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BusinessEurope reaction to the European Commission legislative proposal on distortive foreign subsidies

KEY MESSAGES

1 BusinessEurope welcomes the proposal for a regulation to address distortions caused by foreign subsidies in the Single Market published in May 2021. The Regulation has been given a more proportionate scope, with focus on the potentially more distorting subsidies. Yet, the notification thresholds for concentrations and public procurement procedures may need to be lowered to capture relevant distortive subsidies. At the same time, the administrative burden on companies and public authorities needs to be kept as low as possible. Moreover, the Commission needs to allocate an adequate amount of resources to the operation of this instrument in order that lower thresholds for procurement and concentrations do not negatively impact its ability to use the ex officio tool.

2 The Regulation should include specific provisions to deal with foreign state-owned enterprises (SOEs). For example, the Commission could reverse the burden of proof for foreign SOEs, particularly where it has well-founded evidence of the existence of significant distortions in a third country or a sector in a third country. The WTO compliance of this measure needs to be ensured.

3 The Commission will need to provide detailed guidance on different aspects of the final regulation to companies to give them more legal certainty. This should include guidance e.g. on the application of the ex-officio tool, the definition of foreign subsidies, the calculation of fines and penalty payments, interim measures the Commission can take, commitments companies can offer or inquiries that will be prioritised in case of an excessive number of notifications.

4 The definitions and procedures under the instrument should be aligned as much as possible with relevant EU legislation, e.g. on state aid, trade defence, foreign investment screening, public procurement and antitrust. Duplication of reporting requirements and overlaps in terms of scope should be avoided.

5 BusinessEurope does not favour a retroactive application of the instrument to public procurement procedures and concentrations that were completed or initiated before the regulation enters into force.

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Introduction

It is crucial for European companies that the terms of competition within the internal market are not undermined by economic entities benefitting from distortive foreign subsidies. While the EU regulatory framework sets clear rules and limits for state aid granted by EU Member States, subsidies granted by third countries have thus far not been tackled. Many of the latter are not even notified to the WTO despite the obligation to do so. In recent years, the activity in the EU market of companies benefitting from foreign subsidies has exposed a regulatory gap not addressed by existing EU legislations.

Therefore, BusinessEurope welcomes the proposal for a regulation to address distortions caused by foreign subsidies in the Single Market published in May 2021. The proposal has taken on board many of the recommendations BusinessEurope had brought forward in its reaction to the European Commission White Paper on foreign subsidies in the Single Market from June 2020.

Compared to the White Paper, in particular the following changes are noteworthy:

- The European Commission is now solely responsible for enforcing the regulation. This allows for a homogenous implementation across member states. Nevertheless, smooth cooperation between the Commission and relevant authorities in EU Member States will be important, too.
- The “de minimis” threshold and the notification thresholds for procurement procedures and concentrations have been increased. With this, the European Commission aims to focus its attention on subsidies that cause significant distortions, while minimising the administrative burden on companies and public authorities and keeping the internal market open for investment.
- Companies are required to submit an “ex-ante” notification in procurement procedures and mergers and acquisitions only for the largest and potentially most distortive cases. For all other market situations, distortive foreign subsidies would be identified by the European Commission in an “ex officio” procedure.

While many of the changes are welcome, some concerns and uncertainties remain with regards to the scope and the functioning of the future instrument. These are set out below.

Comments on the legislative proposal

<u>Definition and assessment of distortive foreign subsidies:</u>

- The proposed **definition of foreign subsidy** seems to be similar to the notion of state aid under EU state aid rules. However, it is not clear whether the criterion of selectivity, which is fundamental to identify state aid, is included in the expression "several companies or industries", as defined in Article 2(1) of the

proposal. To ensure greater legal certainty, the proposals should better clarify the definition of foreign subsidy and any similarities or differences with relevant definitions under EU state aid rules. For example, the meaning of "financial contribution" as well as the criteria businesses must take into account to identify entities whose actions can be attributed to a third country should be clarified.

- Article 4 on categories of foreign subsidies most likely to distort the internal market should include **export credits incompliant with the OECD arrangement** on officially supported export credits. Furthermore, the regulation does not explicitly take into account the competitive advantages conferred by the privileged access that a foreign company may have to its domestic market, in particular regarding public procurement (e.g. monopoly supported / encouraged by a foreign State which favours national companies on its domestic market). Such privileged access strengthens a company's position also in other markets and should be included in the regulation.
- The balancing test set out in Article 5 gives the European Commission a large degree of discretion. Therefore, the criteria for this **balancing test** need to be defined much more clearly and comprehensively to avoid legal uncertainty. The assessments should be modelled on similar ones under EU State Aid rules, as well as on the underlying principles of proportionality, appropriateness, and necessity. Moreover, the Commission should be allowed to request information from the public to determine whether the negative effects of a foreign subsidy outweigh its positive effects. Such requests should be made only under pre-determined circumstances. The request for information should be specific and directed at a certain group or a party. Any process of similar nature must be clearly defined in the criteria or guidelines for the balancing test. A preference for the elimination of the negative effects of a foreign subsidy, along the lines of the EU basic anti-subsidy Regulation[1], should be in place. The guidelines for the balancing should be based on a dedicated public consultation.
- In terms of scope and design of the rules, the new instrument must **not be more restrictive than existing EU rules on state aid** to ensure compliance with the rules of the World Trade Organisation.
- Due to the increasing activity of third country **state-owned enterprises** (SOEs) in the EU market, and due to the nature of these entities, the Regulation should include specific provisions to deal with foreign SOEs. For example, the nature of the entity (i.e. foreign SoE) could lead to the presumption that it received distortive financial contributions, and the burden of proof to demonstrate it has not received any such contributions should then be on the foreign SOE, particularly where the Commission has well-founded evidence of the existence of significant distortions in a third country or a sector in a third country. The WTO compliance of this measure needs to be ensured.

[1] Article 31(1) of the EU anti-subsidy Regulation provides that "the need to eliminate the trade-distorting effects of injurious subsidisation and to restore effective competition shall be given special consideration".

Ex officio review of foreign subsidies:

- The “ex officio” review of foreign subsidies gives the European Commission far-reaching powers, the scope of which is not clearly defined in the legislative proposal. The European Commission should provide **specific guidance on how it will exercise these powers**. Clarity, predictability, and coherence with other relevant EU legislation are of great importance, and foreign investments in the EU should not be discouraged. This guidance should include, inter alia, some criteria the European Commission will take into account when requesting “ex officio” notifications as well as information on the obligations applying to companies subject to ad hoc notification requirements.
- The proposal does not stipulate any **time limits** for the ex-officio review. For reasons of predictability, the Commission should set indicative time limits that ensure an efficient conduct of the proceedings.
- The “ex officio” tool should **not allow for reopening “**ex-post” a case already cleared under the relevant procedures for concentrations and procurement – unless the relevant notification requirements were breached, or false, incomplete, or misleading information had been submitted – as this would lead to uncertainty and possibly to conflicting decisions. This should not prevent the European Commission from investigating whether the operations of a company distort the Single Market due to foreign subsidies after it has been acquired by a non-EU company.
- According to Article 47(3), the proposal does not apply to concentrations and tenders already completed prior to the date of its entry into force. However, point (1) suggests that the Commission could still launch an “ex officio” investigation on concentrations and tenders if they were affected by foreign subsidies granted in the ten years prior to the application of the regulation that still distort the internal market after its entry into force. Therefore, the current version Article 47 is confusing, and the Commission should clarify under which circumstances a retroactive application of the instrument is possible. BusinessEurope does not favour a **retroactive application of the instrument**.

Specific instrument regarding concentrations:

- **The timeframe for the preliminary and in-depth investigations** (i.e. 25 days for the preliminary examination and 90 days for the in-depth investigation) is aligned with relevant timeframes under the EU Merger Regulation. This alignment should be preserved in the final instrument.
- When adopting the **implementing acts** referred to in Article 42 on the form, content and procedural details for the notification of concentrations, the European Commission should be guided by existing procedures under relevant EU legislation. Moreover, the European Commission should take into account the results of the ongoing consultation regarding the procedures under the Merger Regulation, which are still considered too time consuming and burdensome for companies.

- Article 18(3) sets out the **thresholds** for which company mergers are subject to notification requirements. The thresholds set in the legislative proposal may need to be lowered to ensure that the instrument covers the most relevant cases. This must be balanced against the need to keep the administrative burden on companies as low as possible, and to make sure that enough of the Commission's investigative resources can be reserved to the ex officio investigations. Moreover, it would be useful to clarify whether turnover and financial contributions to be considered are specific to each company or aggregated for all companies involved in a merger. It seems that turnover should be calculated separately for each individual company, whereas financial contributions should be aggregated for all companies involved and regardless of whether they have been granted by one or more countries, but this should be clarified.
- Regarding **fines and penalty payments** (Article 25), it is not clear whether the percentages refer to the entire turnover achieved by each individual undertaking taking part in the transaction – resulting in the imposition of several penalties calculated on different turnovers - or whether they refer to the total turnover achieved by all the undertakings involved in the transaction – resulting in the imposition of fines calculated on a single basis. This needs to be specified.

<u>Specific instrument regarding large public procurement procedures:</u>

- The **thresholds** of this tool should apply to the overall project (as opposed to individual public tenders) to prevent that tenders are artificially subdivided to avoid exceeding the thresholds. However, the thresholds set in the legislative proposal may still be too high for this tool to be effective and they may thus need to be lowered. This must be balanced against the need to keep the administrative burden on companies as low as possible, and to make sure that enough of the Commission's investigative resources can be reserved to the ex officio investigations. Moreover, the Commission should also have the possibility to investigate public tenders in case their value undergoes a significant change over time (e.g. when a project's global value is minimised at the beginning so that no notification is necessary).
- The obligation to notify foreign financial contributions under this component extends to the **main subcontractors and main suppliers** of the economic operators concerned. Subcontractors and suppliers are deemed to be main if:
    a) their participation ensures key elements of the contract's performance;
    b) the economic share of their contribution exceeds 30% of the estimated value of the contract.

  As criterion a) is ambiguous and creates legal uncertainty for the economic operators involved, the assessment should be limited to criterion b). Moreover, the threshold set by b) may be too high to ensure that companies that have split up but act in a coordinated manner, or companies that cooperate in a tender, are also duly covered by the regulation.

- The **time limit** of 200 days for investigations regarding foreign subsidies in public procurement procedures is overly long. This may have negative consequences for the relevant procurement procedure or project. For example, there may be situations where the time limit extends beyond the period in which the bidder is contractually obliged to maintain their offer. Therefore, the time limit of 200 days should be reduced considerably. To save additional time, companies should have the possibility to inform the European Commission of foreign financial contributions already before submitting their tender for an upcoming procurement procedure (i.e. before the official notification).

Notification requirements and information requests:

- Any **new notification obligations should be streamlined** with existing ones, e.g. under EU legislation on trade defence, foreign investment screening, public procurement and antitrust. Where possible, a single notification system should be put in place for different notification requirements to avoid that companies need to submit multiple notifications for the same transaction and to minimise the administrative burden on business.
- It must be ensured that in the course of the procedure economic operators will not be obliged to disclose **sensitive business information** going beyond the mere notification of foreign subsidies.
- The subsidies that will be received by a company before the end of the year in which a given investigation takes place should also be notified. The Commission will thus be able to better review the cumulative effects of foreign subsidies and possible distortions. For public procurement, it should be explored whether the Commission can review **future foreign subsidies** that would be granted before the execution of the contract.
- It is unclear what defines "an appropriate time limit" for companies to **provide information** at the request of the European Commission (see Article 11(3)(a)). The Commission should provide an indication of criteria that will be considered for determining such an appropriate time limit.
- There is no **mechanism that allows a company to notify a financial transaction** to the European Commission at its own initiative to obtain an assessment of whether the transaction constitutes a distortive foreign subsidy. BusinessEurope asked for this possibility in its contribution to the White Paper as it would increase legal certainty for companies intending to make an acquisition or to bid in a procurement procedure that may exceed the predetermined thresholds.
- For the assessment of whether EU subsidiaries of foreign companies benefit from distortive foreign subsidies, the subsidies received by the **parent company** in its home market should be considered and covered by any notification requirement. The regulation should prevent the circumvention of this requirement, e.g. by means of shell companies, by treating EU subsidiaries and their parent companies as one economic entity.

- The European Commission should establish a **dedicated contact point** through which companies established in the EU, European business organisations, and EU Member States can submit information on companies they suspect of benefitting from distortive foreign subsidies.
- While fines should be set deterrently high from the beginning, they should gradually become even harsher if a company **continuously breaches notification requirements**, in line with the principles of proportionality, appropriateness, and gradation.
- **Companies that have been subject to a negative decision** by the supervisory body for having caused market distortions in public procurement should be monitored on a regular basis. A database on these foreign entities should be made publicly available.
- **Further clarification and guidance** is required as to the extent to which favorable foreign tax regimes, joint ventures with foreign state-owned enterprises, the presence in a free trade zone and other benefits a company active on the EU Single Market enjoys in a third country could fall under the notification requirements for concentrations and public procurement procedures, if the respective thresholds are exceeded. Otherwise, companies will notify the European Commission of irrelevant foreign financial contributions just to be on the safe side.
- The European Commission should establish a **help desk** that companies can contact if they have queries relating to the regulation on distortive foreign subsidies in general and the notification requirements in particular.
- The European Commission needs to allocate an appropriate level of resources to the implementation of the regulation. Moreover, specific guidelines should indicate which inquiries will be **prioritised** in case of an excessive number of notifications.

Inspections:

- According to Article 13, the European Commission needs the consent of both the undertaking concerned and the third country government to carry out an **inspection in the territory of a third country**. However, BusinessEurope believes that the consent of the third country government should suffice whilst the confidentiality of business information and commercial information of the company should be safeguarded. The consent of the company in question is not required for inspections within the EU and foreign companies should not be treated preferentially in this regard.

Redressive measures:

- Article 6 of the draft regulation mainly provides for measures to remedy distortions in the context of mergers. Only two non-merger-related measures are included to deal with distortions occurring in the marketing or supply of goods and services:

  - Paragraph 3(e) providing for the publication of research and development results: this measure seems difficult to implement because it would violate the fundamental principles of intellectual property;
  - Paragraph 3(h) providing for the reimbursement of the foreign subsidy: this measure seems impracticable because it will be very difficult to calculate the precise amount that needs to be reimbursed, and to verify the effective reimbursement of the foreign subsidies in question.

  Consequently, there is a **need to complement the redressive measures** as they are currently inadequate to effectively deal with distortions induced by foreign subsidies in the marketing or supply of goods and services. A reflection on additional measures must be initiated (e.g.: temporary exclusion from the single market could be possible after an *ex officio* review).
- Article 6 should also provide for the possibility for the Commission to **prohibit the award of a public contract to a company**. This is necessary to clarify that the prohibition of a contract award is not only possible under the specific instrument for public procurement (cf. Article 30(2)), but also under an ex officio procedure for smaller procurement cases.

Other issues:

- Distortive foreign subsidies received by competitors are also a growing problem for European companies active in third countries. Therefore, **EU funding for projects in third countries**, for example under the Neighbourhood, Development and International Cooperation Instrument, should not support companies that benefit from distortive foreign subsidies. While the White Paper raised this issue, it is not addressed in the legislative proposal. Therefore, the European Commission should table a separate legislative proposal to tackle distortive foreign subsidies in the context of EU funding. This will be even more important in view of an enhanced EU connectivity strategy.
- The language of the regulation should be **more aligned with other relevant EU rules** to avoid conceptual confusion. For example, whereas this regulation refers to "an ailing undertaking" (Article 4(1)), the description "undertaking in difficulty" is used in the EU state aid rules. In the same vein, the description “an unduly advantageous tender” (Article 4(4)) used in this regulation, differs from the wording “abnormally low tender” found in the EU’s directive on public procurement.
- The proposal seems to use the concepts “**interested parties**” and “undertaking concerned” alternatively (e.g., Article 8(2)(c)). It would be useful to add a specific article containing the relevant definition of these terms.
- It remains unclear according to which criteria the Commission will decide to open an **in-depth investigati**on. There should be a clearer definition or case examples of “sufficient indications” in Article 8(2).
- The **interim measures** the European Commission can take in line with Article 10 should be specified. They need to be proportionate and should in no case be

more far-reaching than the final measures. The word “irreparable” in Article 10(2) should be deleted as its meaning is unclear in this context.

- Undertakings can offer **commitments** to mitigate the distortion created by a foreign subsidy. However, it should be specified under which circumstances such commitments are considered sufficient.
- The principle of **proportionality** is referenced in the introductory paragraphs but not in the body of the legislative proposal itself. As the introductory text will not be part of the final regulation, the European Commission should refer to the principle of proportionality directly in the text of the regulation, where relevant – e.g. in Article 11 concerning information requests, and Article 34 concerning market investigations.
- While Article 40(4) provides for a provisional application of the proposed “ex officio review" tool to the shipbuilding sector, the interplay between that provision and Article 40 (7) must be clarified to ensure that the latter does not prevent the applicability of the regulation to the shipbuilding sector.