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European Economic and Social Committee

OPINION

European Economic and Social Committee

Foreign subsidies distorting the internal market

Proposal for a regulation of the European Parliament and of the Council on foreign subsidies distorting the internal market
[COM(2021) 223 final – 2021/0114 (COD)]

INT/954

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Referral	European Parliament, 07/06/2021 Council, 03/06/2021
Legal basis	Articles 114 and 207 of the Treaty on the Functioning of the European Union
Section responsible	Single Market, Production and Consumption
Adopted in section	30/9/2021
Adopted at plenary	20/10/2021
Plenary session No	564
Outcome of vote for/against/abstentions)	220/3/9

1. Conclusions and recommendations

1.1 The EESC endorses the Commission's work on this matter and agrees that action must be taken to bolster the instruments safeguarding the EU market and its businesses. This will entail plugging a gap in the legislative framework as regards competition, trade and public procurement with a view to guaranteeing fair competition which is not distorted by foreign subsidies.

1.2 The EESC accordingly considers that the Commission proposal tackling foreign state funding for companies operating in the EU market, a market that such subsidies are likely to distort, is a useful and appropriate instrument. That said, some aspects of the intrinsically complex and far-reaching legislative mechanism need to be further refined.

1.3 Under the proposal, the broad definition of foreign subsidy can cover many types of subsidies by a foreign state, including in the field of taxes. The Commission therefore needs to clarify which investigations will be given priority, if necessary establishing criteria for processing the various dossiers with a view to transparency and simplification.

1.4 The proposal gives the Commission responsibility for screening investments in the EU by foreign-subsidised entities. On this point, the EESC considers that the Commission should clearly specify the scope of this regulation, possibly through appropriate guidelines. This would ensure that it is applied uniformly across the EU and reduce as far as possible the danger of diverging interpretations by the Member States, which are responsible for screening foreign investments. The Committee therefore proposes that a helpdesk be set up to provide businesses with information on the rules governing foreign subsidies and the resulting compliance and reporting requirements.

1.5 In order to begin proceedings, the Commission assesses the foreign subsidy, weighing its negative and positive effects on the development of the relevant economic activity. The EESC believes that the Commission should provide further details on how this assessment is to be carried out in practice, what the potential positive effects might be and when balancing is justifiable.

1.6 With regard to the current regime for screening concentrations, the EESC considers that the Commission should clarify how this interacts with the new regime planned, with a view to avoiding inconsistent timing and results resulting in a considerable burden on businesses.

1.7 In order for the Commission to begin proceedings, the total amount of foreign subsidies must exceed EUR 5 million for three consecutive fiscal years. The EESC considers that this threshold is fairly low in absolute terms and the Commission should be encouraged to raise it in order to avoid minor, less significant cases, a shift which would be to the benefit of small and medium-sized companies.

1.8 In the area of public procurement, the likelihood of *ex officio* investigations and a broad review of public procurement could potentially lead to risks and burdens for companies operating and investing in the EU. This is why the Commission needs to simplify and clarify the regime as far

as possible in order to make the new rules easy to apply, particularly when these rules run alongside others which are already in force, lessening the administrative burden on EU businesses.

2. General comments

2.1 The EESC considers that it is crucial that the EU and its markets remain open and competitive, deeming this to be key to the proper and balanced functioning of its society and economy, to ensuring a stable footing for businesses and to the well-being of Europeans, which underpin its model of strategic autonomy[1]. In light of this, the Committee considers that the objective of safeguarding the single market from subsidies which bring about unfair competition must go hand in hand with the goal of having an effective instrument applied consistently to the entire EU, with the smallest possible burden on businesses.

2.2 On 17 June 2020, the Commission adopted a white paper on foreign subsidies to tackle the issue, launch a public debate and propose possible solutions. The white paper identifies a legislative gap in EU state aid rules as regards competition, trade and public procurement, which effectively prevents the EU from taking action when foreign subsidies cause distortions in the internal market, favouring specific concentrations or bidders in public procurement. The white paper also identifies problems linked to access to EU funding for operators receiving foreign subsidies, which could distort the competition for EU funds. To date, no Member State has implemented rules tackling the potential distortion caused by foreign subsidies.

2.3 The issue of foreign subsidies is not new and has been repeatedly raised at EU level. The Council referred to the Commission's white paper in its conclusions of 11 September 2020; in its conclusions of 1-2 October 2020, the European Council called for "further instruments to address the distortive effects of foreign subsidies in the single market". In its February 2020 report on competition policy, the European Parliament called on the Commission to "[investigate the option of having] 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 Commission Executive Vice-Presidents Vestager and Dombrovskis and Commissioner Breton, a group of 41 MEPs expressed strong support for an instrument to tackle "companies from third countries that have received substantial state support".

2.4 As announced in the Commission's work programme for 2020-2021, this proposal for a regulation sets out detailed rules for a new instrument (an *ex ante* notification system for large amounts which could give rise to greater distortion, together with an *ex officio* procedure) to address the regulatory gap in EU legislation and ensure a level playing field in the internal market by avoiding unfair competition. The proposal is also mentioned in point 3.2.6 of the Communication on the Trade Policy Review, on ensuring a level playing field.

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1 Commission communication on *Europe's moment: Repair and Prepare for the Next Generation* (COM(2020) 456 final). See also Commission communication on *The European economic and financial system: fostering openness, strength and resilience* (COM(2021) 32 final).

2.5 In a nutshell, the aim of the proposed legislation is to investigate and, where appropriate, deter or prevent concentrations, public procurement and market behaviour by foreign-subsidised companies that may distort the EU internal market. It provides for mandatory notification of concentrations where the turnover of the company concerned exceeds EUR 500 million and the parties have benefited from more than EUR 50 million in foreign financial contributions in the previous three years, as well as mandatory notification where foreign-subsidised companies take part in public procurement where the contract value is over EUR 250 million. The proposal also aims to enable the Commission to investigate market behaviour, including mergers and acquisitions below these thresholds, by any entity benefiting from foreign subsidies exceeding EUR 5 million for three consecutive years.

2.6 The proposal shows that the problem is not foreign investment, but the subsidies that facilitate the acquisition of EU companies, affect investment decisions, distort trade in goods and services, affect the behaviour of the beneficiaries and harm competition. Unlike subsidies, for which the Commission has exclusive power to intervene, in the case of foreign investment this is the remit of the Member States which in any case are always empowered to screen foreign investments on the grounds of security or public order.

2.7 The latter is governed by Regulation 2019/452[2], applicable from 11 October 2020, which establishes a system for the exchange of information between the Commission and the Member States and improves screening mechanisms, where these are in place, allowing the Commission to comment on or adopt opinions on transactions approved by the Member States. That regulation mainly covers investments in critical infrastructure and technologies, sensitive data and media, without setting minimum thresholds, thus enabling the Member States to scrutinise almost all investments from outside the EU.

3. Specific comments

3.1 The proposal for a regulation defines "foreign subsidies" very broadly (Article 2): it includes any case where a third country provides a financial contribution which confers a benefit to an undertaking engaging in an economic activity in the EU's internal market, whether this contribution is limited to an individual undertaking or affects several undertakings or groups of undertakings. The financial contributions can take any of a wide range of forms, including 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, debt to equity swaps or rescheduling; the foregoing of revenue that is otherwise due; or the provision or purchase of goods or services.

3.2 Under the proposal, the broad definition of foreign subsidy, which in substance is aligned with the EU definition of state aid, is therefore likely to cover many forms of subsidies and incentives from a foreign state, raising questions about how equipped the Commission is in reality to cope with the huge amount of work involved, which will in fact cover subsidies of any kind granted by any country worldwide. This could create legal uncertainty and the potential for

[2] 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 79I, 21.3.2019, p. 1.

litigation from competitors in contested mergers and acquisitions. In this case, it must be made clear which investigations will be a priority for the Commission and whether it intends to set criteria for these to be communicated beforehand.

3.3 The proposal essentially gives the Commission responsibility for screening investments in the EU by foreign-subsidised entities. In fact, some Member States may consider that such decisions fall within their remit as part of their national systems for foreign direct investment screening. On this point, the EESC considers that the Commission should clearly specify the scope of this regulation, possibly through appropriate guidelines. This would ensure that it is applied uniformly across the EU and reduce the danger of diverging interpretations by the Member States as far as possible. The Committee therefore proposes that a helpdesk be set up to provide businesses with information on the rules governing foreign subsidies and the resulting compliance and reporting requirements.

3.4 The proposal for a regulation therefore brings in a new form of control which is simultaneously *ex ante* (for large concentrations and public procurement procedures) and *ex post*, beyond what is currently stipulated for EU concentrations; it is modelled on, but distinct from, those arrangements (Chapter 3). Here too, the transactions requiring notification include mergers, acquisitions of a controlling interest and full-function joint ventures. However, the financial thresholds are different from those in the Merger Regulation.

3.5 The Commission will assess whether there is a "distortion in the internal market" (Article 5). This assessment will be "limited to the concentration at stake", although this does not appear to require the Commission to establish a direct causal link between the transaction and the distortion of the market. A distortion in the internal market would occur where a foreign subsidy could improve the competitive position of the company concerned in the internal market and where, as a result, it actually or potentially negatively affects competition in the internal market.

3.6 The proposal for a regulation therefore gives the Commission considerable room for discretion by listing as potentially relevant indicators the amount and nature of the subsidy, the situation of the company and markets concerned, the level of economic activity of the company on the internal market and the purpose and conditions attached to the foreign subsidy, as well as its use in the internal market.

3.7 Here, the Commission would be entitled to assess the negative effects of a foreign subsidy in terms of distortion of the internal market against its positive effects "on the development of the relevant economic activity" (Article 5). Where the positive effects outweighed the negative, no procedure would be adopted. In this case, we believe that the Commission should provide further details on how this assessment is to be carried out in practice, especially as regards the potential positive effects and when balancing is justifiable. It should be noted here that the Commission has developed comprehensive and detailed guidelines on intra-EU subsidies compatible with the internal market.

3.8 If the Commission considers that a foreign subsidy distorts the internal market, it may impose measures to remedy this (Article 6). Companies may also offer commitments to remedy the alleged distortions and the Commission may make such commitments binding. The

commitments or redressive measures may include offering access on fair and non-discriminatory terms to infrastructure, licensing of assets acquired or developed with the aid of foreign subsidies, reducing capacity or market presence, refraining from certain investments, publication of results of R&D, divestment of assets, repayment of the foreign subsidy to the third country with interest or dissolution of the concentration.

3.9 In this regard, we consider that the relationship between the proposed new regime and the current EU merger control regime should be clarified. While the notification thresholds and the substantive assessment are different, many transactions could be notified to the Commission under both regimes in parallel, with the risk of inconsistent timing and results, resulting in a considerable burden on businesses.

3.10 The proposal for a regulation proposes a separate mandatory notification regime for EU public contracts exceeding EUR 250 million (Chapter 4). Companies participating in such procurement procedures are required to report all foreign financial contributions received during the three years preceding the notification or have to declare that they did not receive any foreign financial contribution during that period (Article 28).

3.11 Contracting authorities are required to send such notifications immediately to the Commission, which has 60 days from the notification to complete a preliminary check and a further 140 days for an in-depth investigation, which may be extended in exceptional cases. Notifications do not suspend the public procurement procedure, but the contracting authority will not be able to define the procedure and award the contract to a company which is being investigated by the Commission. If companies fail to notify a transaction, the Commission may impose fines of up to 10% of their total turnover. This is a rather cumbersome procedure that risks slowing down the completion of complex procedures such as procurement procedures, which are essential for Member States to implement Next Generation EU plans.

3.12 The proposal for a regulation allows the Commission to act on its own initiative to investigate any potential distortion of the EU internal market by a foreign subsidy (Chapter 2). The only requirement for the Commission to investigate is that the total amount of foreign subsidies exceeds the threshold of EUR 5 million for three consecutive fiscal years. This threshold is fairly low in absolute terms, and the Committee considers that the Commission should be encouraged to raise it to avoid minor, less significant cases, a shift which would be to the benefit of small and medium-sized companies. The Commission also has the power to investigate foreign financial contributions granted up to ten years before the start of its investigation, with the possibility of investigating foreign subsidies granted in the 10 years prior to the date of entry into force of the new regulation where the distorting effects come into play after the start of the application of this regulation.

3.13 The proposed regulation will have a significant economic effect as it potentially affects all companies receiving support from third countries and engaging in economic activities in the EU (in particular when it comes to mergers and acquisitions or tenders for public contracts above the threshold set), as well as having a positive impact on all those which do not receive foreign subsidies.

3.14 The proposal will in practice allow the Commission to scrutinise subsidies granted by non-EU governments in a similar way as allowed by the EU state aid rules. This risks adding an additional layer of complexity to an already highly complex regulatory framework, with heavy burdens for businesses in the EU. For instance, one transaction could in the future be subject to three different procedures – merger control, screening of foreign direct investments and scrutiny of foreign subsidies under this proposal – each with its own rules on procedures and deadlines.

3.15 In the area of mergers and acquisitions, the review of foreign subsidies would be added to mandatory merger control notifications (at EU or Member State level) and to national notifications for foreign investments, with the risk of disputes with the businesses involved.

3.16 In the area of public procurement, the likelihood of *ex officio* investigations and a broad review of public procurement could potentially lead to risks and burdens for companies operating and investing in the EU. This would affect foreign stakeholders investing in the EU and EU-based companies that receive foreign financial contributions (through foreign investors or foreign aid for specific projects). In this case, companies would have to closely scrutinise all foreign subsidies received to assess whether the new rules apply.

3.17 This is why the Commission needs to simplify and clarify the regime as far as possible in order to make the new rules easy to apply (particularly when these rules run alongside others which are already in force) and lessen the administrative burden on EU businesses.

Brussels, 20 October 2021

Christa Schweng
The president of the European Economic and Social Committee