerns than by traditional antitrust merger concerns. Moreover, unlike the EU Foreign Subsidy Regulation, which requires the disclosure of all non-EU government subsidies over a certain size, the FMSDA applies to only a handful of countries designated as posing a strategic or economic threat to the United States – specifically, China, Russia, Iran, and North Korea.

As a practical matter, the FMSDA is likely to have its greatest immediate impact on transactions involving Chinese companies, given the Chinese government’s economic plan, which includes growth through acquisitions and investments outside of China. HSR pre-merger notifications will soon likely have to disclose potentially extensive information about government subsidies to those companies.

The Foreign Merger Subsidy Disclosure Act (“FMSDA”)

The HSR Act requires parties to mergers and acquisitions in or affecting U.S. commerce and exceeding certain size-of-transaction and size-of-party thresholds to file premerger notifications with the Federal Trade Commission (“FTC”) and Department of Justice (“DOJ”). The FTC has adopted rules implementing the HSR Act that require certain information and documents to be submitted with the notification. A notified transaction cannot close until all HSR Act waiting periods have expired or

² H.R. 2617, 117th Cong. (2022) (enacted), Division GG, Title II (2022), see pp. 1151-1512, Sections 201-202 of Title II of the Merger Filing Fee Modernization Act of 2022.

³ 15 U.S.C. 18a.

been terminated. The HSR Act thus gives the FTC and DOJ a chance to review and potentially challenge large transactions before they close.

Currently, a relatively limited amount of basic information is required by the HSR premerger notification form, along with certain documents prepared by or for officers or directors of the parties to the transaction directly concerning competitive aspects of the transaction.⁴ The FMSDA requires the FTC to amend the HSR pre-merger notification rules to call for additional information and documents relating to any subsidy received by a reporting party from a “foreign entity of concern” that poses a “strategic or economic threat to United States interests.”⁵ “Subsidies” include direct subsidies, grants, loans and loan guarantees, tax concessions, preferential government procurement policies, and government ownership or control.

A foreign entity of concern is an entity identified as such in Section 40207 of the Infrastructure Investment and Jobs Act (42 U.S.C 18741(a)). In addition to other governmental and non-governmental entities flagged for national security concerns, Section 40207 defines “foreign entity of concern” to include entities owned by, controlled by, or subject to the jurisdiction or direction of, China, Russia, Iran, and North Korea.⁶

⁴ The FTC and DOJ are reportedly more broadly examining the information and documents required in an HSR notification to determine whether they are sufficient to alert the enforcement agencies to possible competitive concern. It seems likely that changes will be made beyond those required by the FMSDA.

⁵ Title II, Sect. 201(b).

⁶ Section 40207 defines a foreign entity of concern to be any entity that:

- the Secretary of State has designated as a foreign terrorist organization;
- the Department of Treasury Office of Foreign Assets Control has included on the list of “specially designated nationals and blocked persons”;
- is owned or controlled by or subject to the jurisdiction or direction of a government of a country that is a “covered nation” as defined in Section 2533c(d) of Title 10;
- is alleged by the Attorney General to have been involved in activities for which a conviction has been obtained under the Espionage Act, Economic Espionage Act, Arms Export Control Act, Atomic Energy Act, Export Control Reform Act, or the International Emergency Economic Powers Act; or
- has been determined by the Secretary of Energy, in consultation with the Secretary of Defense and the Director of National Intelligence, to be engaged in unauthorized conduct that is detrimental to U.S. national security or foreign policy.

The FMSDA is Specifically Targeted at Transactions Involving Chinese Entities

One major objective of the FMSDA is to counter China's efforts to grow the presence and strength of government-owned or supported Chinese enterprises in U.S. and global markets. The FMSDA received bi-partisan support from lawmakers calling out unfair Chinese competitive advantage resulting from Chinese government subsidies and alleged illicit acquisitions of intellectual property.⁷Sec. 201 of the FMSDA

Sen. Cotton (R-AK): "The Chinese government is attempting to gain power by manipulating the market and undercutting American businesses. Our bill will . . . allow regulators to examine whether a company may act anticompetitively because it has the backing of foreign subsidies."

Sen. Haggerty (R-TN): "Congress cannot ignore the malign actions and intellectual property theft of the Chinese Communist Party and its attempt to harm American businesses and workers. This legislation . . . gives regulators the ability to thoroughly examine the influence of foreign governments in business mergers."

Rep. Fitzgerald (R-WI): "The need for Antitrust regulators to follow the money when countries like China utilize state-owned enterprises to distort markets and harm competition is strong and immediate. . . . This legislation will give antitrust regulators the information they need to identify foreign government subsidies and act where necessary."

Rep. Stanton (D-AZ): "By modernizing our existing antitrust laws, we can ensure that businesses with government-controlled investment stakes—owned by China itself or state-sponsored allies—cannot wrongfully influence American markets and jeopardize our national security."

Rep. Speier (D-CA): "America must take seriously the risk that Chinese ownership stakes in American companies poses to American competitiveness as well as our national security. [The law] . . . will give the US government the information it needs to make informed decisions on mergers and acquisitions by Chinese State-Owned Enterprise companies that benefit from government subsidies, which our companies don't receive, and that are seeking to derail American innovation and competition in the global economy while undermining our national security and world standing."

Rep. Loudermilk (R-GA): "When countries like China subsidize businesses in order to undercut the market and gain the upper-hand through IP theft, the United States must take action to level the playing field. [The FMSDA] . . . will require the FTC and DOJ to investigate, and take into account, subsidies a business receives from a foreign government before a merger can happen."

10 U.S.C. § 2533c(d) defines "covered nation" to mean The Democratic People's Republic of North Korea, the People's Republic of China, the Russian Federation, and the Islamic Republic of Iran.

⁷ See Press Release, Office of Congressman Scott Fitzgerald, "Fitzgerald Leads Bipartisan Bill to Track Foreign Money in Mergers, available at: <https://fitzgerald.house.gov/media/press-releases/fitzgerald-leads-bipartisan-bill-track-foreign-money-mergers-0>; Press Release, Office of Senator Tom Cotton, "Cotton, Haggerty Introduce Legislation to Expose Foreign Subsidies in Merger Filings, available at: <https://www.cotton.senate.gov/news/press-releases/cotton-haggerty-introduce-legislation-to-expose-foreign-subsidies-in-merger-filings>.

(“Findings”)⁸ explains that government subsidies can distort the competitive process by enabling subsidized firms to bid higher than non-subsidized firms “or otherwise change the incentives of the firm in ways that undermine competition following an acquisition.”⁹ Subsidies are said to be “particularly problematic” when they are granted by entities that pose a strategic or economic threat to the United States.¹⁰

The Findings address Chinese government subsidies at length. First, they note that, pursuant to its Made in China 2025 Plan, the Chinese government intends to “support enterprises to carry out mergers and acquisitions (M&A), equity investment, and venture capital overseas.”¹¹ Second, the Findings cite a report of the U.S.-China Economic and Security Review Commission (“ESRC”) concluding the Chinese government subsidizes the expansion of Chinese companies in the United States and elsewhere in order to assist Chinese national champions “in surpassing and supplanting global market leaders.”¹² The ESRC’s 2020 report warned that China seeks to “surpass and displace the United States altogether,” especially with respect to emerging technologies.¹³ According to the ESRC report, as quoted in the Findings, “[f]ailure to appreciate the gravity of this challenge and defend U.S. competitiveness would be dire ... [and] risks setting back U.S. economic and technological progress for decades.”¹⁴

The ESRC was established in 2000 “to review the national security implications of trade and economic ties between the United States and the People’s Republic of China.”¹⁵ In its 2020 report, the ESRC recommended that Congress authorize the FTC to “monitor and take foreign government subsidies into account in premerger notification

⁸ “Findings and Purpose.” Title II, Sect. 201.

⁹ *Id.*, 201(a)(1).

¹⁰ *Id.*, 201(a)(2).

¹¹ *Id.*, 201(a)(3).

¹² *Id.*, 201(a)(4).

¹³ *Id.*

¹⁴ *Id.*

¹⁵ See “Charter,” U.S.-China Economic AND Security Review Commission, available at: <https://www.uscc.gov/charter>.

processes.”¹⁶ The report also recommended that the FTC develop a way to identify the extent to which proposed transactions are “facilitated by the support of government subsidies” and, with respect to specific transactions, “either propose a modification to remedy the distortion [of trade] or prohibit the transaction under Section 7 of the Clayton Act”

The ESRC report did not address whether or how the FTC or DOJ could successfully challenge transactions under the U.S. antitrust laws based on the existence or use of government subsidies. The 2020 report cites no evidence that government subsidies caused mergers or acquisitions by Chinese companies to be anticompetitive. Instead, the 2020 report cites China’s plans to expand its innovation capacity to gain competitive leadership positions in areas such as energy-efficient technologies, next-generation information technology, biotechnology, and advanced materials and manufacturing. To achieve its objectives, China is substantially funding applied research in these and other areas, financially backing national champions and encouraging foreign investment in strategic emerging Chinese industries.

The ESRC’s 2020 report also broadly referenced “legal and illicit channels for foreign technology acquisition.” As examples of illicit acquisitions, the report cites “forced technology transfer from foreign companies using the Chinese market as leverage” and “commercial espionage by Chinese government actors.”¹⁷ According to the ESRC, “U.S. workers and companies, no matter how innovative and efficient, struggle to compete when the Chinese government so decisively tilts the playing field in favor of Chinese companies through a variety of legal, regulatory, and financial mechanisms, and when U.S. companies are granted access to the Chinese market, it is at the cost of transferring valuable intellectual property to their Chinese counterparts.”¹⁸

¹⁶ See “Comprehensive List of the Commission’s Recommendations,” available at: https://www.uscc.gov/sites/default/files/2022-11/2022_Comprehensive_List_of_Recommendations.pdf.

¹⁷ See 2020 Report to Congress of the U.S.-China Economic and Security Review Commission, 43–52, 46 n.*, available at: https://www.uscc.gov/sites/default/files/2020-12/2020_Annual_Report_to_Congress.pdf.

¹⁸ *Id.* at 64.

Antitrust Enforcement Agency Support for the FMSDA

In the past, the antitrust enforcement agencies might have been expected to push back on the injection of trade policy into merger review. However, both Assistant Attorney General Jonathan Kanter and then FTC Commissioner Noah Phillips supported enacting the FMSDA.

Former FTC Commissioner Phillips is quoted in the FMSDA Findings as saying that “[o]ne area where antitrust needs to reckon with the strategic interests of other nations is when we scrutinize mergers or conduct involving” entities that are owned or controlled “to varying degrees” by the state and “often are a government tool for implementing industrial policies or to protect national security.”¹⁹

Commissioner Phillips explained his views in remarks before The Hudson Institute addressing the role of national security in antitrust enforcement.²⁰ After first acknowledging that “antitrust works best as a tool for protecting competition, and [is] an imperfect one for vindicating national security goals,” Commissioner Phillips explained that antitrust enforcers nevertheless need to consider the strategic interests of other nations when reviewing transactions or conduct involving state-owned enterprises (“SOEs”).²¹ For example, while modern antitrust analysis assumes that firms act to maximize profits, SOEs may pursue goals other than profit maximization, such as the promotion of national champions, industrial policy, or national security. Unlike a private firm, to accomplish these other goals, a SOE may be willing to sustain losses resulting from predatory pricing for an extended period or forego recoupment.²² Commissioner Phillips also noted that it can be difficult for the FTC or DOJ to determine competitive overlaps and work through complicated common

¹⁹ Title II, Sect. 201(a)(5).

²⁰ Noah Joshua Phillips, *Championing Competition: The Role of National Security in Antitrust Enforcement*, Prepared Remarks, before The Hudson Institute (Virtual) (Dec. 8, 2020), available at:

https://www.ftc.gov/system/files/documents/public_statements/1584378/championing_competition_final_12-8-20_for_posting.pdf.

²¹ *Id.* at 2; *See also id.* at 9-13 (“[T]here is no responsibility more essential for the government than the protection of its citizens. [However], like other non-competition considerations, antitrust is an imperfect tool. And, when it comes to national security, the U.S. government has other tools,” [such as CFIUS]). Of course, CFIUS does not reach foreign investment outside of the U.S.

²² *Id.* at 17-18.

ownership issues with respect to SOEs.²³ Additionally, Commissioner Phillips endorsed the ESRC’s legislative recommendation, arguing that the FTC and DOJ “should follow the money to discover potentially hidden motivations of foreign-subsidized firms playing in the U.S. economy and incorporate that assessment into their enforcement decisions.”²⁴

In testimony before the Senate Judiciary Committee in September 2022, AAG Kanter said that requiring the disclosure of government subsidies “by foreign adversaries such as China and Russia” would help the Antitrust Division protect Americans from anticompetitive behavior. In his testimony, AAG Kanter also noted that the Antitrust Division has “shown skepticism towards state-owned entities whose incentives and market activities, including proposed mergers and acquisitions, could result in increased power over global supply chains.”²⁵

For example, in August 2022, China International Marine Containers Group Co., Ltd. (“CMIC”) abandoned its proposed acquisition of Maersk Container Industry A/S and Maersk Industry Qingdao Ltd. in the face of a likely DOJ challenge. According to the DOJ, the transaction would have combined two of the world’s four largest producers of insulated container boxes and refrigerated shipping containers and resulted in the Chinese government owning or controlling over 90% of production of those products. According to the DOJ, the acquisition would have “substantially increased the risk of coordination among the remaining suppliers in the marketplace, most of whom would have been aligned through common ownership and related alliances.”²⁶

In its statement supporting passage of the FMSSA, the Executive Office of the President of the Office of Management and Budget said that

²³ *Id.* at 18-19.

²⁴ *Id.* at 19.

²⁵ See Press Release, Dep’t of Justice, “Assistant Attorney General Jonathan Kanter of the Antitrust Division Testifies Before the Senate Judiciary Committee Hearing on Competition Policy, Antitrust, and Consumer Rights” (Sep. 20, 2022), available at: <https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-testifies-senate-judiciary>.

²⁶ See Press Release, Dep’t of Justice, “Global Shipping Container Suppliers China International Marine Containers and Maersk Container Industry Abandon Merger after Justice Department Investigation” (Aug. 25, 2022), available at: www.justice.gov/opa/pr/global-shipping-container-suppliers-china-international-marine-containers-and-maersk.

requiring the disclosure of “merger subsidies by foreign adversaries like China and Russia” would help federal antitrust enforcers prevent anticompetitive transactions “through which adversaries could gain influence over important parts of the economy.”²⁷

It remains to be seen how the FTC and DOJ will wield the FMSSDA. It seems likely that a revised HSR form will require ownership information that will identify government ownership interests in the reporting parties and in other entities competing in the same and related product areas. Such information would be relevant to the traditional kind of concern that arose in the proposed CMIC matter, where the Chinese government through various interests collectively controlled a large part of relevant markets. It could also expose significant vertical relationships and interests in significant adjacent markets that would inform an antitrust analysis.

It is less clear, however, how the existence or possibility of government subsidies could be a stand-alone basis for a successful merger challenge. Under current case law, the FTC or DOJ would have to persuade the court that a transaction would enable the merged entity to substantially lessen competition. In theory, government subsidies would enable a firm to offer products or services at a price that non-subsidized competitors cannot match, and a government subsidy is not an efficiency. But even taking Commissioner Phillip’s point about the incentives and ability of a SOE to engage in predatory pricing, the government would still have to show that the SOE would likely sell at prices that would exclude rivals that are at least as efficient in a world without subsidies. What level and type of evidence would be required to move beyond pure speculation?²⁸ Presumably, it would not be sufficient to show that an SOE might invest more in R&D or emerging technology capacity without the

²⁷ See Statement of Administration Policy, H.R. 3843 – Merger Filing Fee Modernization Act of 2022, Sept. 27, 2022.

²⁸ *Cf. Cargill, Inc. v Monfort of Colorado, Inc.*, 479 U.S. 104 (1986) (considering allegations of predatory pricing in the context of competitor standing to challenge a merger, with the DOJ arguing in an amicus that the “danger of allowing a competitor to challenge an acquisition on the basis of necessarily speculative claims of post-acquisition predatory pricing far outweighs the danger that any anticompetitive merger will go unchallenged.”).

certainty of payoff in the short term, or that it may forego profits to gain share through non-predatory pricing.

Next Step: FTC to Adopt Implementing Rule

The FTC, with DOJ's concurrence, is to adopt an implementing rule specifying what information and documents will have to be submitted with the HSR notification to enable the agencies "to determine whether such acquisition may, if consummated, violate the antitrust laws."²⁹ In so doing, the FTC must consult with the Chair of the Committee on Foreign Investment in the United States, the Secretary of Commerce, the Chair of the International Trade Commission, the U.S. Trade Representative and the heads of "other appropriate agencies." There is no deadline by which the FTC must act.

Comparison to EU Foreign Subsidy Regulation

The European Commission ("EC") will also be examining the competitive effects of foreign government subsidies in merger reviews. The EU Foreign Subsidy Regulation ("FSR"), while originally motivated by concern about Chinese competitive advantage, applies to non-EU government subsidies generally (including, possibly, those resulting from the U.S. Inflation Reduction Act). According to the EC, the FSR is intended to address "distortions caused by foreign subsidies" and ensure a "level playing field" for companies operating in the European Union.³⁰

The FSR requires parties to notify the EC prior to concluding their transaction where:

- the target (in the case of an acquisition), one of the parties (in the case of a merger) or the joint venture generated EU turnover of at least 500 million Euros in the preceding financial year, and
- the acquirer and target, merging parties, or JV and its parents received foreign financial contributions cumulatively worth at

²⁹ Title II, Sect. 201(b)(2).

³⁰ See Press Release, Eur. Comm'n, "Foreign Subsidies Regulation: rules to ensure fair and open EU markets enter into force" (Jan. 12, 2023), available at: https://ec.europa.eu/commission/presscorner/detail/en/ip_23_129.

least 50 million Euros in the three years preceding the notification.

The definition of foreign financial contributions requiring notification is very broad. It covers any form of direct or indirect contribution from a non-EU government or state-owned or state-affiliated entity—including (for example), grants, loans, loan guarantees, and tax exemptions. The EC can also require notification on an *ad hoc* basis if it believes that parties to a transaction falling below the turnover and financial contribution thresholds may be benefitting from distortive foreign subsidies. With respect to concentrations, the types of foreign subsidies considered most likely to distort the market are subsidies granted to failing companies, unlimited guarantees of debts or liabilities, export financing measures not in line with the Organization for Economic Co-operation and Development (“OECD”) arrangement on officially supported export credits, and subsidies directly facilitating the scrutinized transaction.³¹

As in the EU merger control process, there is an initial 25-day Phase I review period that may be extended with an in-depth review if the EC determines that the subsidy in question may distort competition. The transaction is prohibited from closing unless and until either a determination has been made not to object or remedies have been imposed to address the alleged distortion.

The notification obligation will start to apply on October 12, 2023, although the EC can start *ex officio* investigations beginning July 12, 2023. On February 6, the EC released a draft regulation and report form for public consultation, with public comment accepted until March 6. The draft form requires the provision of extensive, detailed information about how covered transactions have been financed and the nature of foreign contributions of the type identified in Article 5(1) as being most likely to be distortive. Further guidance is expected to be issued concerning how the EC will determine whether subsidies are distortive and evaluate possible positive effects in the EU market. However, the form itself appears to place the burden on the parties to prove that any subsidies are not on balance distortive.

³¹ See “Categories of foreign subsidies most likely to distort the internal market,” Article 5(1) of Regulation (EU) 2022/2560 of the European Parliament and of the Council of Dec. 14, 2022, available at: <https://eur-lex.europa.eu/eli/reg/2022/2560/oj>.

In the United States, the subsidy review will be wrapped into the FTC or DOJ evaluation of the likely competitive effects of a transaction. It remains to be seen whether the FTC will adopt thresholds for subsidies subject to notification; what information will be required to be disclosed; under what circumstances a company not owned or controlled by a designated country will be deemed to be subject to its jurisdiction or direction; and what substantive standards or principles will guide the agencies' analysis. Unlike in the EU, US authorities must be prepared to convince a court to block a transaction based on the existence of subsidies, which could be challenging under existing antitrust merger case law.

Likely Practical Implications

The FMSDA seems unlikely to result in more or different merger challenges than otherwise would have occurred without it. Aside from potential political retaliation, the legislation's primary impact may be to deter some transactions by state-owned or controlled entities that do not want to disclose government financial arrangements. However, it is also significant for its overt use of U.S. antitrust law as a tool of trade policy.