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**COMMISSION STAFF WORKING DOCUMENT**

**IMPACT ASSESSMENT**

*Accompanying the*

**Proposal for a Regulation of the European Parliament and of the Council  
on foreign subsidies distorting the internal market**

{COM(2021) 223 final} - {SEC(2021) 182 final} - {SWD(2021) 100 final}

## Table of contents

1	INTRODUCTION: POLITICAL AND LEGAL CONTEXT.....	4
2	PROBLEM DEFINITION .....	7
2.1	Scope .....	7
2.2	Problem 1: Distortions in acquisitions .....	10
2.3	Problem 2: Distortions in public procurement .....	17
2.4	Problem 3: Other market distortions .....	21
2.5	What are the problem drivers? .....	29
2.6	How will the problem evolve? .....	34
3	WHY SHOULD THE EU ACT? .....	36
3.1	Legal basis .....	36
3.2	Subsidiarity: Necessity of EU action.....	36
3.3	Subsidiarity: Added value of EU action .....	37
4	OBJECTIVES: WHAT IS TO BE ACHIEVED? .....	37
4.1	General objectives .....	37
4.2	Specific objectives .....	37
5	WHAT ARE THE AVAILABLE POLICY OPTIONS? .....	38
5.1	What is the baseline from which options are assessed? .....	38
5.2	Options considered but discarded at an early stage.....	40
5.3	Option to be further assessed.....	43
6	WHAT ARE THE IMPACTS OF THE POLICY OPTIONS? .....	49
6.1	Problem 1 - distortions in acquisitions .....	50
6.2	Problem 2 - distortions in public procurement .....	59
6.3	Problem 3 - other market distortions .....	63
7	HOW DO THE OPTIONS COMPARE? .....	67
7.1	Problem 1 - distortions in acquisitions .....	68
7.2	Problem 2 - distortions in public procurement .....	70
7.3	Problem 3 - other market distortions .....	72
8	PREFERRED OPTION .....	74
9	HOW WILL ACTUAL IMPACTS BE MONITORED AND EVALUATED?.....	76
ANNEX 1.	PROCEDURAL INFORMATION.....	78
ANNEX 2.	STAKEHOLDER CONSULTATION SYNOPSIS REPORT .....	81
ANNEX 3.	WHO IS AFFECTED AND HOW? .....	84
ANNEX 4.	SUPPORTING DATA AND ANALYSIS FOR THE PROBLEM DEFINITION.....	87
ANNEX 5.	SUPPORTING DATA AND ANALYSIS FOR THE ASSESSMENT OF THE IMPACTS .....	102
ANNEX 6.	COMPLETE SUMMARY OF THE CONSULTATION ACTIVITIES .....	105

## Glossary

<i>Term or acronym</i>	<i>Meaning or definition</i>
AD	Anti-dumping
AS	Anti-subsidy
DG	Directorate-General
DG COMP	Directorate-General for Competition
DG GROW	Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs
DG TAXUD	Directorate-General for Taxation and Customs Union
DG TRADE	Directorate-General for Trade
EEA	European Economic Area
EFTA	European Free Trade Association
ESIA	European Semiconductor Industry Association
EU28	EU27 countries + UK
EUMR	EU Merger Regulation
FCO	German Federal Cartel Office
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
FTE	Full-time equivalent (employee)
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
GDP	Gross Domestic Product
GPA	WTO Government Procurement Agreement
GTA	Global Trade Alert
IPCEI	Important Project of Common European interest
IPI	International Procurement Instrument
MAST	Multi-Agency Support Team
NCA	National competition authorities
NTMs	Non-tariff measures
OECD	Organisation for Economic Co-operation and Development
RAG	Regional aid guidelines
RDI	Research, Development and Innovation

<i>Term or acronym</i>	<i>Meaning or definition</i>
SCM	WTO Agreement on Subsidies and Countervailing Measures
SMEs	Small and medium-sized enterprises
SOEs	State-owned enterprises
TDI	Trade defence instrument
TED	Tenders Electronic Daily
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
UNCTAD	United Nations Conference on Trade and Development
WTO	World Trade Organization

## 1 INTRODUCTION: POLITICAL AND LEGAL CONTEXT

The European Union (EU) is closely intertwined with the global economy. With trade in goods and services amounting to EUR 5 984 billion in 2019<sup>1</sup>, the EU is the world's largest trading block ahead of the United States of America (EUR 4 985 billion) and China (EUR 4 749 billion). As such, the EU accounts for 16.4% of overall global trade. The EU is also the world's leading provider and destination of foreign direct investment (FDI) with outward stocks at EUR 8 990 billion and inward stocks at EUR 7 138 billion in 2019. According to data by UNCTAD, in 2019, the EU accounted for 25% of global inward stocks and 32% of global outward FDI stocks<sup>2</sup>.

Trade is an important element of the EU economy, making up almost 35% of the EU's Gross Domestic Product (GDP) with 35 million European jobs dependent on exports. The flow of products, services and capital into and out of the EU contribute to the EU's growth by enhancing its competitiveness, creating jobs, innovation and opening up new export markets<sup>3</sup>. Trade is particularly important for Small and Medium Enterprises (SMEs), which represent 85% of all EU exporters. Openness to trade and investment is an important building block of the resilience of the economy and will contribute to the recovery from the COVID-19 crisis.

As a destination of one third of the world's investment stocks, in 2017 the EU28 was home to roughly 100 000 companies owned by foreign entities<sup>4</sup>, which employed an estimated 9 million people in the EU28. Based on the Eurostat FATS statistics, these companies had a combined turnover of more than EUR 4 trillion and produced an added value of EUR 917 billion. Overall, 16 million jobs in the EU depend on foreign direct investment<sup>5</sup>. Bringing such benefits to the EU economy, foreign investments are a welcome source of jobs, growth, and competitiveness.

A strong, open and competitive single market enables both European and foreign companies to operate and compete globally. To meet these objectives, on 10 March 2020, the European Commission presented a New Industrial Strategy for Europe<sup>6</sup>, which mapped out a path for the EU to allow its industry to lead the green and digital transitions based on competition, open markets, world-leading research and technologies and a strong single market. The EU is pursuing a model of open strategic autonomy<sup>7</sup> by shaping the system of global economic governance and developing mutually beneficial bilateral relations, while protecting the EU internal market from unfair and abusive practices.

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<sup>1</sup> DG Trade Statistical Guide, August 2020, excluding intra-EU trade.  
[https://trade.ec.europa.eu/doclib/docs/2013/may/tradoc\\_151348.pdf](https://trade.ec.europa.eu/doclib/docs/2013/may/tradoc_151348.pdf)

<sup>2</sup> UNCTAD, Division on Investment and Enterprise, World Investment Report 2020, Statistical Annex.  
[http://unctad.org/en/Pages/DIAE/World%20Investment%20Report/World\\_Investment\\_Report.aspx](http://unctad.org/en/Pages/DIAE/World%20Investment%20Report/World_Investment_Report.aspx)

<sup>3</sup> Report from the Commission on the Implementation of the Trade Policy Strategy Trade for All: Delivering a Progressive Trade Policy to Harness Globalisation. COM(2017) 491 final.

<sup>4</sup> Eurostat, Foreign Affiliates Statistics (FATS), Foreign control of enterprises by economic activity and a selection of controlling countries (from 2008 onwards) [fats\_g1a\_08]. The 100.000 figure includes the UK as part of EU28. Preliminary data shows that this figure is not likely to change significantly for EU27. In 2018, an estimated 84.000 enterprises in the EU27 were owned by foreign entities (excluding the UK), while in 2015-2017, there were around 18.000 UK-owned enterprises in other EU27 countries.

<sup>5</sup> Commission Staff Working Document: on Foreign Direct Investment in the EU, SWD(2019) 108 final. Following up on the Commission Communication "Welcoming Foreign Direct Investment while Protecting Essential Interests" of 13 September 2017.

<sup>6</sup> Communication from the Commission, "A New Industrial Strategy for Europe", COM(2020) 102 final, 10.3.2020. See also the Communication from the Commission, "The European economic and financial system: fostering openness, strength and resilience", COM(2021) 32, 19.1.2021.

<sup>7</sup> Communication from the Commission, "Europe's moment: Repair and Prepare for the Next Generation", COM(2020) 456 final, 27.5.2020. See also the Communication from the Commission, "The European economic and financial system: fostering openness, strength and resilience", COM(2021) 32, 19.1.2021.

As will be illustrated in this report, in recent years foreign subsidies appear to have had in some instances a distortive impact on EU's internal market creating an uneven playing field for companies that compete in the EU internal market. While to date there is a general lack of reliable data on subsidies granted by third countries, there is an increasing number of incidences in which foreign subsidies seem to have facilitated the acquisition of EU undertakings, influenced other investment decisions, distorted the trade in services or otherwise influenced the behaviour of their beneficiaries in the EU market, to the detriment of fair competition.

In this context, foreign subsidies can take different forms. They can for example be granted in the form of zero-interest loans, unlimited State guarantees, zero-tax agreements or dedicated State funding. Many of such foreign subsidies would be problematic if they were granted by EU Member States and assessed under EU State aid rules.

Some EU trading partners have been actively pursuing industrial policies with the declared aim of achieving global leadership in key industrial sectors. For example, the Chinese industrial strategy "Made in China 2025"<sup>8</sup> aims to make the country an industrial leader by providing favourable conditions for growth to a number of industrial and hi-tech sectors such as robotics, electric vehicles, medical equipment, aerospace, maritime and railways<sup>9</sup>. Studies indicate that public financial support is an important part of this strategy and that Chinese direct and indirect subsidies to State owned enterprises (SOEs) have amounted to 1.3 – 1.6% of annual GDP in recent years, with the total subsidy figure in fact likely being higher as private firms receive about a third of total direct subsidies (2018)<sup>10</sup>.

These are just some examples to illustrate broader policy trends such as national industrial strategies to create global champions and unilateralism. Since 2017, the EU has been actively engaged in trilateral talks with the US and Japan to improve multilateral cooperation in a number of key areas. There is a particular recognition of the need to strengthen existing WTO rules on industrial subsidies. The scope of the cooperation includes a strategy to address: "*non-market policies and practices, market-oriented conditions, industrial subsidies and state-owned enterprises, forced technology transfer policies and practices, WTO reform and digital trade and e-commerce.*"<sup>11</sup> The three Trade Ministers agreed in January 2020<sup>12</sup> on ways to strengthen existing WTO rules on industrial subsidies. In June 2018, the European Council gave the Commission a mandate "to pursue WTO modernisation in pursuit of the objectives of making the WTO more relevant and adaptive to a changing world, and strengthening the WTO's effectiveness."<sup>13</sup>

Considering the challenge to find a multilateral solution to subsidies within a reasonable time-frame, the Commission committed, as part of the New Industrial Strategy for Europe, to explore how best to strengthen the EU's anti-subsidies' mechanisms and tools.<sup>14</sup> On 17 June 2020, the

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<sup>8</sup> State Council of the People's Republic of China, Notice on issuing and distributing "Made in China 2025", "中国制造2025". 19 May 2015.

<sup>9</sup> Mercator Institute for China Studies (MERICS). Made in China 2025: The making of a high-tech superpower and consequences for industrial countries. MERICS Papers on China No.2. December 2016. <https://merics.org/sites/default/files/2020-04/Made%20in%20China%202025.pdf>

<sup>10</sup> Business Europe. The EU and China: Addressing the Systemic Challenge. A comprehensive EU strategy to rebalance the relationship with China. January 2020.

[https://www.bussinesseurope.eu/sites/buseur/files/media/reports\\_and\\_studies/2020-01-16\\_the\\_eu\\_and\\_china\\_-\\_addressing\\_the\\_systemic\\_challenge\\_-\\_full\\_paper.pdf](https://www.bussinesseurope.eu/sites/buseur/files/media/reports_and_studies/2020-01-16_the_eu_and_china_-_addressing_the_systemic_challenge_-_full_paper.pdf)

<sup>11</sup> Joint Statement of the Trilateral Meeting of the Trade Ministers of the European Union, Japan and the United States, Washington, D.C., 9 January 2019.

<sup>12</sup> Joint Statement of the Trilateral Meeting of the Trade Ministers of Japan, the United States and the European Union, Washington, D.C., 14 January.

<sup>13</sup> European Commission, Concept Paper: WTO modernisation. September 2018.

<sup>14</sup> A New Industrial Strategy for Europe, COM(2020) 102 final, 10.3.2020.

Commission adopted a White Paper on foreign subsidies<sup>15</sup> to explore the issue, launch a public debate and propose possible solutions. The White Paper, and in more detail, section 2.5 of this report, describes a legislative gap in EU trade, competition and public procurement rules, which effectively prevents the EU from taking action against certain distortions caused by foreign subsidies including distortions caused by subsidies to finance acquisitions or procurement bids. The White Paper notes that while the granting of support by EU Member State authorities is subject to EU State aid control, no comparable regime is in place for support granted by third-country authorities. This puts industry active in the EU and not receiving foreign subsidies at a disadvantage vis-à-vis beneficiaries of foreign subsidies.

Recently, several suggestions for action have been brought forward aimed at addressing the possible distortions from foreign subsidies. The Netherlands have suggested to target undertakings receiving foreign subsidies or having an unregulated dominant position in a third-country market, in order to prevent potentially disruptive behaviour.<sup>16</sup> France, Germany, Italy and Poland have called for an adaptation of the Union's competition rules, notably to take account of the possible distortions created by foreign State support and protected markets.<sup>17</sup> The German Monopolies Commission has proposed a third-country State aid instrument to address the negative effects of non-EU subsidies on the internal market.<sup>18</sup>

The issue of subsidies has also been brought forward by the co-legislators at several occasions. In the Council conclusions of 11 September 2020<sup>19</sup>, the EU Council stated that it *“looks forward, in that respect, to discussing the White Paper on levelling the playing field as regards foreign subsidies”*. This Council position was later endorsed by the Special European Council in its conclusions of 1-2 October 2020<sup>20</sup>, which called for, inter alia, *“further instruments to address the distortive effects of foreign subsidies in the Single Market”*.

The European Parliament, in its February 2020 report on competition policy<sup>21</sup>, also called on the Commission to *“investigate the option to add a pillar to EU competition law that gives the Commission appropriate investigative tools in cases where a company is deemed to have engaged in distortionary behaviour due to government subsidies or to have made excessive profits based on a dominant market position in its home country”*. In a joint letter to Executive Vice-Presidents Vestager and Dombrovskis and Commissioner Breton<sup>22</sup>, a group of 41 Members of the European Parliament have expressed a strong support for an instrument to tackle *“companies from third countries that have received substantial state support.”*

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<sup>15</sup> White Paper on levelling the playing field as regards foreign subsidies, COM(2020) 253 final, 17.6.2020.

<sup>16</sup> <https://www.permanentrepresentations.nl/documents/publications/2019/12/09/non-paper-on-level-playing-field>.

<sup>17</sup> <https://g8fip1kplyr33r3krz5b97d1-wpengine.netdna-ssl.com/wp-content/uploads/2020/02/Letter-to-Vestager.pdf>

<sup>18</sup> Biennial Report XXIII of the Monopolies Commission (“Competition 2020”)

[https://www.monopolkommission.de/images/HG23/Main\\_Report\\_XXIII\\_Chinese\\_state\\_capitalism.pdf](https://www.monopolkommission.de/images/HG23/Main_Report_XXIII_Chinese_state_capitalism.pdf)

<sup>19</sup> Council of the European Union. Conclusions on a deepened Single Market for a strong recovery and a competitive, sustainable Europe. 11 September 2020. <https://www.consilium.europa.eu/media/45641/council-conclusions-on-a-deepened-single-market-for-a-strong-recovery-and-a-competitive-sustainable-europa.pdf>

<sup>20</sup> European Council. Special meeting of the European Council (1 and 2 October 2020)

– Conclusions. 2 October 2020. <https://www.consilium.europa.eu/media/45910/021020-euco-final-conclusions.pdf>

<sup>21</sup> European Parliament. Report on competition policy – annual report 2019. A9-0022/2020. 25.2.2020.

[https://www.europarl.europa.eu/doceo/document/A-9-2020-0022\\_EN.pdf](https://www.europarl.europa.eu/doceo/document/A-9-2020-0022_EN.pdf)

<sup>22</sup> Letter to EU telecom and trade ministers and to European Commissioners Thierry Breton, Margrethe Vestager and Valdis Dombrovskis. 14.10.2020.

<https://reinhardbuetikofer.eu/2020/10/14/letter-to-eu-telecom-and-trade-ministers-and-to-european-commissioners-thierry-breton-margrethe-vestager-and-valdis-dombrovskis/>



Finally, a recent report of the European Court of Auditors<sup>23</sup> finds that certain subsidies granted by the Chinese state, if granted by an EU Member State, would constitute State aid and notes that this “*difference in treatment can distort competition in the EU’s internal market*”.

## 2 PROBLEM DEFINITION

### 2.1 Scope

Foreign subsidies are support measures provided by non-EU governments to undertakings active in the EU that can take various forms such as capital injections, grants, loans, guarantees and foregone public revenue in the form of preferential tax treatments. Foreign subsidies may confer an unfair advantage to their beneficiaries and upset the level playing field between companies in the internal market.<sup>24</sup>

Foreign subsidies, as defined above, and State aid, i.e. subsidies granted by EU Member States as defined in Article 107 TFEU, are very similar concepts. This similarity in the definitions reflects the analogous economic impact of both types of subsidies on the market. Indeed, the distortions caused by subsidies are in principle the same regardless of whether they are granted by a Member State or by a third country: if there is a market, subsidies will distort competition.

However, EU State aid control provides clear and strict rules for determining when subsidies granted by Member States are compatible with the internal market i.e. may be allowed. In particular, State aid has to be proportionate to the objective pursued. As a result, EU State aid rules minimise the competitive distortions and therefore also of negative spill over effects into third-country markets. Moreover, State aid granted explicitly to promote exports is in principle prohibited under EU State aid rules. Additionally, State aid is subject to specific transparency requirements.

Other jurisdictions do not have similar control mechanisms for the subsidies they grant. As described in Section 2.5 and in Annex 4, those foreign subsidies are also not subject to the same transparency criteria as State aid. Consequently, the risk of negative spill over effects from distortive foreign subsidies into other markets, including the EU internal market, are much higher than in case of EU State aid. This leads to an uneven playing field between undertakings operating in the EU that receive foreign subsidies and those that receive no support or compatible State aid. On the other hand, foreign subsidies may have been designed to contribute to the policy objectives of the countries that grant them. Such policy objectives, e.g. environmental protection, may in some cases coincide with those pursued by the EU. Furthermore, foreign subsidies may well only affect the domestic market of the third country concerned without spilling over into the EU internal market. Consequently, a foreign subsidy would only be problematic in the EU if it has caused, or is likely to cause, distortions in the internal market.

When determining whether a foreign subsidy is problematic, it is relevant to consider a number of conditions (or ‘indicators’), such as the type of market conduct, the size and nature of the subsidy concerned as well as the characteristics of affected market(s). Certain types of activities by subsidised companies, including different types of investments, can have a harmful impact on competition in the internal market, e.g. foreign subsidies to facilitate acquisitions or bids in public procurement tenders. Such acquisitions risk entailing the expansion of less efficient companies at the expense of more efficient non-subsidised ones.

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<sup>23</sup> European Court of Auditors. The EU’s response to China’s state-driven investment strategy, Review 03, 2020. [https://www.eca.europa.eu/Lists/ECADocuments/RW20\\_03/RW\\_EU\\_response\\_to\\_China\\_EN.pdf](https://www.eca.europa.eu/Lists/ECADocuments/RW20_03/RW_EU_response_to_China_EN.pdf)

<sup>24</sup> This brief definition effectively summarises the detailed definition of foreign subsidies provided in Annex I to the White Paper on levelling the playing field as regards foreign subsidies, COM(2020) 253 final, 17.6.2020.



Distortions of competition in the internal market can also result from participation in public procurement procedures by bidders that have received foreign subsidies enabling them to submit bids that are economically more advantageous compared to those made by non-subsidised competitors. Subsidised bidding can ultimately lead to the crowding out of more efficient unsubsidised competitors that are not able to compete on an equal footing, thereby missing out on business opportunities and losing market shares. Due to the size of certain procurement markets and the fact that already a few contract awards can give successful subsidised bidders considerable economic advantages over their competitors, this practice can be considered harmful.

Beyond specific types of activities, the size of the subsidy granted to companies needs to be taken into account when determining whether a foreign subsidy is problematic, since excessively large subsidies can be particularly distortive for competition. Likewise, the nature of the subsidy has an influence on how distortive it can be. Based on the EU's experience with enforcing EU State aid rules, an operating subsidy is more likely to cause distortions than an investment subsidy, which indicates that the former can be considered more problematic in the case of foreign subsidies as well.

Lastly, foreign subsidies can be especially problematic if they are granted to companies that operate in markets that already suffer from low levels of competition. For example, subsidies can exacerbate the malfunctioning of markets with high entry barriers and significant economies of scale. Subsidisation can further cement market concentration, thereby leading to increased profit margins and higher prices. Thus, if foreign subsidies are granted to companies that already enjoy a considerable market share in sectors with low levels of competition in the internal market, their impact is likely to be particularly harmful.

In view of the above, the problem examined in this report is centred on the distortions caused by some foreign subsidies in the EU internal market. On the basis of the data in sections 2.2 to 2.4, these distortions fall in three categories:

- Distortions in the acquisition<sup>25</sup> of EU undertakings,
- Distortions in the area of EU public procurement, and
- Other market distortions

Most submissions to the public consultation on the White Paper and the targeted consultation<sup>26</sup> confirmed the concerns that some foreign subsidies distort the internal market.

Most Member State authorities, with the exception of three who requested more information on distortions, supported the problem definition as described by the Commission in the White Paper. A large majority of Member States also agreed that foreign subsidies may have a distortive effect in general market situations (i.e. beyond acquisitions and public tenders).

As far as other EU stakeholders are concerned, almost all<sup>27</sup> agree that foreign subsidies cause or could cause distortions in the internal market. Some stakeholders<sup>28</sup> put forward examples of

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<sup>25</sup> The EU Merger Regulation uses the term 'concentration' while the present document refers to the more commonly used term 'acquisition'

<sup>26</sup> See for the individual contributions here:

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html) and for the summaries see Annex 6 to this report.

<sup>27</sup> This includes the numerous industry associations, business associations, companies, NGOs and research institutes that replied to the public consultation. See e.g. the contributions of IW, Institut der deutschen Wirtschaft, European Aluminium, Fédération nationale des Travaux Publics (FNTP), available here: [https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

cases, especially of distortions in acquisitions or public procurement procedures, which will be addressed further in this report. Others<sup>29</sup>, however, specify that it is difficult to provide concrete examples of cases where such distortions have materialised since reliable information on foreign subsidies is difficult to obtain.

Non-EU stakeholders were generally more critical of the existence of a problem and the need to act.<sup>30</sup> On the other hand, there are also some non-EU stakeholders<sup>31</sup> recognising that foreign subsidies may indeed create distortions on the EU internal market.

As will be described in more detail in sections 2.2 to 2.4, various stakeholders pointed to issues in specific economic sectors: steel and aluminium sector, aviation, railways (especially in the context of public procurement for infrastructure), oil and gas, and semiconductors. More specific stakeholder feedback will be referred to below in the context of the individual examples of sectors and case studies.

Prior to discussing each problem, it has to be emphasised that data on foreign subsidies are currently not systematically collected – neither in the EU nor in third countries. This has to do with the fact that in most third countries there is a lack of transparency for subsidies granted by public authorities. In the absence of regulation, there are few incentives for companies or public authorities alike to make subsidies more transparent.

As highlighted in the introduction, the only international organisation which tracks certain subsidies (for trade in goods) is the WTO, but also in this case the data is not complete because WTO Members do not always comply with the notification obligation. Several other organisations have attempted to track subsidies outside of the EU. At the national level, Good Jobs First, a US NGO, has for instances created an overview of subsidy schemes and individual subsidies in the United States (at both the state and federal level).

At the global level, the Global Trade Alert (GTA) attempts to track subsidies more systematically across countries – the data contain subsidy schemes and individual awards but do not measure the impact of such subsidies. The IMF has carried out research on subsidies especially regarding subsidies granted as a reaction to the Covid-19 pandemic. As will be explained in more detail under problem 3, additional databases exist that track subsidies as part of broader categories (e.g., data collected by World Bank on state expenditure). In addition to the limited availability of data, there are significant methodological challenges when it comes to the definition of subsidies. In any event, even if there were an effective system to track subsidies in third countries, there would be a need to establish their potential link to the internal market.

As regards information on distortions caused by subsidies, several OECD studies<sup>32</sup> have attempted to quantify market and sector specific distortions. In a report on government distortions

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<sup>28</sup> See, among others, the submissions of Aegis Europe, Académie de l'Air et de l'Espace, European Construction Industry Federation (FIEC), accessible here :

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

<sup>29</sup> See e.g. the contribution of Andrea Biondi of King's College London, available here:

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

<sup>30</sup> See, among others, an anonymous submission to the public consultation or the submission of the China Chamber of Commerce to the EU.

<sup>31</sup> See e.g. the contributions of (UK-based) European Competition Lawyers Forum (ECLF) or Information Technology and Innovation Foundation available here:

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

<sup>32</sup> OECD, “Measuring distortions in international markets: The semiconductor value chain”, OECD Trade Policy Papers, No. 234, OECD Publishing, 2019, Paris. OECD, “Measuring distortions in international markets: the aluminium value chain”, OECD Trade Policy Papers, No. 218, OECD Publishing, Paris. OECD, Subsidies in the steel sector: A stocktaking note, 2017, DSTI/SC(2017)11.

in the semiconductors industry, the OECD finds that investment incentives, in particular preferential tax treatment in non-EU countries, distort trade and competition in the relevant markets and might lead to a diversion of investments to less efficient locations.

To sum up, there is evidence of the existence and impact of foreign subsidies, but it is sketchy and scattered across countries and sectors. To address these shortcomings, the Commission has compiled several case studies for each of the three problem areas. The case studies show that non-EU companies with significant links to the internal market have received financial contributions from non-EU public authorities, for example through loans not granted on market terms. The case studies illustrate that foreign subsidies can be traced back for instance by analysing annual reports of publicly listed companies which sometimes list the financial contributions they receive from public authorities. In other cases, specific legislative acts passed in third countries, which institute subsidy schemes or individual payments, can point towards subsidisation. However, these case studies have limitations. In order to confirm that the identified financial contributions have indeed conferred a benefit on the beneficiaries and distorted the internal market, a more detailed investigation based on more advanced investigative tools would be necessary.

## 2.2 Problem 1: Distortions in acquisitions

This subsection will describe the market distortions caused by foreign subsidies in cases when they facilitate the acquisition of EU companies ('subsidised acquisition'). The findings of this section can also partially be applied to the other two problems. The discussion below differentiates between short and long run effects of subsidised acquisitions (and investments more broadly) on producers and consumers in the internal market. The discussion first focuses on effects on producers before proceeding with effects on consumers.

At first glance, it seems that some market players active in the internal market benefit from foreign subsidies. According to some studies<sup>33</sup>, one potential short-run consequence of subsidisation is that subsidised companies may overpay for their acquisitions ('acquisition premiums'). Therefore, it logically follows that sellers of companies in the internal market can benefit financially from inflated purchase prices. However, potentially more efficient competitors of the subsidised acquiring company would be crowded out from the acquisition process. As highlighted by Hufbauer and co-authors<sup>34</sup>, this has to do with the 'soft' budget constraint of public authorities that subsidise companies investing abroad: public authorities can provide funding to companies below market rates or directly support an acquisition through equity participation. In contrast, non-subsidised companies face 'harder' budget constraints when they try to raise funds to finance acquisitions.<sup>35</sup> This crowding out effect is likely to outweigh any benefits for producers associated with reaping acquisitions premiums, i.e., the negative impact of foreign subsidies on companies in the internal market is more significant than any positive effects.

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<sup>33</sup> Hufbauer, Gary, Thomas Moll, and Luca Rubini. "Investment subsidies for cross-border M&A: trends and policy implications." *United States Council Foundation, Occasional Paper 2* (2008), p. 9.

For evidence on higher acquisition premiums: Guo, Wenxin, Joseph A. Clougherty, and Tomaso Duso. "Why are Chinese MNEs not financially competitive in cross-border acquisitions? The role of state ownership." *Long Range Planning* 49, no. 5 (2016): 614-631. The sample of this paper mostly relies on acquisition cases from Australia and Canada. Other studies have not found systematic acquisition premiums when analysing Chinese overseas acquisitions: Fuest, Clemens, Felix Hugger, Samina Sultan, and Jing Xing. *What Drives Chinese Overseas M&A Investment? Evidence from Micro Data*. No. 33. EconPol Working Paper, 2019.

<sup>34</sup> Hufbauer, Gary, Thomas Moll, and Luca Rubini. "Investment subsidies for cross-border M&A: trends and policy implications." *United States Council Foundation, Occasional Paper 2* (2008), p. 9.

<sup>35</sup> *Ibid.*

Whilst one might argue that the negative effect of overbidding might be limited in the short run, it can seriously harm the functioning of the internal market in the long run. For example, overbidding can also deter non-subsidised companies from engaging in acquisitions more generally, which would limit their opportunities to grow in scale through acquisitions. The existence of this problem in the internal market has been confirmed by a recent publication<sup>36</sup> that points out that the EU FDI screening regulation does not address the problem of subsidised acquisitions, which according to the author gives subsidised companies from third countries an unfair advantage. As described above, the paper also points to the issue of distorted acquisition prices that can occur as a result of subsidised acquisitions. Germany, France, and Italy had pointed out this problem during the negotiation process of the EU FDI Regulation.<sup>37</sup> In a similar vein, several studies<sup>38</sup> have pointed out that in the long run, subsidised acquisitions can lead to an expansion of less efficient subsidised companies at the expense of more efficient non-subsidised ones.

Subsidised acquisitions may also help companies to gain easier access to cutting-edge technologies. Some analysts have attributed the strategic use of subsidised acquisitions to the Chinese government which, as part of the Made in China strategy, encourages and supports Chinese investments abroad in the high-growth technology sector.<sup>39</sup> In general, the relevant literature suggests that subsidies granted by countries to encourage foreign investment abroad, especially in so-called “developmental” states, are likely to be widespread and focus on specific firms and sectors as well as specific host countries.<sup>40</sup> In addition, studies have established that an uneven playing field due to subsidisation may ultimately lead to increasing market concentration<sup>41</sup>, which increases risks for anticompetitive outcomes such as increased margins and higher prices.<sup>42</sup> This problem is further exacerbated by an uncontested position of some companies in their home markets.

The latter point already indicates the potential long-run effect of foreign-subsidised acquisitions (and investments more broadly) on consumers. In the short run, though, foreign subsidies could be seen as beneficial for consumers, as the subsidised company’s increased financial strength could allow it to offer cheaper prices for relevant goods or services than its non-subsidised competitors. This effect has been documented by a recent merger control decision of the German Bundeskartellamt (Federal Cartel Office, FCO) which is detailed in the case study boxes below (Example 2, Problem 1). In a nutshell, the decision points out that in the short run low pricing strategies are ‘inherently competitive’ and therefore benefit consumers.<sup>43</sup> But in order to improve competition and foster innovation, such low pricing strategies would need to be grounded on comparative cost advantages of the company concerned vis-à-vis its competitors – if, however,

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<sup>36</sup> Bismuth, Régis. "Screening the Commission's Regulation Proposal Establishing a Framework for Screening FDI into the EU." *European Investment Law and Arbitration Review Online* 3, no. 1 (2018), p. 48.

<sup>37</sup> *Ibid*, p. 58.

<sup>38</sup> E.g., Schwartz, Gerd, and Benedict Clements. "Government subsidies." *Journal of Economic Surveys* 13, no. 2 (1999): 129-130.

<sup>39</sup> Felbermayr, Gabriel, Moritz Goldbeck, and Alexander-Nikolai Sandkamp. "Feindliche Übernahme? Chinas Auslandsinvestitionen unter der Lupe." *ifo Schnelldienst* 72, no. 08 (2019): p. 32.

<sup>40</sup> Florian Becker-Ritterspach, Maria L. Allen, Knut Lange and Matthew M. C. Allen, UNCTAD, “Home-country measures to support outward foreign direct investment: variation and consequences”, [https://unctad.org/system/files/official-document/diaeia2019d1a3\\_en.pdf](https://unctad.org/system/files/official-document/diaeia2019d1a3_en.pdf)

<sup>41</sup> Chinese state capitalism: A challenge for the European market economy”, German Monopolies Commission, July 2019, p. 17.

<sup>42</sup> Hovenkamp, Herbert, and Fiona M. Scott Morton. "Framing the Chicago School of antitrust analysis." *U of Penn, Inst for Law & Econ Research Paper* 19-44 (2020), p. 16.

<sup>43</sup> Bundeskartellamt (B4-115/19) English Case Summary of 27 April 2020, p. 6.

the low pricing strategies are a result of systematic subsidisation, they can distort competition and lead to serious market distortions in the long run.<sup>44</sup>

In practice, both EU and non-EU companies operating in the internal market *without* receiving subsidies risk being crowded out by non-EU subsidised investments. As indicated above, by tilting the level playing field, subsidies contribute to the consolidation of markets and thereby allow beneficiaries to more easily attain dominant positions, especially in markets with high economies of scale and relevant entry barriers. After having attained a dominant position, subsidised companies can use their financial strength to engage in predatory pricing (or ‘dumping’) which further consolidates their position and pushes non-subsidised competitors out of the market.<sup>45</sup> This might eventually negatively affect consumers – provided subsidised companies used their dominant position to increase prices.<sup>46</sup> Altogether, in the long run, foreign subsidies are thus likely to have a negative impact on both producers and consumers alike in the internal market.

It seems reasonable to assume that low pricing strategies could also be leveraged during public procurement procedures to undercut rival bidders or as part of general market distortions. In contrast to greenfield investments, which often require years before they become operational, subsidised acquisitions allow companies to gain a foothold in the internal market more swiftly, which is why subsidised acquisitions can be deemed to be particularly harmful.

A subsidies-induced distortion of competition might have further knock-on effects or ‘indirect’ effects on other policy areas. For example, subsidised companies might shift production facilities abroad after having acquired companies in the internal market, which could affect labour markets in the EU.

Outside of the EU, the idea of regulating the harmful impact of subsidised acquisitions has been discussed in a paper which has been submitted to the US-China Economic and Security Review Commission. The paper highlights that subsidised acquisitions can have adverse consequences for non-subsidised companies in the relevant market.<sup>47</sup> Furthermore, the paper identifies several examples of foreign subsidised acquisitions of US targets, thereby demonstrating that subsidised acquisitions may not only affect the EU internal market.<sup>48</sup> There is currently a discussion in the US on whether rules on foreign-subsidised acquisitions should be adopted. The US-China Economic and Security Review Commission recommended Congress to adopt a foreign subsidy review in its 2020 Report to Congress.<sup>49</sup>

### Case studies

The following case studies illustrate how foreign subsidies may have distorted the acquisition of EU companies. It should be noted that without appropriate investigative tools, it cannot be determined with certainty to what extent the various financial contributions can be qualified as subsidies and whether these funds were used to facilitate the acquisitions of the EU undertakings

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<sup>44</sup> Ibid.

<sup>45</sup> Forsyth, Peter, and Cathal Guiomard. "The economic approach to subsidies for foreign airlines." *Journal of Air Transport Management* 74 (2019): 47-53.

<sup>46</sup> Ibid.

<sup>47</sup> Hufbauer, Gary, Thomas Moll, and Luca Rubini. "Investment subsidies for cross-border M&A: trends and policy implications." *United States Council Foundation, Occasional Paper 2* (2008), p. 1.

<sup>48</sup> Hufbauer and co-authors refer to (attempted) acquisitions from China National Overseas Oil Corporation (CNOOC), Korean-based Doosan Infracore, and Dubai Ports World in the US. CNOOC’s bid also provides evidence of attempted outbidding of private investors, as Unocal, the target of CNOOC’s bid, had already accepted Chevron’s lower offer. CNOOC’s bid ultimately failed due to an intervention to stop the acquisition from the Chinese side (see pp. 3-4, supra note 101).

<sup>49</sup> [https://www.uscc.gov/sites/default/files/2020-12/2020\\_Annual\\_Report\\_to\\_Congress.pdf](https://www.uscc.gov/sites/default/files/2020-12/2020_Annual_Report_to_Congress.pdf)



concerned. The case studies, however, give a clear indication of the potential of foreign subsidies to distort the internal market through subsidised acquisitions.

These case studies also show that potentially subsidised acquisitions are not confined to specific sectors. Some sectors, however, seem to be particularly affected. Among these are the steel, aluminium and semiconductor sectors, which have also been analysed in-depth by the OECD<sup>50</sup> and pointed out by respondents to the public consultation.

#### Example 1, Problem 1: CNCC/Pirelli

In 2015, China National Chemical Corporation (ChemChina) acquired Pirelli, via its subsidiary - the China National Tyre and Rubber Company (CNRC).

In 2018 the European Commission stated in the final decision of an anti-subsidy investigation<sup>51</sup> that CNRC had benefited from several interventions by the Chinese State as the company did not have sufficient own funds to finance the acquisition. The most relevant support measures are listed below:

\* CNRC received a grant of RMB 500m (around EUR 66m) from the Central SASAC (State-owned Assets Supervision and Administration Commission of the State Council) to promote global production capacity cooperation under the Belt and Road Initiative (BRI).

\* CNRC received an EUR 800m preferential loan from a bank consortium, including China Development Bank (state-owned), EXIM Bank (subordinated to the State Council) and China Construction Bank (state-owned). The loan agreement mentions as purpose of the loan the acquisition of Pirelli.

\* CNRC also received a RMB 17m (approx. EUR 2.13m) refund of the interest paid on the loan mentioned above. This refund was granted by the Ministry of Finance for the acquisition of Pirelli's stock rights, as part of the key projects of 2015 special funds for the development of foreign trade.

\* The Government of China also participated in the acquisition of the stake in Pirelli by providing an equity participation worth EUR 533m via Silk Road Fund (SRF), a government investment fund that is part of the Belt and Road Initiative. The investment of SRF corresponded exactly to the amount that was needed by CNRC to gain an absolute majority ownership in the Pirelli Group (65% versus 48.75% without SRF).

As there was no suitable EU instrument, no further investigation of the potential subsidy or its impact took place.

#### Example 2, Problem 1: CRRC/Vossloh Locomotives

Vossloh is a leading rail technology company focussed on rail infrastructure with sales of EUR 916 million and approx. 3,786 employees.<sup>52</sup>

Vossloh attempted to sell its business unit locomotives since 2014 and did not invest in new technologies since then.<sup>53</sup> The business unit locomotives (Vossloh Locomotives) consists of the manufacturing of shunting locomotives and is the market leader in Europe: Vossloh's market shares amounted to 40-50% in

<sup>50</sup> OECD, "Measuring distortions in international markets: The semiconductor value chain", OECD Trade Policy Papers, No. 234, OECD Publishing, 2019, Paris. OECD, "Measuring distortions in international markets: the aluminium value chain", OECD Trade Policy Papers, No. 218, OECD Publishing, Paris. OECD, Subsidies in the steel sector: A stocktaking note, 2017, DSTI/SC(2017)11.

<sup>51</sup> See European Commission Implementing Regulation 2018/1690.

<sup>52</sup> <https://www.vossloh.com/en/company/vossloh-at-a-glance/>

<sup>53</sup> Bundeskartellamt (B4-115/19) English Case Summary of 27 April 2020, p. 1.

[https://www.bundeskartellamt.de/SharedDocs/Entscheidung/EN/Fallberichte/Fusionskontrolle/2020/B4-115-19.pdf?\\_\\_blob=publicationFile&v=5](https://www.bundeskartellamt.de/SharedDocs/Entscheidung/EN/Fallberichte/Fusionskontrolle/2020/B4-115-19.pdf?__blob=publicationFile&v=5)

past years.<sup>54</sup> Shunting locomotives are used by railway undertakings and industrial operators to load wagons in e.g. major industrial installations. In some cases, shunting locomotives are also used on the public rail network, for example to transport wagons from one site to another.<sup>55</sup>

CRRC Zhuzhou Locomotives (the acquirer) is a subsidiary of CRRC Corporation (CRRC). CRRC is listed and is 51 % owned by the Chinese State. CRRC is the world's largest manufacturer of rolling stock.<sup>56</sup>

CRRC benefits from Chinese government subsidies. For example, the company openly reports subsidies of around EUR 75 million in its 2018 annual report.<sup>57</sup> It also receives significant financing from state-owned banks (while no details are known on the actual terms).<sup>58</sup> The merger decision of the German competition authority states that CRRC was using favourable prices to expand its position on foreign markets based on orders for shunting locomotives from several railway companies in the EU.<sup>59</sup>

On 26 August 2019, Vossloh signed the contract to sell its locomotives business unit to CRRC Zhuzhou Locomotive. The agreed purchase price is confidential. By decision of 27 April 2020, the German Federal Cartel Office (FCO) cleared the acquisition unconditionally.<sup>60</sup>

The FCO notes that *“as a state-owned company subsidised in the context of two important strategic plans of China – namely “Made in China 2025” and “Belt and Road Initiative” – CRRC’s access to financial resources is exceptional.”*<sup>61</sup> It further notes: *“CRRC indeed enjoys advantages due to receiving state subsidies” and “for the assessment of CRRC’s scope of action, the fact that granting a loan in China is an important instrument to provide financial resources to state-owned companies is also significant. The Chinese banking sector is characterised by a large share of state-owned banks, which are used strategically to achieve the goals set by state planning by, for example, financing state-owned (sister) companies regardless of their financial situation and the associated credit risk with loans at interests rates that are not in line with the market.”*

In spite of these favourable financial conditions for CRRC, the FCO could not directly take into account in the assessment of the acquisition to what extent support from the Chinese authorities was instrumental in acquiring Vossloh's business, nor whether any such subsidies would support Vossloh's locomotive business in the future. Such considerations are outside the mandate of the competitive assessment of acquisitions which is focused on the probability of the merger leading to a dominant position.

Nonetheless, the FCO hinted at the potential influence of foreign subsidies on the future business of the acquired company:

*“Against this background, CRRC has extensive possibilities for implementing low-price strategies. Based on CRRC’s previous behaviour in foreign markets and also internal documents, it can be concluded that CRRC strategically uses low prices in order to expand its market position in foreign markets. This is indicated, for one thing, by the ordered shunters CRRC sold to DB and the Hungarian RCH, and, for another, by individual locomotive and railcar contracts concluded in other European countries. In addition, over the past years CRRC has won numerous important tender procedures relating to metro trains in the USA by offering particularly low prices.”*<sup>62</sup>

Annex 4, Section 1 contains four additional case studies in which there are indications that the acquirers of EU targets may have received foreign subsidies facilitating these acquisitions. In

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<sup>54</sup> Ibid, p. 7.

<sup>55</sup> Ibid, p. 2.

<sup>56</sup> Ibid, p. 1.

<sup>57</sup> Ibid, p. 6.

<sup>58</sup> Ibid, p. 6.

<sup>59</sup> Ibid, pp. 6-7.

<sup>60</sup> Ibid, pp.7-9.

<sup>61</sup> Ibid, p. 6.

<sup>62</sup> Ibid, p. 7.



these examples, the acquirers benefited from equity injections, grants or loans by public bodies that may qualify as subsidies.

#### General context of foreign subsidisation of acquisitions

Due to the general lack of reliable data on subsidies in many third countries, this section uses alternative methods to indicate the potential amount and origin of foreign subsidies. Notably, whilst foreign subsidies do not necessarily go hand in hand with foreign ownership of the beneficiaries, this section uses foreign ownership as a proxy to indicate which beneficiaries may potentially benefit from foreign subsidies. Such a proxy has also been proposed by other reports.<sup>63</sup> Other proxies such as acquisition premiums paid by acquiring companies could in principle be used, but would require in-depth knowledge of the specific cases and the relevant markets, which are not available in the absence of an investigative tool.

There are detailed data about the total value and the numbers of non-EU acquisitions by country of origin.<sup>64</sup> When ranked by *value*, the US, the UK and Switzerland account for the majority of third country acquisitions in the EU. A similar pattern emerges when the *number* of acquisitions is considered (see Figure 1 and Table 1 below). Following the US, UK and Switzerland, Chinese acquirers have gained in importance. As regards the latter, recent research from the Rhodium Group and the Mercator Institute for China Studies finds that the value of Chinese acquisitions was between 2000 and 2010 on average well below one billion EUR per year.<sup>65</sup> In the meantime, China has become the fourth biggest acquirer of EU undertakings, with acquisition values peaking at almost EUR 20 billion in 2016.<sup>66</sup> Chinese FDI into the EU is largely driven by acquisitions, which account for 95 per cent of Chinese FDI in the EU.<sup>68</sup> ‘Direct government financing’ is a particularly important feature of Chinese overseas acquisitions as noted by a recent study from the Rhodium Group, the Mercator Institute and the Bertelsmann Foundation.<sup>69</sup>

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<sup>63</sup> This appears to be the case for Chinese SOEs but also Chinese private companies that are meant to safeguard China’s competitiveness in key sectors and serve as a main driver of China’s economic growth (“Chinese state capitalism: A challenge for the European market economy”, German Monopolies Commission, July 2019, p. 8).

<sup>64</sup> See Figure 5 and Table 14 in Section 5 of Annex 4.

<sup>65</sup> Kratz, Agatha, Mikko Huotari, Thilo Hanemann, and Rebecca Arcesati. "CHINESE FDI IN EUROPE: 2019 UPDATE." (2020), p. 9.

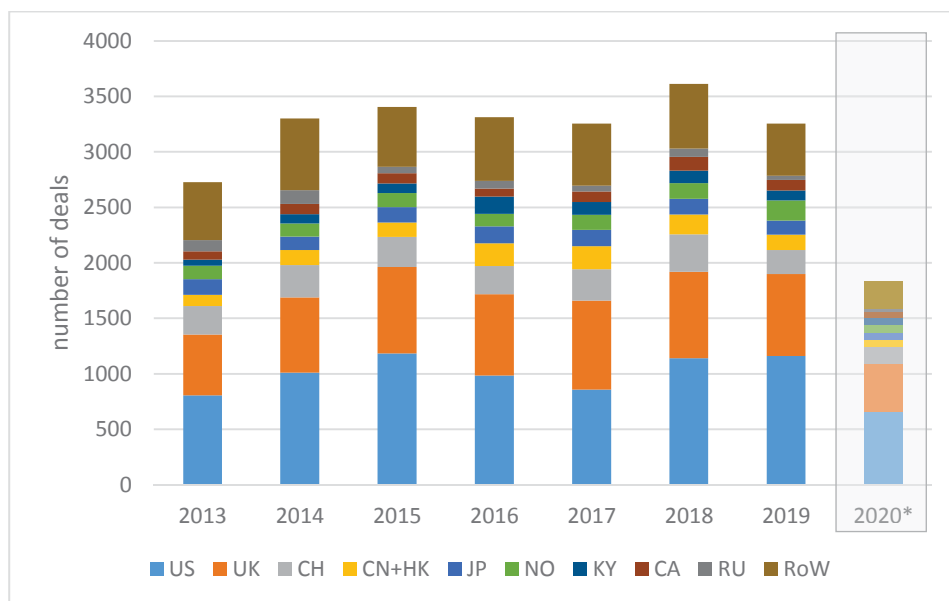
<sup>66</sup> Ibid.

<sup>67</sup> Values for FDI per year might differ between datasets. The reported figures from the JRC are an under-valuation of the true total amount of FDI.

<sup>68</sup> Kratz, Agatha, Mikko Huotari, Thilo Hanemann, and Rebecca Arcesati. "CHINESE FDI IN EUROPE: 2019 UPDATE." (2020), p. 9.

<sup>69</sup> Huotari, Mikko, and Agatha Kratz. Beyond Investment Screening: Expanding Europe's Toolbox to Address Economic Risks from Chinese State Capitalism. Bertelsmann Stiftung, 2019. For more information on China’s state-led investment strategy, see also: European Court of Auditors, The EU’s response to China’s state-driven investment strategy, Review No 03 2020.

Figure 1. Number of foreign investment deals in Europe by country of origin, 30 per cent threshold



Source: JRC elaboration on Bureau van Dijk data. Data extraction: 06/11/2020. The following countries are shown: United States (US), United Kingdom (UK), Switzerland (CH), China and Hong Kong (CN+HK), Japan (JP), Norway (NO), Cayman (KY), Canada (CA), Russia (RU). Rest of the world (RoW) which excludes the countries previously listed. Notes: Data display the total observed number of announced and completed investment deals ( $\geq 30\%$  of capital stakes) done by investors with an ultimate owner outside EU27. (\*) 2020 includes observations between January and end of September.

Table 1. Number of foreign acquisitions of equity holdings in European companies

Equity holdings	2013	2014	2015	2016	2017	2018	2019	2020*
>10%	2897	3507	3551	3476	3438	3751	3370	1906
>25%	2735	3319	3421	3327	3272	3630	3267	1837
>30%	2727	3301	3405	3314	3255	3613	3254	1830
>40%	2694	3267	3384	3286	3232	3586	3231	1823
>50%	2677	3234	3343	3263	3200	3562	3203	1817

Source: JRC elaboration on Bureau van Dijk data. Data extraction: 06/11/2020. Data by year and threshold of the acquisition. Note: cells display the total number of foreign acquisitions of equity holdings higher than the threshold indicated in the first column. European companies refers to EU27. (\*) 2020 includes values between January and September.

The above figure illustrate the overall number of foreign acquisitions (both per equity holding and per country of origin). However, the figures on investments from non-EU acquirers do not include information on foreign subsidiaries. Therefore, the figures give only an indication as to the ranking of trading partners of the EU with regard to non-EU acquisitions ('foreign investment deals') but this ranking does not indicate the importance of a given trading partner as a grantor of foreign subsidies. The data illustrates nevertheless which third countries are potentially relevant to examine the possible existence of foreign subsidies. Table 1 above on equity holdings shows the overall numbers of non-EU acquisitions under different quantitative thresholds for equity holdings (Table 14 on values of acquisitions per equity holding can be found in Annex 5). Most acquisitions (beyond a 10% shareholding) consist of the acquisition of a stake of at least 50% of

the target company.<sup>70</sup> In practice, a 30% threshold for equity holdings would be most closely in line with acquisitions aimed at achieving control of a certain target company.

In general, only a fraction of foreign acquisitions meet the thresholds of the EU Merger Regulation and are thus notified to the Commission (between 73-190 deals with a non-EU acquirer per year<sup>71</sup>). Smaller acquisitions are notified to national competition authorities (NCAs) under national merger laws, whilst some cases do not require notification at all.

Without reporting obligations or a subsidy control mechanism in place, it is difficult to establish the overall magnitude of the problem of subsidised acquisitions. However, given the trends in foreign investment and foreign acquisitions in the EU (see section 5 in Annex 4) combined with the growing number of subsidy measures around the world (see section 7 in Annex 4), there are strong indications that foreign subsidies continue to have an impact on the internal market (which is likely to increase) as also illustrated by the above case examples.

### **2.3 Problem 2: Distortions in public procurement**

This subsection will outline distortions that may occur when foreign subsidies are either granted with the express objective to, or are used to, enable or facilitate the participation of bidders in EU procurement procedures.

The EU's single market in government purchases constitutes a fundamental pillar of economic integration in the Internal Market. Public procurement accounts for over 14 % of GDP in the EU or around 2.1 trillion. It provides important business opportunities for economic operators from the EU and from third countries. The market is well-regulated at EU and national level to ensure compliance with three key principles: equal treatment, non-discrimination and transparency. These principles aim to achieve a procurement market that is competitive, open, and maximises value for money for the public sector and ultimately, the taxpayer. Well-functioning and integrated public procurement markets are essential for ensuring productive spending and investment of public money. To prevent efficiency losses, it is key to ensure fair competition in the internal market between companies without discrimination.

When assessing the impact of participation by subsidised bidders in public procurement, it is necessary to examine the short-term and long-term effects.

Contract awards to subsidised bidders in procurement may lead to short-term advantages for a number of reasons. Opening up procurement market to the highest possible number of interested parties, including subsidised bidders, will lead to a favourable increase of the number of bids submitted, to a decrease in tender prices offered and to increase the competitive pressure on incumbent bidders to be more cost-efficient. Lower bids are as a matter of principle advantageous to the contracting authorities from an economic point of view, regardless of how they come about. This is true in particular where public buyers select the winning bidder simply on the basis of the lowest bid price rather than on the basis of the best price-quality ratio. In the short term, lower prices offered by subsidised bidders benefit public buyers who have to spend less public resources. Furthermore, opening up markets to bidders that are able to offer lower prices can also increase the competitive pressure on incumbent bidders to be more cost-efficient.

However, such short term positive effects have to be weighed against adverse consequences, both short and long term, that result from the participation by subsidised bidders in EU public procurement procedures. By choosing the best value option presented in a subsidised bid, a

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<sup>70</sup> Likewise, the different participation thresholds between 10 and 50 percent do not have a major impact on the importance of the various trading partners.

<sup>71</sup> For more detail about the EU merger data, see the section on the impacts of the policy options.

public buyer will not necessarily achieve value for money. Where subsidised low prices are obtained at the cost of quality and innovation, and ultimately lead to crowding out of innovative companies, they can be an indicator of a reduction of the level of competition in procurement markets.

Similarly to adverse consequences for competition in acquisitions, participation by subsidised bidders in public procurement procedures can lead to short-term negative effects for non-subsidised companies that are competing for the same contracts.

The most damaging consequence is the case when a non-subsidised bidder otherwise offering the most economically advantageous bid is not awarded a public contract only due to the participation of a competitor benefitting from a distortive foreign subsidy, which wins. This is a direct loss of resources and business for the non-subsidised bidder in a specific procedure, as a direct result of the undue advantage stemming from the subsidisation. In the long term, such losses of specific contracts may lead to situations where unsubsidised competitors are not able to compete for contracts at all on an equal footing, thus systematically missing out on business opportunities and losing revenue on a lasting basis. The ensuing uneven playing field may over time discourage unsubsidised bidders from competing.

As in the case of acquisitions, where subsidies can be tools used by foreign governments to pursue strategic goals and to extend their economic influence abroad, bidding by subsidised undertakings for specific contracts can be part of a wider strategy of the subsidising country. Strategic interests play a role in particular when bidding for public concession contracts having as their object the operation and exploitation of large infrastructures (e.g. railways, telecommunications and utilities). Such strategic bidding practices may raise concerns with regard to long-term foreign control over public infrastructure, in particular with regard to natural monopolies. As regards the impact of foreign subsidies on the level playing field, such concerns can be taken into account as a factor, among others, in the overall assessment of the market situation. Foreign subsidies are therefore problematic not only because they lead to inefficiencies and distortions of the level playing field in the internal market, but because they may result in the foreign control of public infrastructure.

In addition, any participation of subsidised bidders in a public procurement, even if the result is not winning a contract, has inherent disadvantages for the functioning of the internal market. Every public procurement is a test of the market, and as such needs to send realistic signals about all of its aspects. Foreign subsidies create unrealistic and false perceptions, whether about prices of material, about the price of quality and technology, about salaries, about the number of companies active in a market, delivery routes and time etc.

Moreover, instead of lowering prices for public buyers, subsidised bidding can lead to higher prices and reduce the efficiency as serious competitors leave the market. A perceived short-term 'gain' for the public purse contributes to a general market failure harming public investors as much as private.

Finally, where foreign subsidies in a winning bid are returned or otherwise forfeited after contract award, they can jeopardise the proper execution of the awarded public contract and lead to subsequent increases in prices through contract amendments.

Concern over the existence of subsidies and unfair practices and their harmful effect on the internal market was strongly voiced by a significant number of contributors to the public consultation on the White Paper. In a number of submissions, contributors to the public consultation, such as the ones from the maritime equipment sector, have outlined that in recent years, European public procurement contracts have been awarded to economic operators from third countries such as South Korea and China that may have benefited from state-backed finance

and government support provided to domestic technology industries. Notably, stakeholders have reported that this is the case in the railway supply, maritime technology and construction sectors. Stakeholders have pointed out that for specific third countries, these sectors are considered of strategic importance, and that behaviours which they see as indicating the existence of export-led government strategies enable their domestic companies (often state-owned) to compete globally with prices that distort competition.

Example 1, Problem 2: Infrastructure Project - construction

As stakeholders have indicated, foreign subsidies may be granted with the express objective of enabling companies to submit bids for public contracts, at prices that are below market price or even below cost, directly “underbidding” to the detriment of competing non-subsidised undertakings. Specific concerns have been raised in cases where EU Funding is given for the project concerned.

A few years ago, a contracting authority awarded a major construction contract closing a gap in the country’s transport network to a consortium led by a non-EU company. The offer, while above the contracting authority’s proposed project budget, was nearly 20% lower than the next-lowest bid. The company structure might indicate that the offer may have relied on state financing.

Example 2, Problem 2: Infrastructure projects – supply

Over the past years, a state-owned non EU supplier of essential transport equipment has won a number of high value tender procedures in the EU. They offered particularly low prices. The company is considered the world market leader in its sector. According to its own disclosure in stock exchange filings, it receives substantial government subsidies.

Within the last 12 months, a consortium led by this company was awarded a public contract for the supply of a substantial number of equipment for local transport in a MS. The contract has an estimated value of EUR between 150 and 200 million EUR. A year before, the company has been awarded a contract valued at EUR over 50 million EUR to supply equipment for local transport in another MS, and at a similar time another consortium led by the company was selected to supply equipment for suburban and regional services for a value up to almost 1 billion EUR, having offered a price that was 25% lower than that of competitors.

As mentioned under 2.2 the German competition authority has stated that specific companies use favourable prices to expand their position on foreign markets. Participation in public procurements is one way of achieving this aim. Contracting authorities like competition authorities, see above 2.2, cannot take into account in their assessment to what extent foreign subsidies were instrumental in winning the contract, and have had a distortive effect.

Example 3, Problem 2 Infrastructure project – local transport

In 2019, a regional council awarded a contract for works/supplies on a transportation network to a state-owned non-EU company for a value of several tens of millions of EUR. The winning bid was 40% lower than the next-lowest offer from competitors.

The above examples are given to demonstrate the potentially distortive effects of foreign subsidies and state-sponsored bidding practices. These practices may be driven by long-term strategic goals, or in order to gain direct access to important markets or regions. In some cases, foreign subsidies are likely granted with the express objective of enabling companies to submit bids for public contracts at prices that are below market price or even below cost, directly

“underbidding” to the detriment of competing non-subsidised undertakings. A response to the public consultation on the White Paper mentioned such an example<sup>72</sup>.

The examples provided above describe the problems linked with foreign subsidies.

As for acquisitions, also for public procurement no specific data are available on the prevalence of subsidised bidding so that alternative methods to indicate the existence of foreign subsidies in public procurement have to be used. While foreign subsidies may be granted to any company, as mentioned under 2.2, the only available data in procurement is the share of contracts won by non-EU companies. Data in the database of Tenders Electronic Daily (TED)<sup>73</sup> are only available for successful bidders, not for all bidders, and these data only report the country of registration of the bidding company, not their ownership. A study covering cross-border procurement in the years 2009 to 2015<sup>74</sup> also investigated so-called indirect cross-border, i.e. awards to foreign owned subsidiaries. This study determined that 3.0 % of contracts in the EU were directly awarded cross-border, and 20.4 % were awarded indirectly. Of the 3.0 % of direct cross-border awards, 78.6 % of all contracts were awarded to EU companies. This share has, however, been decreasing over the reporting period from 87.4 % in 2009 to 73.6 % in 2015. In fact, there were nearly twice as many direct cross-border awards in 2015 than in 2009. The share of non EU companies in indirect cross-border awards amounted to 39.7 % over the period from 2009 to 2015. Specific investigations for contract awards above EUR 250 million recorded in the TED database between 2015 and 2017<sup>75</sup> have shown that 21 of the 435 awardees<sup>76</sup> or 4.8% had an ultimate owner outside the EU. No reliable data is available on foreign participation in the supply chain and as subcontractors. A 2011 study<sup>77</sup>, on the basis of a pan-European survey, estimated the share for intra- and extra-EU cross-border participation of subcontractors, wholesaler, and distributors<sup>78</sup> at 12.9 % of the total procurement<sup>79</sup>.

Overall, the available data show that the share of cross-border awards to non EU companies is increasing over time. This increase shows the openness of the EU market in general, and the EU procurement market in particular. Increasing openness, along with the general trend of increases in subsidies globally as explained under point 2.2, underlines the need to have and maintain a level playing field in the EU procurement market for all economic operators.

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<sup>72</sup> See the contribution of Dutch Province of Overijssel, available here:

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

<sup>73</sup> TED (Tenders Electronic Daily) is the online version of the 'Supplement to the Official Journal' of the EU. TED is an online service of the European Union for the advertisement of public contracts. (<https://ted.europa.eu/TED/main/HomePage.do>)

<sup>74</sup> VVA, LE and JIIP (2017), “Measurement of impact of cross-border penetration in public procurement”, Final report for the European Commission, Brussels, available here: <https://op.europa.eu/en/publication-detail/-/publication/5c148423-39e2-11e7-a08e-01aa75ed71a1>

<sup>75</sup> More recent data are not yet fully available for analysis.

<sup>76</sup> Several contracts have been awarded to multiple companies.

<sup>77</sup> European Commission, DG Internal Market and Services, Cross-border procurement above EU thresholds – Final Report (March 2011), available here: <https://op.europa.eu/en/publication-detail/-/publication/0e081ac5-8929-458d-b078-a20676009324>

<sup>78</sup> At the same time, indirect cross-border procurement through ‘affiliates’ accounted only for 13.4 % of the value of procurement.

<sup>79</sup> It did not distinguish between value and number of contract awards.



#### The special case of EU-funding

Most of the EU budget – about 80% – is implemented under shared management: Member States distribute the funds and manage the expenses in compliance with the applicable EU and national law. A large part of funding under shared management is awarded through public procurement procedures. It follows that any future Union measure(s) addressing the distorting effects foreign subsidies in public procurement will apply to the EU budget expenditure under shared management through public procurement.

The direct management of EU funds is subject to the EU's Financial Regulation. The Commission may explore the possibility to propose to the co-legislators amendments to the Financial Regulation to take into account the impact of foreign subsidies. This is not part of the present impact assessment report.

As regards EU funds implemented through indirect management, the Commission may liaise directly with the International Financial Institutions charged with their implementation.

## **2.4 Problem 3: Other market distortions**

Apart from the specific cases of foreign subsidies facilitating acquisitions of EU companies and distorting public procurement procedures, there are indications that foreign subsidies can distort the internal market in other ways – e.g., through greenfield or other investments.

As indicated in the section on Problem 1, the economic literature cites a number of negative effects that subsidies may generally have on the market.<sup>80</sup> Subsidies may for example lead to an inefficient overall allocation of resources<sup>81</sup> and cause growth differentials between subsidised and non-subsidised undertakings. In terms of the concrete impact of foreign subsidies on the EU internal market, the section on Problem 1 pointed out that subsidised companies may build up market power through low prices by driving competitors out of the market or preventing them from entering.<sup>82</sup> Such market power could then, in the long term, lead to abuse, for instance by allowing the subsidised company to increase its prices (this strategy easier to impose if competitors have been already weakened). Hence, in the long term, undertakings not receiving third country subsidies would become less competitive which negatively affects the EU's overall economic competitiveness.<sup>83</sup> These considerations hold both for subsidised acquisitions and subsidised greenfield investment. Last but not least, foreign subsidies may also result in costly and often wasteful emulation and lead to subsidy races,<sup>84</sup> further deepening the above inefficiencies and distortions. A lack of transparency about subsidies aggravates the distortive effects of subsidies as it leaves competitors unaware of their influence on market prices and production volumes and therefore undermines their own business decisions.<sup>85</sup>

Two types of general market distortions deserve particular attention in the context of this section, namely foreign subsidies that are granted to incentivise the delocalisation of companies active in the internal market as well as subsidised private tenders. Regarding the former, foreign subsidies

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<sup>80</sup> It should be noted that in the EU context, such distortions may be reduced, e.g. by subsidies granted in competitive processes. Moreover, such subsidies may be proportional and contribute to EU public policy objectives, and hence be considered compatible State aid. See e.g. the Communication from the Commission — Criteria for the analysis of the compatibility with the internal market of State aid to promote the execution of important projects of common European interest, OJ C 188, 20.6.2014, p. 4–12

<sup>81</sup> Gurwinder Singh, “Subsidies in the Context of the WTO's Free Trade System - A Legal and Economic Analysis” (2017), p. 23.

<sup>82</sup> The CRRC/ Vossloh decision of the German FCO quoted above points in this direction.

<sup>83</sup> “Chinese state capitalism: A challenge for the European market economy”, German Monopolies Commission, July 2019, p. 17.

<sup>84</sup> David Spector, “State Aids: Economic Analysis and Practice in the European Union”, Chapter 7 in “Competition Policy in the EU: Fifty Years on from the Treaty of Rome” by Xavier Vives.

<sup>85</sup> Md. Rezaul Karim, “Transparency is the Most Important Governance Issue in the WTO Subsidy Control”, SSRN Electronic Journal, January 2014



may be granted to a parent company located outside the EU (e.g., through selective corporate tax measure)<sup>86</sup>, which in turn finances a subsidiary located in the EU through intragroup transactions. In other words, companies can divert their existing investments away from the internal market to third countries in order to benefit from selective corporate measures which in return increases their financial strength and improves their competitive position in the internal market. In practice this means that such foreign subsidies can cause a distortion of the internal market. Apart from distorting competition, foreign subsidies facilitating the delocalisation of companies active in the internal market can have indirect effects on the EU labour market. A key indicator to determine the social impact of delocalisation is to calculate the job losses that followed the delocalisation of a specific company. Such an analysis also needs to factor in job losses of relevant suppliers of the delocalising company.<sup>87</sup> Further knock-on effects on aggregate consumer demand as result of job losses or decline in real wages may also be considered.<sup>88</sup> Lastly, delocalisation may lead to a loss of tax revenues and in the long run to a 'race to the bottom' in corporate taxation between countries, though current research does not yield clear-cut results in that regard.<sup>89</sup>

In addition to the issue of public tenders, which were presented in Problem 2, private tenders may give subsidised companies an opportunity to gain market share by undercutting their competitors through below-cost pricing (see Example 1, Problem 3). Whilst in the short term below-cost pricing may benefit the company organising the tender and potentially also consumers, it can have negative effects in the long term on consumers and producers alike.<sup>90</sup> More specifically, subsidised bidding proves to be particularly harmful for non-subsidised bidders, as they are cut off from relevant opportunities to grow. In the long term, below-cost pricing can therefore create lock-in effects which means that unsubsidised companies might have to leave the market at hand. This could enable subsidised companies to attain a dominant position which could be leveraged to raise prices.

Respondents to the public consultation on the White Paper have brought forward some potential instances of distortive foreign subsidies. They concern, inter alia, greenfield investments from third countries in the internal market<sup>91</sup>. An industry association stipulated that third countries might subsidise EU airlines, such as through the granting of non-arms-length loans, artificially keeping them alive to feed into third-country airlines' hubs and networks, with a clearly distortive effect in the EU aviation market.<sup>92</sup> Another stakeholder pointed to possible distortions through the EU activities of aluminium companies receiving foreign subsidies.<sup>93</sup> In this context not only distortive subsidised acquisitions were mentioned, but also a contract of a non-EU-based subsidiary of a non-EU aluminium producer, which according to the OECD report<sup>94</sup> receives foreign subsidies, to upgrade an aluminium facility in the EU. The aluminium sector is described in more detail in Annex 4.

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<sup>86</sup> Some examples are given in Annex 4 point 3.

<sup>87</sup> Małuszyńska, Ewa. "Delocalisation of Enterprises: Qualitative and Quantitative Effects on the Labour Market." In: *Relocation of Economic Activity*, pp. 163-181. Springer, Cham, 2019, p. 173.

<sup>88</sup> Ibid.

<sup>89</sup> See for example Drezner, Daniel W. "The race to the bottom hypothesis: An empirical and theoretical review." The Fletcher School, Tufts University (2006).

<sup>90</sup> E.g., for a contribution on 5G networks, see BIGS Policy Paper (2020), *The Hidden Costs of Untrusted Vendors in 5G Networks*, p. 40. [https://www.bigs-potsdam.org/app/uploads/2021/02/Policy-Paper-No.8\\_V3.pdf](https://www.bigs-potsdam.org/app/uploads/2021/02/Policy-Paper-No.8_V3.pdf)

<sup>91</sup> See, among others, the contribution of the Union of Entrepreneurs and Employers, available here: [https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

<sup>92</sup> See the contribution of the Airline coordination platform, available here:

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

<sup>93</sup> See the contribution of European Aluminium, available here:

[https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html).

<sup>94</sup> OECD (2019), "Measuring distortions in international markets: the aluminium value chain", *OECD Trade Policy Papers*, No. 218, OECD Publishing, Paris, <https://doi.org/10.1787/c82911ab-en>.

In the EU context, State aid granted by Member States may also lead to a misallocation of resources towards certain economic activities or types of firms. Moreover, there is a risk of competitive distortions between Member States to attract undertakings to their territory ('subsidy races'). That is why Member States must notify planned aid measures to the Commission for validation and must also recover incompatible State aid. The very rationale for controlling State aid at EU level is its potentially negative effect on the EU internal market.<sup>95</sup>

### Case studies

Several examples below illustrate how foreign subsidies may distort the internal market beyond acquisitions or public procurement procedures. As with the previous examples, it should be noted that these examples are only indicative because there is so far no mechanism and no legal framework to unambiguously identify the existence and precise impact of foreign subsidies on the internal market.

#### Example 1, Problem 3

In a recent (private) tender procedure, an EU telecom operator chose Company A to provide equipment for its network. Company A's deal with the EU telecom company concerns the provision of certain telecom infrastructure including the relevant software<sup>96</sup>.

According to confidential information provided by industry officials, Company A underbid a competitor by 60 per cent in the above-mentioned (private) tender – a price that allegedly does not even cover the costs of the provided equipment. Company A is suspected to have received considerable government support from Country X in the form of subsidies over many years. Current research indicates that subsidies, alongside other measures from which Company A benefitted in the past, have in fact had a negative impact on innovation in the respective telecom sector as a whole.

#### Example 2, Problem 3

Company B is a non-EU Country Y state-owned vertically integrated energy group. The group comprises hundreds of enterprises.

Company B and its subsidiaries are active in the EU internal market. Company B's website lists cooperation with various EU Member States. Company B's subsidiary 1, one of the world's largest input suppliers in the field of energy, has contracts with several power plants in various Member States. Company B's subsidiary 2 constructs power plants. It is also the general contractor for one of the on-going projects in the EU.

Country Y has provided subsidies to Company B and its subsidiaries in the past years. Two published government decisions refer to several subsidies. According to Global Trade Alert, Country Y provided another subsidy to Company B in the form of a property contribution to develop the industry concerned. In December 2018, Company B's subsidiary 1 received subsidies to cover 70% of its expenses related to the registration of intellectual property items in external markets. The 2014 annual report of Company B's subsidiary 2 does not report subsidies but notes that Country Y supported its projects in international markets. The report adds that this increases the Company's competitive strength in the global market.

In a recent report, the German Monopolies Commission noted that depending on the type of subsidy, a subsidy may lead to a reduction in the variable costs and therefore directly impact

<sup>95</sup> Ioannis Ganoulis and Reiner Martin, "State Aid Control in the European Union - Rationale, Stylised Facts and Determining Factors", INTERECONOMICS, November/December 2001, p. 289-297

<sup>96</sup> If the provision of equipment only concerned the sale of goods, then the tender could be covered by trade defence instruments. However, given the 'servicification' of manufacturing, i.e., the use of software to operate complex modern hardware, it could be that the tender also involved the sale of services. For the a discussion about the integration of services trade in goods trade, see: [https://trade.ec.europa.eu/doclib/docs/2017/july/tradoc\\_155844.pdf](https://trade.ec.europa.eu/doclib/docs/2017/july/tradoc_155844.pdf)

prices with an effect on competitors and consumers. An investment grant, on the other hand, may have more medium- to long-term effects on market entries or exits. The impact of a subsidy is furthermore dependent on whether it is a one-off or a recurrent support measure, and how selectively it is granted.<sup>97</sup> In this context, an industry association pointed in its submission to the public consultation to potentially subsidised gas prices on the third country market, which allows the local gas users to expand their operations in the EU to the detriment of competitors.<sup>98</sup>

A Dutch report argues that non-regulated state support and market power in a third country market enable local undertakings to achieve cost advantages and surplus profits that in turn may allow them to build up market power on the EU internal market at the expense of other undertakings.<sup>99</sup> Such behaviour, not driven by commercial considerations, may be driven by strategic goals in order to get a foothold in strategically important markets or regions<sup>100</sup>, or to get privileged access to critical and major infrastructure. In terms of impact on the EU internal market, the anticompetitive behaviour based on subsidies may drive competitors out of the market or prevent them from entering the market, reducing their competitiveness and affecting the innovative capacity of the EU economy.

As discussed above, several submissions to the public consultation on the White Paper and the targeted consultation pointed to specific sectors characterised by distortive foreign subsidies. The sectors mentioned included: steel, aluminium aviation, oil and gas and semiconductors.<sup>101</sup> Moreover, the OECD has carried out several sector studies to examine the amount and distortive effects of subsidies. The sectors investigated are semiconductors, steel, and aluminium. These studies are described in detail in Annex 4. In addition to the OECD studies and the examples of transactions that contained potentially distortive subsidies mentioned in Annex 4, the European Semiconductor Industry Association (ESIA) confirmed in the targeted consultation that foreign subsidies in the semiconductor sector tend to provide significant benefits to their recipients and can lead to subsequent distortions in the market.

#### General information on foreign subsidies

According to a WTO report on subsidies issued in 2006<sup>102</sup>, data on the use of subsidies are scarce and difficult to compare across countries and sectors because of methodological differences and data gaps.<sup>103</sup> There are no more recent studies on subsidies covering all sectors. Data from various sources is available, but not necessarily on subsidies.<sup>104</sup>

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<sup>97</sup> “Chinese state capitalism: A challenge for the European market economy”, German Monopolies Commission, July 2019, p. 16

<sup>98</sup> As brought forward by among others Fertilizers Europe, gas dual pricing in Russia and North Africa (i.e. gas commodity price for national industry below the export price) has encouraged significant market share growth of foreign undertakings in the EU. The definition of "material injury" under Trade defence instruments does not address unfair competitive practice with the current 6% return on sales target being set too high. See the contribution of Fertilizers Europe, available here: [https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html).

<sup>99</sup> Netherlands, Non-paper – Strengthening the level playing field on the internal market (9 December 2019), see [www.permanentrepresentations.nl/documents/publications/2019/12/09/non-paper-on-level-playing-field](http://www.permanentrepresentations.nl/documents/publications/2019/12/09/non-paper-on-level-playing-field)

<sup>100</sup> Please also see in this context the example 4, Problem 3 in Annex 4, Section 3

<sup>101</sup> [https://ec.europa.eu/competition/international/overview/foreign\\_subsidies.html](https://ec.europa.eu/competition/international/overview/foreign_subsidies.html)

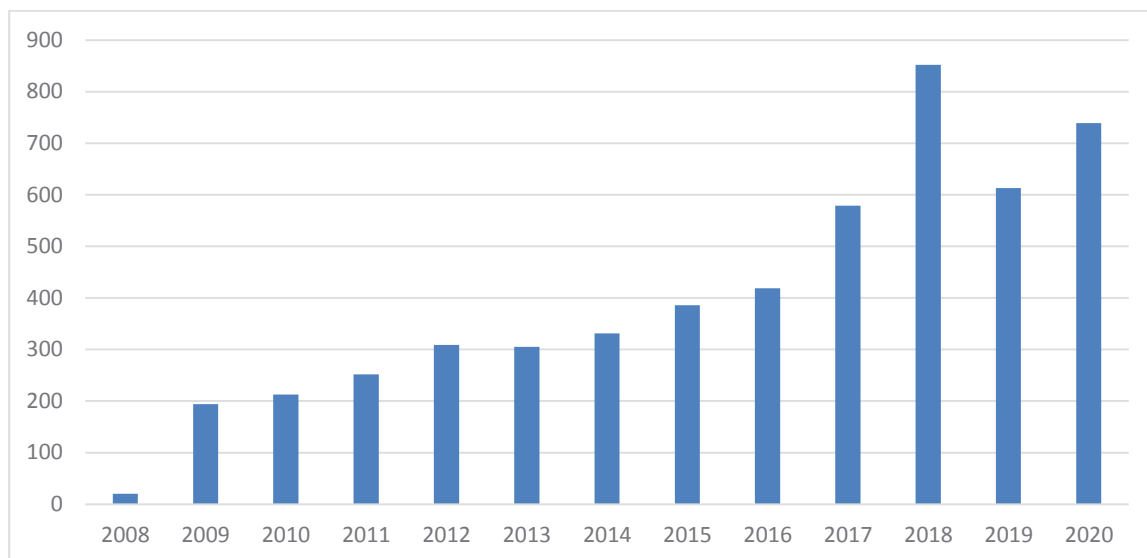
<sup>102</sup> World Trade Report 2006, Exploring the Links Between Subsidies, Trade and the WTO; this report analysed amongst others how much countries subsidise according to different data sources.

<sup>103</sup> Ibid, see pp. 45 and 114.

<sup>104</sup> See e.g. World bank development indicators, <https://databank.worldbank.org/reports.aspx?source=world-development-indicators>, which include

The information presented in the figure below shows that the number of subsidy measures implemented worldwide has in the recent years been increasing steadily.

Figure 2. Number of newly implemented subsidy measures (worldwide) per year



Source: Global Trade Alert (GTA)<sup>105</sup>

The subsidy measures covered here are both subsidy schemes and individual subsidy grants outside schemes.<sup>106</sup>

To identify foreign subsidy measures that may affect the EU, this impact assessment examines in more detail the EU's five main trading partners in terms of imports<sup>107</sup>. These are (in decreasing importance): China, USA, UK, Russia and Switzerland. Three of these countries (USA, Switzerland and China) are also the main partners in terms of greenfield FDI<sup>108</sup> into the EU<sup>109</sup>.

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information on “subsidies and other transfers”, which covers however also grants to international organisations, social security, social assistance benefits as well as employer social benefits; see also the OECD corona policy response tracker. <https://www.oecd.org/coronavirus/en/> Information is sorted by country, and there is a section “fiscal measures” (not “subsidies” strictu sensu).

<sup>105</sup> GTA provides information on state interventions taken since November 2008 that are likely to affect foreign commerce. It includes state interventions affecting trade in goods and services, foreign investment and labour force migration. For the classification of the measures analysed, GTA uses the taxonomy established by the UNCTAD Multi-Agency Support Team (MAST). This classification, the so-called MAST chapters, provides a clear and concise definition of non-tariff measures (NTMs) and is the standard classification for NTMs in goods. The MAST chapter of interest in the context of this report is the Chapter L - Subsidies group. Only measures currently in force have been taken into account. Source: <https://www.globaltradealert.org/>

<sup>106</sup> Please note that this section presents general information on subsidies across all possible purposes (including in particular subsidised acquisitions and procurement).

<sup>107</sup> EU's 5 biggest trading partners as far as imports are concerned in 2019 were China, USA, UK, Russia and Switzerland. [https://trade.ec.europa.eu/doclib/docs/2006/september/tradoc\\_122530.pdf](https://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_122530.pdf)

<sup>108</sup> Greenfield FDI is a type of investment in which a parent company creates a subsidiary in a different country, building its operations from the ground up.

<sup>109</sup> EU's 5 main partners in greenfield FDI are: USA, Switzerland, Japan, China and India.

Source : <https://ec.europa.eu/assets/epsc/files/EPSC%20-%20The%20State%20of%20Investment%20in%20Europe%20and%20the%20World.pdf>

However, it should be noted that greenfield FDI by the UK has also been steadily increasing and grew by 37.5% in the period 2015-2017.<sup>110</sup>

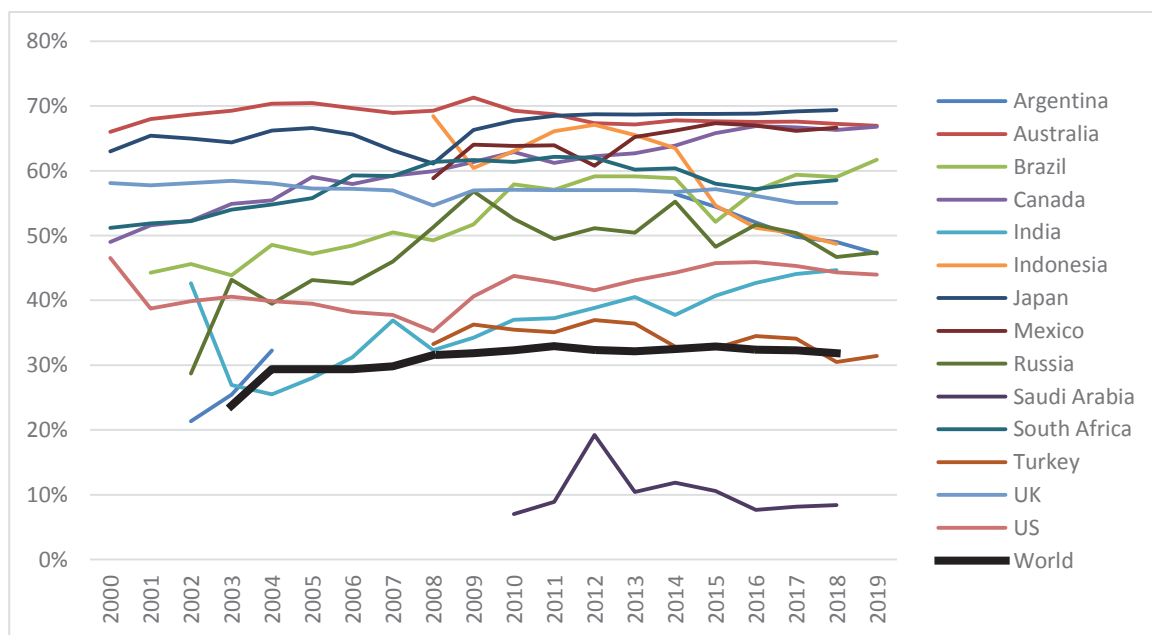
When looking in more detail at the EU's five main trading partners, based on the reporting by GTA,<sup>111</sup> the US seem to have the highest number of subsidy measures in place<sup>112</sup>. However, this is not necessarily indicative of the value of subsidies because the data in the table below refers only to the number of measures without specifying the subsidy amount per measure. Moreover, the specific foreign subsidies may not always be considered distortive.

Table 2. Number of subsidy measures currently in place in EU's five main trading partners<sup>113</sup>

Country	Number of subsidy measures in place
China	205
USA	999
United Kingdom <sup>114</sup>	104
Russia	414
Switzerland	2
<b>Grand Total</b>	<b>1724</b>

In terms of trends, subsidies display a relatively flat or slightly upward trend if measured as percentage of total State expenditure, as can be seen in the below figure.

Figure 3. Subsidies and other transfers in selected G20 economies (as % of total expenditure)<sup>115</sup>



Source: World Bank; data for China and Korea not available; EU countries excluded.

<sup>110</sup> UK was still an EU Member State at that point in time.

<sup>111</sup> Source: <https://www.globaltradealert.org/>

<sup>112</sup> This covers both subsidy schemes and individual subsidy grants outside schemes.

<sup>113</sup> All the figures in the below table were taken from Global Trade Alert: <https://www.globaltradealert.org/>

<sup>114</sup> During the period covered, the UK measures were subject to EU State Aid control.

<sup>115</sup> The World Bank definition of subsidies and transfers includes social benefits and other transfers that would not be regarded as subsidies under different definitions (e.g. used by the SCM Agreement or in the White paper on foreign subsidies)

This being said, since the year 2000, subsidies and other transfers<sup>116</sup> have been an important element of economic policy for governments around the world. Countries such as Brazil, Canada, India, Japan, Mexico or South Africa have even seen an increase over the past two decades expressed as percentage of their expenses. The share of subsidies as percent of expenses of other major EU trading partner such as the US or the UK has remained relatively stable.

It is difficult to obtain data on the total amount of foreign subsidies affecting the EU internal market. Some country-specific data is available on subsidy schemes in the United States via the Good Jobs First Subsidy Tracker, including the amount of subsidies granted to specific companies.<sup>117</sup> However, this data cannot be used to clearly identify foreign subsidies that have an effect on the internal market. Table 8 below shows the publicly available information on the subsidies granted by the EU's main trading partners for the production of export goods that were notified to the WTO in the period 2017-2018. It should be kept in mind, though, that this information concerns only subsidy schemes, not individual subsidy grants outside schemes. Consequently, it likely underestimates the total amount of subsidies. Moreover, for many measures notified to the WTO the budget and/or the expenditure were not yet known at the moment of the notification, and are hence not included in the total subsidy amount. Finally, some subsidies may have been omitted in the WTO notification.

Table 3. Subsidy amounts reported to the WTO based on 2019 notifications by EU's 5 main trading partners<sup>118</sup>

In million Euros <sup>119</sup>	2017	2018
<b>China</b>	380,132.7	520,012.9
<b>USA</b>	14,932.8	17,008.4
<b>UK</b>	919.7	888.1
<b>Russia</b>	3,959.52	3,803.94
<b>Switzerland</b>	515.0	697.4

As briefly mentioned above, there is a lack of transparency and low compliance with the obligation to notify subsidies under the WTO Agreement on Subsidies and Countervailing Measures (SCM Agreement)<sup>120</sup>. Less than half of the WTO Members complied with the notification obligation in 2019<sup>121</sup>. Moreover, the information included in the notifications is not

<sup>116</sup> The World Bank definition includes social benefits and other transfers that would not be regarded as foreign subsidies under other definitions (e.g. used by the SCM Agreement or in the White paper on foreign subsidies).

<sup>117</sup> <https://www.goodjobsfirst.org/subsidy-tracker>. Next to the subsidy tracker, some research papers criticise the lack of effectiveness of some US subsidy schemes, most prominently the economic development programmes by US states to attract new companies. See: Mitchell, Matthew D., Michael Farren, Jeremy Horpedahl, and Olivia Gonzalez. "The Economics of a Targeted Economic Development Subsidy." *Mercatus Research Paper* (2020).

<sup>118</sup> Source: [https://docsonline.wto.org/dol2fe/Pages/FE\\_Search/FE\\_S\\_S003.aspx](https://docsonline.wto.org/dol2fe/Pages/FE_Search/FE_S_S003.aspx)

<sup>119</sup> Recalculated to Euros on the basis of the average ECB exchange rates for the years 2017 and 2018:

[https://www.ecb.europa.eu/stats/policy\\_and\\_exchange\\_rates/euro\\_reference\\_exchange\\_rates/html/index.en.html](https://www.ecb.europa.eu/stats/policy_and_exchange_rates/euro_reference_exchange_rates/html/index.en.html)

Moreover, amounts of certain subsidies were averaged in case of longer-term schemes. Specific agricultural subsidies (which in the EU are granted under the CAP and would not be considered State aid) and subsidies granted to individual consumers are not taken into account in the table. Additionally, amounts of subsidies granted at national level in China and subsidies given at the regional/State level in the USA are rarely reported and thus not included in the table.

<sup>120</sup> Article 25.1 of the SCM Agreement requires that all Members submit a full notification of all specific subsidies every three years, with updates in the intervening years. SCM Agreement applies only to subsidies that are specifically provided to an enterprise or industry or group of enterprises or industries. It should be noted that the notification obligation extends to all specific subsidies related to goods, in any sector (including agriculture), and provided by any level of government.

<sup>121</sup> As indicated by the Chair of WTO's Committee on Subsidies and Countervailing Measures (SCM) at a meeting on 27 October 2020, only 81 (out of 164) WTO Members complied with this obligation in 2019. Source: ([https://www.wto.org/english/news\\_e/news20\\_e/scm\\_27oct20\\_e.htm](https://www.wto.org/english/news_e/news20_e/scm_27oct20_e.htm)).



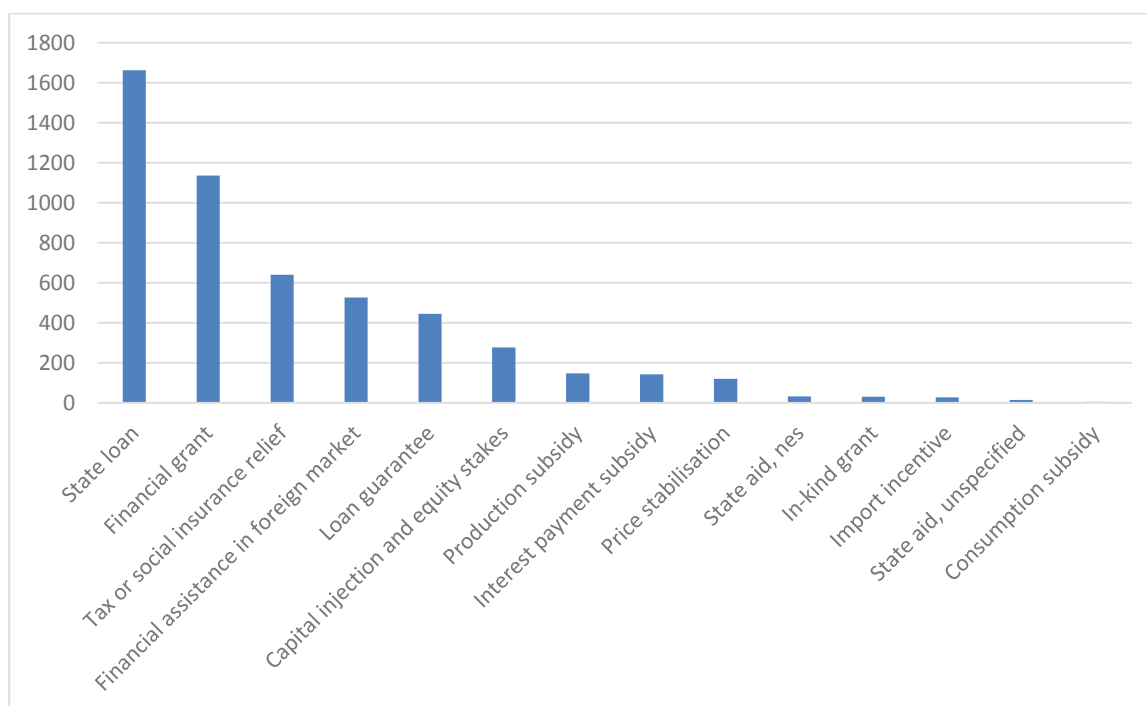
uniform across WTO members. Additionally, WTO members do not appear to declare in their notifications all the subsidies they grant. This is, among others, evidenced by the fact that in the period 2014-2019 USA counter-notified Chinese subsidies four times<sup>122</sup>.

While the present report focuses on other ways than the import of goods to investigate the impact of foreign subsidies on the internal market, the SCM Agreement may nonetheless be a valuable source of information about the general subsidy policy of third countries. The most common types of foreign subsidies reported under the SCM Agreement are as follows<sup>123</sup>:

- foregone or not collected public revenue, such as preferential tax treatment or fiscal incentives such as tax credits;
- the transfer of funds or liabilities (capital injections, grants, loans, loan guarantees, fiscal incentives, setting off of operating losses, compensation for financial burdens imposed by public authorities, debt forgiveness or rescheduling);
- the provision of goods or services or the purchase of goods and services.

These types of subsidies are largely confirmed by the information from GTA in the figure below. This being said, the transfer of funds and liabilities appears to be more prevalent according to GTA.

Figure 4. Subsidy measures in place<sup>124</sup> by type according to GTA



For an indication of third countries granting distortive subsidies and of sectors concerned, the countervailing subsidy cases started by the Commission in the period 2010-2020 may be

<sup>122</sup> USA counter notifications to WTO of Chinese subsidies are present on the WTO website:

[https://docs.wto.org/dol2fe/Pages/FE\\_Search/FE\\_S\\_S001.aspx](https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S001.aspx)

<sup>123</sup> This overview is based on the types of subsidies covered by the countervailing measure cases initiated by the EU in the period 2010-2020. According to the overview prepared by DG TRADE, 52% of cases concerned government revenue foregone, 34% concerned direct transfer of funds, and 13% government provision or purchase of goods. Source: <https://trade.ec.europa.eu/doclib/html/157607.htm>

<sup>124</sup> This covers both subsidy schemes and individual subsidy grants outside schemes



illustrative. The overview enclosed in Annex 4 shows that the five countries against which the Commission opened most countervailing subsidy cases in the period 2010-2020 were: China, India, Turkey, USA, and Indonesia. As mentioned previously, China and the USA are amongst the top-5 trading partners of the EU and, according to WTO notification data, seem to be granting substantial amounts of subsidies to their industries.

In terms of sectors, the main sectors affected by countervailing subsidy cases, as presented in Annex 4, are the following: iron and steel, electronics, glass fibre products and biodiesel. This seems to confirm stakeholder views expressed in the public consultation about the prevalence of distortive foreign subsidies in the sectors of, among others, steel and semiconductors.

## **2.5 What are the problem drivers?**

The main root cause of the problem is the existence of foreign subsidies, causing distortions in the EU internal market, in the absence of any regulatory mechanism to prevent or remedy such distortions. Subsidies are typically part of broader industrial strategies of third countries. While the existing EU tool box includes some rules to deal with foreign subsidies in certain market circumstances, these rules are not sufficient, leaving a ‘regulatory gap’. In other words, there are foreign subsidies that are not captured by any of the existing legal instruments and can therefore impact the EU internal market.

Countries have the right to develop and implement their own industrial policies including the granting of subsidies. Subsidies as part of these industrial strategies may however distort markets in other countries. There is a particular risk of distortions when there is no regulatory mechanism to control them. For illustration purposes, Annex 4, Section 9 includes the example of the role that subsidies play in China’s industrial policy with potential spill-over effects in foreign markets including the EU internal market.

While the role of potentially distortive subsidies in the industrial policy of third countries is the very source of the problem, its actual impact ultimately depends on whether there are control mechanisms to prevent distortions in the EU internal market. Below, an overview is given of existing EU and international instruments in the area of competition, trade, public procurement and in certain sector specific legislation. The analysis demonstrates the existing regulatory gap to address the distortions in the EU internal market caused by foreign subsidies.

As regards EU competition rules, the EU merger and antitrust rules aim to prevent significant distortions of competition due to mergers and acquisitions that would create a ‘significant impediment to effective competition’ or due to anticompetitive practices of undertakings. They do not specifically take into account whether an undertaking’s conduct, for instance in the form of anti-competitive pricing<sup>125</sup> results from or was facilitated by foreign subsidies. In the area of merger control, a concentration is only declared incompatible with the common market if it significantly impedes effective competition, in line with the underlying objective of merger control to protect the market structure. The merger control rules therefore do not take into account which means are employed to bring about changes in the market structure, i.e. whether an acquisition is facilitated by foreign subsidies or not. Last but not least, EU State Aid rules only apply to financial support granted by EU Member States and aim to ensure that EU government interventions do not distort competition and intra-Community trade. No such control mechanism exists as regards subsidies granted by third countries which puts EU industry at a disadvantage in competition vis-à-vis undertakings receiving foreign subsidies.

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<sup>125</sup> See above, section 2.1.1.

In the area of trade policy, the WTO SCM Agreement as well as the trade defence instruments (TDIs) allow the EU to react to unfair competition in terms of injurious imports of goods which are unfairly priced below their normal value (anti-dumping instrument) or subsidised (anti-subsidy instrument). These instruments, however, have their limitations.

The EU anti-dumping<sup>126</sup> and anti-subsidy rules<sup>127</sup> apply to the import of goods and do not cover services, investment or other financial flows in relation to undertakings operating in the EU. In addition to the limitation on goods, the EU's anti-subsidy rules in principle only apply to subsidies to companies in the granting (third country) jurisdiction while addressing subsidies supporting companies in a third country market (i.e. the EU internal market) remains exceptional.<sup>128</sup> As regards the EU's anti-dumping rules, unfair price practices of a third country exporter (dumping) are not always problematic in terms of competition<sup>129</sup> and are not necessarily the types of distortions a new EU instrument on foreign subsidies aims to address. Furthermore, the FDI Screening Regulation<sup>130</sup> allows Member States to screen foreign investments, which are likely to have an impact on a Member State's security and public order by considering its effects on critical assets and infrastructure. The Regulation, however, does not specifically tackle the issue of distortions caused by foreign subsidies on the internal market.

At the international level, the EU can bring litigation against a WTO Member before a WTO panel for breaches of the SCM Agreement. However, the scope of application of the SCM Agreement is also limited to trade in goods. Subsidies are not excluded from the scope of application of the WTO General Agreement on Trade in Services (GATS). In fact, GATS includes an inbuilt mandate to further negotiate disciplines for services subsidies.

As regards bilateral Free Trade Agreements (FTAs), there are large differences as regards the provisions on subsidies. Most FTAs focus on transparency and consultations in case of distortive subsidies. Some include provisions prohibiting subsidies considered particularly harmful (such as unlimited guarantees). Agreements signed with some neighbouring countries include the commitment to put in place a subsidy control system inspired by EU State Aid rules. Although the scope of those agreements is to address subsidies that affect trade between the EU and the respective third country, jurisdictions that have in place such subsidy control systems are expected to be better placed to identify and address subsidies that distort the EU internal market. If there was a case under an FTA of a potentially distortive foreign subsidy impacting the EU, the Commission could have the choice to open the case under the FTA or take separate legal action for example under a possible new legal instrument. For instance, even if the Commission decides to initiate proceedings under the FTA, the Commission could take separate legal action if the trading partner does not take corrective action or stalls the procedure.

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<sup>126</sup> Regulation (EU) 2016/1036 of the European Parliament and of the Council of 8 June 2016 on protection against dumped imports from countries not members of the European Union, OJ L 176, 30.6.2016, p. 21.

<sup>127</sup> Regulation (EU) 2016/1037 of the European Parliament and of the Council of 8 June 2016 on protection against subsidised imports from countries not members of the European Union, OJ L 176, 30.6.2016, p. 55.

<sup>128</sup> Commission Implementing Regulation (EU) 2020/379 of 5 March 2020 imposing a provisional countervailing duty on imports of continuous filament glass fibre products originating in Egypt, OJ L 69 of 6 March 2020, p. 14 and Commission Implementing Regulation (EU) 2020/870 of 24 June 2020 imposing a definitive countervailing duty and definitively collecting the provisional countervailing duty imposed on imports of continuous filament glass fibre products originating in Egypt, and levying the definitive countervailing duty on the registered imports of continuous filament glass fibre products originating in Egypt, OJ L 201 of 25 June 2020, p. 10.

<sup>129</sup> Price differentiation between different countries may be simply an expression of different demand elasticities in the countries of export and import. In addition, the importing country may also benefit from low import prices, provided the low prices are not an expression of a predatory pricing strategy ("Chinese state capitalism: A challenge for the European market economy", German Monopolies Commission, July 2019, p. 32)

<sup>130</sup> Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union, OJ L 791, 21.3.2019, p. 1.

The Agreement on the European Economic Area (EEA) brings together the EU Member States and the three European Free Trade Association (EFTA) States — Iceland, Liechtenstein and Norway — into a single market. EFTA has in place a State aid control system based on EU State Aid rules, with an independent supranational State aid control authority. As a result, the system is in practice well placed to prevent EFTA States from granting subsidies that would distort the EU internal market.

In the following, two recent Bilateral Agreements are described and analysed in more detail, the EU-UK Trade and Cooperation Agreement and the EU-China Comprehensive Agreement on Investment.

#### EU – UK Trade and Cooperation Agreement

The EU-UK Trade and Cooperation Agreement (TCA), agreed by the EU and the UK on 24 December 2020<sup>131</sup> and, pending European Parliament consent, provisionally applicable since 1 January 2021 (until 28 February 2021), sets out preferential arrangements in areas such as trade in goods and in certain services. It is underpinned by provisions ensuring a level playing field (provisions on environmental protection and climate, competition, subsidies, labour, etc.).

The TCA thus mainly applies to trade in goods by providing for zero tariffs and zero quotas on all goods that comply with the appropriate rules of origin. As regards free trade in services, the TCA limits the fees that customs may charge for services rendered and includes several modern disciplines that go beyond standard WTO commitments. In addition, rules applicable to individual subsidies are prescribed by the TCA but these are only enforced domestically by each Party (Art. 3.4.3). The arbitration tribunal under the dispute settlement mechanism of the TCA does not have jurisdiction over individual subsidies (Art. 3.13.2(a)).

In principle, all subsidies fulfilling the conditions of the subsidies chapter (chapter 3 of the TCA) are covered by the TCA. Specific exceptions exist as regards agriculture, fisheries and the audio-visual sector. However, even if a remedial measure is taken under the TCA because a subsidy causes a significant negative effect on trade or investment between the parties (Article 3.12), the TCA may fail to remove the distortive impact of the foreign subsidy on the EU internal market.

#### EU-China Comprehensive Agreement on Investment

On 30 December 2020<sup>132</sup>, the EU and China reached an agreement in principle on the Comprehensive Agreement on Investment (CAI). The CAI seeks to improve market access conditions for European companies by eliminating discriminatory laws and practices that prevent them from competing in the Chinese market on an equal basis with Chinese companies and companies from other third countries. As such, the CAI has a different objective – creating a level playing field for investors on the Chinese market – than a possible EU instrument to address distortive foreign subsidies on the EU market and may rather be seen as complementary.

In relation to subsidies, it contains a provision imposing transparency obligations as regards subsidies related to certain service sectors, thus complementing transparency requirements as set out in the existing multilateral rules on subsidies related to goods. A specific consultation procedure will apply requiring either side to engage in consultations in order to provide additional information on any subsidies that could have a negative effect on the investment interests of the other party and to seek to address such negative effects. However, the CAI does not set out an effective mechanism (i.e. it excludes State-to-State dispute settlement) to address and remedy the distortive impact that Chinese subsidies may have on the EU internal market. Thus, separate legal action on foreign subsidies could provide for more effective tools to fill the gap left open by the CAI, and FTAs more generally, in terms of effectively remedying the distortions caused by foreign subsidies. The CAI and a possible new instrument on foreign subsidies would therefore be complementary and mutually reinforcing each other.

<sup>131</sup> Press release: [https://ec.europa.eu/commission/presscorner/detail/en/ip\\_20\\_2531](https://ec.europa.eu/commission/presscorner/detail/en/ip_20_2531)

<sup>132</sup> Press release: [https://ec.europa.eu/commission/presscorner/detail/en/IP\\_20\\_2541](https://ec.europa.eu/commission/presscorner/detail/en/IP_20_2541)

As regards public procurement, the existing EU legal framework<sup>133</sup> aims at ensuring compliance with the principles of the Treaty on the Functioning of the European Union (TFEU). In particular, this includes the principles of free movement of goods, freedom of establishment and the freedom to provide services, as well as the principles deriving therefrom, such as equal treatment, non-discrimination, mutual recognition, proportionality and transparency. However, it does not specifically address distortions to the EU procurement markets caused by foreign subsidies. While Directives 2014/24/EU<sup>134</sup> and 2014/25/EU<sup>135</sup> allow contracting authorities to reject abnormally low offers if it can be established that a bidder has obtained incompatible State aid, the Directive does not contain any corresponding provision for foreign subsidies. In addition, while the grant of foreign subsidies can be considered in the overall assessment of a bid, any rejection of an offer as abnormally low needs to be justified by demonstrating that the foreign subsidy impedes the viability of the offer and the bidder's capacity to execute the contract at the (abnormally low) price offered.<sup>136</sup> However, contracting authorities enjoy a wide margin of discretion and are not legally required (and are probably not able) to investigate the existence of foreign subsidies when evaluating offers, and the Public Procurement Directives foresee no dedicated redress measures against distortive foreign subsidies. The International Procurement Instrument (IPI)<sup>137</sup> aims to incentivise trading partners to negotiate with the EU the opening of their procurement markets for EU business. Once adopted, it would enforce the principle of balanced reciprocal market access for EU business to third countries' procurement markets but it will not tackle distortions caused by foreign subsidies within the EU. The lack of such rules damages competition in the internal market in specific procedures and has long term harmful effects for economic operators as well as public authorities as described above under 2.3. In some cases the problem may be exacerbated by the fact that contracting authorities may feel an incentive to accept the lowest bids.

Inter-governmental agreements (IGAs) are concluded to facilitate investment. They may cover organising procurements intended for joint implementation or exploitation of a project, especially in large infrastructure. Such procurements are exempted from EU public procurement legislation provided the conditions laid down in Article 9 of Directive 2014/24/EU are fulfilled<sup>138</sup>, though they always have to be compatible with the EU Treaties. Distortive effects of foreign subsidies are not specifically scrutinised under such agreements. Therefore, a level playing field should be ensured within the proposed framework also for procurements under such agreements, especially due to their size and economic importance.

Finally, there are a number of sectoral rules which allow the EU to act to protect the internal market in the specific sectors. Regulation (EU) 2019/712 on safeguarding competition in air transport outlines the investigative powers of the Commission and the redressive measures it may

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<sup>133</sup> Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC, OJ L 94, 28.3.2014, p. 65.

Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC, OJ L 94 28.3.2014, p. 243

Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts OJ L 94 28.3.2014, p. 1

<sup>134</sup> Article 69(4) of Directive 2014/24/EU

<sup>135</sup> Article 84(4) of Directive 2014/25/EU

<sup>136</sup> Communication of the European Commission, "Guidance on the participation of third-country bidders and goods in the EU procurement market", C(2019)5494 final, chapter 3.

<sup>137</sup> Amended proposal for a Regulation of the European Parliament and of the Council on the access of third-country goods and services to the Union's internal market in public procurement and procedures supporting negotiations on access of Union goods and services to the public procurement markets of third countries, COM(2016) 34 final, 29 January 2016.

<sup>138</sup> This includes a provision that all such agreements must be communicated to the Commission, indicating a clear need for EU-wide scrutiny.

impose relating to practices which distort competition between EU and non-EU air carriers, and which cause, or threaten to cause, injury to EU air carriers. As such, Regulation (EU) 2019/712 covers discriminatory treatment adopted by a third country or subsidies granted by a third country government to the detriment of EU air carriers. To date, Regulation (EU) 2019/712 has not been applied, mainly because the investigation pursuant to Regulation 2019/712 can only be triggered by a complaint, i.e. in the absence of a complaint the Commission cannot investigate under this Regulation.

As regards the interplay between Regulation (EU) 2019/712 and a possible new legal instrument on foreign subsidies, the former as *lex specialis* takes precedence as regards situations and actors that fall within its scope. However, as the scope of application of the Regulation is limited to air carriers, a possible legal instrument on foreign subsidies could apply to other actors active in the aviation sector (such as ground handling). Similarly, Regulation (EU) 2019/712 does not apply to acquisitions and public procurement procedures.

Regulation 2016/1035 on protection against injurious pricing of vessels allows the EU to act against the sale of vessels that are sold at less than normal value and therefore cause injury to the Union industry. However, while this Regulation has formally entered into force, it has never been applied as its application is conditional on the ratification of the OECD Shipbuilding Agreement by South Korea and the US. Regulation (EEC) No 4057/86 of 22 December 1986 concerns unfair pricing practices in maritime transport but since its 35 years of existence, it has been used only once. This is because *inter alia*, it has therefore proven difficult to show that the conditions (e.g. the existence of dumping prices) under the Regulation are fulfilled. Therefore, in practice foreign subsidies are not captured by this Regulation..

A secondary root cause of the problem is the lack of transparency and data on foreign subsidies. Transparency is an essential governance element of subsidy control. It promotes compliance at all levels of government. It also offers the general public an overview of the expenditure of tax money thereby nudging the recipient of the subsidy into compliant behaviour, and to ultimately provide for better accountability of public spending. Furthermore, it allows undertakings to examine whether subsidies granted to competitors are in compliance with existing rules.<sup>139</sup> This is also why EU State aid rules include detailed transparency requirements.<sup>140</sup> In addition, Member States are obliged under the Transparency Directive<sup>141</sup> to be transparent on the financial relations between the State and public undertakings.

In terms of international subsidy policy, information is needed to better understand the impact that subsidies might have on international trade in goods,<sup>142</sup> and more generally on international trade and investment. Peer pressure between governments can also have a nudging effect towards more subsidy discipline.

As explained in Annex 4, Section 7, despite transparency obligations in international rules and other international efforts, comparable data on subsidies are difficult to find. In the absence of

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<sup>139</sup> Lillerud, K. The National Transparency Registers in Action, *European State Aid Law Quarterly* 2019 pp. 239 – 248; see also Vincent Verouden and Philipp Werner, *EU State aid Control: Law and Economics* (Kluwer Law International 2016), 247.

<sup>140</sup> These require Member States to publish all state aid awards above €500,000 on a dedicated website (see 2014 Communication on transparency and the General Block Exemption Regulation, OJ C 198, 27.6.2014, p. 30-34). Transparency extends also to fiscal aid, with specific rules ensuring that tax confidentiality is preserved. Moreover, complementary information on all authorized State aid in the EU, including information in relation to the transparency requirement, can be found in the database of competition cases: ISEF registry of the European Commission: <https://ec.europa.eu/competition/eojade/isef/>

<sup>141</sup> Directive 2006/111/EC.

<sup>142</sup> Communication from the European Union to the WTO negotiating group on rules, improving disciplines on subsidies notification, TN/RL/GEN/188.



information on subsidies, it is difficult to analyse to what extent trade and competition are influenced by subsidies, and it is more difficult to develop rules on subsidies in international negotiations, such as in EU trade agreements. In addition, there is less peer pressure among governments, from competing undertakings or from the public to diminish distortive subsidies.

## 2.6 How will the problem evolve?

The problem definition in sections 2.2, 2.3 and 2.4 described the issue of distortive foreign subsidies in the context of acquisitions, public procurement and other market situations. The following section describes how the problem will likely evolve in the future and why it is becoming more pressing.

### Third countries continue to use industrial policies, which include large volumes of subsidies.

Figure 2 in the previous section shows an upward trend in subsidy measures globally over the last decade. This increase has been consistently observed well before the pandemic, but is likely to accelerate as a result. Figure 5 in the same section illustrates that subsidies and other transfers have been an important element of economic policy in the last decades for countries around the world, which is also likely to continue into the future. Almost all countries have seen an increase of subsidies and transfers after the 2008-2009 financial crisis, which is manifested in the global increase from 29.4% of expenses in 2006 to 32.9% in 2011. This increase persisted in the following decade as the share of subsidies on a global scale did not go back to the pre-2008 levels. Using the Global Trade Alert (GTA) data, Evenett and Baldwin (2020) have shown that 32.7% of discriminatory trade policy interventions from 2009, including various types of subsidies, were still in place in 2020<sup>143</sup>.

### Post-COVID economic crisis will lead to higher levels of subsidisation around the world

According to the World Bank, global GDP is estimated to decrease by 4.3% in 2020 with a projected growth of 4% and 3.8% in 2021 and 2022 respectively. By comparison, the 2008-2009 financial crisis slowed down global GDP growth to 1.8% in 2008 and led to a drop of -1.7% global GDP in 2009<sup>144</sup>. The same World Bank report also estimates that the fiscal stimulus in 2020 (based on a sample of 61 countries) has been more than double compared to the fiscal response to the 2008-2009 crisis. As after the 2008-2009 crisis, there is a risk that a part of such incentives remain in place and continue to distort trade and investment flows in the coming years.

Based on the GTA data, Evenett and Fritz (2020) calculate that in the first ten months of 2020, G20 countries put in place 1.371 policy interventions, 1067 of which have harmed their trading partners<sup>145</sup>. 670 of these measures are considered trade-distortive subsidies, which includes 98 export incentives and support to firms in foreign markets and 581 non-export-related subsidies.

### Trade in services is expected to continue growing faster than trade in goods

As described in the problem definition section of this report, trade in services is not covered by the existing trade defence instruments. It is therefore more threatened by possible distortions caused by subsidies. According to the 2019 World Trade Report, global trade in services has

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<sup>143</sup> Evenett, S. J. and Baldwin, R. Revitalising Multilateralism: Pragmatic Ideas for the New WTO Director-General. CEPR, 2020. <https://voxeu.org/content/revitalising-multilateralism-pragmatic-ideas-new-wto-director-general>

<sup>144</sup> World Bank. Global Economic Prospects. January 2021. <https://www.worldbank.org/en/publication/global-economic-prospects>

<sup>145</sup> Evenett, S.J. and Fritz, J. Collateral Damage: Cross-Border Fallout from Pandemic Policy Overdrive. The 26th Global Trade Alert Report. CEPR, 2020. <https://voxeu.org/article/cross-border-fallout-pandemic-policy-overdrive>

been growing faster than trade in goods in 2005-2017 and the share of services in the global output has been projected to further increase from 74% in 2018 to 82-84% in 2040<sup>146</sup>.

The COVID crisis has provided an impulse for digitalisation of some services, but also had a negative impact due to various travel restrictions, which have limited transport and tourism, two areas with a large share in the services sector. The World Bank projects a 9.5% contraction of total global trade in 2020, comparable to the 2008-2009 financial crisis, followed by an average growth of 5.1% in 2021-2022<sup>147</sup>. Despite this slowdown, international trade in services is set to grow by 31% between 2019 and 2025 by some estimates.<sup>148</sup>

#### The deflated valuation of EU companies may lead to a higher number of acquisitions

The mergers and acquisitions (M&A) activity in Europe is closely linked to the economic cycle. In recent years, the number and total value of transactions have been growing since their lowest recorded levels in 2009<sup>149</sup>. While the number of transactions peaked in 2015, the total value only reached its highest level in 2018. This means that the average transaction value has increased over the decade, which corresponds to the number of notifications to the Commission, which also peaked in 2018<sup>150</sup>.

Due to the deflated value of some EU companies as a result of the COVID crisis, a similar wave of acquisitions may ensue. According to a survey of leading euro-area companies on the impacts of the COVID crisis, more than 50% of respondents expect to see an increase in concentration of their markets<sup>151</sup>. Due to the disruptions to the global production chains, some companies are also considering diversifying or localising parts of their supply chains. UNCTAD estimates a 40% drop in FDI in 2020 with a further decrease in 2021 and signs of recovery in 2022, noting, however, that investment activity by digital companies has actually increased<sup>152</sup>.

#### Large parts of the fiscal stimulus of the EU and Member States will be spent through public procurement

Public investment will play a key role in the recovery of the European economy from the crisis due to COVID-19. The major part of it will be implemented through public procurement. With significant fiscal stimulus put in place by Member States and an EU recovery budget of EUR 1.8 trillion (Multiannual Financial Framework of EUR 1.074 trillion for the next seven years + Next Generation EU of EUR 750 billion), public procurement contracts will present an attractive business opportunity for both EU and foreign(-owned) companies. They are likely to grow in importance beyond their pre-COVID 19 share of around 14% of EU GDP<sup>153</sup>.

The combination of these factors increases the likelihood that foreign subsidies may be used to distort the EU internal market in the future, in particular as regards subsidised acquisitions and public procurement.

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<sup>146</sup> WTO. World Trade Report 2019. The future of services trade. Available from:

[https://www.wto.org/english/res\\_e/booksp\\_e/00\\_wtr19\\_e.pdf](https://www.wto.org/english/res_e/booksp_e/00_wtr19_e.pdf)

<sup>147</sup> World Bank. Global Economic Prospects. January 2021. p. 10.

<sup>148</sup> The Western Union Company. The Global Services Trade Revolutions: Fuelling post-pandemic economic recovery and growth, 2020. <https://business.westernunion.com/en-gb/p/cmp/2020/the-global-trade-services-revolution>

<sup>149</sup> <https://intrawelt.com/en/mergers-acquisitions-pandemic-north-america-and-europe/>

<sup>150</sup> <https://ec.europa.eu/competition/mergers/statistics.pdf>

<sup>151</sup> Maqui, E. and Morris, R. The long-term effects of the pandemic: insights from a survey of leading companies. ECB Economic Bulletin, 8/2020. [https://www.ecb.europa.eu/pub/economic-bulletin/focus/2021/html/ecb.ebbox202008\\_06~bad87fcf9b.en.html](https://www.ecb.europa.eu/pub/economic-bulletin/focus/2021/html/ecb.ebbox202008_06~bad87fcf9b.en.html)

<sup>152</sup> UNCTAD. Impact of the COVID-19 Pandemic on Trade and Development. Transitioning to a new normal. 2020. p. 17. Available from: [https://unctad.org/system/files/official-document/osg2020d1\\_en.pdf](https://unctad.org/system/files/official-document/osg2020d1_en.pdf)

<sup>153</sup> European Council Conclusions of 1-2 October 2020. p. 2. <https://data.consilium.europa.eu/doc/document/ST-12802-2020-INIT/en/pdf>



### **3 WHY SHOULD THE EU ACT?**

#### **3.1 Legal basis**

A possible legal basis for EU interventions is Article 207 of the Treaty on the Functioning of the European Union (“TFEU”), possibly combined with Article 114 TFEU.

Article 207 TFEU provides for the adoption of measures defining the framework for implementing the common commercial policy. The scope of the common commercial policy is defined in Article 207(1) TFEU, which refers inter alia, to trade in services, foreign direct investment and measures to protect trade in the event of subsidies. The initiative is about foreign subsidies and their distortive impact on the internal market, including in situations where a subsidised company plans to acquire an EU target or participate in an EU procurement. Other EU instruments dealing with foreign subsidies (namely the EU anti-subsidy Regulation) or with foreign investment (namely the FDI Screening Regulation) were based on Article 207(2) TFEU.

Article 114 TFEU is about the approximation of laws, and could be a suitable additional legal basis given the internal market dimension of the initiative. Article 114 provides for the adoption of measures which have as their object the establishment or functioning of the internal market. While the initiative is indeed about foreign subsidies distorting the internal market, to date there are no national rules dealing with foreign subsidies. However, several Member States<sup>154</sup> have indicated that they see a need to address the distortions caused by foreign subsidies. Therefore, in the absence of EU action, some Member States may decide to put in place national legislation. Consequently, it would be more efficient to put in place a uniform EU-wide solution to address distortive foreign subsidies that applies across the entire internal market. Therefore, Article 114 TFEU could also be a suitable additional legal basis given for the initiative.

#### **3.2 Subsidiarity: Necessity of EU action**

Article 5(3) of the Treaty on European Union (TEU) provides that the principle of subsidiarity applies in areas which do not fall within its exclusive competence of the European Union. Article 3(1)(e) of the TFEU provides that the EU shall have exclusive competence in the area of common commercial policy. The possible legal basis (Article 207(2) TFEU) falls into this category of exclusive competence. While legally speaking, the question of subsidiarity does not arise with respect to Article 207 TFEU, it would arise with respect to Article 114 TFEU.

In any event, there seems to be a need for action at EU level. Subsidies cause distortions on the internal market including in the context of acquisitions of EU targets and of public procurement. The situation is comparable to State aid granted by EU Member States, which by its very nature has effects on more than one Member State. Likewise distortions caused by foreign subsidies may have a Union dimension comprising one or more Member States, so that foreign subsidies can best be tackled through legislative action at the EU level.

Finally, pursuant to Article 3(1)(e) TFEU, the EU is exclusively competent for trade defence instruments, including the EU anti-subsidy Regulation, which are also based on Article 207(2) TFEU. The same is true for legislation on State aid. According to Article 3(1)(b) TFEU, the EU shall have exclusive competence in the area of "the establishing of the competition rules necessary for the functioning of the internal market". The EU has thus experience in legislating on subsidies as well as on State aid, and it is therefore more effective if the EU, and not Member States, legislates also on foreign subsidies.

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<sup>154</sup> Among others The Netherlands, France, Germany, Poland and Italy.

### **3.3 Subsidiarity: Added value of EU action**

There seems to be an added value of EU action. Notably, the objectives and added value of a control of foreign subsidies can be compared to those of the existing State aid control i.e. to ensure effective competition and a level playing field in the internal market. The compatibility criteria in State aid ensure that the amount of aid is kept to the minimum necessary and proportionate to achieving an objective of common interest. Member States are therefore prevented from spending excessive and thus distortive amounts of State aid or from entering into ‘subsidy races’ with each other. The publicly available information on Member States’ support also fosters market discipline.<sup>155</sup> Such benefits could not be achieved at Member State level.

Moreover, having a Regulation at EU level allows potential beneficiaries of foreign subsidies to know ex ante the rules that the competent supervisory authority will use to assess the existence of and possible distortions caused by foreign subsidies. This guarantees predictability and increases the legal certainty of the system across different Member States.

## **4 OBJECTIVES: WHAT IS TO BE ACHIEVED?**

### **4.1 General objectives**

The general objective of this initiative is to restore the level playing field on the internal market so that it is not distorted by foreign subsidies.

### **4.2 Specific objectives**

This initiative has two specific objectives.

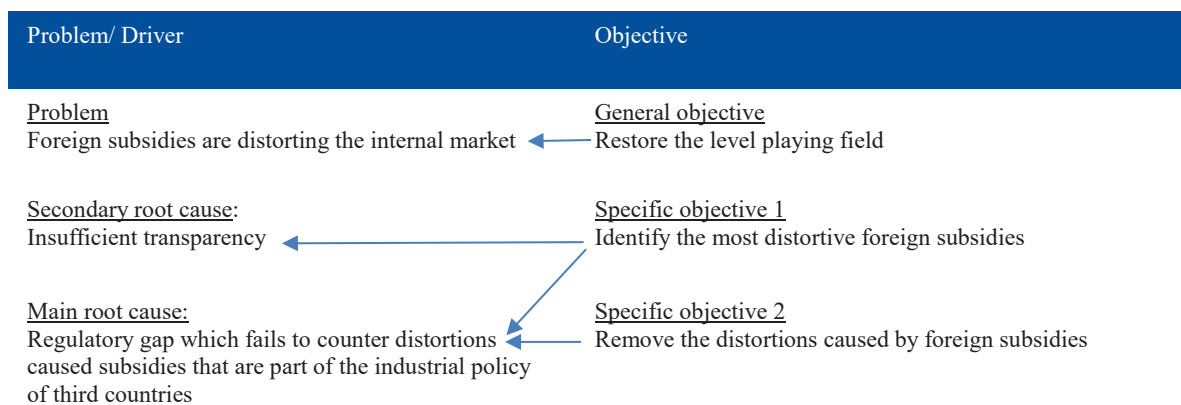
1. Identify the most distortive subsidies: This specific objective addresses on the one hand the root cause that there is a general lack of information about subsidies at international level and on the second hand that there are no criteria and procedures to assess the potential distortion of the EU internal market caused by foreign subsidies.
2. Remove the distortions caused by foreign subsidies: This objective addresses the root cause that there are no tools to remove distortions caused by foreign subsidies once identified.

The table below illustrates the intervention logic, that is, the main relations between the problem, the driver and the objectives.

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<sup>155</sup> Commission Staff Working Document: Fitness Check of the 2012 State aid modernisation package, railways guidelines and short-term export credit insurance, SWD(2020) 257 final.

Table 4. Intervention logic



## 5 WHAT ARE THE AVAILABLE POLICY OPTIONS?

This report considers four types of policy options to address the three problems. The four types of policy options are as follows:

- Option 1: do nothing;
- Option 2: develop guidance;
- Option 3: change existing EU rules;
- Option 4: develop a new legal instrument.

The Inception impact assessment report proposed a fifth policy option, which entailed changing international rules. This report no longer presents such fifth option and instead includes its substantive elements in the baseline scenario, as the Commission will in any event pursue such policy initiative, namely to aim to promote the development of international rules to address negative impacts of subsidies.

### 5.1 What is the baseline from which options are assessed?

To date, there are several areas with rules in place allowing to address certain aspects of foreign subsidies across the three problems described in Section 2 of this report.

In particular, there are **international rules on subsidies**, namely the GATT and the WTO SCM Agreement. These rules allow the EU to bring litigation against a WTO Member before a WTO panel for breaches of the SCM Agreement. They also set out the possibility to take countervailing measures against the subsidising WTO member. However, the scope of application of the SCM Agreement is limited to trade in goods. While the GATS includes an inbuilt mandate to further negotiate disciplines on service subsidies, as well as the possibility to subject subsidies to non-discrimination obligations, the GATS – unlike the GATT and the SCM Agreement - does not set out the possibility to countervail subsidies. The EU is aiming to increase international transparency on subsidies to goods.<sup>156</sup> It is more generally calling for new rules on industrial subsidies (i.e. subsidies to goods) as essential to counter negative effects of heavy subsidisation on international trade, as outlined in the Commission’s Communication on the trade policy review.<sup>157</sup> It is also considering new international rules on State owned enterprises, focusing on

<sup>156</sup> See e.g. JOB/GC/204.

<sup>157</sup> Communication from the Commission on the Trade Policy Review - An Open, Sustainable and Assertive Trade Policy. COM(2021) 66 final. Page 21.

the behaviour of SOEs in their commercial activities, in line with the disciplines already agreed in several bilateral free trade and investment agreements. There is a GATS mandate to develop disciplines on service subsidies, but this is not actively pursued by WTO Members at this stage. While reforming WTO is one of the EU's priorities, it has to be borne in mind that any changes to WTO rules have to be negotiated at the level of the WTO, with the timeline and prospects dependent on achieving consensus among WTO Members. The success of reform depends on the commitment of WTO Members and would in any event only partially address the identified regulatory gap. Even revised multilateral rules would not cover services, investment or other financial flows in relation to the establishment and operation of undertakings in the EU. The EU's endeavours to reform the WTO agenda are therefore complementary to any of the options discussed below. This was also confirmed in the feedback received on the Inception Impact Assessment.<sup>158</sup> A third of the contributors indicated that they consider the reform of international rules complementary to legislative action at EU level, but not realistic in the near future.

The **EU's bilateral FTAs** normally cover goods, services and investment. They generally prohibit the most harmful types of subsidies (such as unlimited guarantees), and include transparency and consultation clauses. However, comprehensive bilateral trade agreements exist only with a limited number of third countries. Agreements with some neighbouring countries include the commitment to put in place a subsidy control inspired by State aid rules, but normally do not provide for timely solutions to address distortive subsidies.<sup>159</sup> FTAs also contain a chapter covering countervailing duty provisions, which restate the WTO rights and obligations including those in the ASCM, and contain some WTO-plus provisions. However, those chapters do not cover services and investments. The EU is continuing to negotiate FTAs, and could aim to develop more comprehensive provisions on subsidies in future bilateral trade agreements. This was also proposed in the feedback received on the Inception Impact Assessment. At the same time, it is considered unrealistic to change the subsidy provisions of existing agreements. In any event, even for new agreements, any changes to the current approach would have to be accepted by the respective negotiating partners, and their impact would be limited to bilateral relations.

The **EU anti-subsidy rules**<sup>160</sup> are based on the SCM Agreement and thus apply to injury caused by the import of subsidised goods. They do not cover services, investment or other financial flows in relation to the establishment and operation of undertakings in the EU. In addition to the limitation to goods, the EU's anti-subsidy rules apply in principle only to subsidies provided to companies in the granting (third country) jurisdiction. These features of the EU anti-subsidy Regulation could be changed only if the SCM Agreement were to be changed.

The Treaty includes provisions on **State aid** granted by EU Member States. These rules do not cover subsidies granted by non-EU countries. They therefore do not allow to control and remove distortions caused by foreign subsidies. Already to date, however, foreign subsidies could – to a limited extent – be taken into account when assessing the compatibility of aid granted by a Member State. Indeed, the Research, Development and Innovation (RDI) Framework<sup>161</sup> and the IPCEI Communication<sup>162</sup> include a 'matching aid' clause, which provides for the possibility of granting higher aid intensities to match the aid amount received for similar projects by competitors located outside of the EU. Foreign subsidies can in principle also be taken into

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<sup>158</sup> [https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12621-Trade-investment-addressing-distortions-caused-by-foreign-subsidies/feedback?p\\_id=8607947](https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12621-Trade-investment-addressing-distortions-caused-by-foreign-subsidies/feedback?p_id=8607947).

<sup>159</sup> For details, see section 2.5 above.

<sup>160</sup> Regulation (EU) 2016/1037 of the European Parliament and of the Council of 8 June 2016 on protection against subsidised imports from countries not members of the European Union, OJ L 176, 30.6.2016, p. 55.

<sup>161</sup> Communication from the Commission: Framework for State aid for research and development and innovation, OJ C 198, 27.6.2014, p. 1.

<sup>162</sup> Communication from the Commission: Criteria for the analysis of the compatibility with the internal market of State aid to promote the execution of important projects of common European interest, OJ C 188, 20.6.2014, p. 4.

account when assessing the proportionality of investment aid under the Regional aid guidelines (RAG).<sup>163</sup> The use of these provisions would allow the Member State concerned to give more State aid to counter harmful foreign subsidies.

**EU antitrust rules** apply to anticompetitive behaviour of undertakings emanating from agreements between undertakings or from market dominance. Whether an undertaking receives financial support is irrelevant for the assessment whether an agreement with another undertaking distorts competition. Likewise, market dominance as such is not forbidden but only anticompetitive behaviour (abuse) resulting from market dominance. Subsidies allowing an undertaking to become dominant therefore do not as such lead to a violation of EU antitrust rules. Nor can a foreign subsidy facilitating anticompetitive behaviour of a non-dominant firm be addressed under existing rules.

As regards specifically problem 1, there are two sets of relevant existing rules, namely the **EU Merger Regulation (EUMR)** and the EU Foreign Direct Investment (FDI) Screening Regulation.<sup>164</sup> Under the EUMR, undertakings have to notify to the Commission relevant ‘concentrations’ with an EU dimension prior to their implementation.<sup>165</sup> The Commission then assesses whether the concentration is detrimental to competition i.e. whether it causes a ‘significant impediment to effective competition’. This test is not designed to take into account possible foreign subsidies involved in concentrations. In practice, foreign subsidies are therefore unlikely to play a role, let alone decisive in the assessment of concentrations under the EUMR.

The **EU FDI Screening Regulation** allows EU Member States to take mitigating measures on certain third-country investments on grounds of security or public order. The Regulation considers subsidies only to determine the extent to which a foreign investor is under state influence but does not allow to investigate economic distortions caused by foreign subsidies.

As regards specifically problem 2, the relevant existing rules are the **Public Procurement Directives** (Directives 2014/23/EU, 2014/24/EU, 2014/25/EU and 2009/81/EC), which do not address foreign subsidies. Contracting authorities do not investigate distortions caused by foreign subsidies.<sup>166</sup> The provisions in the Directives on abnormally low tenders, Art. 69 of Directive 24/2014/EU and Art. 84 of Directive 25/2014/EU, stipulate that contracting authorities should assess whether the tenderer is able to correctly carry out the contract at the price offered, irrespective of whether the (low) price level is due to the existence of a foreign subsidy. A foreign subsidy may in fact make the offer more viable.

The plurilateral **WTO Government Procurement Agreement (GPA)** does not address the question of foreign subsidies. The existing provision on abnormally low tenders merely allows procuring entities to verify with the supplier that it satisfies the conditions for participation and is capable of fulfilling the terms of the contract. The GPA might be reviewed to include specific rules to deal with distortive foreign subsidies; however, this is currently not being pursued.

## 5.2 Options considered but discarded at an early stage

Options 2 and 3 below propose issuing guidance or amending EU State Aid rules (to address problem 3), the EU Merger Regulation (to specifically address problem 1) and the Public

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<sup>163</sup> Guidelines on regional State aid for 2014-2020, OJ C 209, 23.7.2013, p. 1, prolonged until end 2021, see OJ C 224, 8.7.2020, p. 2.

<sup>164</sup> Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union, OJ L 791, 21.3.2019, p. 1.

<sup>165</sup> The EUMR uses the term ‘concentration’ while the present document refers to the more commonly used term ‘acquisition’.

<sup>166</sup> They also do not investigate distortions caused by state aid.

Procurement Directives (to specifically address problem 2). Furthermore, below the list of other set of rules that were not found suitable to examine in detail under options 2 and 3:

- The EU anti-subsidy Regulation is based on the SCM Agreement, which is limited to subsidies to goods imported in the EU. Without changing international rules, neither developing guidance to nor adapting the EU anti-subsidy Regulation would allow to fully address the three problems. None of the respondents providing feedback on the Inception Impact Assessment considered guidance or changing the EU anti-subsidy Regulation a suitable option. Some respondents called however for a better implementation of existing legislation.
- Antitrust rules focus on anticompetitive behaviour of undertakings, either due to agreements between undertakings or market dominance and therefore have a different objective. These rules require to a large degree that undertakings assess themselves whether their behaviour is in line with the rules. This seems difficult to envisage if distortions on the internal market are caused by foreign subsidies, given that no experience exists to date in the absence of rules. Therefore, neither guidance nor adapting the existing rules is considered further in the following. None of the respondents providing feedback on the Inception Impact Assessment considered guidance or changing antitrust rules as an option.
- As regards the EU FDI Screening Regulation, its scope is limited to public security and order in line with GATS. Guidance or changes to the FDI Regulation are therefore not further considered, as this would allow to address distortive subsidies only for a small number of concentrations. Only one respondent providing feedback on the Inception Impact Assessment considered guidance to the EU FDI Screening Regulation a suitable option to address foreign subsidies.

## **Option 2**

As pointed out in the baseline, some **State aid provisions** allow to take into account foreign subsidies in the assessment of State aid. Foreign subsidies are explicitly mentioned in the matching aid clause under the RDI Framework and the IPCEI Communication. They could also be taken into account in the proportionality assessment under the RAG. Neither of these provisions has however been used to date. Option 2 thus proposes to provide guidance to make it easier for Member States to show that there was a foreign subsidy when invoking the matching aid clause, or in the proportionality assessment under RAG. If there was a foreign subsidy, the matching aid clause as well as the RAG allow EU Member States to provide a higher amount of State aid than in the absence of a foreign subsidy. This option would be particularly targeted to address problem 3. This option would however apply only to a small subset of cases involving foreign subsidies, and it would only indirectly redress distortions caused by foreign subsidies. Only one respondent providing feedback on the Inception Impact Assessment considered guidance on State aid rules a suitable option to address the problem. Furthermore, this option risks triggering a subsidy race with third countries or even inside the EU, causing wasteful public support, and causing even more distortions on the internal market. Providing guidance on State aid rules is therefore discarded as it is likely to be ineffective.

To specifically address problem 1, option 2 considers developing guidance on collecting information on foreign subsidies in merger cases under the **EUMR**. Already to date, companies have in principle to provide information on financial support according to the notification form, which could be used more extensively to systematically collect information on foreign subsidies. While this solution may contribute to gathering better data on foreign subsidies over time, the information collected could not be used to effectively address foreign subsidies when assessing



concentrations. Only one respondent providing feedback on the Inception Impact Assessment considered guidance on merger rules a suitable option to address the problem. To address the potential impact of foreign subsidies on the internal market, the legal test set out in the EUMR would need to be changed. It currently focuses on the significant impediment of effective competition, and does not allow to specifically take into account foreign subsidies. Providing guidance for the EUMR is therefore discarded as ineffective.

To specifically address problem 2, option 2 considers developing guidance on the application of the existing rules in the **Public Procurement Directives** without changing them. The provisions on abnormally low tenders in the Directives, Art. 69 of Directive 2014/24/EU and Art 84 of Directive 2014/25/EU, are the only provisions currently allowing to address foreign subsidies in public procurement, albeit in a very limited and indirect way. As the Public Procurement Directives do not address foreign subsidies, guidance could not propose criteria on how a contracting authority should assess the distortive effect of foreign subsidies and reject a tenderer on the sole ground that it received foreign subsidies. None of the respondents providing feedback on the Inception Impact Assessment considered guidance on the Public Procurement rules as an adequate option to sufficiently address the regulatory gap in the existing framework.

In conclusion, Option 2 i.e. issuing guidance on EU State Aid rules, the EU Merger Regulation or the Public Procurement Directives would not be effective.

### **Option 3**

As pointed out in the baseline, **State aid rules** only apply to aid granted by EU Member States. Changing the Treaty to extend State aid control to subsidies granted by non-EU States is not considered a realistic option as Treaty changes for this purpose are generally considered politically unrealistic. An important element of the State aid rules set out in the Treaty is also that they prevent EU Member States from putting an aid measure into effect until the Commission has found it compatible with the internal market. The Treaty does not have such binding effect on non-EU States. The only possibility that could be considered in option 3 is therefore to adapt EU State aid rules in a way that a Member State could grant compensatory State aid to an EU undertakings if its competitor receives foreign subsidies. This would mean that the possibilities similar to the matching aid clause provided for in the RDI Framework and the IPCEI Communication, as well as to the proportionality assessment under RAG would be extended to all State aid rules. None of the respondents providing feedback on the Inception Impact assessment considered changing State aid rules a suitable option. While changing State aid rules to allow for more State aid may be more effective than Option 2 due to its legally binding nature, it has the same downsides as option 2, even exacerbated by the fact that option 3 would go beyond the current possibilities of matching aid set out in the RDI Framework, the IPCEI Communication and RAG. Option 3 does not allow to directly address the distortion caused by a foreign subsidy, and even risks causing new distortions. It might ultimately lead to harmful subsidy races. Amending EU State aid rules is therefore discarded because considered ineffective.

To specifically address problem 1, option 3 considers changing the **EUMR** and including an additional assessment standard, allowing it to take into account distortions caused by foreign subsidies in the context of concentrations. It is the purpose of the EUMR to investigate whether a concentration distorts competition by giving rise to a “significant impediment to effective competition” (SIEC). A very different question is whether the concentration process as such was distorted. That latter question is however the most relevant if foreign subsidies are granted in the context of a concentration. Including an assessment of foreign subsidies in the EUMR would therefore fundamentally alter the legal test and introduce considerations that are alien to the current assessment approach. In addition, including an assessment of foreign subsidies would risk overburdening the review process and rendering it less clear. None of the respondents providing

feedback on the Inception Impact Assessment considered changing the EUMR a suitable option to address the problem. Including any consideration of foreign subsidies in the EUMR would at a minimum blur the purpose of the legislation as two different assessment standards would be included. Their interplay and respective importance would be unclear. This option would therefore risk weakening both the EUMR and undermine the effectiveness of the control of foreign subsidies. Amending the EUMR is therefore discarded because considered ineffective.

To specifically address problem 2, option 3 would propose to amend the **Public Procurement Directives**. Under this option, new provisions would be introduced in the Directives enabling or obliging contracting authorities to address foreign subsidies in specific public procurement procedures. The new provisions would set out how (procedure and criteria) contracting authorities assess whether a tender involves a foreign subsidy, under which conditions this foreign subsidy distorts the public procurement procedure, and would include redressive measures such as the rejection of tenders from the public procurement procedure. Under the Directives, the contracting authorities at Member State level are the responsible authorities, and amendments of the Directives would have to follow largely this regulatory logic. Setting out the methodology for assessing foreign subsidies (and the balancing test, to be applied in an EU-wide manner) would not be appropriate in the Directives and would require the adoption of a horizontal instrument. Such an amendment would also leave the implementation to a great extent in the hand of the contracting authorities that are not equipped for that task. Most stakeholders favour legislative action at EU level. Commenting on the Inception Impact Assessment, five respondents (out of 23) – i.e. one Member State and four other stakeholders – specifically indicated favouring changing the PP Directives.

In conclusion, all three possibilities contemplated under option 3 are either politically unfeasible (changes to the EU Treaty) or ineffective.

### 5.3 Option to be further assessed

Option 4 considers developing new legislation to address the distortions of the internal market caused by foreign subsidies.

This reflects the necessity to have effective tools in place to deal with distortions in the internal market and ensure a level playing field. Indeed, increasing the EU's capacity to pursue its interests and enforce its rights, including autonomously where needed, was set out as one of the objectives of the EU's new trade policy<sup>167</sup>. Assertiveness and rules-based cooperation form a key component of the model of Open Strategic Autonomy that the EU is pursuing.

New legislation was also the preferred option of more than half of the respondents providing feedback to the Inception Impact assessment.

In such legislation, a supervisory authority would investigate whether foreign subsidies granted to undertakings active in the internal market distort the internal market and, if so, may adopt redressive measures. The relevant counterpart would be the undertaking receiving a foreign subsidy, and not the public authority granting it. This is different from EU State aid control, where the relevant counterpart is the EU Member State granting the State aid. This is because the EU Treaty defines as counterpart the EU Member States, and the Commission is empowered by the Treaty to order Member States to alter or recover incompatible aid. This is not the case for third countries.

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<sup>167</sup> Communication from the Commission on the Trade Policy Review - An Open, Sustainable and Assertive Trade Policy. COM(2021) 66 final.

Hence, while new legislation to address distortive foreign subsidies would emulate to a large extent State aid rules, there would also be differences between the two. Against this backdrop, the design parameters for drawing up a new instrument on foreign subsidies are as follows:

- the competence level i.e. which level of government would enforce the legislation;
- the investigative approach, including possible notification thresholds;
- the assessment criteria to determine distortive foreign subsidies;
- the balancing test to take into account possible positive impacts of foreign subsidies and;
- the redressive measures to remedy the negative effects of distortive foreign subsidies.

The White Paper proposed as preferred option a new legal instrument based on three modules. Each module had a different scope: Module 1 for addressing general distortions, module 2 for addressing distortions in large acquisitions and module 3 for distortions in large public procurement procedures. Each module consisted of a different configuration of the design parameters presented above.

The options presented in this section of the impact assessment refer to the options for each design parameter. The combination of options of these parameters into policy packages (or modules) will be described and compared in section 7 of this report. Section 8 of this report will then present the preferred policy packages (or modules) and will explain the differences with those presented in the white paper.

The options under each design parameter are presented below. Differences with the White paper - at the level of design parameters- will be also explained below.

### *5.3.1 Design parameter (a): Competence level*

There are two possible options, which were also outlined in the White Paper:

- a1) Only the Commission to enforce the legislation;
- a2) Shared enforcement competence between the Commission and Member States.

The enforcement of the new instrument could either rest exclusively with the Commission or be shared between the Commission and Member States' authorities. If the Commission were exclusively competent, Member States could nonetheless be involved in the decision-making process through an Advisory Committee. This Committee would be consulted on any decision adopted under the new legal instrument and the Commission would take utmost account of the opinions issued by the Committee. In a shared system of enforcement, national authorities could investigate foreign subsidies in their own countries, while the Commission would focus on EU-wide impacts but would also be free to also investigate national cases. Exclusive Commission enforcement power would mirror the system of enforcement for trade policy and State aid rules.

In response to the White Paper, many Member States and most stakeholders argued in favour of exclusive Commission enforcement. There were however also a few Member States that favoured shared enforcement.

### *5.3.2 Design parameter (b): Investigative approach*

In terms of investigative approach, and as also presented in the White Paper, there are five options:

**Option b1 (Ex officio):** The supervisory authority can act upon market information submitted for example by competitors and upon its own market investigations, sector studies (i.e. by the OECD), or trade distortion reports. An ex officio system is less burdensome for the undertakings

receiving foreign subsidies (compared to a notification system as explained below). It puts the burden to collect the relevant facts and information on the supervisory authority, which would however need to have effective tools to gather information. The supervisory authority should be able to ask undertakings and business associations to supply the relevant information and may have the possibility to impose sanctions or assess on the basis of the facts available if undertakings refuse to submit complete and accurate information. It should also have the possibility to inspect company premises. If it is not possible to gather all necessary information, the supervisory authority could decide on the basis of the facts available.

Options based on a notification system: Undertakings would be required to notify foreign financial contributions to the supervisory authority. Such a notification requirement would be linked to financial contributions in the context of certain transactions, namely acquisitions and public procurement procedures. Like under option b1 (ex officio), the supervisory authority would have deterrent sanctions at its disposal if undertakings refuse to submit complete and accurate information. In addition, a failure to notify could result in fines and penalty payments, but would also trigger the corresponding procedure, which would have a suspensive effect on the transaction and could result in the prohibition of an acquisition or a prohibition of award in the case of public procurement.

The notification requirement would only apply if certain threshold are met, to avoid an overly high administrative burden. Setting the notification threshold(s) implies a trade-off between administrative burden and general effectiveness of the instrument.

As regards those thresholds, there are different options:

**Option b2 (no thresholds)**, implying that every transaction or financial contribution must be notified;

**Option b3 (moderate thresholds)**, implying that substantial amounts of financial contribution/important transactions must be notified;

**Option b4 (high thresholds)**, implying that only very high amounts of financial contribution/very important transactions must be notified. The final option, **option b5, would combine ex-officio with notification**. In particular, a notification for the highest financial contributions or most important transactions and an ex-officio review for other cases.

Section 6 of this report introduces several scenarios as regards quantitative thresholds, categorised as moderate and high. Section 6 then estimates the number of cases that would be caught under each scenario and in Section 7, different quantitative thresholds are compared as regards effectiveness and efficiency which then leads to choosing the preferred threshold level.

During the consultation on the White Paper, views on the investigative approach were mixed, but overall, stakeholders favoured combining an ex officio approach with notification of financial contributions for certain types of transactions.

As regards the thresholds for notification, most stakeholders considered quantitative thresholds as most suitable, while some others also suggested qualitative thresholds. There was no consensus on the right level of the threshold.

Given the high thresholds used for notification in option 4, cases notified would account for only a small part of all cases dealt with under existing instruments such as EU merger control and public procurement rules. In the few cases where there would be an overlap, procedural synergies could be ensured in practice, to the extent possible. For instance, the timelines of parallel reviews under different instruments (notably under the new instrument and the EU Merger Regulation) could be aligned, thereby avoiding unnecessary delays or legal uncertainty. Similarly, the type and format of the information to be provided in notifications under different instruments could be

aligned as much as possible, enabling businesses to simply replicate documents and amend or complement them only in a limited way for each specific notification. By contrast, existing instruments prohibit the use of information provided under one procedure for procedures under different legal instruments. It would thus not be possible to use a notification under the EU Merger Regulation to exempt an undertaking from providing the same information under a possible new legal instrument.

In that regard, business transactions already today often face scrutiny under several regulatory regimes globally (notably parallel merger control in several jurisdictions, as well as FDI screening). A new legal instrument would only be one addition. Undertakings and public authorities thus have significant experience in dealing with such parallel reviews and seeking alignment, which in the case of a new instrument will be facilitated by the Commission also handling EU merger control.

As regards the interaction between a possible new instrument and specific public procurement procedures, it is envisaged that the instrument would be designed in such a way as to have minimum, if any, impact on the ongoing procurement procedure. Under mandatory notification, the investigation of the foreign subsidy would be carried out in parallel with the evaluation of tenders. The deadlines for concluding the investigation would be in line with the time needed for the typical evaluation to be finalised. The contracting authority would be able to award the contract to a non-subsidised bidder if it proposes the best tender, and would only have to wait for the outcome of the investigation if the subsidised bidder would be set to win the contract. In any case, they would be free to award the contract to the best bid should the deadline for the investigation lapse without a decision. Under ex-officio, such investigations would usually take place only after award, and thus have no impact on the outcome of the procurement procedure, and would focus on correcting the damage to the internal market through the use of fines.

### 5.3.3 *Design parameter (c): Thresholds below which, subsidies are unlikely to be distortive*<sup>168</sup>

In addition to a notification threshold for financial contributions in the context of certain transactions, the White Paper suggested also a general threshold below which, foreign subsidies could be presumed not to distort the internal market.

Two options are considered for the new instrument:

- c1) EUR 200 000
- c2) EUR 5 million

The new instrument could include a threshold below which foreign subsidies would be presumed not to distort the internal market. This threshold could be either set at EUR 200 000, i.e. at the same level as in EU State aid rules, or at a substantially higher level, notably, EUR 5 million over a consecutive period of three years. The White Paper suggested to set the amount at EUR 200 000.

The main argument for setting a higher threshold than under EU State aid rules is that large categories of EU State aid are exempted from scrutiny by block exemptions and other secondary legislation. In the EU, only about 5% of the aid granted needs to be submitted to the Commission for clearance. Section 6 of this report shows that a threshold of EUR 5 million would capture at least five per cent of the highest aid amounts in the EU. Section 6 also analyses the relevance of

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<sup>168</sup> In the White Paper, this term was referred to as *de minimis*



such threshold in the context of foreign subsidies. In response to the White Paper, some respondents argued for a substantially higher threshold given that foreign subsidies are not subject to block exemptions. However, other respondents considered EUR 200 000 appropriate.

#### *5.3.4 Design parameter (d): Assessment criteria*

The White Paper suggested a combination of categories of foreign subsidies considered likely to distort the internal market. These categories were broadly based on those of prohibited State aid. Foreign subsidies outside these categories would require a more detailed assessment based on indicators that help to determine whether the subsidy distorts the internal market.

The new instrument would pursue the approach outlined in the White Paper, and further refine it.

Under the new legal instrument, a foreign subsidy would distort the internal market if it improves the competitive position of its recipient, and thereby distorts competition. Such a distortive foreign subsidy would cause negative impacts on the recipient's competitors or more broadly on market functioning. The distortive effect does in principle not depend on whether the subsidy was granted by a Member State (State aid) or by a third country (foreign subsidy). However, for a foreign subsidy, it would be necessary to establish whether it has an impact in the EU internal market or just in the domestic market of the third country granting it.

Subsidies which are usually considered distortive include those which directly facilitate concentrations, which are given to an ailing undertaking without a restructuring plan, export subsidies or unlimited guarantees.

Beyond these categories, the following indicators would help establishing whether a subsidy results in negative impacts:

- the size of the subsidy, as very large subsidies can be particularly distortive;
- the nature of the subsidy, as operating subsidies are more likely to distort than subsidies promoting investments;
- the characteristics of the affected market, for instance subsidies granted to companies that already enjoy a considerable market share in sectors with low levels of competition in the internal market, are likely to have a harmful impact.

Finally, the possible distortion on the internal market caused by a given subsidy could be balanced with the positive effects on the development of the relevant economic activity, as outlined in 5.3.5 below.

#### *5.3.5 Design parameter (e): Balancing test*

The White Paper suggested that the EU's policy objectives would be taken into account when assessing whether a distortive foreign subsidy has a positive impact. The distortion caused would be balanced against the possible positive impact of the subsidised economic activity.

There are two options as regards the new instrument:

e1) No balancing test

e2) Balancing test

The balancing test would allow balancing the distortion caused by the foreign subsidy with the positive effects on the development of the relevant economic activity where warranted. As regards the implementation, and inspired in EU State Aid rules, the Commission would take the balancing between the negative and the positive effects into account when determining the



appropriate redressive measures and on the nature and level of those redressive measures. For instance, if the distortion is fully outweighed by the positive effects, the Commission may abstain from imposing redressive measures.

While the White Paper referred to “EU public policy objectives”, it is now suggested to rather refer to a balancing between negative and positive effects to better align the instrument with EU State aid rules. Therefore, it is proposed to refer to the test as “Balancing test” instead of “EU interest test”.

In response to the White Paper stakeholders were generally supportive of including a balancing test and some asked for more explanations. Moreover, some respondents argued that the application of a balancing test should not prevent the imposition of redressive measures.

It should be noted that the balancing test would always work in the advantage of the recipient of foreign subsidies. It could not lead to the imposition of redressive measures for subsidies that are not found to be distortive. The application of the balancing test would rely on information provided by the undertaking, possibly also by public authorities. In any case, the Commission would be bound by the principle of proportionality, further limiting discretion.

### 5.3.6 *Design parameter (f): Redressive measures*

The new instrument could include a ‘toolbox’ of redressive measures, which builds on the measures used in State aid. As this toolbox could address in principle all potential distortions caused by subsidies, there is no need to decide on alternative redressive measures. However, as for State aid control the supervisory authority would have to decide on a case-by-case basis, which specific redressive measures to use to redress the distortion caused by a specific foreign subsidy.

In any event, it would first need to be investigated if and how a foreign subsidy distorts the internal market. Depending on this case-specific assessment of the distortion and the application of the balancing test, it could be envisaged to impose a reimbursement of the distortive foreign subsidy. In other cases, it could be more appropriate and effective, to directly redress the identified distortion with a behavioural or structural remedy adapted to the specific situation. This approach is in line with State aid control, for example, with the remedial measures under the Rescue and Restructuring Guidelines<sup>169</sup>, in the financial sectoral guidelines<sup>170</sup> or under the Covid-19 Temporary Framework<sup>171</sup>.

In the replies to the consultation on the White Paper various stakeholders commented on the redressive measures mentioned therein. Several Member State authorities for example indicated that a redressive payment may not be an effective remedy as it would be difficult to monitor. Some other stakeholders stressed that strong and effective redressive measures coupled with sanctions for non-compliance would be necessary. In contrast, some voiced concern that redressive payments to foreign or EU states may lead to political tension and that it may be difficult to establish if the subsidy was effectively paid back in a third country.

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<sup>169</sup> Communication from the Commission — Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty, OJ C 249, 31.7.2014, p. 1–28

<sup>170</sup> Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis ( ‘Banking Communication’ ) Text with EEA relevance, OJ C 216, 30.7.2013, p. 1–15

<sup>171</sup> Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak as adopted on 19 March 2020 (C(2020) 1863) and its amendments C(2020) 2215 of 3 April 2020, C(2020) 3156 of 8 May 2020, C(2020) 4509 of 29 June 2020, C(2020) 7127 of 13 October 2020, and C(2021) 564 of 28 January 2021 are those published in the Official Journal of the European Union

Taking into account these views redressive measures envisaged in the new instrument could be as follows:

- Behavioural measures, including third party access, reducing capacity or market presence, refraining from certain investments, licensing on fair, reasonable and non-discriminatory (FRAND) terms of assets developed or acquired with subsidies, prohibition of a specific market conduct, publication of R&D results, transparency in accordance with Directive 2006/111/EC, prohibition to award the public contract to the undertaking concerned in an ongoing public procurement;
- Structural measures: divestment of certain assets, prohibition of an acquisition, unwinding of an acquisition;
- Redressive payment to the third country concerned.

In terms of enforcement, the EU has jurisdiction over companies active on the EU internal market. Consequently, the competent supervisory authority would be able to impose investigative and redressive measures on such companies, irrespective of their ownership or place of establishment. The situation would hence be similar to the enforcement of prohibitions, commitments and fines in the area of antitrust and merger control.

Below the summary table showing the design parameters and the options.

*Table 5. Summary table design parameters in option 4*

Design parameter	Options to be considered				
a) Competence level	a1) Commission only	a2) Shared competence between the Commission and Member States			
b) Investigative approach	b1) Ex-officio	b2) Notification with no thresholds	b3) Notification with moderate thresholds	b4) Notification with high thresholds	b5) Combination of ex-officio and notification with moderate or high thresholds
c) Thresholds unlikely to distort	c1) EUR 200 000	c2) EUR 5 million			
d) Assessment criteria	stemming from EU State Aid rules				
e) Balancing test	e1) No balancing test	e2) Balancing test			
f) Redressive measures	Toolbox stemming from EU State Aid rules				

## 6 WHAT ARE THE IMPACTS OF THE POLICY OPTIONS?

This chapter assesses the impact of a new instrument and, where relevant, of the policy options as regards its main design parameters, against the baseline scenario and for each of the three problems identified.

## 6.1 Problem 1 - distortions in acquisitions

### Economic impacts

#### *Public authorities*

The new instrument would require more resources for public authorities compared to the baseline scenario regardless of which sub-options for the design parameters are considered. Public authorities would have to identify, assess and remedy distortive foreign subsidies. However, as mentioned in Section 5.3, the types of subsidies considered to be likely distortive would be similar to those considered under State aid and international trade rules.<sup>172</sup> Moreover, indicators for assessing distortions would build on the ones used in State aid control. To the extent public authorities are already familiar with State aid control and trade defence rules, the additional administrative burden on them resulting from the assessment of foreign subsidies would be more limited.

As regards the **impact of the options for the investigative approach**, State aid control uses both ex officio and notification procedures similar to the two types of procedures that could be used for scrutinising foreign subsidies. Merger control typically uses notification procedures for acquisitions. As the administrative tasks in relation to the control of State aid, mergers and foreign subsidies are likely to be comparable, this report builds to a large extent on the experience in the State aid and merger areas. Options b1 to b5 – on the design parameter related to the investigative approach – would influence particularly the number of cases and therefore the impact on the resources of public authorities. Due to the lack of transparency on foreign subsidies, it is not possible to precisely estimate the number of acquisitions potentially facilitated by foreign subsidies. Instead, this report takes as a starting point the total number of acquisitions of EU undertakings by third country undertakings. In other words, foreign ownership is taken as a proxy to identify the number of potentially subsidised acquisitions.

- **Option b1 (Ex officio approach):** If there are no ex ante notifications, the public authority could rely on market intelligence to identify potentially distortive foreign subsidies in the context of acquisitions. As a result, the supervisory authority would open cases based on the human resources it has available for such investigative tool. In general, it is likely that fewer acquisitions would be investigated than in a notification system because the information would be less readily available. An ex officio investigation of subsidised acquisitions may also have the drawback that an acquisition is completed before the investigation is finalised. Such an approach may therefore undermine legal certainty for the merging parties.<sup>173</sup> The redressive measures would therefore need to cover the situation that some acquisitions might already be completed at the start of an investigation, which means that for example behavioural measures may be easier to implement. Lastly, it should also be taken into account that even the acquisition of relatively small EU targets may distort the internal market and would not be captured by a notification system with moderate or high thresholds.<sup>174</sup>

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<sup>172</sup> See e.g. Joint Statement of the Trilateral Meeting of the Trade Ministers of Japan, the United States and the European Union of 14 January 2020, available here:

[https://trade.ec.europa.eu/doclib/docs/2020/january/tradoc\\_158567.pdf](https://trade.ec.europa.eu/doclib/docs/2020/january/tradoc_158567.pdf)

<sup>173</sup> For a discussion see: <https://www.concurrences.com/en/conferences/ex-post-review-of-merger-control-decisions-pros-and-cons-en->

<sup>174</sup> Some of these deals have been referred to as 'killer acquisitions'. A killer acquisition occurs when incumbent undertakings acquire innovative start-ups to eliminate future competition by absorbing or discontinuing their projects. Cunningham, Colleen, Florian Ederer, and Song Ma. "Killer acquisitions." *Journal of Political Economy*, forthcoming.

- Option b2 (Notification with no turnover threshold): As illustrated by the JRC data compiled in Table 17 of Annex 5, a full notification approach for all non-EU acquisitions (option b2) could result in hundreds or even thousands of notifications. Bringing all non-EU acquisitions to the attention of public authorities, this option would facilitate action by these authorities to fill the current gap in addressing distortive foreign subsidies. However, considering that many of these cases would in fact be unlikely to involve distortive foreign subsidies, requiring such a large number of notifications would appear excessive, and a disproportionate burden on public authorities (and businesses).<sup>175</sup> In order to come to a more realistic number of the acquisitions that are most likely to benefit from distortive foreign subsidies, and thus warrant notification, this section first uses the Commission's internal data on notifications under the EUMR (option b3, detailed in the paragraph below).<sup>176</sup> Further data on global turnover thresholds from the JRC can be found in Annex 5, Section 1.
- Option b3 (Notification with moderate EU turnover threshold): The Commission receives 350-400 notifications per year under the EUMR. Among these, 89 cases involve one or several non-EU acquirer(s)<sup>177</sup> of an undertaking established in the EU (based on 2019 figures). This figure should be seen as a minimum value because it does not take into account transactions among undertakings from outside the EU (but notified under the EUMR because of their activities in the EU – this is referred to as scenario 1 below). If such acquisitions between undertakings from outside the EU are taken into account, the overall number of cases rises to 155 (scenario 2, including acquisitions between undertakings from different non-EU countries) and 186 (scenario 3, including also acquisitions between undertakings from the same non-EU country). Based on the years 2015 to 2019,<sup>178</sup> the potential number of notifications would vary for scenario 1 between 73 and 89, for scenario 2 between 131 and 157 and for scenario 3 between 155 and 190. These three scenarios illustrate that even with the EUMR thresholds, the supervisory authorities would likely be faced with numerous notifications, of which many may in fact not involve distortive foreign subsidies. Thus, option b4, which is detailed below, aims at reducing the number of cases.
- Option b4 (Notification with high EU turnover threshold): First, the EU merger data is used to assess how a higher EU turnover threshold (EUR 500 million EUR) would affect the number of potential notifications.<sup>179</sup> Such a 'scenario 4' (see Figure 8 in Annex 5) illustrates that in the years from 2015 and 2019 between 26 and 38 EU undertakings with

<sup>175</sup> The proposed thresholds for distortive subsidies would likely limit this, but their impact cannot be quantified at this stage given the lack of sufficient available information on foreign subsidies.

<sup>176</sup> The EU merger data divides each notification into several components corresponding to each party of a case. For example, most cases include one acquiring and one target company. For the purpose of this section, acquirers from non-EU countries have been identified. Moreover, each case is allocated to a specific category based on the country of origin of each of the parties. For example, if a US company buys a company from an EU Member State, the case is coded as a 'cross border EU-non EU' case. If a case includes multiple parties which renders the decision to allocate it to a single category difficult, the case is classified based on which companies played the biggest role in a specific acquisition.

<sup>177</sup> The EU merger database covers the years 2015-2019 when the UK and its overseas territories were still members of the EU. To estimate the number of non-EU acquirers including the UK, the underlying data has been recoded.

<sup>178</sup> See Figure 7 in Annex 5.

<sup>179</sup> The merger data includes turnover values for each company that is part of an acquisition. The above figure includes all companies in the EU from 2015-2019 that were targets of foreign acquisitions. In the vast majority of EU notifications, there is only one target company per case (as well as one acquiring company). Hence, the above numbers approximate the overall number of cases/ notifications in which a foreign undertaking acquired an EU undertaking. It is likely that the above number slightly underestimates the numbers of potential cases, since undertakings from non-EU countries can also be subject to EU thresholds. The above figure only includes acquisitions of EU undertakings that have triggered relevant thresholds of Article 1(2) EUMR.

an EU turnover of more than EUR 500 million were acquired by third country undertakings (32 cases in 2019, 33 cases on average between 2015 and 2019). Using data provided by the JRC yields a similar number of cases for 2019.<sup>180</sup> Such a higher turnover threshold would therefore about halve the number of potential notifications compared to scenario 1 and focus the notification requirement on the largest and potentially most distortive cases, thereby facilitating action by public authorities. This would alleviate the administrative burden on public authorities and undertakings. Notably, this scenario would de facto exclude SMEs from the notification obligation.

Second, in order to further reduce the administrative burden and focus on the relevant acquisitions, a threshold for foreign financial contributions may be considered. Such a threshold would consist in a minimum amount of EUR 50 million of foreign financial contributions provided during the three years prior to the notification. This amount corresponds to 10 per cent of the above-mentioned turnover under scenario 4 and can therefore be considered to risk distorting the acquisition process sufficiently to require ex ante notification. With such threshold, the number of notifiable acquisitions is likely to decrease. However, given the lack of available information on foreign financial contributions, it is not possible to precisely quantify this decrease.

- Option b5 (Combined notification – ex officio approach): In view of the more systematic but more burdensome nature of a notification system and a ‘lighter’ ex officio system, it appears reasonable to strike a balance between the two. Combining an ex ante notification system for the largest and potentially most distortive subsidised acquisitions with an ex officio approach for smaller acquisitions would allow the supervisory authority to receive relevant information for the potentially most distortive cases whilst retaining enough discretion to pursue relevant smaller cases on its own initiative.

The paragraphs above have examined the expected number of cases for each of the options under the investigative approach design parameter. The estimated resulting resource implications for dealing with those cases are detailed below.

- Option b1 (Ex officio approach): In order to estimate the resources and administrative burden for option b1 (ex officio work for subsidised acquisitions),<sup>181</sup> reference can be made to the work of a DG COMP unit of 20 FTEs whose casework is based almost exclusively on ex officio case handling. The work of the unit deals with a new area of competition enforcement exclusively based on ex officio cases. In terms of type of work, it is therefore comparable to ex officio work as would be carried out under problems 1 and 3. The unit’s work consists of identifying possible cases, mostly through public reporting or through information received from the Member States, collecting the necessary information to conduct an assessment and shaping the cases. Especially the task of collecting information is time-consuming, as public authorities and companies are often not forthcoming in providing the information and the relationship is contentious (different to notifications where companies are interested in having their transactions cleared quickly). Information is also often only available in companies outside the EU (mainly 3<sup>rd</sup> country head offices). Therefore, companies often claim that they do not have the requested information. In addition, the investigated cases concern complex company structures, require a detailed assessment of intragroup transactions and concern high

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<sup>180</sup> See Annex 5 Annex 5, Section 1. Since the JRC data contains global turnover and not EU turnover, the threshold of EUR 500 million EU turnover is proxied by using EUR 1 billion global turnover. In the JRC data the figures for 2018 are significantly different from those for 2017 and 2019, and seem less representative.

<sup>181</sup> This goes for both problem 1 and problem 3, as will be also mentioned later on in this report.



amounts of funding which render the assessment difficult and time consuming. All these characteristics are most likely to play also a role for ex officio cases under problem 1.

Once a sufficient amount of information is collected, the preparatory case shaping also requires extensive discussions within the Commission as the cases are new and the approach needs to be tested thoroughly. As formal investigations in ex officio cases are started usually only if there is a serious concern about incompatible business practices and typically end with the adoption of a final negative decision, a large part of the unit's work is spent on appeal procedures before the Union courts. So far, all negative decisions in this area have been appealed. Moreover, in some cases, the phase from identifying a potential case to opening a formal investigation procedure took over 2 years. The ex officio cases that would be pursued under problem 1 would most likely involve a similar type and amount of case work: time-consuming information collection and preparatory work, investigations requiring a detailed assessment of complex structures and follow-up litigation. In terms of horizontal work and given that this concerns a new enforcement system, advocacy would also require resources. Consequently, the resource need for the preferred combined notification – ex officio approach would amount to approximately 60 FTEs (40+20).

- Options b2, b3 and b4: As the notification requirement focuses on the largest and likely most distortive acquisitions, it is assumed that the average workload per case is rather high. Based on DG COMP workload data for comparable 'heavy' procedures, it is estimated that for instance option b4, which involves an average number of 33 notifications of large potentially subsidised acquisitions per year, would require resources of the order of 40 full-time equivalents (FTE).

More generally, as regards options b2, b3 and b4 on suitable notification thresholds, the public consultation on the White Paper revealed a large variety of views. Many stakeholders agreed with the threshold that was originally proposed (EU turnover of EUR 100 million of the EU target). Several also called for combining it with a qualitative threshold for transactions below the threshold. This view was expressed by research institutions<sup>182</sup> and business representatives<sup>183</sup>. In some instances, lower thresholds were proposed.<sup>184</sup> Some law firms expressed preference for clear-cut quantitative thresholds,<sup>185</sup> some for alignment with the EUMR<sup>186</sup> as was the case for several Member States.<sup>187</sup> Some stakeholders also advocated for a dual threshold consisting of an EU turnover of EUR 100 million and a sufficiently high amount of foreign financial contribution.<sup>188</sup>

#### *Administrative burden on companies*

The development of a new EU legal instrument would likely increase the administrative burden on undertakings compared with the baseline scenario because undertakings would need to notify or at least monitor the foreign financial contributions that they receive. The considerations are to a large extent similar to the above ones on the administrative burden on public authorities.

As regards the **impact of the options for the investigative approach**:

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<sup>182</sup> Such as the German Economic Institute, Information Technology and Innovation Foundation, King's College London.

<sup>183</sup> Such as SEA Europe, European Aluminium, Eurometaux, ArcelorMittal, UNIFE, AEGIS, EURATEX, EUCCC.

<sup>184</sup> e.g., European Panel Federation – EUR 50 million, AFEP – lower sector-based thresholds

<sup>185</sup> e.g., DLA Piper, Allen & Overy LLP

<sup>186</sup> e.g., International Bar Association, Enel SpA

<sup>187</sup> e.g., CZ, DK, FI

<sup>188</sup> e.g., Business Europe, NCTM



Option b1 (ex-officio): A system that relies on ex officio investigations (option b1) may reduce the overall administrative burden as undertakings would not be obliged to notify. However, it may also reduce legal certainty for undertakings somewhat because they may not always be sure whether financial contributions from third countries actually qualify as distortive foreign subsidies.

Options b2 to b4: An ex ante notification system for acquisitions (options b2 to b4) increases legal certainty for companies but is also likely to increase their administrative burden. In terms of number of cases, the previous section on public authorities gave an estimate which would apply vice versa to undertakings. In terms of cost per notification, limited information is available as the stakeholders consulted indicated that this will depend on the exact requirements. Taking merger notifications as a proxy, it has been estimated that the costs of filing a notification form (Form CO) ranges from a low end of around EUR 50.000 – 75.000 to a high end of EUR 500.000, whereas a ‘lighter’ transparency system for minority share mergers would yield costs in the range of EUR 5.000 to EUR 50.000.<sup>189</sup> This being said, several other ex-ante notification systems already exist for acquisitions in the EU, namely under merger control and FDI screening. To the extent notifiable acquisitions under this option would also be notifiable under one or more of these other pre-existing instruments – which would likely be the case for the two notification systems with thresholds proposed as b3 and b4 since thresholds under merger control or FDI screening would typically be lower –, the additional administrative burden to prepare a notification would be appear relatively small because it would be largely limited to gathering information on the foreign financial contributions received.

As regards the *impact on Small and Medium Enterprises*, options b3 and b4, which propose moderate and high thresholds for the notification of acquisitions, are unlikely to have a significant administrative burden on SMEs because they are likely to remain under the relatively high notification thresholds.

#### *Functioning of the internal market*

A new EU legislative instrument would aim at levelling the playing field among market players by identifying and removing distortions caused by foreign subsidies, which ultimately improves the functioning of the internal market. To achieve this objective, the new instrument would provide effective tools for identifying, investigating and redressing distortions caused by foreign subsidies.

Empirical studies substantiate the general importance of competition law enforcement to ensure effective competition in markets<sup>190</sup>. A study which examined how different antitrust systems affect the degree of competition in individual countries found that increasing the range of competition instruments has a significant positive impact on the intensity of competition in the country's economy<sup>191</sup>. Studies also confirm the positive effects of competition on the productive efficiency of companies. This is due to a "between-firms" effect, by which better companies

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<sup>189</sup> Commission Staff Working Document, Impact Assessment Accompanying the White Paper: Towards more effective EU merger control. SWD(2014) 217 final. p.30.

<sup>190</sup> The best evidence for the effectiveness of competition law enforcement tends to be that based at the level of the enforcement itself. Competition authorities and academics have published a large number of ex-post studies of the results of enforcement actions, which were surveyed by the OECD in 2013: "Evaluation of competition enforcement and advocacy activities: The results of an OECD survey".

<sup>191</sup> Keith N. Hylton and Fei Deng, (2007) Antitrust Around the World: An Empirical Analysis of the Scope of Competition Laws and Their Effects

succeed while the worst ones fail and leave the market, and a within-firm effect by which companies in competitive environments are better managed<sup>192</sup>.

The above findings can be applied by analogy to distortions caused by foreign subsidies. In particular, a legislative instrument to address distortions caused by foreign subsidies would complement EU State aid control and fill the legal gap described in Section 2.5. It would ensure a level playing field where business decisions on prices, production, innovation and trade are based on efficiencies and commercial opportunities rather than ‘rent seeking’ and securing subsidies.

With regard to acquisitions, foreign subsidies may give their beneficiaries an undue financial advantage which they can use to outbid competitors to acquire target companies and subsequently subsidise the operation of the acquired target by e.g. offering below-cost prices.<sup>193</sup> As a result, drawing up new rules on subsidised acquisitions could improve the functioning of the internal market in the long term since non-subsidised companies would no longer run the risk of being outbid by foreign-subsidised companies in the acquisition process.

At the same time, addressing distortions caused by foreign subsidies would help to restore the effectiveness of price signals and market-based valuations of companies, since subsidisation can lead to distorted pricing of acquisitions.

The **redressive measures** included in the new instrument would improve the functioning of the internal market. Under EU State aid control, a typical measure is the reimbursement (recovery) of incompatible State aid to the granting authority. If the same approach is followed in the case of foreign subsidies, the beneficiary of a distortive foreign subsidy should pay back the subsidy to the granting authority in the third country. Such repayment may however not be easy to enforce or monitor as some parties involved are located outside the EU. Alternative measures for removing the distortion therefore appear warranted and can also be observed in other competition instruments. As regards distortions in acquisitions, an undertaking could be required to divest certain assets or to refrain from certain investments, all requirements that have been imposed in EU State aid cases. It can also be envisaged to prohibit an acquisition to remove the distortion caused by the foreign subsidy. An acquisition ban is a measure that has also been used in State aid control in the past e.g. in the banking restructuring cases.

Finally, the **impact of the options as regards the competence level** can influence the effectiveness of the instrument and its impact on the functioning of the internal market. In the specific case of acquisitions, legal certainty and a quick assessment are essential for the parties concerned. In response to the public consultation on the White Paper, the large majority of stakeholders therefore favoured a one-stop-shop at EU level (option a1) to assess acquisitions potentially facilitated by foreign subsidies. In contrast, a decentralised control of subsidised acquisitions at Member State level (option a2) risks leading to an inconsistent application and interpretation of the legislation that has no precedent. If a foreign subsidy affects several Member States at the same time, there is need to coordinate action that risks delaying the assessment. At the same time, to draw on the expertise of Member State authorities and develop a common approach across the EU, Member States could be involved in the decision process by means of an advisory committee.

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<sup>192</sup> Arnold, J. M., Nicoletti, G., & Scarpetta, S. (2011) Regulation, Resource Reallocation and Productivity Growth. European Investment Bank Papers, 16(1), 90-115; OECD's project of 2013 on Supporting Investment in Knowledge Capital, Growth and Innovation

<sup>193</sup> For a discussion see a recent decision of the German competition authority: German Federal Cartel Office, Case Summary CRRC/Vossloh, B4-115/19, 27 April 2020, p. 10-11.

### *Consumers and households*

A new instrument to address distortive foreign subsidies in acquisitions could have a negative impact on consumers in the short run since it may lead to an increase in prices in the absence of subsidies. However, this should be seen as correcting unfair competition and artificially low prices. Instead, in the long run, consumers would benefit. Notably, preventing distortive foreign subsidies in acquisitions would spur innovation and more generally improve competition which ultimately benefits consumers through lower prices and better products. In the consultation on the White Paper and in the targeted consultation, the European Trade Union Confederation noted that the impact of foreign subsidies on consumers concerns not only prices. Consumers also consider other attributes such as product quality and labour and environmental standards. This view was echoed during the targeted consultation by the European Consumer Organisation (BEUC) that also mentioned that any instrument that helps to tackle distortive subsidies would be likely to have a positive effect on consumers. On the basis of the information available it was, however, not possible to quantify the order of magnitude of the short-term and long-term impact on consumers.

### *Trade and investment flows*

A new instrument on foreign subsidies may impact trade and investment flows. Trade and investment may diminish if, for example, the instrument is particularly burdensome for market players or introduces a high degree of legal uncertainty. The risk of a new instrument having a negative impact is however low in view of the limited administrative burden on undertakings (see above section) and the clear framework it establishes. As regards investment flows, acquisitions from third countries are indeed particularly important. Such acquisitions account for the majority of FDI in the EU compared to greenfield investments. Apart from the risk due to administrative burden, the new instrument on foreign subsidies may in practice reduce the number of acquisitions by preventing subsidised acquisitions. However, this would be the intended effect of the new instrument and should be outweighed by the benefits of restoring an undistorted internal market and by facilitating commercially driven acquisitions that were previously hindered. In order to estimate the potential negative impact on FDI, the impact of introducing national FDI screening mechanisms in various Member States<sup>194</sup> has been assessed. This may serve as an appropriate proxy as the impact may be expected to be broadly comparable to the introduction of this policy option. Specifically, the impact has been assessed using the OECD FDI restrictiveness index<sup>195</sup> and the value of inward FDI flows<sup>196</sup>. For Member States that introduced FDI screening mechanisms during the timeframe considered by the OECD (i.e. 1997-2017), the FDI restrictiveness index remained stable. The introduction of national screening mechanisms was therefore not generally considered as restrictive for FDI. Looking at the value of inward FDI flows into the aforementioned countries, OECD data shows that some decrease in inward FDI could be observed in the year of the introduction of the screening mechanism, but in most cases, inward FDI increased again in the following year. In the longer term, the value of inward FDI flows has returned to a level similar to one before the introduction of FDI screening. The introduction of national screenings mechanisms therefore appears to only have reduced FDI into the EU only temporarily, rather than structurally. This can be explained by temporarily increased uncertainty and the tendency of companies to frontload certain investment decisions prior to the

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<sup>194</sup> Source: [https://trade.ec.europa.eu/doclib/docs/2019/june/tradoc\\_157946.pdf](https://trade.ec.europa.eu/doclib/docs/2019/june/tradoc_157946.pdf)

<sup>195</sup> FDI restrictiveness is an OECD index gauging the restrictiveness of a country's foreign direct investment (FDI) rules by looking at four main types of restrictions: foreign equity restrictions; discriminatory screening or approval mechanisms; restrictions on key foreign personnel and operational restrictions. Implementation issues are not addressed and factors such as the degree of transparency or discretion in granting approvals are not taken into account. The index here shows the total and nine component sectors taking values between 0 for open and 1 for closed. Source: <https://data.oecd.org/fdi/fdi-restrictiveness.htm#indicator-chart>

<sup>196</sup> Source: <https://data.oecd.org/fdi/fdi-flows.htm#indicator-chart>

introduction of the new screening mechanisms. In view of the foregoing, while it is not possible to quantify the impact of the proposed instrument with certainty, the option does not appear to have a substantial long-term impact on FDI flows into the EU, similarly to the introduction of the national screening mechanisms.

During the public consultation on the White Paper, several non-EU stakeholders raised the issue that a possible new instrument on foreign subsidies could create barriers to foreign investment in the EU. A few Member States echoed that concern and proposed to avoid this e.g. by setting the **threshold for subsidies unlikely to be distortive** (options c1 and c2) and the notification thresholds (options b2-b4) at a relatively high level. Additionally, some EU industry and legal associations proposed that a new legal instrument should tackle only the most distortive subsidies to avoid discouraging FDI. These proposals converge with the above considerations about the appropriate level of the threshold for subsidies unlikely to be distortive (options c1 and c2) and **the notification thresholds for the investigative approach** (options b1 to b5), which would focus on the largest and most distortive subsidies. In any event, even stakeholders that expressed some concern about a potentially chilling effect of new rules on foreign subsidies on FDI in the EU were in favour of tackling distortions caused by foreign subsidies.<sup>197</sup> Moreover, even certain non-EU stakeholders openly supported such a new tool.<sup>198</sup>

### *Third countries and international relations*

Third country governments may perceive a new instrument on foreign subsidies to be protectionist, especially if it may lead to the prohibition or unwinding of subsidised acquisitions. Trade tensions may ensue and third countries may take measures against EU undertakings that receive State aid. Such measures would however not be likely to be in line with WTO rules as they would be discriminatory if a third country does not have in place an equivalent system for the control of domestic subsidies. In any event, even some stakeholders who cautioned against such tensions in their submissions to the public consultation were overall in favour of a new instrument on foreign subsidies in the EU.<sup>199</sup> To counter any such concerns it needs to be ensured that new rules on foreign subsidies are based on principles similar to EU State aid rules. Such new instrument closes an existing legal gap and restores the level playing field across the internal market. Additionally, the legislation will apply in an objective and non-discriminatory manner to all undertakings active in the EU irrespective of their ultimate ownership ('nationality'). At the same time, this option may further incentivise non-EU countries to have a State aid control system similar to the EU. Finally, this option could incentivise other countries to (re-) engage in negotiations to agree on international rules for subsidies, for example under the WTO.

### **Social impact**

It is not possible to estimate the social impact with certainty. In the short term, foreign direct investors would need to acquaint themselves with this new instrument which might have a limited impact on overall FDI and thus also employment. In the long-term, however, the impacts on employment can be expected to be positive as this option would ensure that non-subsidised, competitive companies remain in operation and are not crowded out by subsidised companies. Furthermore, it could help to tackle the issue of delocalisation of jobs to a third country following an acquisition subsidised by the respective third country. ESIA for example mentioned during the targeted consultation that distortive foreign subsidies, if not addressed, may lead to job losses in the EU. An example quoted in this context was the acquisition of Pirelli by ChemChina in 2015

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<sup>197</sup> See, among others, the submissions of Italy, Confederation of Swedish Enterprise, European Competition Lawyers Forum and International Bar Association.

<sup>198</sup> See, among others, the submissions to the public consultation of the US-based Information Technology and Innovation Foundation, various UK-based law firms and associations and Andrea Biondi.

<sup>199</sup> See e.g. the Polish Union of Entrepreneurs and Employers and of AmCham.

(see section 2.2). After the acquisition, a part of the tyre production was moved from the EU to China.

As regards the **impact of the options on the balancing test**, the option of including a balancing test (option e1) would have positive impacts on the various policy objectives including social ones. In general terms, under a balancing test it would be possible to weigh the distortion caused by a foreign subsidy against positive effects on the development of the relevant economic activity in the internal market. If on balance, the distortion on the internal market caused by the foreign subsidy is sufficiently mitigated by the positive impact of the economic activity, the investigation of the foreign subsidy would terminate without the need for a redressive measure. The balancing test corresponds to the idea of balancing positive and negative effects of State aid under EU State aid control.

The concept of a balancing may be difficult to precisely define in all relevant circumstances.<sup>200</sup> The views of stakeholders on a balancing test were quite mixed. While it seems to be supported by several Member States<sup>201</sup> and non-EU stakeholders<sup>202</sup>, other EU stakeholders seem more divided.<sup>203</sup> However, in order to assure coherence with EU State aid rules and generally to take into account potentially positive impacts of foreign subsidies, it seems important to introduce a balancing test. To ensure a consistent interpretation and application of this concept, it would in any event be very important to assign this task only to one supervisory authority at EU level.<sup>204</sup>

### **Environmental impact**

It is not possible to estimate the environmental impact with certainty. However, generally speaking, new legislation may help to address potentially negative environmental effects of foreign subsidies caused by delocalisation as explained in the baseline scenario. In this regard, some respondents to the public consultation and the targeted consultation noted that undertakings receiving foreign subsidies may apply lower environmental standards than non-subsidised ones – if they are located outside the EU. A new instrument on foreign subsidies may therefore have a positive effect on the environment globally (and hence potentially in the EU as well).

As regards the **impact of the options for the ‘balancing test’**, the option of including a balancing test (option e1), which could allow to approve subsidised acquisitions that have significant positive effects, could give more weight to environmental considerations and therefore have a further positive impact on the environment.

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<sup>200</sup> Indeed, during the public consultation on the White Paper, certain Member States (e.g. Poland, Czechia, Austria) and other stakeholders (among others various law firms) referred to this issue.

<sup>201</sup> See, among others, the submissions to the public consultation of The Netherlands, Sweden, France, Denmark, Italy and Belgium.

<sup>202</sup> See, among others the submissions of the China Chamber of Commerce.

<sup>203</sup> Some respondents consider an EU interest test to be relevant, e.g. ESF, Confederation of Swedish Enterprise, International Bar Association and Bundesarbeitskammer Österreich. On the contrary, other contributors oppose it, e.g. ERT, Fédération nationale de travaux publics.

<sup>204</sup> This view was also expressed by stakeholders during the public consultation, among others by The Netherlands, European Aluminium, ESF and China Chamber of Commerce to the EU.



## 6.2 Problem 2 - distortions in public procurement

### Economic impacts

#### *Public authorities*

A new EU legislative instrument would require more resources in the supervisory authorities as compared to the baseline scenario and may require more resources on the side of the contracting authority regardless of which sub-options are considered i.e. irrespective of the investigative approach and the threshold for distortive subsidies. Implications in terms of the work and methodology of the supervisory authorities are similar here to Problem 1 (see point 6.2.1 on public authorities), as the supervisory authorities would have to carry out tasks related to the identification, assessment and remedying of distortive foreign subsidies. Contracting authorities would only have a role as regards receiving and transmitting notifications

As regards **the impacts of the options for the investigative approach**, in Problem 2, much like in Problem 1, the number of cases would be influenced by the choice of the design parameters b1 to b5 (including the choice of responsibilities within each of the systems) . Below the estimated number of cases for each option:

- Option b1 (Ex officio approach): Similarly to problem 1, a purely ex-officio review, relying solely on market intelligence, could not close this data gap, and therefore not allow protecting the level playing field effectively. If public procurement were predominantly examined only after the conclusion of the respective public contracts, this could undermine legal certainty stemming from a completed procedure and signed contract. Overall, fewer procurements would be examined. In addition, the effectiveness of some redressive measures would be impeded, whereas the preferred redressive measure of prohibition of award would typically not be available.
- Option b2 (Notification with no threshold): Similarly as for problem 1, this approach would likely result in thousands of notifications. While this option would facilitate action to fill the current gap in addressing distortive foreign subsidies in a comprehensive way, it would create disproportionate workload and require resources which would not be justified by the potential positive impacts.
- Options b3 and b4 (Ex ante notification procedure with medium and high notification thresholds): In an 'ex ante' system, an investigation would start with a notification to be submitted to the contracting authority<sup>205</sup>. For the 'ex ante' system, this section analyses the impact of different thresholds for the submission of a notification on the number of cases. As for problem 1, no information is currently available on foreign subsidies received by tenderers in public procurement. In addition, as outlined in section 2.3, no information is available on tenderers that have not been awarded a contract. No mechanism currently exists that would require tenderers to submit a notification for an investigation, e.g. into state aid received, during a procurement procedure. The only data set that allows to estimate the number of notifications is the number of procurement procedures published in TED above the thresholds for the application of the procurement directives<sup>206</sup>. In the years 2015 to 2017, on average 184 169 contract notices and 178 284

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<sup>205</sup> The contracting authority would transmit this information to the supervisory authority. Alternatively, the information could also be submitted directly to the supervisory authority, see below impact on companies.

<sup>206</sup> EUR 5 350 000 for public works contracts; EUR 139 000 for public supply and service contracts awarded by central government authorities, EUR 214 000 for public supply and service contracts awarded by sub-central contracting



contract award notices have been published. They attract on average 4.36 bidders. Using the mentioned thresholds of the procurement directives would entail a much wider application of the instrument to procurement than to acquisitions. This does not seem justified by any structural difference between the risks of distortions in acquisitions and in procurement. Like for acquisitions, it is important to have a targeted instrument that focusses on the largest and potentially most distortive cases. The number of potential cases has therefore been looked at for the threshold of the EUMR, EUR 250 million, and for the higher threshold of EUR 500 million, examined under 6.2.2. In view of the very limited data available, the estimation can only give a rough indication: For the last three available years 2015 to 2017, 108 contract award notices have been published for a value of above EUR 250 million, and 38 contract award notices for a value of over EUR 500 million. So, per year, an average of 36 contract award notices have been published above EUR 250 million and an average of just under 13 above EUR 500 million. In all the contracts covered by the contract award notices above EUR 250 million between 2015 and 2017, 21 of the 435 awardees<sup>207</sup> or 4.8 % had an ultimate owner outside the EU. The number of ‘notifications’ that may be received could be in the range of the number of foreign successful bidders, understood as single companies or consortia (data for which is collected and reported by the leading member of the consortium), but also in the range of the number of contract notices. For a threshold of EUR 250 million, there may be up to 36 cases per year, for a threshold of EUR 500 million up to 13 cases. These numbers, however, are susceptible to significant annual variations both upward and downward. Without the notification obligation, there is – as shown – limited information on the participation of foreign and foreign owned companies, and no information on whether any participating company receives foreign subsidies.

- Option b5 (Combined notification – ex officio approach): Similarly to Problem 1, a combination of an ex ante system for the largest and potentially most distortive subsidised procurements, and an ex officio approach for smaller procurements, as outlined above, would both allow the receipt of relevant information for the potentially most distortive cases whilst retaining enough discretion to pursue relevant smaller cases.

The paragraphs above have examined the expected number of cases for each of the options under the investigative approach design parameter. The administrative effort on the part of the authority charged with investigating the existence and distortive effects of foreign subsidies cannot be estimated in a reliable way. It will depend on the competence level, the complexity of each case, the information made available. No investigations currently exist in public procurement that could serve as a basis. As a proxy, adapted to the estimates presented above the administrative effort as described in 6.2.1 above can be used for the work on the notification approach. This would amount roughly to 45 FTE in the case of 36 cases (threshold of EUR 250 million), and 15 for 13 cases, if the threshold would be EUR 500 million. The current Commission workload of a unit dealing specifically with ex officio State aid cases was described under problem 1 (see section 6.1.2). The resource implications of an ex officio procedure under problem 2 would be similar, resulting in approx. 10-15 ex officio cases per year and a resource need of around 20 FTEs. Combined with the ex-ante approach this would make for a total of 35 (15+20) FTEs for a EUR 500 million threshold. If the threshold is set to above EUR 250 million, 65 FTE (45+20) would be needed. However, in the latter case, there might be a slightly lower need of staff for the ex-officio approach as it would only cover procurements below EUR 250 million.

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authorities and EUR 750 000 for public service contracts for social and other specific services listed in Annex XIV. More information [here](#).

<sup>207</sup> Contract award notices may cover several contracts awarded to different economic operators.

As regards the **impacts of the options for the competence level**, if the Commission is the sole supervisory authority, it is not to be expected that national administrations would need additional resources, as their role would be limited to transmitting information to the Commission. The actual workload for public administrations depends on the precise model chosen. In a model, where both national authorities and the Commission have competences and contracting authorities may have to analyse the distortive effects, additional workload would fall on all those three different actors. All competent authorities would have to build expertise and provide for sufficient human resources, entailing additional costs. Investigations and expertise might overlap and reduce the efficiency and effectiveness of the review.

As regards the budgetary implications for the contracting authorities, the continued participation of subsidised bidders would, at least in the short term, continue to reduce the prices of awarded contracts.

#### *Administrative burden on companies*

The new instrument would increase the administrative burden on companies as compared with the baseline regardless of which sub-options are considered.

As regards the **impacts of the options for the investigative approach**, options b1-b5 would all result in administrative burden, though b1 likely the least. Under b2-b4, companies will have to prepare and submit a notification form, which is not the case in b1. In terms of number of cases, the previous section on public authorities gave an estimate which would apply vice versa to undertakings. In terms of workload per procedure, there is no data to estimate the administrative burden on undertakings, also confirmed by stakeholders (see below).

In the ambit of targeted consultations (see Annex 2), only eight stakeholders provided input on the specific topic of administrative burden. However, the information from those responses could not help estimate the amount of added administrative burden. A general comment from the stakeholders was that every procedure and tender is different and it is difficult to estimate average figures. Moreover, the total number of full-time equivalents (FTE) devoted to this exercise would depend heavily on whether the information should be submitted only for the consortia members, or also for (certain) subcontractors, and especially if the supply chain needs to be consulted.

As regards the **impact of the options for the threshold for distortive subsidies**, and similarly to the case of public authorities, a high threshold for distortive subsidies would reduce the administrative burden on companies.

High notification thresholds and a high threshold for distortive subsidies, would also imply a low administrative burden for SMEs as they will not likely fall under the notification obligation, nor would their subsidised investments likely be investigated as they would fall below the threshold for distortive subsidies.

As regards the **impact of the options for the competence level**, the administrative burden on companies should not change significantly depending on whether the supervisory authority is the Commission or if there is shared responsibility with the Member States. If supervisory authorities of Member States are involved, however there may be a higher need for coordination and guidance to align practices.

As regards other opinions of stakeholders, the response of the rail industry indicates a strong preference for the ex-ante notification/structured information system to be applied only in the context of EU-funded projects, so as to limit the burden for European companies while guaranteeing a strong approach when it comes to EU funds.

For more information, see point 6. 1. above.

#### *Functioning of the internal market*

The new instrument option would add another tool aimed at creating a level playing field in public procurement. This would result in more competitive procurement markets, where companies compete more fairly on their merits and commercial terms and enable them to provide best quality for the lowest cost to the taxpayer. Subsidies in the most important procurements would no longer distort the economic operators' incentives and market signals. This prevention of distortion would lead to better efficiency and thus lowering of the costs on the economy as a whole. As a result, the impact of distortive effects on the market signals and investment flows will decrease and create more long-term efficiency in allocation of capital. The purpose of the new instrument is to restore the level playing field, resulting in reduced participation of bids supported by distortive subsidies. In the mid and long-term it is likely the non-subsidised bidders will be more motivated due to an improved level playing field, after an initial period of familiarizing with the procedural requirements of the new instrument. Finally, crowding-out of non-subsidised but innovative economic operators would be less, leading to overall more innovation in public procurement.

As regards the **impact of the options for the investigative approach**, the system of mandatory notification, if effectively implemented, has the potential to have the highest positive impact on the functioning of the internal market. It would ensure that all foreign subsidies over the applicable thresholds are screened, as all tenders could potentially win the public contract. Options b2-b5, with the system of mandatory submission, including the reporting of market information by other undertakings involved in the public procurement procedure, would have a positive effect in so far as market players identify and report on companies which have benefitted from foreign subsidies.

As regards the **impact of the design parameter on redressive measures**, the different possibilities to remove distortions caused by a foreign subsidy would improve the functioning of the internal market. The same observations regarding repayment of subsidies and other possible measures as laid out in the corresponding paragraph under 6.1 apply. However, in public procurement the most effective tool could be a prohibition of award of the public contract, as it is easily enforced and completely removes any risk of the distortion.

Business relations between potential consortia members, subcontractors and suppliers, which would be motivated to examine the level of subsidies they all receive and be more predisposed to cooperate with more transparent or unsubsidised economic operators, could be enhanced.

As regards the **impact of the options for the balancing test**, the introduction of the balancing test could have positive impacts on public procurement policy aims.

#### *Consumers and households*

The main impact of this option is on undertakings, but there are indirect impacts on consumers, understood as households, as taxpayers and beneficiaries. In monetary terms, this option would likely have a negative impact on EU citizens and households in the short term, as they may benefit from lower prices of subsidised goods and services delivered under public contracts. However, in the longer term, increased competition and an increased offer of products and services that are not subsidised would result in improved price-quality ratio through increases in quality. In addition, such improved offer will facilitate full achievement of public policies through the public procurement process, positively affecting the European citizens. Consumers do also consider other attributes such as quality, labour and environmental standards.

### *Third countries and international relations*

A new legislative instrument risks retaliation measures by those third countries which perceive the option as hampering their companies. Companies from third countries which do not benefit from subsidies are however supportive of this option. Some third countries also favour the option which they see as a template to develop their own foreign subsidy control instruments. Ultimately, this option could incentivise other countries or regions to have a State aid control system similar to the EU. This option could also incentivise third countries to seek resolution of issues as regards subsidies and public procurement in the ambit of various trade agreements, WTO Government Procurement Agreement (GPA) or the International Procurement Instrument IPI, once adopted. In any case the instrument will apply in an objective and non-discriminatory manner to foreign and EU companies alike and thus it would be consistent with the EU's international obligations.

### **Social impacts**

#### *Employment*

This option should eventually have positive impacts on employment as explained above for problem 1, especially regarding crowding-out. In addition, no major negative impact as regards FDIs is foreseen, as public procurements are financed by national or EU funds, and are not foreign investments. In the longer term, as indicated by some respondents to the targeted consultation, foreign companies that have favourable access to the EU public procurement market thanks to distortive foreign subsidies, may undermine specific social policy aims of public procurement.

### **Environmental impacts**

EU environmental policies attract investment that green the EU's economy regardless of whether companies have received or not distortive foreign subsidies. To the extent that some of these foreign subsidised companies are subject to lower environment standards than in the EU, a new instrument would have a positive effect on the environment.

As regards the **impact of the options for the balancing test**, the sub-option of including a balancing test, which would favour foreign subsidies that have a positive effect on the development of the relevant economic activity, would have further positive impacts on the environment.

Some responses from the targeted consultation suggest that the balancing test is in line with the EU climate neutrality goals.

## **6.3 Problem 3 - other market distortions**

### **Economic impacts**

#### *Public authorities*

As for problem 1, a new EU instrument covering other market distortions would require more resources for public authorities as compared to the baseline scenario regardless of which design parameters<sup>208</sup>, are considered.

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<sup>208</sup> These design parameters are described in chapter 5

As regards the **impact of the options for the competence level**, if the Commission is the sole supervisory authority, national administrations would not need additional resources. In case of shared enforcement competences, the resource needs would be split but might imply a higher overall number of FTEs than the scenario of exclusive enforcement competence because of additional coordination needs.

As regards the **impacts of the options for the investigative approach**:

- Option b1 (Ex officio procedure): The option of putting in place an ex-officio system may reduce the number of cases that would be investigated. In order to give a proxy for the potential number of such cases and related resource implications, the current Commission workload of a unit dealing specifically with ex officio State aid cases was described under problem 1 (see section 6.1). The resource implications of an ex officio procedure under problem 3 would be similar, resulting in approx. 10-15 ex officio cases per year and a resource need of around 20 FTEs. An ex-officio system could be complemented by a formal complaint procedure. This is likely to increase the number of cases and thus the resources needed by the supervisory authorities. By comparison, under EU State aid control, the Commission deals every year with about ten ex officio cases and one hundred cases originating from complaints.<sup>209</sup> However, even in the absence of a formal complaint procedure, third parties would be able to provide market information on potentially distortive foreign subsidies to the supervisory authority, which could then take this up ex-officio.
- Options b2, b3 and b4 (Ex ante notification procedure): A mandatory notification system would require supervisory authorities to review the notifications from all undertakings receiving foreign subsidies and potentially affecting the internal market. As explained above in the problem definition, no precise data are currently available on the numbers and/or amounts of foreign subsidies granted to undertakings active in the EU. However, with a mandatory notification system, upon entry into force of the new instrument, undertakings would have to notify all foreign subsidies they received within the last ten years. Moreover, each time a company operating in the EU receives a new foreign subsidy, it would have to notify it to the supervisory authority. Around 100 000 foreign-owned companies are active in the EU market<sup>210</sup>. Additionally, EU-owned companies – i.e. around 22 million undertakings<sup>211</sup> – can potentially receive foreign subsidies. Consequently, even if only a small percentage of all the companies active in the EU

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<sup>209</sup> The Commission dealt with 549 complaints (classified as CP-complaints or FC-formal complaints) and 81 ex-officio cases in the period 1 January 2015 – 27 November 2020. This represents a total of 630 cases and corresponds to an average of 107 cases per year.

<sup>210</sup> In 2017 (the last year for which full data are available), 99 300 non-financial non-EU-owned companies were active in the EU. Source: [https://trade.ec.europa.eu/doclib/docs/2013/may/tradoc\\_151348.pdf](https://trade.ec.europa.eu/doclib/docs/2013/may/tradoc_151348.pdf)  
According to the ECB database, 93 branches of non-EEA based banks were operating in the EU-27. Source: <https://sdw.ecb.europa.eu/browse.do?node=9691593>. Consequently, this brings the total number of – financial and non-financial – enterprises with a foreign owner approximately to 99 393 number of foreign undertakings, as it only considers the number of non-EEA owned bank branches, and not branches of EEU, but non-EU-27, banks, nor any subsidiaries of non-EU-27 banks.

<sup>211</sup> According to the Eurostat database, in 2017 (last year where full figures are available), in total 22 234 234 non-financial enterprises (including those with a foreign owner) were active in the EU-27. Source: <https://ec.europa.eu/eurostat/databrowser/view/tin00145/default/table?lang=en>

According to the ECB database, in 2017 (to use the same basis as the non-financial enterprises), 6 019 financial institutions were incorporated in the EU-27. In addition thereto, 93 branches of non-EEA based banks were operating in the EU-27, thus bringing the total number of financial institutions operating in the EU-27 to 6 112. Source: <https://sdw.ecb.europa.eu/browse.do?node=9691593>

As a result, the total number of – financial and non-financial – enterprises operating in the EU-27 in 2017, which could have theoretically benefitted from State aid grants, amounted to 22 240 346 undertakings.



receive foreign subsidies and hence needed to notify them to the supervisory authority, this would result in an extremely high number of notified cases. To illustrate, if in a given year only 1% of the foreign-owned undertakings active in the EU received a third country financial contribution, the number of notifications would amount to around 1 000 per year.

As regards the **impact of the options for the threshold for distortive subsidies**<sup>212</sup>, such a threshold would generally reduce the burden on the supervisory authority. The higher the threshold, the lower the number of subsidies that would need to be examined and hence the lower the resource implications.

- Option c1 relies on the value currently used in State aid control, where there is a threshold of EUR 200 000 per beneficiary over three years. It should however be noted that to alleviate the administrative burden on the supervisory and granting authorities as well as on the beneficiaries, State aid control has developed a sophisticated system of guidelines and block exemptions that guide the various stakeholders and attempt to minimise the need to notify and assess non-distortive State aid measures. Notably, more than 95% of the State aid measures are block-exempted and Member States do not need to notify them to the Commission. It would not be possible to replicate such sophisticated system of guidelines and block exemptions for foreign subsidies in the absence of limited information on foreign subsidies and of any practice in applying new legislation on foreign subsidies.
- Hence, this report examines to what extent a relatively high threshold for distortive subsidies can reduce the administrative burden on the supervisory authority and undertakings. Notably, a relatively high threshold would allow the supervisory authorities to focus their investigations on the largest and likely most distortive subsidies. Commission internal data on the distribution of State aid awards suggests that option c2, with a threshold of EUR 5 million, would capture at least five per cent of the highest aid amounts (see Annex 4).<sup>213</sup> As just mentioned, more than 95% of the aid awards in the EU are not notified to the Commission but are block exempted. By analogy to State aid, the threshold of EUR 5 million for foreign subsidies would therefore also focus on a probably relatively small share of foreign subsidies, but capture the largest and therefore most distortive ones. Certain US subsidy data show that the subsidy awards to the largest US undertakings largely exceed EUR 200 000, and even EUR 5 million<sup>214</sup>. Even a relatively high threshold of EUR 5 million would therefore capture many potentially subsidies in third countries. On this basis, a threshold of EUR 5 million appears appropriate.
- The public consultation on the White Paper revealed a large variety of views on the question of an appropriate threshold below which subsidies are unlikely to be distortive. Many stakeholders agreed with the originally proposed threshold of EUR 200 000 (in the last three years) aligned with EU State aid rules. This includes multiple associations<sup>215</sup>,

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<sup>212</sup> The same findings are applicable to problems 1 and 2.

<sup>213</sup> Internal Commission data on State aid awards communicated to the Commission for transparency reasons discussed in Annex 5 Section 2. In practice, the percentage is likely to be higher than 5% as the underlying data records individual State aid awards, but a number of beneficiaries are likely to receive more than one aid award during three years which may put them above the threshold of EUR 5 million.

<sup>214</sup> E.g. the data from the Subsidy Tracker shows that the subsidy awards granted by the US to the top-100 companies are largely above USD 5 million, Source: <https://www.goodjobsfirst.org/subsidy-tracker>

<sup>215</sup> Among others EUROALLIAGES, Construction Confederation, ESF



trade unions<sup>216</sup> and several Member States.<sup>217</sup> Some stakeholders expressed the view that this threshold may be too high<sup>218</sup>, should be sector-specific<sup>219</sup>, or that cumulative effects of smaller subsidies should be considered<sup>220</sup>. Some Member States consider the threshold to be relatively low<sup>221</sup>, a view shared by some industry representatives<sup>222</sup> as well as some law firms and law societies<sup>223</sup>.

#### *Administrative burden on companies*

In analogy with the case of public authorities, this option would increase the administrative burden on undertakings as compared with the baseline regardless of which design parameters are considered. Considering that the indicators and assessment criteria for foreign subsidies are modelled after those in State aid, undertakings would have increased legal certainty, even if they would face a higher administrative burden.

As regard the **impact of the options for the investigative approach**, compared to an ex-officio system (option b1), a notification system (options b2, b3 and b4) would require undertakings to prepare and submit notification forms whenever they receive a foreign subsidy. In terms of number of notifications, the previous section on public authorities gave an estimate which would apply *vice versa* to undertakings. In terms of workload per procedure, there is no data like the Commission workload data to estimate the administrative burden on undertakings.

As regard the **impact of the options for a threshold for distortive subsidies**, as in the case of public authorities, making use of a threshold below which subsidies are unlikely to be distortive (options c1 and c2) would reduce the administrative burden of undertakings. The higher the threshold, the lower the administrative burden as was shown above in the case of the public authorities. A threshold for distortive subsidies of EUR 5 million (option c2) would have a beneficial effect on SMEs which due to their size are less likely to receive foreign subsidies of such amounts. At the same time, they stand to benefit from a more level playing field where market prices are not distorted by foreign subsidies.

During the consultation on the White Paper, the inception impact assessment and the targeted consultation many stakeholders raised the issue of administrative burden on companies. In this context, some Member States<sup>224</sup> called for limiting administrative burden, especially on SMEs. Also several EU industry and business associations, law firms, and a few non-EU stakeholders mentioned their concern about administrative burden<sup>225</sup>. Some industry associations cautioned in this context that a notification procedure may increase such burden. One Member State and certain industry/business associations proposed that this could be limited by setting a sufficiently high threshold below which subsidies are unlikely to be distortive<sup>226</sup>. Some industry associations added that a complaint-based procedure, if similar to the one in TDI, would create important

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<sup>216</sup> E.g. European Trade Union Confederation, Polish Union of Entrepreneurs and Employers, Bundesarbeitskammer Österreich.

<sup>217</sup> Among others Italy and France

<sup>218</sup> e.g. Province of Overijssel.

<sup>219</sup> E.g. China Chamber of Commerce to the EU, Fédération nationale des Travaux Publics, Enel SpA, AFEP

<sup>220</sup> E.g. Airline Coordination Platform, EUCCC, Business Europe.

<sup>221</sup> Among others Czechia and Poland

<sup>222</sup> E.g. European Round Table for Industry, Confederation of Danish Industry, Bundesverband der Deutschen Industrie, Eurometaux

<sup>223</sup> E.g. Linklaters LLP, City of London Law Society

<sup>224</sup> Among others Czechia, Belgium, Denmark and Poland

<sup>225</sup> See among others the contributions to the public consultation of Freshfields, European Competition Lawyers forum, China Chamber of Commerce to the EU, American Chamber of Commerce to the EU

<sup>226</sup> See among others Poland's contribution to the public consultation on the White Paper and the contribution on the IIA of Bundesverband der Deutschen Industrie

costs for companies, as it is very time consuming and difficult for companies to prove the existence and the distortions due to a foreign subsidy.<sup>227</sup>

#### *Functioning of the internal market*

The impacts section on Problem 1 (section 6.1) already discussed the main impacts of a new instrument on foreign subsidies on the functioning of the internal market, notably in relation to the design parameter ‘**competence level**’ and the design parameter on ‘**effective redressive measures**’.

In addition, subsidised greenfield investments may for example create an artificially induced situation of over-capacity or below-cost pricing in a specific market.<sup>228</sup> A new instrument on foreign subsidies could therefore help to restore market prices and to base investment and pricing decisions on commercial considerations.

#### *Consumers and households*

It is not possible to quantify the order of magnitude of the short-term and long-term impact on consumers. This being said, as for subsidised acquisitions under problem 1, an instrument covering other market distortions could have a negative impact on EU consumers in the short term. However, in the absence of legislation on distortive foreign subsidies, competitive undertakings risk being crowded out by undertakings receiving distortive foreign subsidies, thus potentially leading to higher prices for consumers.

#### *Trade and investment flows*

The **general impact** would be the same as under problem 1. As to the **impact of the options for the investigative approach**, the options encompassing a notification system (options b2, b3, b4 and b5) may have a more immediate effect to change trade and investment flows as the undertakings receiving foreign subsidies would be subject to the notification obligation. At the same time, an ex-officio system (option b1) would target in particular the cases of the largest and most distortive foreign subsidies so that its impact on trade and investment flows may be less immediate but more focused. It is therefore difficult to conclude which effects would prevail and how the procedural options would impact trade and investment flows.

#### *Third countries and international relations*

Same as under problem 1.

#### **Social impacts**

Same as under problem 1.

#### **Environmental impacts**

Same as under problem 1.

## **7 HOW DO THE OPTIONS COMPARE?**

Following the assessment of the impacts of the various options in section 6, this section presents for each problem the most suitable configuration of design parameters. Before presenting the

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<sup>227</sup> See the minutes of the targeted consultation meeting with European Aluminium in Annex 6, point 3.

<sup>228</sup> Such claims have been made for example in relation to the steel industry and shipbuilding, as discussed in section 2.4.

various configurations or policy packages, the below table summarises the configuration of the three ‘modules’ as presented in the White Paper. The differences between the three modules and the ‘policy packages’ as developed in this impact assessment are also explained in this section.

*Table 6. Summary table presenting the three modules of the White Paper*

	Module 1 (for general market distortions)	Module 2 (for acquisitions)	Module 3 (for public procurement)
Competence level	Shared between Commission and Member States	Commission	Commission
Investigative approach	Ex officio for general market distortions	Ex ante control (Possibility to use thresholds was left open)	Ex ante control (Possibility to use thresholds was left open)
Thresholds for subsidies unlikely to be distortive	EUR 200 000	EUR 200 000	EUR 200 000
Assessment criteria	Establish if there is a distortion of the internal market using indicators and categories of likely distortive subsidies	Establish if there is a distortion of the internal market using indicators and categories of likely distortive subsidies	Establish if there is a distortion of the procurement procedure either directly or indirectly. Presumption of a distortion where the subsidy enables submission of an offer would be economically less sustainable without the subsidy.
Balancing test	Yes, but mechanism not specified	Same as in module 1	Not specified
Redressive measures	Indicative list based on State Aid rules	Same as in module 1	Indicative list, different from the one in module 1

## 7.1 Problem 1 - distortions in acquisitions

### 7.1.1 Policy option packages

Based on the assessment of the various impacts, the below table combines various sub-options to form possible policy packages to tackle distortions in acquisitions caused by foreign subsidies (problem 1).

*Table 7. Policy option packages for problem 1 – distortions in acquisitions*

Policy package Design parameter	Policy Package 1 Ex officio tool with shared powers	Policy Package 2 Notification tool at EU level	Policy Package 3 Combined ex ante – ex officio tool at EU level
Competence level	Option a2 (Shared between Commission and Member States)	Option a1 (Commission only)	Option a1 (Commission only)
Investigative approach	option b1 (Ex officio)	Option b4 (Ex ante control with notification threshold of EUR 500m EU turnover, 50m financial contribution)	Option b5 (Ex ante control for large acquisitions and ex officio for smaller ones)
Thresholds for subsidies unlikely to be distortive	Option c1 (EUR 200 000)	Option c2 (EUR 5m)	Option c2 (EUR 5m)
Assessment criteria	As explained in Section 5.3	Same as policy package 1	Same as policy package 1
Balancing	option e1	Same as policy package 1	Same as policy package 1

Redressive measures	Measures listed in Section 5.3	Same as policy package 1	Same as policy package 1
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The rationale for establishing these policy packages is as follows:

Policy package 1 would be equivalent to using module 1 in the White Paper to address the distortions caused by foreign subsidies. It proposes an investigative tool based purely on an ex-officio approach to detect and assess distortive foreign subsidies in acquisitions with shared competences between the Commission and Member States. This procedural and institutional set-up is similar to what currently exists for antitrust control in the EU.

Policy package 2, would be equivalent to using module 2 as defined in the White Paper but with more detail than in the White Paper and also some differences. It proposes an ex-ante notification system using high notification thresholds to focus on the largest transactions to limit the number of cases and hence the administrative burden on companies and resource implications on the supervisory authority. On the basis of the results of the impacts in Section 6, it also proposes establishing a much higher threshold for the subsidies unlikely to be distortive (EUR 5m instead of EUR 200k).

Policy package 3 proposes using refined versions of module 1 (for small acquisitions) and module 2 (for the largest acquisitions). Combining (refined) modules 1 and 2 would allow the supervisory authority to investigate acquisition cases that fall below the notification thresholds. The refinement is based on two differences. First, it is proposed to use a high threshold for distortive subsidies (option c1) to focus on the cases most likely to cause significant distortions. Second, it is proposed to appoint the Commission as the only supervisory authority not only for the notification module but also for the ex-officio module. This was introduced on the basis of the results of the impacts in Section 6 and stakeholder feedback.

### 7.1.2 Effectiveness

All policy packages would be more effective than the baseline, which cannot currently address distortive foreign subsidies in acquisitions.

Policy packages 2 and 3, which include a compulsory notification mechanism, would be more effective than policy package 1 for two reasons: First, for having easier access to information and second, for being able to redress the distortions before the acquisition is finalised. Policy package 3 would be more effective than 2, because having the possibility to also use ex-officio would allow identifying and addressing potentially distortive acquisitions below the notification threshold.

### 7.1.3 Coherence with other instruments and policies

All three policy packages in principle address the existing asymmetric situation that foreign subsidies are not subject to State aid control. All three also stay within the remit of the regulatory gap identified in chapter 2 of this report. They would therefore complement existing rules and not overlap with them. In particular, compatibility with the EU's international obligations would be ensured. If international trade rules change in the future (see option 5), the legal framework may have to be adapted to ensure continued coherence. In line with the Commission's exclusive competence for EU trade defence and State aid instruments, policy packages 2 and 3 would appear to ensure a more coherent interpretation and application of new legislation than policy package 1.

### 7.1.4 Efficiency

Policy packages 1 and 2 would be less efficient than policy package 3. In terms of costs, a pure ex-officio system (policy package 1) would have lower costs than a notification system (policy package 2). But the notification obligation in policy package 2 would bring more benefits than policy package 1, as the supervisory authorities would receive systematic and structured information about the planned acquisitions including possible foreign subsidies. The higher costs of the notification system in package 3 are offset by the benefits to be certain to investigate particularly distortive cases before the acquisitions are concluded.

Table 8. Overview of the policy option packages for problem 1 compare

		Baseline	Policy Package 1	Policy Package 2	Policy Package 3
Effectiveness	Objective 1: identifying distortions	0	+	++	+++
	Objective 2: removing distortions	0	+	++	+++
Coherence with other EU policies		0	+	++	++
Efficiency (costs vs benefits)		0	++	++	+++

## 7.2 Problem 2 - distortions in public procurement

### 7.2.1 Policy option packages

After having examined the impacts of the sub-options, the report shows below the most viable policy packages to tackle problem 2.

Table 9. Policy option packages for problem 2 – distortions in public procurement

Policy package	Policy Package 1	Policy Package 2	Policy Package 3
Design parameter	Ex-officio tool addressing distortions in public procurement (PP) with shared powers	Notification tool for large public procurement procedures at EU level	Combined ex ante - ex officio tool at EU level
Competence level	Shared between Commission and MS	Commission	Commission
Investigative approach	Ex officio; information provided by market actors on their own initiative.	Ex-ante control for large PP procedures with notification thresholds of EUR 250m or EUR 500m contract value	Ex-ante control for specific PP procedures (same thresholds as in 2), ex officio for smaller ones
Thresholds for subsidies unlikely to be distortive	EUR 200 000	EUR 5m	EUR 5m
Assessment criteria	Use of indicators	Same as policy package 1	Same as policy package 1
Balancing test	Positive effects in option 4	Same as policy package 1	Same as policy package 1
Redressive measures	Measures listed in option 4	Same as policy package 1	Same as policy package 1

The rationale for establishing these policy packages is as follows:

Policy package 1 for problem 2 would be equivalent to module 1 in the White Paper to address the distortions in public procurement caused by foreign subsidies. This policy package proposes an investigative tool based on an ex-officio approach with shared competences. The Commission and the Member States would investigate ex officio distortions in public procurement in general; no value threshold would apply.

Policy package 2 would be equivalent to using module 3 as defined in the White Paper but with more level of detail than in the white paper and also some differences. This policy package proposes an ex-ante notification system for specific procurement procedures, with an exclusive EU competence. To focus on the most significant procurements and to limit the administrative burden on companies and resource implications on the supervisory authority, it proposes the two notification thresholds, as explained in Chapter 6.

Policy package 3 proposes a combination of the first two packages, refining certain elements proposed in module 1 (for public contracts of a smaller contract volume) and module 3 (for public contracts of a high contract volume) of the White Paper. This policy package a notification system for large procurement procedures, with a high notification threshold to capture the largest and most distortive procedures, combined with an ex-officio system to give the possibility to investigate other procurement procedures in general. In this case, the ex officio would also be a Commission competence.

### *7.2.2 Effectiveness*

All Policy packages would be more effective than the baseline which cannot currently address distortions caused by the participation of subsidised bidders in EU public procurement procedures.

As regards both objective 1 (identifying the most distortive subsidies) and objective 2 (removing the distortions), Policy packages 2 and 3 are more effective than Policy package 1. Full reliance on market information under an ex officio approach (Policy package 1) risks failing to identify some procurement procedures involving distortive subsidies. In addition, Policy packages 2 and 3 would allow to tackle not only distortions in public procurement in general, but also distortions in specific public procurement procedures with high contract values.

Policy package 3 would be the most effective, as the participation in high contract value procurements would be notified, while still having the possibility to identify and assess participation in other procurement procedures using an ex officio approach. In ex officio investigations, the relevant information would be made available from various sources, including competitors providing market sector knowledge. In addition, information could be gathered and accumulated on the same undertaking participating in multiple procurements. Policy package 2 would be less effective as it would not allow investigation of (potentially distortive) participation in contracts below the notification threshold.

### *7.2.3 Coherence with other instruments and policies*

All three policy packages stay within the remit of the regulatory gap identified in chapter 2 of this report. The proposed legal instrument would not cover subject matters that are already covered by other legal instruments. This is true in particular as regards the existing public procurement framework, which does not address foreign subsidies at all. It is therefore considered that all policy packages are coherent with other instruments and policies.

If international trade rules change in the future as it may be eventually pursued under option 5, the policy packages might have to be adapted to ensure coherence. As in EU trade defence and State aid instruments, the Commission has exclusive powers, Policy packages 2 and 3 would be more coherent than Policy package 1.

### *7.2.4 Efficiency*

Compared to the baseline, all policy packages would require more resources, both for the supervisory authority and for companies bidding in procurement procedures.



As regards the supervisory authority, the mandatory notification (policy packages 2 and 3) would require significant resources insofar as all companies would need to submit the relevant information in a notification. In comparison to that, a system where the information is collected ex officio by the supervisory authority (policy package 1) would require less resources, as the supervisory authority would have more discretion in deciding who will be investigated based on the collected information. As regards companies, more companies would be affected by a system of mandatory notification (Policy packages 2 and 3) than by an ex officio system (Policy package 1). Consequently, for both the supervisory authority and for companies, Policy package 1 would be less costly than Policy packages 2 and 3.

The baseline, while being the least costly option, does not allow to tackle the problem of foreign subsidies in public procurement.

While Policy package 1 is less costly than Policy packages 2 and 3, the higher cost of the notification system is offset by its benefits: Policy package 3 covers not only distortions in public procurement in general (which is the only scope of Policy package 1), but also covers distortions in specific public procurement procedures above the notification threshold.

*Table 10. Overview of the policy option packages for problem 2 compare*

		Baseline	Policy Package 1	Policy Package 2	Policy Package 3
Effectiveness	Objective 1: identifying distortions	0	+	++	+++
	Objective 2: removing distortions	0	+	++	+++
Coherence with other EU policies			++	++	++
Efficiency (costs vs benefits)			++	++	+++

### 7.3 Problem 3 - other market distortions

#### 7.3.1 Policy option packages

Based on the assessment of the various impacts, the below table combines various sub-options to form two possible policy packages to tackle problem 3 i.e. distortive foreign subsidies in other market situations than acquisitions and procurement.

*Table 11: Policy packages for problem 3 – other market distortions*

	Policy Package 1 Comprehensive investigative tool involving Member States	Policy Package 2 Focused investigative tool at EU level
Competence level	Option a2 (Shared between Commission and Member States)	Option a1 (Commission only)
Investigative approach	Option b1 (Ex officio)	Same as policy package 1
Thresholds for subsidies unlikely to be distortive	Option c1 (EUR 200 000)	Option c2 (EUR 5 million)
Assessment criteria	No sub-options. See description in Section 5.3	Same as policy package 1
Balancing test	Option e2 (use a balancing test)	Same as policy package 1
Redressive measures	No sub-options. See description in Section 5.3	Same as policy package 1

The rationale for establishing these policy packages is as follows:

Policy package 1 would be identical to the module 1 as proposed in the White Paper, that is, an ex-officio investigative tool with shared competences between the Commission and Member States, a threshold of distortion at EUR 200 000 and using a balancing test to account for positive effects of the foreign subsidy. Building from the analysis in Section 6, this combination of sub-options would result in a comprehensive screening tool for two reasons. First, because using a low threshold of distortion (EUR 200 000) could catch a wide range of foreign financial contributions and second, because a combined level of enforcement would draw from a diverse pool of resources, at MS and EU levels.

Policy package 2, would be very similar to policy package 1 except for two differences. First, the Commission would be the sole supervisory authority and second, the threshold of distortion would be high, at EUR 5 million. The choice of sub-options aims at a targeted and uniform investigative tool by setting a high distortion threshold and a single supervisory authority.

### *7.3.2 Effectiveness*

Both policy packages would be more effective in contributing to the objectives than the baseline. Policy package 1 would score higher than policy package 2 as regards objective 1 (identifying the most distortive subsidies), as its comprehensive design entails less risk of missing out distortive foreign subsidies. Both policy packages include the same set of redressive measures and balancing test and therefore would score equally high as regards objective 2 (removing the distortions).

### *7.3.3 Coherence with other instruments and policies*

Both policy packages would be more coherent than the baseline, for the same reasons given under problem 1. As also explained under problem 1, exclusive Commission powers in policy package 2 would be more coherent than shared powers in policy package 1.

### *7.3.4 Efficiency*

#### Costs

Both policy packages entail more costs than the baseline as they require resources from the public enforcer and increase administrative burden on the companies receiving foreign subsidies. Due to a lower threshold for distortive subsidies and involvement of many more supervisory authorities, policy package 1 would lead to more administrative burden and more investigations and therefore have higher costs than policy package 2.

#### Benefits

Both policy packages would bring significantly more benefits than the baseline, notably to the companies competing with those that benefit from foreign subsidies. The benefits of both policy packages can be expected to be similar as the assessment criteria, redressive measures and the balancing would be the same.

#### Conclusion

As the benefits of both policy options are comparable but the costs of policy package 1 are significantly higher than of package 2, the latter would be the most efficient.

Table 12. Overview of the policy option packages for problem 3 compare

		Baseline	Policy Package 1 Comprehensive investigative tool	Policy Package 2 Focused investigative tool
Effectiveness	Objective 1: identifying distortions	0	++	+
	Objective 2: removing distortions	0	++	++
Coherence with other EU policies		0	+	++
Efficiency (costs vs benefits)		0	+	++

## 8 PREFERRED OPTION

The preferred options for each of the problems can also be presented as a three-tiered investigative tool with the following components:

- Component 1: A notification-based investigative tool for acquisitions when the turnover of the target or one of the merging parties exceeds EUR 500 million and the foreign financial contributions EUR exceed 50 million.
- Component 2: A notification-based investigative tool for bids in public tenders with a contract value above either 250 or 500 million.
- Component 3: An ex-officio investigative tool for all other market situations and for acquisitions and public procurement procedures below the thresholds of the investigative tools 1 and 2.

The combined tool would be enforced by the Commission. Foreign subsidies below EUR 5 million would not be considered distortive.

The preferred option largely corresponds to the approach presented in the White Paper with one main exception.<sup>229</sup> While the White Paper envisaged a role for Member States in scrutinising public procurement procedures, the preferred option proposes to enforce all components at EU level. This approach responds to widespread stakeholder concern that a new instrument on foreign subsidies would be applied inconsistently across Member States and overburden national authorities.<sup>230</sup> The preferred option also includes more details than the White Paper, notably on notification thresholds and the threshold for distortive subsidies. Such thresholds also respond to widespread stakeholder concerns about a high administrative burden and are in line with feedback from several stakeholders that a higher threshold for distortive subsidies than the initially proposed EUR 200 000 (over a three-year period) would be necessary.<sup>231</sup>

The preferred option would allow to deal with distortions in the internal market caused by foreign subsidies and would thus add to the EU's capacity to confront new challenges and protect businesses and citizens from unfair trading practices. It would fill the current legal gap with a new legal instrument. The new instrument would therefore complement existing EU instruments such as merger control, foreign direct investment screening and public procurement rules. Each instrument would have a distinct purpose and legal standard, as is the case today.

<sup>229</sup> While some stakeholders raised doubts about the approach presented in the White Paper, the majority of EU stakeholders (both Member States and other stakeholders) and some non-EU stakeholders support the initiative (see contributions referenced in sections 2 and 6).

<sup>230</sup> See e.g. the contributions of the Netherlands, ESF and other stakeholders in Annex 2 and Annex 6.

<sup>231</sup> Among others Czechia, Poland, European Round Table for Industry, Confederation of Danish Industry, Bundesverband der Deutschen Industrie, Eurometaux.

Moreover, given the high thresholds used for notification in components 1 and 2 of the new instrument, cases notified under these components would account for only a small part of all cases dealt with under existing instruments such as EU merger control and public procurement rules. In the few cases where there would be an overlap, procedural synergies could be ensured in practice, to the extent possible. For instance, the timelines of parallel reviews under different instruments (notably under the new instrument and the EU Merger Regulation) could be aligned, thereby avoiding unnecessary delays or legal uncertainty. Similarly, the type and format of the information to be provided in notifications under different instruments could be aligned as much as possible, enabling businesses to simply replicate documents and amend or complement them only in a limited way for each specific notification. By contrast, existing instruments prohibit the use of information provided under one procedure for procedures under different legal instruments. It would thus not be possible to use a notification under the EU Merger Regulation to exempt an undertaking from providing the same information under the new instrument.

In that regard, business transactions already today often face scrutiny under several regulatory regimes globally (notably parallel merger control in several jurisdictions, as well as FDI screening). The new instrument would only be one addition. Undertakings and public authorities thus have significant experience in dealing with such parallel reviews and seeking alignment, which in the case of the new instrument will be facilitated by the Commission also handling EU merger control.

As regards the interaction between the proposed instrument and specific public procurement procedures, it is envisaged that the instrument would be designed in such a way as to have minimum, if any, impact on the ongoing procurement procedure. Under mandatory notification, the investigation of the foreign subsidy would be carried out in parallel with the evaluation of tenders. The deadlines for concluding the investigation will be in line with the time needed for the typical evaluation to be finalised. The contracting authority will be able to award the contract to a non-subsidised bidder if it proposes the best tender, and would only have to wait for the outcome of the investigation if the subsidised bidder would be set to win the contract. In any case, they will be free to award the contract to the best bid should the deadline for the investigation lapse without a decision. Under ex-officio, such investigations would usually take place only after award, and thus have no impact on the outcome of the procurement procedure, and will focus on correcting the damage to the internal market through the use of fines.

Annex 3 describes who is affected and how by the preferred option.

The preferred option would contribute to the specific objectives as follows:

#### *8.1.1 Contribution to specific objective 1 (identifying the most distortive foreign subsidies)*

For problems 1 (acquisitions) and 2 (public procurement), the investigative tool comprises a system of ex ante notification for the largest and potentially most distortive cases. Such ex ante approach ensures a systematic identification of distortive foreign subsidies in these situations of highest economic value. For all other market situations including smaller acquisitions and smaller procurement procedures, distortive foreign subsidies would be identified in an ex officio procedure. Such ex officio approach enables the supervisory authority to focus its attention on the most relevant cases of distortive foreign subsidies. Based on relevant market information, the supervisory authority will then apply the assessment criteria described in chapter 5 of this report to establish the degree of the distortion.

### 8.1.2 Contribution to specific objective 2 (removing the distortions)

The redressive measures described in chapter 5 are based on measures applied in EU State aid control to remove the distortive effect of State aid. As the potentially distortive impact of foreign subsidies on the internal market must be considered similar to that of State aid, the State aid toolbox of remedies provides in principle for an efficient set of measures to also remove distortions caused by foreign subsidies.

There are only some nuances to this general finding. Firstly, the reimbursement of a foreign subsidy to its granting authority in a third country may often not be effective as it is more difficult to monitor and enforce outside the EU. Hence, behavioural or structural remedies may be more effective and used more frequently. Secondly, in the case of acquisitions facilitated by foreign subsidies, the prohibition of such acquisitions may be more common as a redressive measure than under State aid rules. The reason is that there is in principle no legal basis under EU rules to approve State aid granted for an acquisition. As a result, acquisitions financed by State aid hardly occur in the EU.

In conclusion, the preferred option provides for an effective toolbox of redressive measures to remove the distortion caused by foreign subsidies. In the case of large acquisitions and large procurement procedures, the ex ante approach ensures that the redressive measures can be decided before the transactions are closed which gives legal certainty to the undertakings concerned. For smaller transactions, the ex-officio procedure would still allow to remedy the distortion ex-post. For instance, the toolbox of redressive measures includes options such as granting third party-access on non-discriminatory terms, publication of R&D results or divestments if a foreign subsidy is found to have distorted a specific activity, acquisition or investment.

#### Nature of the instrument and legal basis

When taking EU legislative action, a choice has to be made between a Regulation or a Directive. A Regulation is directly applicable, and thus automatically deemed to be enshrined in Member State law. There is no need for implementing legislation. However, it leaves Member States very limited or no scope to adapt to their national specificities. A Directive is only binding as to the result to be achieved, which gives Member States a choice as to the form/method to achieve this goal. Directives can set minimum standards which do not prevent Member States from having in place provisions which go further. It also allows for more uniform and detailed requirements to be put in place where appropriate.

The aim of the preferred policy option proposes the Commission to be sole enforcer to address in a uniform manner across the EU the distortions that some foreign subsidies are causing in the internal market. Therefore, it would not be suitable to adapt the rules at national level. As a result, a Regulation is deemed the appropriate instrument. Chapter 3 of this report has already described the legal basis.

## **9 HOW WILL ACTUAL IMPACTS BE MONITORED AND EVALUATED?**

The Commission should review the implementation of any (legislative or non-legislative) proposal with regards to the achievement of policy objectives identified in this Impact Assessment.

The indicators proposed to monitor the achievement of policy objectives identified in this Impact Assessment are presented below.

Table 13. Monitoring indicators

Specific objectives	Monitoring indicators	Sources of data and/or data collection methods	Data collected already?	Actors responsible for data collection
Identify the most distortive subsidies	The yearly number of cases of alleged distortive foreign subsidies dealt with by the supervisory authority	Sources of information - Notifications - Third party submissions of market information - Ex officio cases - Market investigations	No	Commission
	Share of cases of foreign subsidies found to be distortive vs. total number of cases	Record of all final decisions finding distortions caused by foreign subsidies.	No	Commission
	Share of cases cleared thanks to the balancing test vs. total number of cases.	Record of all final decisions finding that positive effects outweigh the distortions.	No	Commission
Remove distortions caused by foreign subsidies	Stakeholder perceptions of the impacts of the imposed redressive measures	Consultation with EU stakeholders on their perceptions of the impacts of redressive measures	No	Commission

To avoid putting any additional administrative burden on companies or Member States due to the collection of information used for monitoring, the proposed indicators mainly rely on internal Commission data sources or consultations that will be conducted by the Commission.

The initiative is foreseen to be evaluated 5 years after entry into force. The evaluation will examine in particular whether, and to what extent, the above objectives have contributed to the improvement of the functioning of the Internal Market. In addition, in view of its novelty, the initiative will be subject to continuous monitoring on the part of the Commission. In the context of such monitoring, the Commission will pay special attention to the potential need of review of design parameters, such as notification thresholds. Should such a need arise, the parameters could potentially be modified.



# Annex 1. Procedural information

## Lead DG, Decide Planning/CWP references

The Directorate-General (DG) for Competition and the Directorate-General (DG) for Internal Market, Industry, Entrepreneurship and SMEs led the preparation of this initiative and the work on the Impact Assessment in the European Commission. The planning entry was approved in Decide Planning under the reference PLAN/2020/8943. It is included in the 2021 Commission Work Programme (ref. COM(2020) 690 final) under the policy objective “A Europe fit for the digital age”.

## Organisation and timing

The planned adoption date included in the Commission Work Programme adopted on 19 October 2020 is on Q2 2021. An inter-service steering group (ISSG), was established for preparing this initiative composed of the following Commission services: AGRI, BUDG, CLIMA, CNECT, DEFIS, DEVCO, EMPL, ENER, ESTAT, ECFIN, EAC, FISMA, FPI, JUST, JRC, MARE, MOVE, OLAF, REGIO, RTD, SJ, SG, TAXUD and TRADE plus the EEAS. The ISSG had five meetings between September 2021 and the adoption in May 2021.

Milestones	Dates
Publication of the White Paper	17 June 2020
Feedback period on the White Paper	17 June 2020 to 23 September 2020
Publication of the inception impact assessment	6 October 2020
Feedback period on the inception impact assessment	6 October 2020 to 29 October 2020
Targeted consultations	November 2020 to January 2021
Submission to the Regulatory Scrutiny Board	3 February 2021
Meeting with the Regulatory Scrutiny Board	3 March 2021

## Consultation of the RSB

RSB requested improvements	Changes in the revised report
<p>The problem analysis should emphasise more the difficulties to collect information on the potential distortions caused by foreign subsidies (in the absence of a dedicated instrument) and the limitations of the case studies and the data. Moreover, the report should clarify the difference between potential distortions that may arise from subsidies granted by Member States and those resulting from foreign subsidies. It should also provide a more balanced explanation of the possible positive short-term effects (e.g. lower public procurement costs) and the negative long-term effects (e.g. development of dominant positions). The problem analysis should include the indirect consequences of subsidised acquisitions and subsidised imports from third countries. The report should detail the analysis of the problems in public procurement. It should be clearer on the risks of third country (co-) ownership in public natural monopolies, earned by subsidised bidding.</p>	<p>Section 2 of the report has been changed as follows:</p> <ol style="list-style-type: none"> <li>1/ Description of the data available in the public domain and its limitations for drawing un-rebuttable conclusions</li> <li>2/ Clarification that the distortions caused by subsidies are in principle the same regardless of whether they are granted by a Member State or by a third-country</li> <li>3/ Additional detail as regards the short-term, long-term and indirect effects of foreign subsidies for all three problems.</li> <li>4/ Analysis of the risks of public natural monopolies managed by foreign operators as a result of a subsidised bid</li> </ol>
<p>The policy options should be redesigned to focus more clearly on the main choices for the policy</p>	<p>Section 5 of the report has been changed as follows:</p> <ol style="list-style-type: none"> <li>1/ Early discarded options (options 2 and 3) are</li> </ol>

RSB requested improvements	Changes in the revised report
<p>makers. The report should present self-standing options for the design parameters of the policy instrument, i.e. competence level, investigative approach, EU interest test and institutional implementation. It should explain the retained policy options more in detail (e.g. investigative powers, redressive measures and their enforcement). The range of explored options for notification and de minimis thresholds should be justified in terms of adequacy. They should be sufficiently broad to reflect positions likely to emerge in the legislative process. A separate section on discarded options should give an overview of the initially considered options and justify why options that looked promising at first view (sometimes with stakeholder support) were then discarded from further analysis.</p>	<p>presented and analysed separately 2/ Two main changes as regards the presentation of option 4. First, identification of all the relevant design parameters and the sub-options under each parameter. Second, more level of detail of what option 4 and its sub-options entail.</p> <p>As a result of changing the presentation of option 4 in section 5, the presentation of Sections 6 and 7 has been adapted accordingly.</p>
<p>The report should explain how the new instrument would work in conjunction with existing EU instruments in the public procurement, merger control and foreign direct investment screening areas. It should describe how procedural synergies (e.g. for notifications, timelines) would be ensured without causing unnecessary delays or legal uncertainty. It should clarify the envisaged redressive measures, including in situations where the foreign subsidy distortions would be detected only after the implementation of the procurement or transaction.</p>	<p>The interplay between the preferred option and existing instruments (EU Merger Control Regulation; EU FDI Regulation and EU Public procurement procedures) is explained in Section 8.</p> <p>The report also explains now in Section 8 (preferred option) how certain redressive measures of the proposed toolbox would be effective to address the distortion of transactions ex-post</p>
<p>Linked to the issues detailed in the problem analysis, the report should explain how the responsible authority would apply the EU interest test. It should clarify how it would judge when foreign subsidies may overall promote or conflict with EU policy objectives and how this may influence the design of possible redressive measures.</p>	<p>As part of the restructuring of Section 5, the design parameter on the ‘balancing test’ is explained in more detail as well as its interplay with the design parameter on ‘redressive measures’.</p>
<p>The impact analysis should present positive and negative effects of the policy intervention in a more balanced way. Particularly for the short term, it should assess more thoroughly the risks to economic activity and employment in case foreign direct investment declined. The analysis should also cover possible (short-term) adverse impacts on consumers and on public procurement costs.</p>	<p>Section 6 has been reviewed to present the positive and negative impacts of Option 4 in a more balanced way. The section now includes more details in the short term impacts</p>
<p>The monitoring and evaluations arrangements should reflect the novelty of this instrument and the potential need for timely review, including of key design parameters, such as notification and de minimis thresholds.</p>	<p>The monitoring section (Section 9) includes now the possibility to review the design parameters of the preferred option,</p>

### Evidence, sources and quality

The report uses several sources of information.

First, reports from academics, competition authorities, the OECD and the European Court of Auditors. All references are cited in the main text of the report. To list a few:

- Chinese state capitalism: A challenge for the European market economy”, German Monopolies Commission, July 2019
- Hufbauer, Gary, Thomas Moll, and Luca Rubini. "Investment subsidies for cross-border M&A: trends and policy implications." *United States Council Foundation, Occasional Paper 2* (2008), p. 9.
- Various OECD reports on distortive subsidies: OECD, “Measuring distortions in international markets: The semiconductor value chain”, OECD Trade Policy Papers, No. 234, OECD Publishing, 2019, Paris. OECD, “Measuring distortions in international markets: the aluminium value chain”, OECD Trade Policy Papers, No. 218, OECD Publishing, Paris. OECD, Subsidies in the steel sector: A stocktaking note, 2017, DSTI/SC(2017)11.
- European Court of Auditors, The EU’s response to China’s state-driven investment strategy, Review No 03 2020.

Second, public information available in the Decisions of the European Commission, national competition authorities, press and company websites to illustrate the case studies showcasing the distortions caused by foreign subsidies.

Third, the Commission Services have used quantitative data from internal data on EU merger notifications and JRC data on foreign direct investment cases and processed the data from several specialised databases on subsidies including [list several databases]. The Commission Services have also used confidential internal Commission data from several competition instruments to estimate the resource needs.

Finally, the report relies on the feedback from the three stages of public consultations described in Annex 2 and Annex 6 of this report as well as from tens of conferences and webinars organised on the topic.

## Annex 2. Stakeholder consultation synopsis report

### 1. Introduction

The [consultation of the initiative on addressing distortions caused by foreign subsidies](#) was organised in several phases in order to allow all the relevant stakeholders to express their views on the proposal at various stages of preparation.

- On 17 June 2020, the [White Paper on foreign subsidies](#) was adopted by the Commission, which launched a 14-week public consultation that finished on 23 September.
- On 6 October 2020, the Commission published an Inception Impact Assessment (IIA) outlining the available policy options, their impacts, and other elements to be assessed in the Impact Assessment report.
- In October 2020 – January 2021, the Commission services organised a number of bilateral targeted consultations with the most relevant stakeholder representatives. The minutes of these bilateral discussions will be [published on this website](#).

### 2. Public consultation on the White Paper (17 June – 23 September 2020)

The White Paper was very comprehensive in its scope, as it provided for a forum to express views and ideas on the problem definition, the policy options to address it (including beyond those proposed in the paper), the enforcement mechanism (notification system versus ex-officio action), the assessment criteria, the organisational set-up, procedure and the redressive measures. The questionnaire for the public consultation can be found in the [Annex II of the White Paper](#) (pp. 48-49). The replies to the public consultation on the White Paper and the [full summary](#) are published on [this website](#).

A detailed summary of the public consultation on the White paper is also available in Annex 6 to the IAR.

The Commission received 150 submissions from a wide range of stakeholders:

- 17 from public authorities of Member States;
- 24 from third country stakeholders;
- 100 from business/industry associations and individual companies;
- and the remainder from law firms, academic institutions, trade unions, NGOs, other public authorities and individual citizens.

The replies received in the public consultation on the White Paper have been highly relevant for the drafting of the Regulation. Almost all EU stakeholders, including Member States, welcome the initiative and share the view that there is a need to tackle the distortive effects of foreign subsidies on the internal market. The majority agrees with the scope of the approach as outlined in the White Paper, but stress the need for a proportional measure in order not to stifle foreign investment, a concern echoed also by non-EU contributions. A large part of respondents also highlighted transparency issues.

To remedy the possible adverse effect on foreign investment and minimize the administrative burden on companies and public authorities, which has been pointed out by several respondents, the notification thresholds for Modules 2 and 3 have been set relatively high in order to only capture the potentially most distortive subsidies. Similarly, to increase the legal certainty for companies active in the EU, it has been proposed to increase the threshold for distortive subsidies, which will have a positive impact particularly on SMEs. Given the numerous requests for consistency in the application of the instrument, it is also proposed that the Commission retains the enforcement power while only a limited number of cases will be subject to a notification obligation and the Commission remains able to pursue cases ex-officio.

### **3. Feedback on the inception impact assessment (6 October – 29 October 2020)**

The Inception Impact Assessment (IIA) outlined the available policy options, their impacts, and other elements to be further assessed in the Impact Assessment report. The Commission received 22 submissions as feedback on the Inception Impact Assessment from the following: 3 Member States (4 submissions) and 18 other respondents provided their feedback. All the replies are [available online](#).

A detailed summary of the feedback received on the IIA is available in Annex 6 to the IAR.

Almost all respondents who provided feedback on the Inception Impact Assessment support Option 2: legislative action at EU level, possibly complemented by Option 3: international rule-making. While an action at EU level seems to be most favoured approach in the short and medium term, the international approach (WTO reform and pursuit of stronger subsidy commitments in future FTAs) is not a mutually exclusive solution to an EU action and will be further pursued in the future.

The feedback on the IIA confirmed the general approach of this Impact Assessment report in terms of the elements that should be considered as part of the available policy options and their impacts. Several respondents also pointed to existing EU legislation, which could be amended to address the issue of foreign subsidies. The corresponding sections of this Impact Assessment report discuss the feasibility of this option.

### **4. Targeted consultation (November 2020 – January 2021)**

Based on the information received in the public consultation on White Paper (e.g. level of interest, relevance of information provided, examples of possible third-country subsidies, future relevance of a possible new instrument), the targeted consultation aimed to collect further information and feedback from the following stakeholder groups:

- EU business associations in the field of the production of goods and services most exposed or potentially exposed to foreign subsidies;
- the legal community (law firms advising companies on related competition and trade issues);
- Member States and their relevant national public authorities;
- relevant stakeholders from third countries;
- trade unions and consumers.

The targeted consultation was designed to help produce concrete examples of distortive subsidies including their type, the sector affected, third country granting it, the type of possibly distortive subsidies that can be most commonly observed as well as their impacts on the company, sector or market. Furthermore, the questions were aimed to assess the policy options proposed in the Inception Impact Assessment as well as other possible policy options, the elements of these policy options that should be considered in the Impact Assessment, the impacts of the various policy options proposed including economic, social, environmental and impacts on administrative burden.

The minutes of the bilateral meetings will be available on [this website](#). Short summaries of these meetings are available in Annex 6 to the IAR.

The feedback provided in the targeted consultation was used to provide examples of subsidies, including the type, sector and concrete distortive effects. These examples were used in the Problem definition section of this report. The examples, which were not included in the IAR, can be found in the minutes of the bilateral meetings. The stakeholders also expressed their preferred policy options and answered which elements and types of impact should be considered as part of

the Impact Assessment report. This feedback was also taken into consideration in assessing and evaluating the policy options.

## **5. Conclusion**

The feedback received during all phases of the stakeholders consultation were used in the drafting of the legal instrument and accompanying Impact Assessment report. It has been described throughout the whole report and in this section how the concrete elements of stakeholder feedback were used.



## Annex 3. Who is affected and how?

### 1. Practical implications of the initiative

Stakeholder group	Practical implications
Public authorities	The European Commission would be the most affected public authority by the preferred option for all three problems, as the Commission would become the sole enforcer of the investigative tool. Component 1 may require about 40 FTE; component 2, between 15-45 FTE and component 3, 60 FTE. To a much lesser extent, national authorities and contracting authorities (for component 2) are likely to be affected by the preferred option in the mid and long term as the European Commission is likely to seek establishing coordination mechanisms with national authorities to better enforce the investigative instrument.
Businesses	First, businesses potentially benefitting from foreign subsidies would be the group of stakeholders mostly affected by the initiative. As described in chapter 6 of the report, this may concern undertakings ultimately owned by both foreign and EU nationals. Components 1 and 2 would require companies that exceed the notification thresholds to submit a notification. This would result in an administrative burden as described in chapter 6. Furthermore, if the Commission initiates an ex-officio investigation in all other market situations, the undertakings concerned would need to submit the requested information. If undertakings are found to have benefitted from distortive foreign subsidies, they would be subject to redressive measures such as the repayment of the subsidy. Second, undertakings which do not benefit from distortive foreign subsidies, would benefit from the preferred option because it would restore and preserve the level playing field in the internal market. Thirdly, the preferred option would not affect much SMEs. The notification thresholds are likely to be too high to affect them. Furthermore, the high threshold for subsidies not deemed distortive in the preferred option – which is 25 times higher than the de minimis for State Aid – is also likely to be too high to affect most SMEs.
Consumers	Although consumers would not be directly affected by the new legislation, the preferred options could have a slightly negative economic impact on consumers in the short run since it may lead to an increase in prices, although this is not expected to be significant. In the long run, however, consumers would benefit from ex ante control of potentially subsidised acquisitions. Notably, a control of subsidised acquisitions could spur innovation since non-subsidised undertakings have better chances to achieve economies of scale. Moreover, addressing distortive foreign subsidies also beyond acquisitions, should improve competition in the internal market which ultimately benefits consumers through lower prices and better products.
Third country States	Public authorities from third countries would not be directly affected by the preferred options. The European Commission as an enforcer may however engage with them as regards information requests or more generally, in consultations throughout the procedure. In general, this instrument might prompt third countries to increase efforts to seek multilateral solutions as well as to reassess the use of subsidies in their investment policies.

## 2. Summary of costs and benefits

<i>I. Overview of Benefits (total for all provisions) – Preferred Option</i>		
<i>Description</i>	<i>Amount</i>	<i>Comments</i>
<i>Direct benefits</i>		
Improved level playing field between companies	Could not be quantified	The preferred option would reduce the risk that non-subsidised companies are crowded out by companies that benefit from distortive foreign subsidies. The benefits include access to technology, scaling up through acquisitions, more competitive and fair procurement markets providing realistic quality price ratios to the taxpayer and more generally, growth
<i>Indirect benefits</i>		
Economic growth	Not possible to quantify	Improving competition by removing distortive foreign subsidies would lead to more efficient companies, innovation and more choice, and in the long-term lower prices for consumers
Third countries incentivised to resolve any issues in the ambit of various trade agreements	N/A	In order to avoid unilateral measures, third countries will be motivated to explore multilateral solutions

<i>II. Overview of costs – Preferred option</i>							
		Citizens/Consumers		Businesses		Administrations	
		One-off	Recurrent	One-off	Recurrent	One-off	Recurrent
<b>Notification of subsidised acquisitions (a)</b>	Direct costs	none	none	negligible	Around 30 companies per year may be affected. Notification costs range between EUR 5,000 and EUR 500,000. If the Commission would find an infringement, the company may have to pay back the subsidy or if found not effective, other redressive measures can apply.	negligible	Around 40 full time equivalent (FTE) employees excluding costs for administrative tasks
	Indirect costs	Not possible to quantify	Not possible to quantify		If the Commission opens an in-depth investigation there may be indirect costs linked to the impact that the legal uncertainty over the outcome could have on the business. But in this regard, the same	none	none

					applies to any infringement instrument by a public authority		
<b>Notification procedure for public procurement procedures</b>	Direct costs	none	none	Negligible	The costs per company should be similar to those in action 1. The number of cases expected to be between 13 and 36, depending on threshold. Further difficulty in calculation is the fact that number of cases does not equal number of companies as many tenders are provided in consortia.	Negligible	Relying on resource assessments as explained in Chapter 6, the Commission would need between 15 and 45 full time employees, depending on the threshold.
	Indirect costs	none	Increased risk of higher prices in public procurement due to fewer cheap bids facilitated by foreign subsidies	none	none	none	none
<b>Ex-officio tool for all other market situations and acquisitions and public procurement below the thresholds</b>	Direct costs	Same as above	Same as above	Negligible	30-45 cases per year including other market situations, acquisitions and public procurement.	Negligible	Around 60 FTEs
	Indirect costs	Same as for 1	Same as for 1	Same as for 1	Not applicable	Not applicable	Not applicable

## Annex 4. Supporting data and analysis for the problem definition

### 1. Additional case studies illustrating the distortions caused by foreign subsidies under Problem 1

#### Example 3, Problem 1

In 2010, Company A, a nominally privately owned company, and Company C jointly purchased Company B from Company D for 1.6 billion USD. In the aftermath of the financial crisis, Company D was in a critical financial condition and thus decided to sell Company B. There were three other bidders to acquire Company B.

Company B was Company A's most prominent acquisition. It allowed Company A to expand into the high-end segment of the [...] manufacturing market. Moreover, through Company B, Company A was able to acquire cutting-edge technology in the new energy sector. Company A's acquisition coincided with the strategy of the Country A government to promote the development of the new energy sector.

To finance the acquisition of Company B, Company A received inter alia support from public funds from local governments of Country A. Main funding sources of the acquisition were as follows:

\* Company C provided [...] (USD 440 million) in return for equity; [...]. Company C is owned by the government of Country A. Its sole business is the investment and management of state-owned assets.

\* The Country A local Government established [...] in February 2010 that provided [...] to the acquisition (USD 147 million) in return for equity.

\* A branch of the state-owned Country A Construction Bank provided loans of USD 200 million to Company A.

\* Company A set up a [...] fund that provided USD 600 million for the acquisition.

\* Company D likewise provided financing of USD 200 million to Company A.

As a result of the acquisition, Company A received a 51% share in equity participation of Company B, Company C 37% and Country A local government 12%.

The case of Company A illustrates that not only SOEs but also privately owned companies may receive substantial support from Country A central and local governments. The Chief Executive of Company A openly admitted at the time that the acquisition of Company B would not have been possible without Country A government support.

Last but not least, Company A is a major beneficiary of subsidies from the Country A government (beyond the Company B acquisition): e.g., in 2011, half of Company A's net profits came from subsidies, which made it the biggest recipient of subsidies amongst privately owned Country A companies.

#### Example 4, Problem 1

To acquire control, Company A offered to pay a substantial acquisition premium for Company B. Company A's offer amounted to EUR 4.6 billion which allowed Company A to become the majority shareholder of Company B.

The acquisition was also assessed and eventually approved by the Commission under the EU Merger Regulation. Some financial details of the acquisitions are as follows:

Financing of the acquisition (cash acquisition): EUR 4.6 billion were financed through the company's own funds and a bridge loan, then refinanced with a syndicated loan from seven banks of Country A.

In order to refinance the previous bridge loan, Company A obtained a 5-year syndicated loan of EUR 3.7 billion. The loan interest rate was 0.65% (EUR 26 million) in addition to a one-time transaction cost of EUR 35 million.

#### Example 5, Problem 1

Company A acquired Company B for a reported amount of EUR 2.2bn. Company A is a large state-owned IT conglomerate which is controlled by two government departments of Country A.

Company B is active in the IT sector with an annual turnover of EUR 500m, whilst employing 3,500 people at nine production sites globally. The overall strategy followed by Country A in favouring its IT industry is outlined in relevant guidelines.

#### **National fund financing**

The Guidelines led to the creation of the Country A's national fund, now endowed with USD 29bn to support the national IT industry. From its inception, the fund has had significant interactions with Company A and committed up to USD 7bn to the development of the company.

#### **Regional IT funds**

The relevant Industry Association estimated that, as of 2017, while the National Fund had secured already roughly USD 21bn in funding (compared to 29 bn in 2019 as highlighted above), provincial and municipal IT-related funds had raised over USD 80 bn and were well on their way to reaching USD 150bn in size.

#### **Below market equity and below market borrowings**

According to the OECD, in the period from 2014-2018, Company A received below market loans from Country A's state controlled banks amounting to USD 2.2bn.

The Country A's Development Bank additionally agreed to provide Company A with USD 14bn in financing from 2016-2020 in the context of the development of the IT industry. Other below-market loans also include two loans worth USD 1 bn and USD 7 bn committed by two banks of Country A.

#### **Preferential tax treatment**

As of 2019, chip designers and software producers will be exempt from corporate taxes for two years, followed by a 50% reduction during the 3 following years.

#### **Below market purchase of land**

Based on data provided by a government department of Country A, the OECD calculated that Company A purchased land for one of its foundries for USD 37.34 per m<sup>2</sup>, while the official average price for industrial land in similarly sized cities was of USD 112.4 per m<sup>2</sup>.

#### Example 6, Problem 1

Company A is a non-listed private enterprise mainly specialised in processing. In 2018, Company A produced about 11 million tonnes of steel, reported revenues for USD X billion and profits for USD Y billion. Company A is based in a specific region in Country A that receives government support. As such, it is eligible for support under a support plan of a local government of Country A, enabling it to shift the production abroad and curb overcapacity in the Country A. In particular, the latest implementation plan establishes that undertakings from the above mentioned province should reach out to the central government's relevant departments in order to transfer their production capacity abroad.

In 2019, Company B was placed into compulsory liquidation after it failed to secure government funding to continue its operations. In 2020, Company A completed the acquisition of Company B, with a deal that is estimated to have cost USD Z million. Company A pledged to spend USD W billion to modernize Company B's plants and businesses.

In view of the above, it appears that due to the potentially subsidised acquisition of Company B, Company A may have shifted its steel overcapacity abroad.

## **2. Additional case study and tables illustrating distortions under Problem 2**

#### Example 4, Problem 2

Over a year ago, the government of an EU Member State awarded a contract for an energy facility to a consortium led by a majority state-owned petroleum company and a majority state-owned shipbuilding company. Both had benefitted from substantial government subsidies from a third country. The public tender contract was valued at EUR 500 million. The project is co-financed by a grant from the European Union, with additional financial support from International Financial Institutions.

## **3. Additional case studies illustrating distortions under Problem 3**

#### Example 3, Problem 3

The case of Company C may illustrate the application of selective tax relief by Country Z resulting in a financial advantage to Company C, which operates in EU.

Company C is a supplier of products for major manufacturers within the EU. It generates almost half of its sales in Europe. Its 2018 annual report refers to increasing corporate taxes as a potential risk for its business.

Country Z tax laws allow it to fully exempt newly founded companies or companies that move to Country Z from corporate profit taxes for up to 10 years. Newspaper articles indicate that Country Z agreed on such a comprehensive, selective, tax deal with Company C. As a result, in late 2018, Company C announced that it would move its headquarters from an EU Member State to Country Z. A legal opinion commissioned by the Country Z Parliament's Economic Commission points out that integrating state aid provisions modelled after EU law in a potential future Country Z-EU FTA could undermine Country Z sovereignty to use such selective tax reliefs as a means to attract foreign companies. In this context, the legal opinion makes a direct reference to the selective profit tax relief granted to Company C, indicating that it is 'doubtful' whether such schemes could be classified as regional aid or aid for research and development.



The selective financial advantage granted by Country Z thus likely enabled Company C to increase its net profits. Additionally, some stakeholders during the targeted consultation mentioned that when undertakings move outside the EU, this may lead to a decrease of employment within the EU, causing a further distortion of the internal market.

#### Example 4, Problem 3

Company D is a majority state-owned engineering and construction company that has benefitted from substantial government subsidies from Country W. Company D has been a contractor for numerous projects, also in the EU. It has recently been placed on the US Department of Commerce's Entity List. This means that Company D will require specific licenses to import or transfer goods.

Recently, Company D acquired a controlling stake in an EU construction company. This acquisition effectively valued the EU company at more than double its pre-existing market capitalisation.

Company D has thus paid a high premium to acquire its stake, thus potentially distorting the EU acquisition market. Through this participation Company D is also thought to pursue its strategic goal of expanding its operations in the EU and from there entering the US market thus circumventing US restrictions imposed on Company D. Such strategy seems to be one of the main drivers of Country W (potentially subsidised) investments in the EU.

## **4. Examples of sectors affected by foreign subsidies**

### 1. The semiconductor industry<sup>232</sup>

#### *The industry*

The largest semiconductor vendors are located in the US, the EU, Korea and Japan. Many outsource the manufacturing, assembly and testing to other firms located in mainland China, Taiwan and Singapore. Overall, the top 20 companies in the sector, all of which are located in the aforementioned locations, supply over 80% of the market, which was estimated at USD 470 billion in 2018.

#### *Subsidies*

According to the OECD study, support to the industry is granted through the following channels:

- Grants
- Favourable tax treatment
- Budgetary government support
- Support through the financial system:
  - *Below-market borrowings*. This is consistent with China's own 2014 IC Guideline, which instructs "domestic development banks and commercial banks to continually provide financial support to the integrated circuit industry."
  - *Below-market equity* (for instance by providing direct funds to build new manufacturing plants.)

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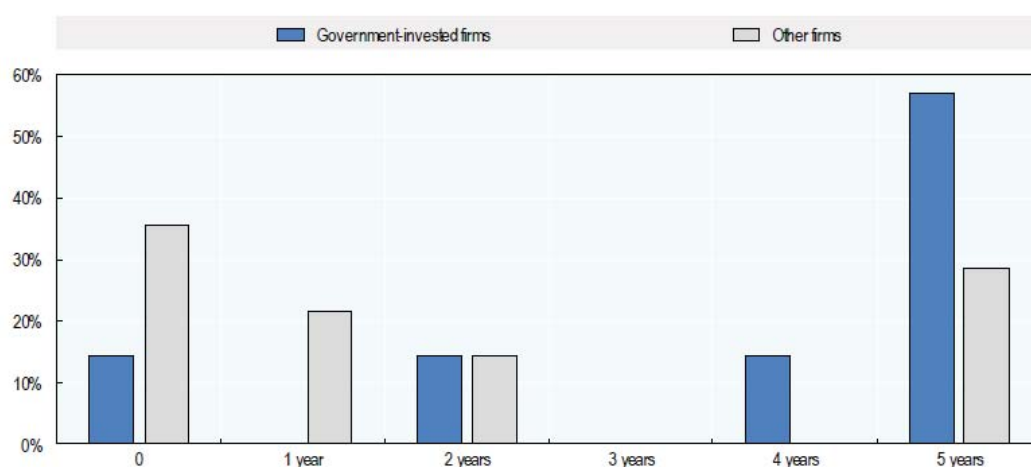
<sup>232</sup> OECD (2019-12-12), "Measuring distortions in international markets: The semiconductor value chain", OECD Trade Policy Papers, No. 234, OECD Publishing, Paris. <http://dx.doi.org/10.1787/8fe4491d-en>

The OECD estimates the total government support for all 21 firms in OECD’s sample amounted to USD 50 billion over the period 2014-2018.

Government support provided through government budget (in particular for R&D) and tax incentives is common in the industry, with various jurisdictions competing for manufacturing and research jobs. However, the provision of below market equity and below market borrowings appears to be concentrated in China, where the government frequently owns equity in semiconductor companies.

### *Impact of subsidies*

The OECD notes that government subsidies may have a negative effect on the industry. As can be seen from the figure below, below-market equity returns are more frequent and persistent for government-invested firms. Consequently, the OECD study concluded that the effectiveness of the support for semiconductors has a particular resonance for China, where support tends to be relatively large.



Source: OECD calculations; Number of years for which results indicate below-market equity returns, % of firms<sup>233</sup>

The OECD analysis shows that support provided through the financial system – particularly through the equity channel – is a significant contributor to total government support in the semiconductor value chain. As with other forms of support, below-market equity can distort production and investment decisions by firms, particularly where it is tied directly to the construction of new semiconductor fabs. Unlike most other forms of support, however, government equity injections also expand the role of the state in the economy by increasing the proportion of assets that are government-owned and -controlled.

One important implication of the global value chain in the semiconductor industry is that it is difficult to determine the harm that might result from government support at any one point of the supply chain. With semiconductor firms interconnected through complex production networks, the impacts of any one measure may trickle down the value chain or instead affect companies upstream that provide crucial parts and components.

<sup>233</sup> The graph refers to below-market equity returns calculated using the parameter values corresponding to the middle estimate. Government-invested firms in the sample include (in alphabetical order): Hua Hong, JCET, Renesas, SMIC, STMicroelectronics, Tsinghua Unigroup, and Vanguard Semiconductor. Private firms that have not had high-enough returns for all five years considered are Toshiba, UMC, and two OSAT companies (Amkor and ASE).

### *Potential distortions on the EU internal market*

Providing support through the financial system, alongside cross-border acquisitions in the semiconductor industry by Chinese firms, appears to have gathered pace following the creation of China's state-backed national semiconductor fund in 2014, a USD 23 billion fund with the purpose to invest in the country's semiconductor industry. This national fund has since been flanked by a series of sister funds at provincial and city levels, e.g. Beijing IC Industry Equity Investment Fund. One explicit aim of the National IC Fund is "to promote industry upgrades", including through "mergers and regroupings", in the context of broader efforts to "encourage domestic integrated circuit companies to strengthen international cooperation, integrate international resources, and open up international markets."

In this context, a specific transactions involving EU target companies, which may have distorted the Internal Market, was discussed in more detail under problem 1.

## 2. The aluminium sector

### *The industry*

The aluminium sector has seen major changes over the last 15 years, notably the rise of China as the leading producer by a wide margin in most segments of the value chain. This unprecedented increase in output has fuelled concerns about excess capacity in the sector that is depressing global aluminium prices and threatening the viability of producers worldwide.

According to the OECD report, the 17 largest firms operating along the aluminium value chain are located in China, India, Russia, Bahrein, US, Australia and Norway. Together they make up more than half of global smelting capacity.

### *Subsidies*

The OECD estimates that the total government support for all 17 firms in the sample amounted up to USD 70 billion in the period 2013-2017, depending on how financial support (i.e. concessional loans) is estimated. Although all 17 firms received some form of support, it is highly concentrated. The top 5 recipients receive 85% of all support, most of it at the smelting stage of the value chain. While government support is common all along the value chain, it is especially large in China and the Gulf countries, even under the conservative assumptions used in the OECD report.

There are also important differences in the nature and scale of support received. Chinese firms obtained all of their support from Chinese authorities, notably financial subsidies, which overwhelmingly benefitted Chinese producers. Together with energy and input subsidies, these measures accounted for the vast majority of all support in China. By contrast, most other firms in the study tend to be multinationals that obtained support in the different places in which they operate (e.g. Australia, Brazil, Canada, and countries of the Gulf Cooperation Council), predominantly in the form of nonfinancial support (e.g. energy subsidies) and in lesser amounts. For all firms, support for R&D and labour was relatively minor.

### *Impact of subsidies*

The OECD notes that looking at the value chain reveals that subsidies upstream confer significant support to downstream activities. Direct support at the smelting stage is important, but trade measures also matter. China's export taxes on primary aluminium, as well as its incomplete VAT rebates on exports of certain aluminium products, have served to discourage exports of primary aluminium and encourage production (and export) of semiproducts and fabricated articles of

aluminium. Access to cheap inputs has enabled Chinese producers of semis to expand production and compete in global markets at lower cost.

While governments participate in the aluminium value chain via SOEs, state influence is at least as important as ownership, including because SOEs are both recipients and providers of support. This seems, according to the OECD, especially the case in China, where SOEs provide SOEs and private producers alike with below-market-cost inputs and loans.

Overall, the OECD concludes that non-market forces, and government support in particular, appear to explain some of the increases in capacity in the aluminium sector in recent years. Excess capacity thus appears to be a genuine concern in aluminium, and one with implications for global competition and the design of trade rules.

#### *Potential distortions on the EU internal market*

According to European Aluminium, one of the consequences of China's subsidised expansion of aluminium production combined with lower growth of China's internal demand has been the big increase of Chinese exports to the EU. These exports, allegedly in some cases at unjustifiably low prices, have more than doubled in recent years. Additionally, likely also backed by subsidies, Chinese companies have begun acquiring domestic EU production capacity and participating in other ways on the EU internal market. In this context, the example of Chinalco's general contract for the upgrade project of the electrolytic aluminium plant in Portovesme has been mentioned.

### 3. The steel sector

#### *The industry*

The steel industry is characterised by overcapacity which is exacerbated by subsidisation from third countries. Since steel serves as an input product for various other industries, distortions in this industry can have spillover effects into other industries as well.

#### *Subsidies*

Several OECD reports attempt to conceptualise and quantify subsidies in the steel sector. One of the OECD reports particularly focuses on China<sup>234</sup>, identifying 2923 distinct subsidy schemes, though not all of them include information on the amount of subsidies involved.<sup>235</sup> On aggregate, the OECD can identify subsidies awarded by Chinese public authorities amounting to more than 30 billion USD since 2008.<sup>236</sup>

#### *Impact of subsidies*

Subsidies exacerbate existing distortions which stem from overcapacity. In this regard, the OECD first highlights that public authorities can promote capacity expansion through subsidies, for example by directly providing support to investments in steelmaking facilities.<sup>237</sup> Second, the

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<sup>234</sup> Another report from the OECD, albeit less detailed and less up to date, focuses on subsidisation in several countries, namely Algeria, Brazil, Canada, India, Indonesia, Kazakhstan, Kenya, Korea, Russia, South Africa, Taiwan, Turkey, United States, and Vietnam. See Here: OECD, DSTI/SU/SC(2015)2/REV1, Public financial support to new investments in the global steel industry: work in progress.

<sup>235</sup> OECD, DSTI/SC(2020)11, Steel subsidies and government support measures: a progress report, p. 36., 2020.

<sup>236</sup> Ibid, p. 38.

<sup>237</sup> OECD, DSTI/SC(2017)11, Subsidies in the steel sector: A stocktaking note, p. 3, 2017.

OECD also emphasises that subsidies can provide a safety net for beneficiaries, thus effectively reducing their risk of having to exit the market.<sup>238</sup>

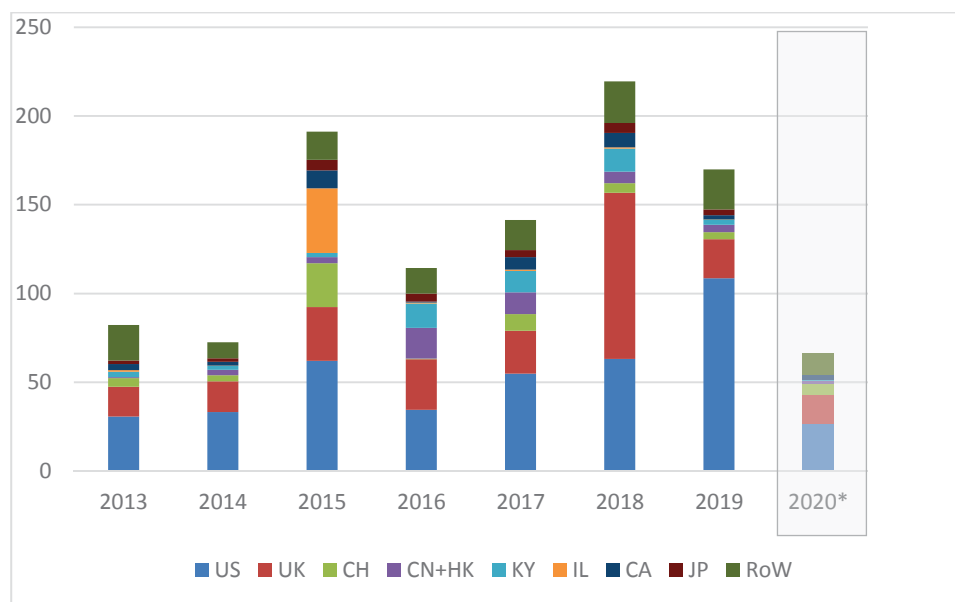
#### *Potential distortions on the EU internal market*

Though subsidised steel imports can and have been addressed in trade defence investigations<sup>239</sup>, subsidised steel companies increasingly try to circumvent those rules (which only apply to trade in goods) via greenfield investments and acquisitions.<sup>240</sup>

According to EUROFER, subsidised companies can offer better prices than competitors. Likewise, EUROFER notes that subsidised companies can undercut rival bidders in public procurement tenders. Lastly, according to EUROFER, subsidised companies can also sustain loss-making periods better than non-subsidised ones, which is particularly relevant for the steel, i.e., an industry facing low margins and high production costs.

### **5. Figures and tables supporting the analysis on the general context of subsidies in the field of acquisitions (Problem 1)**

*Figure 5. Value of foreign investments deals in Europe (in billion EUR) by country of origin, 30 per cent threshold*



Source: JRC elaboration on Bureau van Dijk data. Data extraction: 06/11/2020. The following countries are shown: United States (US), United Kingdom (UK), Switzerland (CH), China and Hong Kong (CN+HK), Cayman Islands (KY), Canada (CA), Israel (IL), Japan (JP), Russia (RU), Rest of the world (RoW) which excludes the countries previously listed. Notes: Data display the total observed value of transactions for announced and completed investment deals (above 30% of the capital of the target company) done by investors with an ultimate owner outside EU27. (\*)2020 includes observations between January and end of September.

<sup>238</sup> Ibid.

<sup>239</sup> E.g., see Implementing Regulation 2020/1408 imposing a definitive anti-dumping duty and definitively collecting the provisional duty imposed on imports of certain hot rolled stainless steel sheets and coils originating in Indonesia, the People’s Republic of China and Taiwan.

<sup>240</sup> OECD, DSTI/SC(2020)7/REV1, Cross-border investment by state enterprises, p. 37, 2020.

Table 14. Value of foreign acquisitions of equity holdings in European companies

Equity holding	2013	2014	2015	2016	2017	2018	2019	2020*
>10%	92.47	84.70	196.85	122.39	151.62	221.67	175.66	72.32
>25%	82.34	73.02	191.58	114.84	141.46	219.80	170.31	67.19
>30%	82.31	72.45	191.10	114.43	141.33	219.49	169.93	66.37
>40%	78.38	71.17	190.73	113.42	137.82	218.88	166.49	66.32
>50%	77.77	69.94	186.46	113.30	136.52	216.89	163.21	64.19

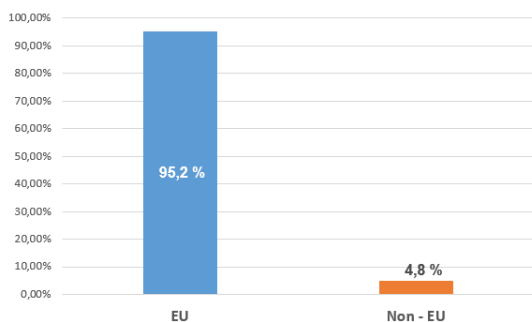
Source: JRC elaboration on Bureau van Dijk data. Data extraction: 06/11/2020. Data by year and threshold of the acquisition. Values in billion Euro.

Note: cells display the total available values of foreign acquisitions of equity holdings higher than the threshold indicated in the first column. European companies refers to EU27. (\*) 2020 includes values between January and September.

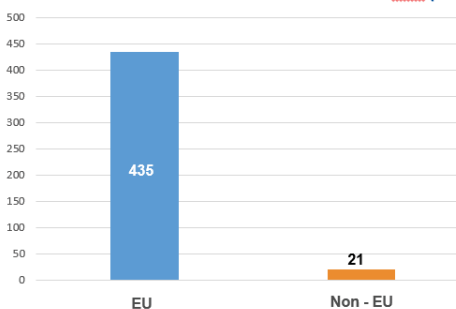
## 6. Figures and tables supporting the general context of subsidies under problem 2

### Chapter 2.3:

2015-2017 Awardees in contracts >250 Mil Euro (percentage)

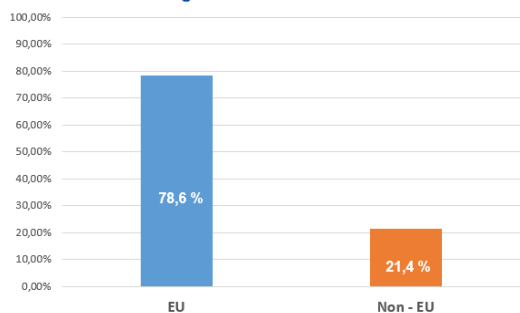


2015-2017 Awardees in contracts >250 Mil Eur (values)

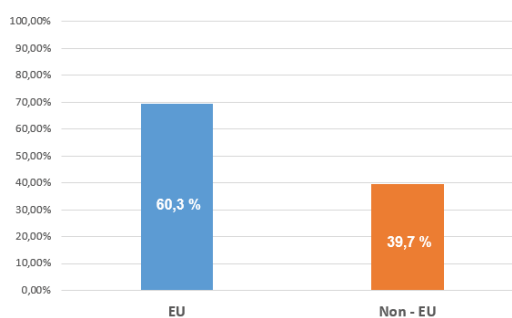


### Chapter 2.3:

2009-2015 Percentage in total direct cross-border awards



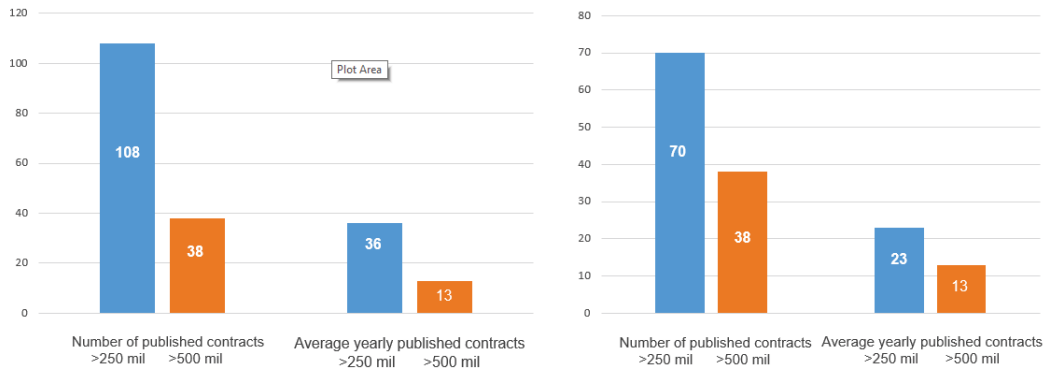
2009-2015 Percentage in total indirect cross-border awards



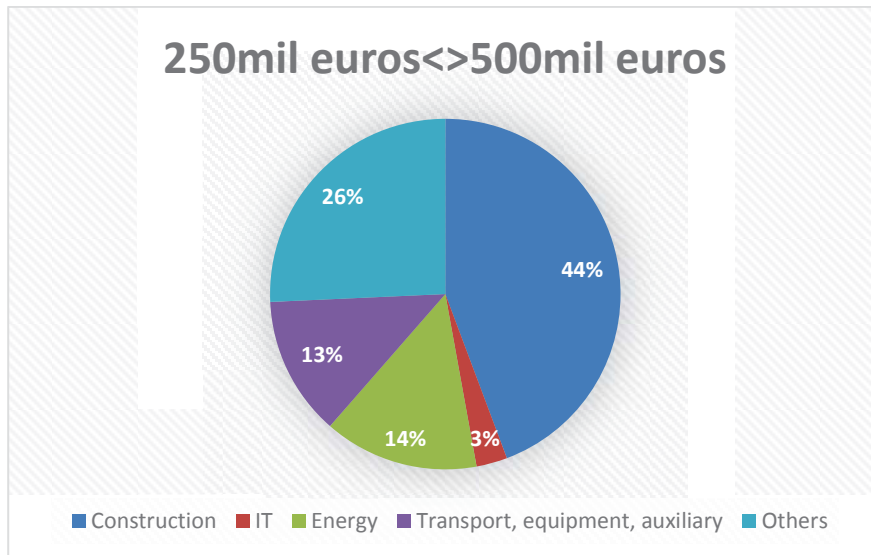


**Chapter 6.2.2:**

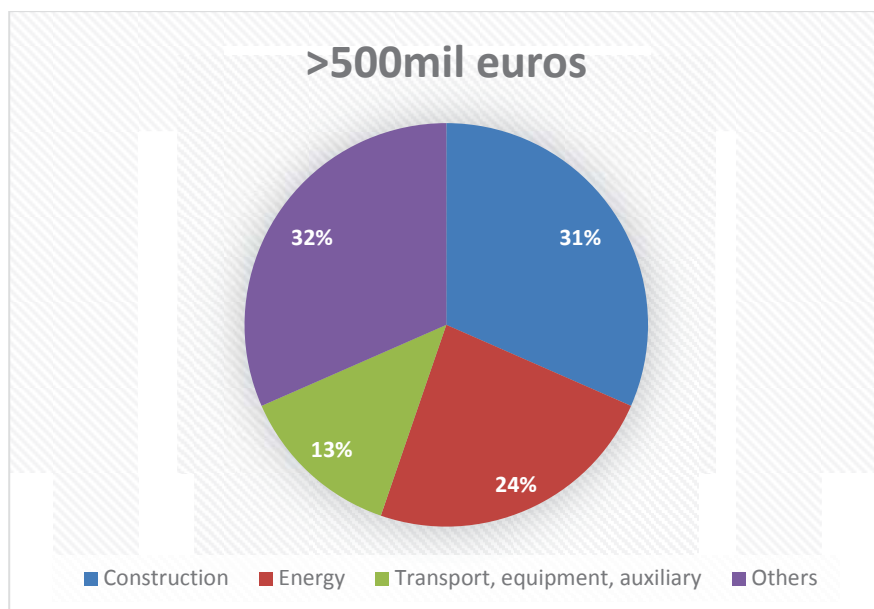
**2015-2017 >250 mil Euro vs >500 mil Euro contract award notices published**



**Distribution of high-value contracts among sectors (2015 to 2017)<sup>241</sup>:**



<sup>241</sup> These data are based on an estimation using CPV-codes, the classification of procurements. They are not the same as NACE.



## 7. Figures and tables supporting the general context of subsidies under problem 3

### 2. Countries and sectors concerned by countervailing subsidy cases started by the EU

Table 15. Number of countervailing subsidy cases per country concerned

Country	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Grand Total
Argentina			1						1			2
Egypt										2		2
India	4	2	3	2	2	2	1	2	2	2	1	23
Indonesia			1						1	1		3
Israel	1											1
Malaysia								2				2
Oman		1										1
P.R. China	2		3	3	1	5	2	3	1	4		24
Pakistan				1								1
Saudi Arabia		1										1
Turkey					1	1		1		1	2	6
USA	2	1			1						1	5
Vietnam				1								1
Canada				1		1						2
Grand Total	9	5	8	8	5	9	3	8	5	10	4	74

In addition to the foregoing, the sectors affected by the countervailing subsidy cases started by the Commission are presented in the table below.

Table 16. Number of countervailing subsidy cases by sector

Sectors	
Chemical and allied	6%
Biodiesel	9%
Glass fibre products	11%
Electronics	16%
Iron and Steel	37%
Wood and Paper	5%
Solar glass	8%
Other	9%
<b>Total</b>	<b>100%</b>

It should be noted that there may be sectors that are strongly distorted by subsidies, but about which the EU industry never lodged complaints, e.g. for fear of retaliation or because there has so far been a limited impact on trade in goods. Moreover, in order to capture the full extent of the distortions, several anti-dumping measures have been imposed by the Commission, often in parallel with countervailing subsidy cases.

## 8. Trade in Services

Subsidisation of trade in services has been a pressing issue for decades with numerous attempts at the international level to find a solution. In particular, the GATS provides a mandate to develop rules for subsidies in this area, but to date, no such rules have been developed. Trade in services is therefore more prone to distortions as there no countervailing measures available as there are for trade in goods.

The import of services into the EU through all 4 modes of supply (as defined in GATS)<sup>242</sup> has been growing over the past decade (see Figure 6). In 2017, around 2.1 billion EUR of services were imported into the EU27 compared to 1.7 billion EUR of imported goods<sup>243</sup>. Around 57% of these services were supplied through commercial presence of foreign-owned companies, 32% were provided by means of cross-border supply and the remaining services were supplied by consumption abroad (7%) and presence of natural persons (4%). In terms of sectors, business and trade-related services make up the largest part of these imports, followed by insurance and financial services, telecommunications and information services and transport.

It is argued that the current four modes of supply do not fully reflect the existing means of providing services and that a Mode 5 should be considered for services contents embodied in manufactured goods, which can include R&D, design, engineering, energy, etc. Antimiani and Cernat (2017) estimate that the global GDP gains from liberalizing mode 5 services at the multilateral level could reach up to 300 billion EUR.<sup>244</sup> The combination of these factors is likely to lead to a continued growth of trade in services in the mid and long-term.

<sup>242</sup> See for details on the methodology:

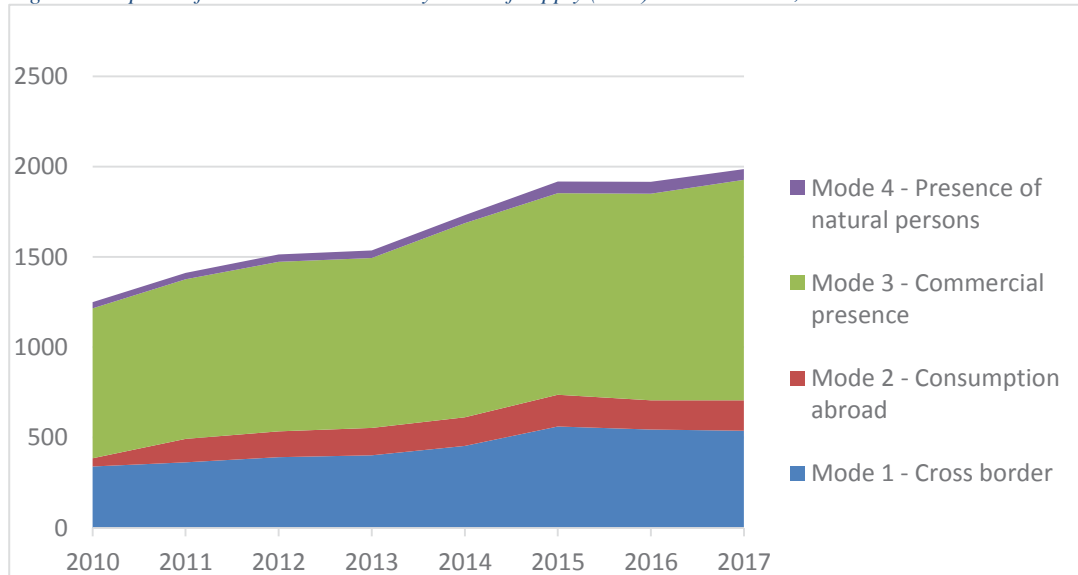
[https://trade.ec.europa.eu/doclib/docs/2016/december/tradoc\\_155119.pdf](https://trade.ec.europa.eu/doclib/docs/2016/december/tradoc_155119.pdf)

<sup>243</sup> Eurostat. Service statistics by modes of supply. Data extracted in March 2020.

[https://ec.europa.eu/eurostat/statistics-explained/index.php/Services\\_trade\\_statistics\\_by\\_modes\\_of\\_supply](https://ec.europa.eu/eurostat/statistics-explained/index.php/Services_trade_statistics_by_modes_of_supply)

<sup>244</sup> Antimiani, A., Cernat, L. Liberalising global trade in mode 5 services: How much is it worth? DG TRADE. July 2017. [https://trade.ec.europa.eu/doclib/docs/2017/july/tradoc\\_155844.pdf](https://trade.ec.europa.eu/doclib/docs/2017/july/tradoc_155844.pdf)

Figure 6. Imports of services into EU28\* by mode of supply (Bn €). Source: WTO, DG TRADE<sup>245</sup>



## 9. Illustration of the role of the role of subsidies in a third country industrial policy.

### China's industrial policy

China's use of state subsidies is the most researched among the largest trading partners of the EU. A recent report<sup>246</sup> of the German Monopolies Commission notes the extensive direct or indirect subsidies selectively granted to individual Chinese companies or industries by the Chinese State for industrial policy purposes. The report notes that these state support measures in China lead to cost advantages for the benefitting Chinese companies or to additional financial resources. The report adds that while distortions may occur in the Chinese market first, they may also impact the EU internal market. The report further notes that Chinese companies which have high levels of financial resources might have the incentive to build up market power on the EU internal market by gaining market share with low prices that are subsidised by the Chinese State or by surplus profits in their home market, for example due to an unregulated dominant position.

Mercator's 2016 report 'Made in China 2025'<sup>247</sup> examined China's industrial policy and more specifically, China's policy in the high technology sector. Chinese industrial policy includes large government funds and subsidies and the ability to channel them into priority areas. The Advanced Manufacturing Fund for example amounted to 20 billion CNY (2.7 billion EUR) in 2016.

In addition, the government has also provided substantial sums for the development of smart manufacturing technologies. Among them are the China National Integrated Circuit Industry Investment Fund (National IC Fund) and the Emerging Industries Investment Fund with capital of 139 billion CNY (19 billion EUR) and 40 billion CNY (5.4 billion EUR) respectively. In the specific example of robots, many local governments support the purchase of robots with subsidies of between 15 and 30 per cent of the sale price. In some cases, subsidies for producers and users add up to 100 per cent. The state's subsidy glut

<sup>245</sup> includes the UK while data for the whole period is not available for EU27

<sup>246</sup> "Chinese state capitalism: A challenge for the European market economy", German Monopolies Commission, July 2019

<sup>247</sup> "Made in China 2025: The making of a high-tech superpower and consequences for industrial countries"; Jost Wübbecke, Mirjam Meissner, Max J. Zenglein, Jaqueline Ives, Björn Conrad; Mercator Institute for Chinese studies; December 2016

has led to a tremendous increase in the number of Chinese robot companies. More than 800 Chinese robot companies are registered in China, approximately half of them in 2015. The majority of these companies have not yet reached the stage of mass production. Many of them just serve as vehicles to receive government subsidies and do not make any profit.

Chinese sovereign investment funds and governmental investment management companies play an increasing role in high-tech FDI. While these funds and their management often present themselves as private undertakings, the State is active through a network of ownership and funding structures. The State Council and local governments primarily use these funds to channel subsidies to Chinese undertakings in a more efficient manner, pursuing overarching national policy goals at the same time. In particular, these funds are becoming increasingly active with regard to investment in overseas markets. Examples of such funds and investment vehicles are the National IC Fund (first and second editions), the China Investment Corporation and its subordinate funds. One example of an investment by a Chinese state-owned investment corporation is the acquisition of the radio frequency power business of Dutch semiconductor enterprise NXP by JAC Capital Ltd., of which an investment vehicle of the State Council owns 51 per cent. The China Investment Corporation also contributed USD 550 million to the Asia-Germany Industrial Promotion Capital (AGIC), a private Chinese-owned investment fund based in Germany targeting investment in European Industry companies.

## 10. Further analysis on the lack of transparency as a driver to the problem

### WTO rules and sector specific efforts

According to the SCM Agreement all WTO members are obliged to notify any subsidy granted or maintained in their territory to the WTO secretariat, which publishes this information on the WTO website. However, the level of compliance by WTO members has deteriorated significantly in recent years.<sup>248</sup> As regards service subsidies, no similar notification obligation is set out in the GATS, which includes however in its Article XV a provision on the exchange of information on subsidies related to trade in services for the purpose of further negotiations. Little information has however been exchanged recently.<sup>249</sup>

Efforts are made in various fora to gather information on subsidies or government support in specific sectors, such as in the Global Forum on Steel Excess Capacity (GFSEC), an international platform to discuss and find collective solutions to the challenge of excess capacity and enhance market functioning in the steel sector.<sup>250</sup> The OECD has recently published reports on distortions in international markets on both the semiconductor and the aluminium value chain, also pointing to distortions through subsidies.<sup>251</sup> It also undertakes work on subsidies and other support measures in other sectors.<sup>252</sup>

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<sup>248</sup> Further details on the notification obligation are set out above in section 2.5.3.

<sup>249</sup> P. SAUVÉ, M. SOPRANA, "Disciplining Service Sector Subsidies: Where do we stand, and where can we (realistically) go?", *Journal of International Economic Law*, Volume 21, Issue 3, September 2018, p.599 [610].

<sup>250</sup> See <http://steelforum.org/>

<sup>251</sup> OECD, *Measuring distortions in international markets: The semiconductor value chain*, OECD trade policy paper, 2019, [https://www.oecd-ilibrary.org/trade/measuring-distortions-in-international-markets\\_8fe4491d-en](https://www.oecd-ilibrary.org/trade/measuring-distortions-in-international-markets_8fe4491d-en); OECD *Measuring distortions in international markets: The aluminium value chain*, OECD trade policy paper, 2019, [https://read.oecd-ilibrary.org/trade/measuring-distortions-in-international-markets-the-aluminium-value-chain\\_c82911ab-en#page1](https://read.oecd-ilibrary.org/trade/measuring-distortions-in-international-markets-the-aluminium-value-chain_c82911ab-en#page1) .

<sup>252</sup> E.g. shipbuilding: <http://www.oecd.org/sti/ind/shipbuilding.htm>; Gourdon, K. (2019), "An analysis of market-distorting factors in shipbuilding: The role of government interventions", OECD Science, Technology and Industry Policy Papers, No. 67, OECD Publishing, Paris.

### Lack of suitable data

While sector specific efforts as regards transparency on subsidies are made in different fora, there is lack of information in other sectors, such as aviation.<sup>253</sup> Generally, according to a WTO report on subsidies issued in 2006,<sup>254</sup> data on the use of subsidies are scarce and difficult to compare across countries and sectors because of methodological differences and data gaps.<sup>255</sup> There are no more recent studies on subsidies covering all sectors. Data from various sources is available, but not necessarily on subsidies.<sup>256</sup>

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<sup>253</sup> See Commission staff working document, impact assessment, accompanying the proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on safeguarding competition in air transport, repealing Regulation (EC) N° 868/200, WD(2017) 182 final, pp. 42, 43.

<sup>254</sup> World Trade Report 2006, Exploring the Links Between Subsidies, Trade and the WTO; this report analysed amongst others how much countries subsidise according to different data sources.

<sup>255</sup> See pp. 45, 114 of the report.

<sup>256</sup> See e.g. World bank development indicators, <https://databank.worldbank.org/reports.aspx?source=world-development-indicators>, which include information on “subsidies and other transfers”, which covers however also grants to international organisations, social security, social assistance benefits as well as employer social benefits; see also the OECD corona policy response tracker. <https://www.oecd.org/coronavirus/en/> Information is sorted by country, and there is a section “fiscal measures” (not “subsidies” strictu sensu).



## Annex 5. Supporting data and analysis for the assessment of the impacts

### 1. Problem 1 (acquisitions) – Supporting analysis on the impact on the public authorities<sup>257</sup>

The JRC data shown in Table 17 provides the number of foreign acquisitions for different thresholds of global turnover of the acquired EU undertaking. The EU merger data which is illustrated in Figure 6 offers an approximation of the proposed EU turnover threshold since notification under the EUMR primarily relies on an EU-wide turnover of EUR 250 million (of at least two merging parties to a case). Figure 7 relies on EU-wide turnover of at least EUR 500 million. The below figures give a more detailed overview of the estimated notifications received under Problem 1 (in particular Figure 7) as discussed in the section on impacts of a new instrument for Problem 1.

Table 17. Total and foreign acquisitions by global turnover threshold

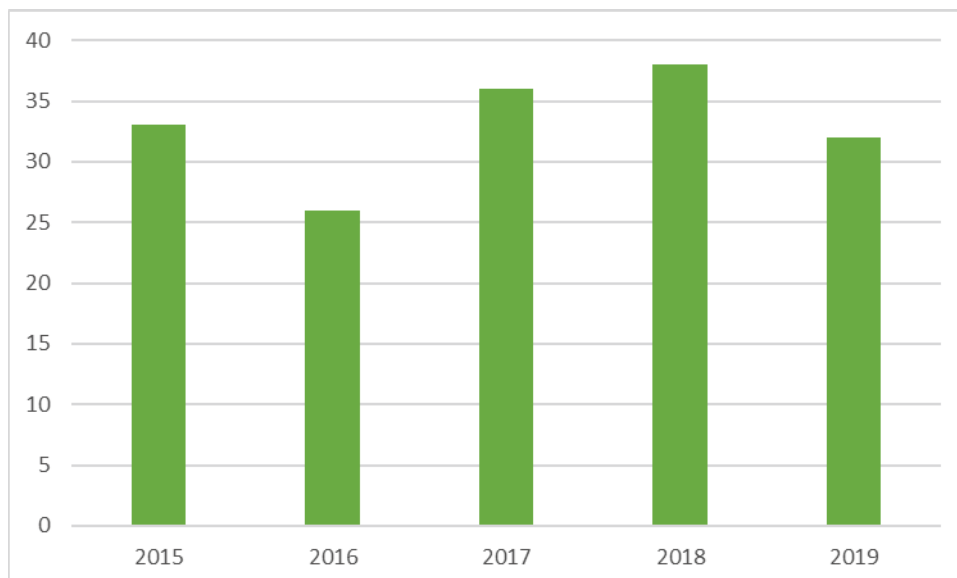
	Target turnover	Total all cases	Total non-EU	US	UK	CN+HK	JP	CH	RU
2019	No min/ all cases	1 210	567	153	132	31	23	38	5
	At least 250m	<b>107</b>	<b>44</b>	<b>11</b>	<b>13</b>	<b>6</b>	<b>3</b>	<b>4</b>	<b>1</b>
	At least 500m	56	21	6	8	2	0	0	0
	At least 1bn	29	11	5	5	0	0	0	0
2018	No min/ all cases	1997	981	237	219	67	56	81	14
	At least 250m	136	86	13	24	8	8	3	2
	At least 500m	87	62	7	16	7	4	2	2
	At least 1bn	55	40	3	12	4	4	1	2
2017	No min/ all cases	2270	1112	241	283	99	60	76	15
	At least 250m	117	81	15	12	13	8	1	3
	At least 500m	59	40	5	4	4	8	0	1
	At least 1bn	32	19	2	0	2	4	0	1

<sup>257</sup> Please note that, because the JRC data contains turnover information for the target only for part of the identified acquisitions (49.5% in 2017, 44.1% in 2018 and 33.1% in 2019), the numbers contained in the JRC dataset – summarised in Table 17 – need to be multiplied (respectively by 2, 2.27 and 3) to reach a number likely to reflect reality.

Figure 7. Non-EU acquisitions of EU undertakings based on three different scenarios



Figure 8: Scenario 4, number of EU undertakings acquired by non-EU undertakings (above 500 million EUR EU turnover for EU undertakings)



## 2. Problem 3 (other market distortions) – Figures concerning notifications of State aid

The Commission has analysed the distribution of State aid awards that Member States have communicated for transparency reasons<sup>258</sup>.

More than 95% of the State aid measures fall under the General Block Exemption Regulation and are therefore exempted from notification to the Commission.<sup>259</sup> Awards below EUR 500,000 are

<sup>258</sup> The dataset described hereafter and presented in the table concerns information on all awards reported to the Commission from the entry into force of the Transparency obligations (1 July 2016) to end of May 2020, when the last dataset was received from Member States.

in principle exempted from transparency obligations<sup>260</sup>, but some Member States report them nonetheless to the Commission as this is easier than to limit the reporting to larger amounts and miss possible accumulation of aid amounts.

In spite of the voluntary nature of the reporting of aid awards below EUR 500,000, almost half of the reported aid awards are below EUR 500,000. In approx. 75% of the cases the State aid awarded remained below EUR 1 million, and 95% below EUR 5 million. It should be noted, though, that SMEs receive a big part of EU State aid, which can be one of the explanations of the low average amount per award. Moreover, Member States may also often grant amounts below the GBER limits in order to avoid notifications of State aid to the Commission.

*Table 18. Ranges of reported State aid awards*

<b>State aid amount range</b>	<b>Percentage of aid awards</b>
< €500,000	45.75%
€500,000 - €1,000,000	28.44%
€1,000,000 - €2,500,000	14.59%
€2,500,000 - €5,000,000	5.75%
€5,000,000 - €10,000,000	2.87%
€10,000,000 - €25,000,000	1.94%
€25,000,000 - €50,000,000	0.48%
€50,000,000 - €100,000,000	0.09%
> €100,000,000	0.10%
<b>Total</b>	<b>100%</b>

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<sup>259</sup> Commission Staff Working Document: Fitness Check of the 2012 State aid modernisation package, railways guidelines and short-term export credit insurance, SWD(2020) 257 final.

<sup>260</sup> As such, it is not possible to make a meaningful comparison with the EUR 200 000 threshold initially evoked in the White Paper.

## Annex 6. Complete summary of the consultation activities

### 1. Public consultation on the White Paper (17 June – 23 September 2020)

#### General

The Commission received 150 submissions to the public consultation:

- 17 from public authorities of Member State;
- 24 submissions from third country stakeholders and governments;
- around 100 submissions from business and industry associations and individual companies;
- the remainder from law firms, academic institutions, trade unions, NGOs, other public authorities and individual citizens.

Submission by type of contributor	
Academic/research institution	2
Business association	52
Company/business organisation	52
EU citizen	5
Non-EU citizen	1
Non-governmental organisation (NGO)	3
Other	12
Public authority	19
Trade union	4
<b>Grand Total</b>	<b>150</b>

Submissions by country of origin			
Austria	6	Malta	2
Belgium	35	Mozambique	1
Canada	2	Netherlands	5
China	4	Norway	1
Czechia	2	Poland	6
Denmark	4	Portugal	2
Finland	4	Romania	1
France	13	Serbia	2
Germany	19	Singapore	2
Hungary	1	South Korea	1
Ireland	1	Spain	7
Italy	8	Sweden	5
Latvia	1	United Arab Emirates	1
Lithuania	1	United Kingdom	7
Luxembourg	3	United States	3
<b>Grand Total</b>	<b>150</b>		

#### *Member State contributions*

Almost all Member States are generally in favour of legislative action to tackle the distortive impact of foreign subsidies, with some nuances in the degree of support and alignment, though.

Individual Member States ask for more evidence or support the White Paper as a basis for further discussions, but are not yet convinced about the need for a new instrument.

A large number of Member States agree with the proposed material scope of the legislative action. Individual Member States consider that the subsidy definition may not cover certain cases of fiscal support or that lower labour law or environmental protection standards in third countries should also be considered equivalent to subsidies.

A number of Member States point to difficulties with detecting foreign subsidies, in particular when it comes to state-owned enterprises.

Member States generally agree with the proposed redressive measures, which they often see as a non-exhaustive list. However, they make various comments, among other on the ineffectiveness of redressive payments / the reimbursement of the subsidy, structural remedies being seen as too far-reaching or having to be used with caution, asking for an indication if and how redressive measures can be appealed.

Several Member States refer to potential negative impacts on Foreign Direct Investment, administrative burden and stress that the new instrument should not be stricter than EU competition/State aid law. The majority of Member States highlight the importance of coherence with other instruments, in particular with the EU Merger Regulation, the Public Procurement Directives, the planned International Procurement Instrument, the Foreign Direct Investment screening Regulation and Trade Defence Instruments.

Certain Member States advocate that foreign subsidies should be taken into account in the context of EU funding and are overall in favour of legislative action. The Member States focused their reply on shared management and submitted few individual and diverse observations.

#### *Other EU stakeholders' contributions*

Almost all contributors welcome the initiative and consider that there is a real need for the new tool. Many point to sector specific issues or indicate industry sectors which they see as heavily subsidised by foreign governments. A large number of respondents also highlight that transparency is one of the big issues that needs to be tackled in a new instrument.

Several respondents call for the intervention to be targeted and proportionate in order not to stifle foreign investment. Various submissions highlight the necessity to coordinate the new instrument with the existing ones (Public Procurement Directive, Merger Regulation, IPI, TDI, FDI screening). A number of respondents also consider that a thorough impact assessment is necessary to prepare a legislative proposal.

As regards the overall scope of a new instrument, the majority of the respondents generally agree, but provide various comments and precisions. Various business contributors emphasise that key concepts (foreign subsidies, distortion, redressive measures, EU interest) need to be more clearly defined and that the assessment criteria need to be specified. Some suggest that the Commission should publish guidelines.

Many contributors support a broad definition of subsidies and applying the tool to businesses active (not just established) in the EU. They often mention among others protected domestic markets (but also domestic subsidy assessment frameworks), negative presumptions for State-owned Enterprises and lower standards than in the EU as an element to consider.

Several contributors suggest an exclusive or at least very prominent coordination/supervisory role for the Commission, to ensure consistent practice. Many contributors also suggest the introduction of a complaint procedure.

A few associations call for a sector-specific approach, e.g. based on the revision of existing sector-specific Regulations.

### *Non-EU contributions*

As a general rule, while acknowledging the possibility that foreign subsidies might distort the internal EU market, the contributions submitted by third country-based respondents are generally critical of any form of regulation on top of the existing rules.

Most contributions from third countries advocate no new regulation or as little as possible. In that regard, the contributions vary in their openness to a new instrument or whether a particular country should be exempted from its application. Subsequently, only some contributions deal with the substance of the White Paper.

As far as these remaining submissions are concerned, several respondents indicate that the proposed instrument creates overlaps and could be built into existing rules. Indeed, some contributors state that the instrument is not necessary. Others suggest integrating Modules 2 into merger control, Module 3 in the Public Procurement Directives and EU Funding in the EU Financial Regulation or alternatively incorporating Modules 2 and 3 under Module 1.

Several respondents also question whether the new instrument would not violate international obligations by imposing a different standard on foreign companies compared to EU companies, and criticise additional administrative burden.

## **Module 1**

### *Member State contributions*

Member States generally agree on the proposed 2-step approach for Module 1, but some raise questions as to the potential delays that it may cause.

Individual Member States consider that Module 1 is sufficient to address all situations including acquisitions and public procurement.

Some Member States raise the difficulty of gathering information.

As to the substantive criteria, individual Member States point out that the size of the undertaking is not always an adequate criterion or that categories of subsidies likely to be distortive need to be detailed further.

Individual Member States favour adding a specific redressive measure for public procurement, i.e. excluding a subsidised company from Public Procurement procedures and doubt that reimbursement of the subsidy is an effective remedy. Another one, on the contrary, views redressive payments as the best remedy.

In relation to enforcement, some Member States argue that sharing responsibilities between Member States and the Commission should e.g. be based on thresholds. Others ask for the sole enforcement of this module by the Commission.

The EU interest test is supported by several Member States. Certain criteria are brought forward or are particularly stressed in this context, such as:

- (i) Effects on innovation, sustainability, competitiveness of EU economy;
- (ii) quality, production in EU and jobs in EU;
- (iii) public order and public security and resilience, climate impact, environmental impact.

Other Member States state that the test should be based on clear and objective criteria and better defined or that the definition of strategic Union interest used in the context of IPCEI projects should be considered.

Several Member States agree with the de minimis threshold aligned with State aid rules as proposed in the White Paper. Individual Member States argue that the de minimis threshold in Module 1 should be aligned with the one under Module 3 or, that the proposed €200 000 is



relatively low and should be set higher because (i) it may discourage Foreign Direct Investment; (ii) enforcement should focus on the most distortive subsidies or (iii) in view of the administrative burden. Individual Member States ask to determine the threshold only after an in-depth market analysis and not to set it so high as to miss problematic cases.

#### *Other EU stakeholders' contributions*

A large majority of contributors consider that Module 1 adequately addresses distortions caused by foreign subsidies. A large proportion considers that Module 1 should apply also to companies “active in the EU” and that it should allow for complaints.

In terms of assessment, some contributors indicate that more detail/guidance is needed, others advise against using an exhaustive list of substantive criteria and yet others suggest adding a few criteria to cover several market issues, subsidy-specific issues and the effects on the market. Certain contributors indicate that assessment under Module 1 should be aligned with the assessment under EU State aid rules. Some respondents highlight that the burden of proof should be reversed when it comes to the distortion caused by subsidies in sectors with overcapacity or when it comes to the existence of a subsidy (in particular for State-owned enterprises).

The respondents generally view favorably the proposed redressive measures, but indicate that they should be clarified, among others in relation to their duration and in terms of respect of fundamental rights of those concerned. Several respondents call for strong redressive measures and sanctions for non-compliance. In contrast, a few others voiced the concerns that redressive payments to foreign or EU states may lead to political tension and/or that it may be difficult to establish if the subsidy was effectively paid back in a third country.

Certain respondents suggest to allow voluntary notification for legal certainty or propose a State aid Compliance certification that would be required for non-EU State-owned Enterprises before allowing them to be active and operate in the EU.

The majority of contributors consider that the Commission should be exclusively responsible for the enforcement of Module 1. In case of shared enforcement responsibilities, they advocate for strong leadership by the Commission.

The views on the necessity of a de minimis threshold are mixed. Some respondents agree with a threshold in line with the one under State aid rules, some consider that it should be higher or there should be no threshold at all, others yet believe that the threshold should be lower or sector-based and set following an impact assessment.

Views on whether Module 1 should also cover subsidised acquisitions which are outside the scope of Module 2 vary.

The views on whether there should be an EU interest are varied. Some respondents consider an EU interest test to be relevant, but are in favour of applying it narrowly. Some point in this context to the balancing test under EU State aid law or the interest test that is undertaken as part of Trade Defence Instruments. They also mention the need for clarity as to when and how it is applied, and stress that its application should not result in absence of redressive measures. Other contributors either do not see the need for an EU interest test or oppose it, because of the political dimension and/or discretion it would bring into the assessment.

#### *Non-EU contributions*

Most contributions from third countries advocate no new regulation or as little as possible.

A number of respondents raise the issue that the subsidy definition is too broad and vague, the concept of distortion unclear and that it leaves too much discretion to the authorities. In this context, some point out that there should not be any presumption about State-owned Enterprises and caution against a reversed burden of proof. Moreover, they plead for assessment at the level of undertaking, not group and are in favour of (higher) de minimis thresholds. Individual

respondents argue that in Module 3, the bidder might not know whether the suppliers/contractors have been subsidised.

As to the procedure, some contributors propose that the investigation should only be initiated upon a written complaint with sufficient evidence.

Several contributors are critical of redressive payments to the Commission or Member States, as there would be no legal basis, or stress that redressive measures should not discriminate against non-EU companies.

Several contributors are in favour of an EU interest test to balance the distortion with positive impacts some investments may have. Criteria for such a test should be clear and as measurable as possible. It is proposed that a potential benchmark could be the compatibility assessment under EU state aid rules.

## **Module 2:**

### *Member State contributions*

#### General need and scope of module 2

Most Member States support Module 2. Others are more cautious and support it, but indicate that duration of the procedure and administrative burden should be considered.

Some Member States oppose the introduction of Module 2, for fear of creating overlaps with Merger control and Foreign Direct Investment screening, in view of the administrative burden, or because they favour dealing with acquisitions under Module 1.

Individual Member States propose that the definition of acquisition under Module 2 should be the same as under the Merger Regulation or raise questions in relation to potentially subsidised acquisitions, as they may not always distort the internal market and involve self-assessment by the undertakings. Some Member States raise the question of appeal and/or review of negative decisions under Module 2.

#### Competent authority

Several Member States oppose to the Commission being the sole competent authority and want shared enforcement powers also for Module 2.

#### Notification requirement

As concerns the notification requirement, Member States propose a variety of criteria. Several Member States consider that only subsidised acquisitions should be notified and some of them plead for only having quantitative criteria for notification.

Individual Member States question whether turnover thresholds and notification obligation contribute to the effectiveness and proportionality of the proposed instrument or state that the proposed turnover thresholds for Module 2 are quite high. While this limits the administrative burden on the Commission, it means that very few investments in, and acquisitions of, for example, innovative start-ups and scale-ups would fall within the scope of this module. It could also be argued that the notification obligation places too high an administrative burden on both market operators and supervisory authorities. In their view, the Commission could launch investigations into specific investments and acquisitions on its own initiative.

Individual Member States generally support the proposed thresholds but ask for special attention for innovative and specialised companies that are still in the scale-up phase or that are smaller (SMEs) and hence more prone to being taken over, or they state that EU target thresholds should not be too high if that would mean that we miss certain problematic cases.

Other Member States consider that all acquisitions should be notified. Among those, individual Member States propose that the follow-up procedure should only apply where foreign subsidies

exceed a certain threshold and the EU target is active in sectors that do not fall under Foreign Direct Investment Screening Regulation.

#### Other points

Some Member States request further discussion on the subject, potentially underpinned by studies.

Several Member States specifically advocate the use of EU interest also under Module 2.

#### *Other EU stakeholders' contributions*

A large majority of contributors is supportive of Module 2 in terms of scope and procedural set-up. A minority of respondents, on the other hand, cautions that Module 2 should not be applied too broadly, e.g. in relation to the concept of de facto facilitation or certain types of investments (e.g. portfolio or passive financial investments). Some respondents indicate that there are some ambiguities in terms of procedure, assessment criteria and definitions. Several contributions call for alignment of Module 2 with the EU Merger Regulation, e.g. in relation to legal deadlines.

In terms of notification criteria, most respondents consider that only subsidised acquisitions should be notified under Module 2. Most respondents also agree with quantitative thresholds, but without consensus on the right level of the threshold. Some respondents propose to introduce a qualitative threshold in parallel to examine smaller transactions of a strategic nature. Others propose to use the impact assessment to calibrate Module 2.

The majority of contributors agree with exclusive Commission power for this Module.

#### *Non-EU contributions*

Most contributions from third countries advocate no new regulation or as little as possible.

Individual contributors indicate that if Module 2 is established, only State-owned Enterprises or previously distortive companies should be required to notify.

Several contributors are critical of redressive payments to the Commission or Member States, as there would be no legal basis, or stress that redressive measures should not discriminate against non-EU companies.

### **Module 3**

#### *Member State contributions*

The majority of Member States who replied agree with legal action in the area of public procurement but not necessarily with the proposed framework of module 3. These Member States consider that the White Paper rightly identifies the problem (risks associated with the participation in public procurement procedures by subsidised bidders) and agree broadly with the gap analysis. Several Member States are opposed or sceptical about the need for a dedicated legal instrument to tackle the distortive effects of foreign subsidies in public procurement. Some of these Member States disagree with the premise in the White Paper that foreign subsidies have a negative effect on public procurement. Others consider that the issue could be addressed, or at least partially addressed, by recurring to the existing rules on abnormally low tenders in the PP Directives: either by issuing guidance on existing rules or by a modification of these rules and integrating some of the features of Module 3 (e.g. notification obligation, review procedure, adding an exclusion ground).

#### Sharing of enforcement powers

A majority of Member States expressed their concern about the proposals in the WP on the sharing of responsibilities between contracting authorities and supervisory authorities with regard to the assessment of distortions caused by foreign subsidies. Member States broadly agree that contracting authorities should not be responsible for assessing whether a foreign subsidy distorts

the public procurement procedure, and that this task should instead be incumbent on the national supervisory authority or the Commission. A number of reasons are presented for this view: lack of capacity (contracting authorities lack the necessary expertise, information and manpower, and to assess distortions would unduly increase the already heavy administrative burden), lack of impartiality (contracting authorities may be susceptible to award tenders to subsidised bidders offering low prices) and lack of efficiency (if contracting authorities are ill-equipped for the assessment of foreign subsidies, this will negatively impact the procedure and accessibility of procurement markets).

In addition, some Member States express the view that the Commission should have exclusive powers for assessing whether a foreign subsidy is distortive, in the interest of consistency and legal certainty.

#### Other points

Furthermore, a number of issues are raised in relation to Module 3, by both Member States in favour and against the proposal:

- (i) Some Member States are concerned that a separate Module 3 addressing distortions of a single public procurement procedure risks being administratively heavy;
- (ii) some Member States indicate that the relationship between Module 3, the Public Procurement Directives and the International Procurement Instrument should be clarified;
- (iii) some Member States ask whether the proposal cannot be implemented by adapting the Public Procurement Directives, in particular the rules on abnormally low tenders;
- (iv) Member States welcome the strict deadlines for public procurement procedures foreseen in the White Paper but raise doubts whether they are realistic in practice;
- (v) exact criteria and guidance for an in-depth investigation should be worked out in detail;
- (vi) need for uniform methodology to decrease the risk of diverging decisions if a subsidised entity participates in Public Procurement in several Member States;
- (vii) some Member States are critical as to the termination of closed contracts;
- (viii) issues with reliability of information received or lack of information on subsidies.

Individual Member States state that the EU interest test should also apply in Module 3.

#### *Other EU stakeholders' contributions*

Not all of the other contributors address public procurement specifically in their reply. Of those that do, a large part generally agree with the gap analysis in the White Paper and support legal action to tackle distortions caused by foreign subsidies in public procurement. A vast majority of business respondents stress that a new instrument must not lead to additional administrative burden on bidders and must not cause delays to public procurement procedures. The majority of respondents also argues that competent supervisory authority should be responsible for the whole investigation and contracting authorities should only enforce redressive measures in the respective tender procedure.

A number of respondents are also sceptical about the need for a dedicated instrument in the field of public procurement, arguing that current rules (Public Procurement Directives, particularly on abnormally low bids) could be used or adapted to tackle the issue of foreign subsidies.

Regarding practicalities, some contributors propose that an ex-ante notification obligation should only apply to main/first-rank suppliers of tenderers. As regards competence sharing, there is a clear call by businesses for the Commission to have a strong coordination/guiding role in order to guarantee a uniform assessment methodology. Most contributors agree that contracting authorities are unable to make the assessment of a distortion, for the same reasons as those given by Member States. Several contributors argue that, consequently, this assessment should be done

by the national supervisory authority, possibly in cooperation with the Commission. Some also suggest the Commission should be able to overrule Member States supervisory authorities and to take on cases where it deems the participation of subsidised bidders to be particularly problematic. Furthermore, as regards procedure, some respondents argue in favour of a complaints-based system: instead of an ex-ante-notification obligation foreseen in the White Paper, investigations into distortive foreign subsidies would only be launched in the standstill period prior to the final award decision if complainants inform the supervisory authority about potential distortions caused by foreign subsidies.

Some contributors suggest introducing foreign subsidies as an (additional) ground for appeal against the winning bid in the existing interval before the contract is actually signed. This would thus cause no further delay, and build on existing practice and procedures.

#### *Non-EU contributions*

Non-EU contributors in general do not specifically address public procurement.

### **Interplay between modules**

#### *Member State contributions*

Member States have diverse views as regards the interplay between the proposed modules.

Several Member States consider that each module should operate on a stand-alone basis, rather than as one single instrument for all three modules. Some others argue only for Module 1 to operate on a stand-alone basis. Others yet see Module 1 as back up for subsidised acquisitions, either under thresholds if there is an effect on the internal market, or in strictly defined cases only. Some Member States indicate that it would be desirable to coordinate the use of Modules 1 and 3.

Several Member States support grouping all three Modules together in one instrument.

Individual Member States suggest addressing foreign subsidies in public procurement under the Public Procurement Directives or do not agree with Modules 2 and 3.

Individual Member States point out that the relationship between Modules and with existing instruments should be better defined.

#### *Other EU stakeholders' contributions*

The views about the interplay between different Modules are very diverse.

Some contributors consider that Modules 1, 2 and 3 should operate together, but that it is important to clarify the complementarity of Module 1 with the other two Modules. Some consider that only Module 1 should apply. Some other respondents support all three Modules, but to be applied separately.

Certain contributors agree that Module 1 is used for subsidised acquisitions not covered by Module 2, while others specifically state that Module 1 should not cover acquisitions at all. Some contributors also stress that Module 1 should function as a “safety net” for cases that are not treated Module 3.

Some respondents indicate that the application of one module to a given subsidy does not rule out the application of another module, while others take the opposite view.

#### *Non-EU contributions*

Individual respondents suggest integrating Modules 2 into merger control, Module 3 in the Public Procurement Directives and EU Funding in the EU Financial Regulation or alternatively incorporating Modules 2 and 3 under Module 1.



## **Interplay with other existing instruments**

Some respondents (all categories taken together) mention the necessity of creating a coherent legal framework taking into account Public Procurement Directives, International Procurement Instrument, EU Merger Regulation, EU State aid rules, Trade Defence Instruments and Foreign Direct Investment screening. Some also warn of potential overlaps. A few suggest the possibility to expand Foreign Direct Investment screening rather than implementing the new tool.

## **EU Funding**

Nearly all respondents who replied on this issue support action on foreign subsidies in access to EU funding.

### *Member State contributions*

Individual Member States are concerned that the solution proposed in the White Paper for shared management might make tenders more burdensome and delay their award. Within that context, some refer to their observations to Module 3.

Some Member States call for an ‘EU interest test’ to assess whether certain companies that have received foreign subsidies can receive EU funding.

Few Member States add no specific comments to the solutions proposed or submit that further steps might be considered based on an in-depth analysis of the issue, also in relation to financial instruments.

Individual Member States note respectively that (i) the EU funding section does not consider subsidies/tenders in the context of EUROPAID, (ii) foreign companies should not be treated more strictly than European companies, (iii) social, labour, innovation-related and environmental criteria may play a role for the award of EU funding under shared management.

### *Other EU stakeholders’ contributions*

The contributors agree overall with the approach proposed for EU funding. Most of them advocate for more reciprocity, stating that foreign companies should not receive EU funding if their procurement markets are not open to European companies. Some also ask for a wider use of the Most Economically Advantageous Tender criteria across the board, to take into account qualitative, technical and other aspects to award funding, instead of recurring to the cheapest bid/lower cost.

As regards direct management, the contributors call on the Commission to identify the EU funding to be affected by the proposed solution, to set out clear measures and to take into account some strategic sectors, such as research (Horizon) and transport (Connecting Europe). Some respondents explicitly ask for the possibility to rearrange consortia applying for EU funding, in case a member was to be found in receipt of distorting foreign subsidies. Some also requested to establish a system based on notifications from applicants/bidders coupled with *ex officio* investigative powers of the Commission. The majority agree that undertakings having received distortive foreign subsidies should not access EU funding for a number of years.

As regards shared management, the contributors consider that national contracting authorities and bidders should not have an excessive burden and the Commission should be the only supervisory authority for distorting foreign subsidies – or be in charge for projects worth more than EUR 50 million.

As regards indirect management, the contributors advocate for foreign entities and international financial institutions to align their standards to those of the Union. Some asked the Union to stop blending funds or to attribute funds to other institutions, in case those are not able to apply measures similar to those proposed in the White Paper.



## *Non-EU contributions*

The non-EU contributors oppose the measures set out in the White Paper.

### **2. Feedback on the inception impact assessment (6– 29 October 2020)**

#### ***Feedback from national Member State authorities***

The authorities of all three Member States favour Option 2 as presented in the Inception Impact Assessment – taking legislative action at EU level – as the way forward. One specifically indicated that their preference would be to embed new provisions in existing rules, while another mentioned that such legislative action could consist of a new Regulation for Modules 1 and 2, and a modification of existing rules on Public Procurement.

Two Member States indicate that they view Option 3 (international rule making) as complementary to Option 2. The third Member State stated that Option 2 should be combined with Option 1 (non-regulatory approach), but that they also support Option 3.

Two Member States indicate several issues to carefully consider in the Impact Assessment, among others: administrative burden and the interplay with other legislation. One also indicates that new legislation and definitions should be sufficiently precise.

Two Member States consider that the legal basis for a new legal instrument should be Article 114 TFEU. One of them specified that in case the initiative were split up in several proposals, the choice of the instrument would depend on the legal basis.

#### ***Feedback from other contributors***

Almost all contributors favour Option 2 presented in the Inception Impact Assessment, i.e. taking legislative action at EU level. One contributor specifically indicates that this should take form of new legislation. Four others indicate that it should be a combination of new legislation and amending existing rules. In this respect they mostly point to strengthening the rules for abnormally low tenders (Article 84, Directive 2014/25 and Article 69, Directive 2014/24), but also mention the review and refit of State Aid guidelines and potential sector-specific situations.

One contributor argues that the nature of the maritime technology sector and its current state call for the urgent adoption of a sector-specific solution. This could be done through a major overhaul of existing EU tools (e.g. EU Regulation 2016/1035) based on elements from the White Paper's Module 1, but adapted to the specificities of the industry, and/or tailor-made measures within a new EU tool that provide for effective remedies.

Two other submissions specifically mention the aviation industry. They argue that Regulation (EC) 1008/2008 is not applicable to many of the cases described in the impact assessment. The yet untried Regulation (EU) 2019/712 addresses the competitive distortion caused by subsidies to third-country carriers, not to EU carriers and is, therefore, also not applicable to the cases contemplated by the consultation. Consequently, they advocate legislative action at EU level (Option 2) that complements the existing EU acquis (e.g. aforementioned Regulation (EC) 1008/2008 and Regulation (EU) 2019/712).

In terms of legal basis, three of the respondents specifically state that the new measures should be based on Article 207 TFEU. They indicate that, while there must be a role for Member States in enforcing the new discipline, a common centralised approach towards both investigations and redressive measures under the EU's common commercial policy is essential. Additionally, four contributors indicate that the Commission should have the sole responsibility for the enforcement of any new legislation.

Several contributors indicate that the Impact Assessment should focus, among others, on:

- The interaction with other legal instruments;
- Types of foreign subsidies covered and definition of distortions;

- The notification thresholds and resulting administrative burden;
- Redressive measures and sanctions;
- EU interest test.

Approximately a third of contributors indicate that they see Option 3 (international rule making) as complementary to Option 2 (legislative action at EU level). They indicate, however, that they do not consider Option 3 on its own as a viable route. While in the long term the strengthening of international rules can ensure a level playing field, this option faces many obstacles and is not realistic in the near future.

On the other hand, one contributor believes that efforts to tackle illegal foreign subsidies should be first and foremost made at the WTO or bilateral level. Therefore, they are in principle supportive of Option 3 on “addressing foreign subsidies through international rule-making”. However, they also mention that they can support Option 2 (legislative action at EU level) provided, among others, that a new instrument does not collude with existing legislation and does not create red tape for EU companies.

Some respondents see Option 1 (non-regulatory approach) as complementary to Option 2 (legislative action at EU level), especially when it concerns providing guidance to the Member States and contracting authorities in the field of public procurement. However, they consider that Option 1 on its own would not be sufficient.

One contributor considers that there is no need to establish a separate new tool to regulate foreign subsidies. They argue that the legal instruments proposed under the White Paper may discourage foreign investments into EU, thus causing negative impact on the EU in the economic, social and environmental aspects. If it is indeed necessary to establish separate rules, they consider that Option 1 (non-regulatory approach) should be followed. In such case, developing guidance based on existing EU rules would, in their view, be the most suitable and efficient option.

Finally, one contributor did not provide feedback on the Inception Impact Assessment itself, but rather on the content of the White Paper. They support the objectives of the Modules proposed in the Commission’s White Paper. However, they consider that certain adjustments are needed as regards the design and interaction of the various Modules with each other and in relation to existing legislation. They also indicate that the administrative burden on businesses must be reasonable.

### 3. Targeted consultation (November 2020 – January 2021)

The minutes of the bilateral meetings will be available on [this website](#).

Date	Stakeholder name	Stakeholder group
7/12/2020	European Steel Association (EUROFER)	Business association
	Steel sector is affected by subsidies from China and India, but also Indonesia, Turkey and Russia. Other countries (e.g. those targeted by Chinese investments), may start distorting the EU market as well (Vietnam or the MENA countries). Excess capacity and all types of subsidies in the sector are problematic, also in procurement tenders (e.g. in BRI signatory countries). Ideal solution are stronger rules at WTO and EU level.	
15/12/2020	Eurometaux	Business association
	Copper sector is most affected by localized prices in China, in the aluminium sector the most predominant are Chinese preferential loans and subsidy for energy and inputs. Subsidies impacts global metal/scrap prices, which complicates access to raw metals. They favour a new EU instrument and improved enforcement of existing rules. They support Modules 1 and 2, their customers are impacted in procurement (Module 3). It may be useful to reverse the burden	

	of proof on subsidised companies.	
1/12/2020	European Aluminium	Business association
	Subsidies in the aluminium sector mainly stem from China, there may be similar cases in the Gulf Countries, but not of the same scale. The subsidies are given to a company at the very beginning of the value chain (primary aluminium producers) that pass on the benefits to companies down the chain (producers of semi-fabricated products), who import into the EU at lower prices. China also exports final products like trains, taking market shares from EU companies. This is difficult to address under existing trade rules. Chinese carbon footprint is also three times higher than of EU production.	
26/11/2020	Airline coordination platform (ACP)	Business association
	Countries most prone to subsidies in the sector are those with state-owned airlines such as China, UAE, Qatar, Russia (cargo). Currently, there are two legislations that address unfair competition and control in EU carriers (Regulation (EC) 1008/2008 and Regulation (EU) 712/2019). The most relevant subsidy-induced effects are distortions in pricing and expanding operation in the EU to the detriment of EU air carriers. On a short term, restrictions might reduce consumer choice, however, foreign subsidies in the long term might lead to reduced competition among EU carriers.	
3/12/2020	Association des Constructeurs Européens d'Automobiles (ACEA)	Business association
	ACEA presented recent developments in the sector of electric busses, from vehicles originated from third countries. ACEA referred to the overall system with subsidies for manufacturers to produce buses and operating subsidies for operators, via also discounts on the purchase of electricity. Installation and operation of electric charging infrastructure may also be provided by third country governments. Third countries may benefit from economies of scale due to huge domestic markets and production capacity much bigger than the EU. ACEA expressed concerns that with the large numbers of e-buses forecasted in the EU, but limited content requirements, the situation will not improve and e-buses might risk replicating the collapse of the EU photovoltaic sector.	
26/11/2020	Association of the European Rail Supply Industry (UNIFE)	Business association
	UNIFE observed that the most predominant types of subsidies are tax deductions, grants and export finance supports. As regards non-EU countries granting subsidies, UNIFE gave as examples China (CRRC, CRSC, CCC) and South Korea (support of train builders, through development programmes, KRRI). UNIFE stressed that China is not the only source of concern, and that the Commission should be aware of other cases and other countries. UNIFE underlined that in addition to the types of subsidies discussed and listed in the presentation, there are other forms of "hidden" subsidies. In the rail sector, it is apparent that the strong concentration of domestic players on the Chinese market creates a significant price advantage for these operators when they enter foreign markets or export. Domestic dominance should therefore also be considered as a criterion in the legal instrument for the assessment of distortions. UNIFE pointed out that any quantification of distortive effects is very difficult, especially with regard to public procurement, as the real effects of contract awards can often only be fully appreciated in the long term.	
3/12/2020	European Association of Shipyards and Maritime Equipment Manufacturers (SEA Europe)	Business association
	Foreign subsidies enable foreign shipyards to engage in predatory pricing, in the last decade, European yards have lost entire ship market segments. Subsidies can be below-market financing from state banks, low-interest loans and bonds, preferential guarantees, debt forgiveness, etc., but also non-monetary support to adjacent industries (e.g., steel, oil, electricity and real estate)	

	or loans to non-creditworthy or insolvent enterprises without a restructuring plan. SEA Europe favours EU legislative action, shipbuilding is not covered by TDI instruments, maritime sector favours a sector-specific solution.	
23/11/2020	European Semiconductor Industry Association (ESIA)	Business association
	The semiconductor industry is capital intensive. Public support exists in various jurisdictions to offset some costs related to carrying out research and development or establishing / expanding facilities, etc. Outside the EU, governments tend to grant significant benefits. The new instrument can have positive effects on the functioning of the internal market, competition, sustainable economic growth and productivity and help SMEs, provided it does not unduly increase the administrative burden.	
7/12/2020	European Union Chamber of Commerce in China (EUCCC)	Business association
	Subsidization is a high priority for EUCCC along with market access, non-discrimination and transparency on authorization and licensing in China. Many EU companies do not oppose subsidies as long as they have equal access to them, some benefit from subsidies through their partners. Subsidies in China are provided at various levels and in various forms (entry, production, investment, procurement). SOEs often offer prices below variable costs. Vertical integration, mergers and acquisitions in China and aid to 'zombie companies' are also very problematic. The proposal should not threaten EU open economy and it needs to be considered how it will affect EU companies who benefit from subsidies in China.	
3/12/2020	American Chamber of Commerce to the EU (AmChamEU)	Third country stakeholder
	AmCham EU acknowledges the regulatory gap and tentatively supports the initiative, but companies must not be unduly affected – especially if they come from countries transparent about subsidies, such as the US. Distortive effects of subsidies in certain jurisdictions present a global challenge. A WTO solution is desirable and the EU should take a proactive approach in reforming the WTO. Subsidies which would be allowed under EU State aid rules should also be allowed under the foreign subsidy instrument. AmCham EU favours the Commission as the sole competent authority for the whole instrument. AmCham EU is concerned about the administrative burden on companies. The instrument may create a risk of loss of innovation.	
30/11/2020	China Chamber of Commerce to the EU (CCCEU)	Third country stakeholder
	CCCEU members are concerned about the market openness in the EU towards foreign investments, justification for a new and separate legal instruments, legal certainty and disproportional burden, which would hinder their activities or unnecessarily increase transitional costs. WTO rules and FTAs allow the formulation of instruments compliant with EU international obligations. New rules should avoid creating overlaps or conflicting legal norms, the existing system is appropriate. The scope should be based on objective criteria and appropriate, the burden of proof should not be reversed. A new instrument will increase administrative burden and may discourage foreign companies from investing in the EU.	
4/12/2020	The European Consumer Organisation (BEUC)	Consumer organisation
	As an example, BEUC mentioned subsidies granted to Chinese e-commerce companies for postal services. Products manufactured by subsidised companies can be cheaper because they are lower quality, which is not beneficial for consumers. Distortive subsidies might help third country suppliers to gain an advantage over EU suppliers. FTAs could enhance cooperation (e.g. exchange information on subsidies), a solution at WTO level may be problematic as the EU would be bound by dispute settlement.	
30/11/2020	European Trade Union Confederation (ETUC)	Trade union

	ETUC recognizes the regulatory gap and need for new legislation. Environmental and social impacts seem to be downplayed and need to be taken seriously. Outsourcing negative externalities is a form of subsidy (e.g. unsustainable working conditions against human rights or social dumping), which is particularly relevant for mergers and international public procurement. Need to assess the impact on jobs, pandemic has shown that we need re-localization and not delocalization of services and of the production of goods on European territory. Important to assess broader ‘consumer interest’ (e.g. sustainability aspects), EU interest should have qualitative criteria.	
2/12/2020	BusinessEurope	Business association
	While other countries (e.g. Russia or Gulf Countries) also provide subsidies, China is the most prominent example. Subsidies are often granted through complex, non-transparent investment structures and vehicles (e.g. semiconductor industry). It has become more difficult for EU companies to win in public procurement procedures, as the Chinese competitors bid unreasonably low prices. Sectors most prone to distortions are the technologically advanced ones, like telecom, healthcare etc. The new instrument should be proportional, WTO compliant and non-discriminatory.	
13/11/2019	Meeting of the International Subsidy Policy Group (ISPG)	Public authorities
	On 13 November 2020, the European Commission discussed the White Paper and outcome of the public consultation with Member States as part of the ISPG. It also presented the targeted consultation strategy to Member States. Most Member States showed their support for the initiative on foreign subsidies. Modules 1 and 2 were generally supported by most Member States. Some Member States raised some doubts regarding the viability of Module 3. This Module is found to be more complex and potentially raises concerns when it comes to effective enforcement. Member States also asked questions about the timeline of the initiative and about the interplay of the potential instrument with international obligations.	
30/11/2020	Stakeholder Expert Group on Public Procurement (SEGPP)	Expert group
	The participants in the Stakeholder Expert Group on Public Procurement expressed differing views concerning the necessity of a legal instrument addressing the distortive effects of foreign subsidies in public procurement. Some supported the idea, in relation to major projects, and to specific sectors. Others pointed to high compliance costs and favoured a combination of light regulatory measures and guidance. The members of the group also provided diverse answers concerning the potential compliance costs in relation to notification obligations and the follow-up to an investigation process. For the former, an additional full time equivalent (FTE) depends on the required procedural steps, and respondents declared that this may take on average 4 FTE. For the latter, the respondents agreed that this would require professionally trained experts, extending the administrative burden from 1 to 4 FTE, depending the complexity and number of tenders.	
16/12/2020	Government Experts Group on Public Procurement	Expert group
	The members of the Commission’s “Government Experts Group on Public Procurement” (EXPP) acknowledged the importance to ensure a level playing field, addressing the distortive impacts of foreign subsidies in the internal market. It was also suggested by the members that any new provisions should be proportionate as regards compliance costs, and new rules should be coherent with international obligations. Regarding the compliance costs, in relation to notification measures and the follow-up to an investigation process, the feedback received differs significantly, depending on the different types and the complexity of public contracts. For the former, estimations vary, with an average between 1 to 4 FTE. Some members also expressed concern about the potential additional burden that the treatment of provided data would add to the workload. Concerning the latter aspect, a majority expressed the opinion that contracting authorities do not have the necessary expertise, skills and capacity to assess the	

	relevant information. They estimated that an average of 2 to 3 FTE may be required.	
15/12/2020	SME representatives (EUROCHAMBRES and Business Europe)	SME representatives
	Business Europe welcomed the Commission's work on an instrument addressing the distortive impacts of foreign subsidies in the internal market. The importance of public procurement for its members was stressed, however without a concrete opinion on potential thresholds for its application. Regarding potential compliance costs relating to notification measures and the follow-up to an investigation process, the feedback received was limited. The answers given vary for the former to 2 working days and for the latter to 3 working days.	
11/01/2021	Ministry of Housing and Transport (Denmark)	Public authority
	The Ministry expressed a positive opinion on the Commission's White Paper and the initiative for a new legal instrument to address the distortive impact of foreign subsidies in the internal market. Concerning the potential compliance costs in relation to notification measures and the follow-up to an investigation process, the authority was not able to provide estimations regarding these aspects.	
22/01/2021	Red Eléctrica de España (Spain) EirGrid plc (Ireland) Réseau de Transport d'Électricité (France)	Public authority
	The participants expressed a positive view on the Commission's efforts to address the distortive impact of foreign subsidies. The main concerns of the participants related with potential delays that any new mechanism may have in the procurement process, as well as that EU commitments at international level are respected. Concerning the potential compliance costs, specific estimations were not provided due to the complexity and variety of different procurements. However the impacts will rest in the actions and processes relating with the investigation phase, rather than from solely the notification obligations.	