BRIEFING

EU Legislation in Progress

European Parliament

Distortive foreign subsidies regulation

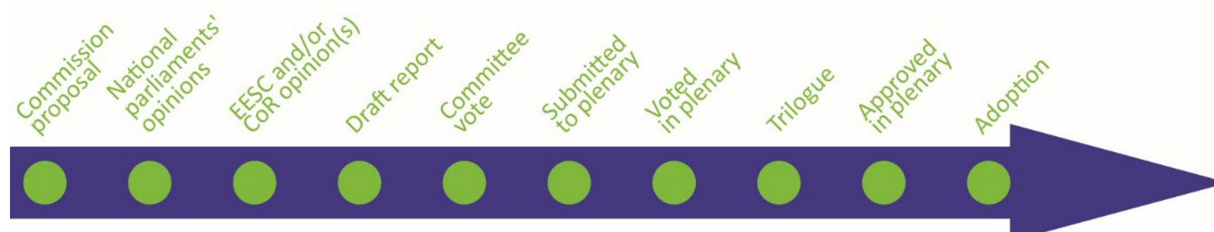
A level playing-field for the single market

OVERVIEW

Public financing of enterprises, which has been on the rise globally, can have a distortive effect on competitive markets. In response to this trend, in May 2021 the European Commission published a proposal for a regulation to tackle foreign subsidies with a distortive effect on the EU single market. It would enable the Commission to investigate subsidies granted by non-EU public authorities to companies operating on the single market, and to apply countervailing measures, should these subsidies be found to be distortive. The Commission would have three tools at its disposal: two are notification-based, allowing it to investigate foreign subsidies in companies' mergers and acquisitions, and to investigate the bids in large public procurement procedures involving third-country government support. The acquirer or bidder would have to give ex-ante notification of external financial contribution. The third would enable the Commission to investigate other market situations.

The Parliament adopted its position in plenary in May 2022, and trilogue negotiations concluded successfully in June 2022. Parliament approved the agreement in plenary by a large majority on 10 November 2022 and the final act was signed on 14 December 2022. The regulation entered into force on 12 January 2023.

Regulation (EU) 2022/2560 of the European Parliament and of the Council on foreign subsidies distorting the internal market		
Committee responsible:	International Trade (INTA)	COM(2021) 223 5.5.2021 2021/0114(COD)
Rapporteur:	Christophe Hansen (EPP, Luxembourg)	
Shadow rapporteurs:	Inmaculada Rodríguez-Piñero Fernández (S&D, Spain) Catharina Rinzema (Renew, the Netherlands) Reinhard Bütikofer (Greens/EFA, Germany) Marco Campomenosi (ID, Italy) Geert Bourgeois (ECR, Belgium) Emmanuel Maurel (The Left, France)	Ordinary legislative procedure (COD) (Parliament and Council on equal footing – formerly 'co-decision')
Procedure completed:	Regulation (EU) 2022/2560 OJ L 330 23.12.2022, pp. 1-45	



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Introduction

The European Commission defines a subsidy as 'a financial contribution made by (or on behalf of) a government or a public body that gives the recipient a benefit'. Subsidies have played a pivotal role in the history of the World Trade Organization (WTO); agricultural subsidies are considered to be the main reason behind the breakdown of the Doha Round of negotiations. Recently, foreign subsidies have gained prominence in the international trade debate, in particular because of the growing role of China in the global economy and legal uncertainty as to whether WTO rules apply where the subsidised entity is located abroad in relation to the public authority dispensing the subsidy. Foreign subsidies can be broadly defined as those granted by a government to a firm outside its territory (jurisdiction). The developed economies, such as the EU and the US, have become increasingly aware of possible distortions on their domestic markets and an uneven playing-field created by industrial subsidies. This is because economies that are open to foreign investment and competitors, and that at the same time operate under strict domestic State aid and subsidy control rules, are vulnerable to foreign competitors that actively use subsidies to support their firms. Those competitors can enter the open markets of these open economies with an unfair advantage, through, for instance, their subsidised firms, their branches or subsidised acquisitions of the open economy's companies. The EU is indeed a particularly open economy: it is one of the world's largest trading blocs with 16 % of global trade and, before the pandemic, the world's largest FDI destination with 31 % of worldwide FDI stock.[1] World Bank data confirm that EU trade corresponds to as much as 91 % of its GDP – while globally the average is at 60 % – the United States is at 26 %, and China's trade stands at 36 % of its GDP.

Accordingly, in 2017 the Commission signalled that the global rulebook on harmful government subsidies remained far from complete. In the same year, the European Parliament highlighted the problem in its resolution on an EU industrial strategy. In 2019, the European Council called on the Commission to identify how the relevant gaps in EU legislation could be closed. With massive worldwide state support for the economy as a result of the coronavirus crisis, the issues of subsidisation have become more pertinent than ever.

Examples of distortive foreign subsidies

Mergers and acquisitions: a third-country company attempts to acquire an EU company. The company's public authorities support it with a direct grant and/or unlimited state loan guarantee. These subsidies help to finance the acquisition by enabling the company to outbid competitors that do not have such state support.

Public procurement: a non-EU infrastructure enterprise supported by its government through direct subsidies and/or government ownership bids in a public call for tender organised in the EU. As a result, the foreign bidder is able to make an offer at a low price – one impossible to offer without a subsidy.

General market operation: subsidies such as below-market state-backed financing reach a European subsidiary of a non-EU parent company. This low-cost financing allows the subsidiary to purchase machines that lower its production costs and the price of goods offered on the EU market. With these cheaper prices, it can outcompete EU rivals, which must finance themselves on market terms.

Source: European Commission.

WTO framework

At multilateral level, subsidies are governed by the WTO framework. When it comes to subsidies for the production of goods and countervailing measures, Articles VI and XVI of the General Agreement on Tariffs and Trade (GATT) set out the basic rules. These are elaborated in more detail in the WTO Agreement on Subsidies and Countervailing Measures (SCM), which applies only to 'specific' subsidies.[2] More specifically, the SCM defines the key legal notions and groups subsidies in two categories: prohibited and actionable (subject to challenge in the WTO or to countervailing measures). It also sets out in detail the multilateral disciplines that regulate the provision of subsidies, and the use of countervailing measures to offset injury caused by subsidised imports. However, the Commission and legal experts argue that the SCM does not provide adequate multilateral remedies to address foreign subsidies specifically.

The subsidies prohibited under the WTO framework that could lead to proper multilateral remedies fall into two sub-categories. First, there are those that are granted if the receiving entity increases exports ('export subsidies'). Export performance cannot be subsidised to displace unsubsidised competitors. Examples include subsidies contingent on export performance, currency retention schemes, favourable freight or shipping terms, tax deferrals or exemptions for exports. The second sub-category concerns subsidies to the entity that are contingent on the use of domestic over imported goods ('local content subsidies'). These subsidies, such as tax incentives or reduced tariffs affording cheaper access to imported products, are granted to industries that agree to use a certain level of domestic input products in the final product. The automotive industry is an example of an economic sector in which these subsidies are frequently applied. In practice, foreign subsidies are not likely to fall under either of these types of prohibited subsidies, and thus be addressed in the WTO framework. The foreign subsidising government would have no economic interest either in giving a subsidy to a firm to encourage it to increase its exports from the foreign territory, thereby creating jobs and generating taxes there (in the case of the export subsidy), or in giving it financial support to make greater use of local goods of another country (in the case of local content subsidies).

Services are governed by the General Agreement on Trade in Services (GATS), which does not contain equivalent rules on subsidies or countervailing measures. Furthermore, the SCM Agreement provides some flexibility for developing countries. It exempts least-developed countries, countries with a gross national product (GNP) of less than US$1 000 per capita, and 'other developing countries' from the rules on prohibited export subsidies. Forms of permitted subsidies include general ones such as financial incentives, credit finance, infrastructure financing, subsidies on services, sector-specific subsidies (even though they are actionable) and subsidies in support of research and development and innovation.[3] While the EU has a strict domestic State aid framework, its scope does not cover subsidies granted by foreign governments, even when they have an effect on the EU single market. It is worth noting that the EU State aid rules are stricter than the WTO framework in terms of scope of application, penalties and possibilities to contest.

Table 1 – Comparison of the EU State aid framework and the WTO subsidy rules

Issue	EU	WTO
Main principle	State aid is considered illegal and incompatible with the internal market.	Export and local content subsidies are prohibited.
Exceptions	There are few exceptions, for instance: aid promoting an important project of common European interest, aid remedying a serious economic disturbance or natural disaster, or block exemptions.	Other subsidies are 'actionable', i.e. allowed in principle but, like prohibited subsidies, are subject to challenge either through multilateral dispute settlement or countervailing action.
Scope	Economic activity: goods, services, capital	Trade in goods
Time of application	All State aid, unless covered by exceptions, must be notified for approval by the Commission.	Rules are triggered only if a member challenges an existing subsidy.
Claimants	Any third party (also individuals and competitors affected by the measure in question) can bring legal action before national courts against the granting Member State and beneficiary.	A WTO member government can request consultations with another government under the WTO dispute settlement procedures.
Penalties	Withdrawal of aid and recovery of amount granted	Withdrawal of subsidy, removing its adverse effects or imposition of countervailing duties

Source: Prepared by the author on the basis of the texts mentioned above, a comparative analysis from Lund University, Sweden, and a UK House of Commons Library briefing.

The EU has been trying to advance subsidy policy at WTO level, coordinating its efforts since 2017 with the US and Japan. In January 2020, EU, US and Japanese trade representatives issued a joint statement in which they pointed to the need to strengthen WTO rules on industrial subsidies. They furthermore argued that the current list of subsidies prohibited under the WTO rules is insufficient to address market and trade-distorting subsidisation ongoing in certain jurisdictions, and therefore new types of unconditionally prohibited subsidies should be added to the SCM. In the context of the 2021 trade policy review, the EU announced that it would begin developing proposals for WTO rules that can tackle various competitive distortions occurring due to state intervention in the economy, including industrial subsidies. WTO-level solutions are however very challenging to find within a reasonable timeframe, and it takes time before the subsidy process is suspended. The Organisation for Economic Co-operation and Development (OECD) has estimated – based on a sample of the 306 largest manufacturing firms in 13 industrial sectors – that below-market finance amounted to approximately US$66 billion over the 2005-2019 period.

Existing situation

When it comes to subsidies granted abroad – similar to the WTO, of which it is a member – the EU does not outright prohibit them. This is because some subsidies are deployed to achieve domestic or social policies, such as aiding selected economic sectors to generate jobs. They can also incentivise companies to invest in research and development, which would have spill-over effects to industry and society, or to finance environmental goals. This is widely accepted in economics; for example, the IMF considers that some subsidies can be a good policy tool when used to correct market imperfections.[4] Subsidies can also play a positive role for developing countries and for the transformation of centrally planned economies into market economies.[5] On the other hand, in today's highly interlinked world, unfair subsidies can distort the EU market, create unfair competition and cause damage to sectors of the EU economy. The key issue is that there is a legal gap with regard to addressing a specific kind of public financial assistance to enterprises – distortive foreign subsidies – across EU policies that touch upon trade, competition, state support and the level playing-field more generally.

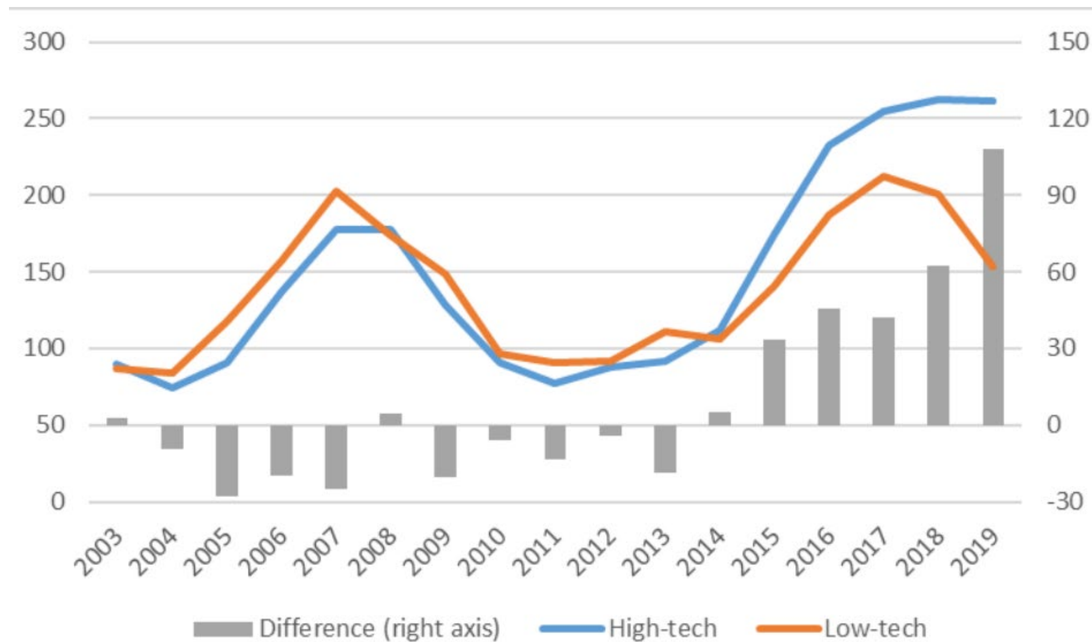
Provisions on subsidies in bilateral free trade agreements (FTAs) vary to a significant degree. The majority of FTAs have provisions on subsidies with regard to transparency obligations and bilateral consultations. Some also include provisions that prohibit particularly harmful subsidies, such as unlimited state guarantees. A smaller number, namely agreements signed with some neighbouring countries, include a commitment to establish a subsidy control system not much different from EU State aid rules. While theoretically FTAs are best placed to identify and address distortive foreign subsidies, the Commission underlines that they also generally lack remedies that can address such distortive subsidies in a timely manner, in part because countervailing duties take time to implement.

There is also a unilateral system in place regarding subsidies that distort trade and cause injury to EU industry. In such cases, the EU can deploy its anti-subsidy rules. After an investigation, the Commission may apply a countervailing duty to counterbalance the negative effects of the subsidised imports and restore fair competition.[6] EU trade defence instruments (and the WTO subsidy rules) permit such action when subsidised goods are imported into the single market – but not when subsidies take the form of subsidised investments, acquisitions or bids in procurement procedures or when they concern services and financial flows. Neither services nor actions by externally-subsidised companies in the EU that do not concern any trade in goods are therefore covered. This regulatory gap extends to other areas as well. EU rules prohibit mergers and acquisitions that would distort competition in the single market to a significant extent. These rules are designed to disallow the creation or the strengthening of dominant companies that are likely to raise prices for consumers. However, these rules do not equip the Commission with the tools to enable it to assess whether a company involved may have benefited from distortive foreign subsidies.

As shown in Figure 1, the issue is increasingly assuming strategic importance: cross-border merger and acquisition flows into the EU high-technology sector have grown substantially in recent years.

The Commission argues that in some cases, the granting of foreign subsidies may be driven by a strategic objective to gain access to and later transfer technologies to other, possibly external, production sites.

Figure 1 – Cross-border merger and acquisition flows into the EU



Source: European Commission, JRC, 2021.

State aid rules apply when financial support granted by EU Member States to undertakings distorts or threatens to distort competition in the single market. However, these rules do not cover financial support granted by third-country public authorities, or on their behalf, to firms in the EU.

The framework for screening foreign direct investment (FDI), adopted in March 2019, aims to mitigate risks stemming from foreign takeovers and investments. It is limited to threats to Member States' security and public order, and does not address the need to ensure a level playing-field. In essence, the framework aims to enhance cooperation and information-sharing on FDI screening between the Commission and the Member States, but only on those investments that are likely to have effects on critical assets and infrastructure. The FDI Regulation subsequently adopted states that 'it should also be possible for Member States and the Commission to take into account the context and circumstances of the foreign direct investment, in particular whether a foreign investor is controlled directly or indirectly, for example through significant funding, including subsidies, by the government of a third country or is pursuing State-led outward projects or programmes'. On the minimum relevant information shared it says that it 'should include aspects such as the ownership structure of the foreign investor and the financing of the planned or completed investment, including, *when available*, information about subsidies granted by third countries'. As such, it lacks an effective mechanism for obtaining information on foreign subsidies.

A similar situation exists on the procurement market, which is one of the largest (around €2 trillion a year) and the most accessible in the world. The directives on public procurement cover tenders above specified thresholds agreed under the WTO Agreement on Government Procurement. The main principles of these directives are transparency, equal treatment, open competition, and sound procedural management. Their aim is to achieve a European procurement market that is competitive and open to fair competition. However, this framework does not have tools dedicated to addressing distortions to the EU procurement markets resulting from foreign subsidies. There is

no way to verify if bidders are supported by third-country governments. Moreover, it is not mandatory for the contracting authorities to investigate the existence of foreign subsidies when evaluating offers, and no specific legal consequences would ensue should distorting foreign subsidies actually be present. Directives 2014/24/EU and 2014/25/EU permit contracting authorities to reject abnormally low offers if a bidder has obtained State aid that is incompatible with the internal market (under Article 107 of the Treaty on the Functioning of the European Union, TFEU). They do not however contain an equivalent provision for foreign subsidies. Similarly, the proposed international procurement instrument deals with reciprocity of access, not subsidies. While intergovernmental agreements, concluded to facilitate investment, may cover the organisation of procurement, they are not designed to scrutinise the distortive effects of foreign subsidies.

These issues highlight that there is indeed a gap in the EU toolbox. While the EU economy is open and based on fair competition, this lack of efficient measures creates an uneven playing-field and distorts the internal market in various ways.

Parliament's starting position

Parliament's resolution of 5 July 2017 on building an ambitious EU industrial strategy as a strategic priority for growth, employment and innovation called on the Commission to 'pay more attention to the role of foreign-based state-owned enterprises that are supported and subsidised by their governments in ways that EU single market rules prohibit for EU entities'.

In its resolution of 26 November 2020 on the trade policy review, Parliament called on the Commission to deepen its international cooperation with strategic partners and welcomed 'the ongoing discussions on how to address and effectively mitigate distortions caused by industrial subsidies, knowing that market-distorting practices can have considerable negative impacts on fair competition and the level playing-field'. It also welcomed the white paper on foreign subsidies as a 'necessary complementary tool to trade defence measures'.

Council and European Council starting position

In its conclusions of 22 March 2019, the European Council highlighted: 'Fair competition should be ensured within the single market and globally, both to protect consumers and to foster economic growth and competitiveness, in line with the long-term strategic interests of the Union. We will continue to update our European competition framework to new technological and global market developments. The Commission intends to identify before the end of the year how to fill gaps in EU law in order to address fully the distortive effects of foreign state ownership and state-aid financing in the single market'.

In December 2019, the Netherlands published a non-paper on 'Strengthening the level playing-field on the internal market'. It recognised the problem of foreign states financing entities operating on and distorting the single market. The document proposed that 'economic operators with (discriminatory) aid benefits and unregulated market power should be subject to stricter supervision, in order to prevent potentially disruptive behaviour'. Companies to be scrutinised would be those towards which there is a reasonable suspicion that they follow potentially distortionary conduct, enabled by government support or excess profits from an unregulated dominant position in their own country. The Dutch government suggested granting the European Commission powers to conduct an ex-ante investigation into any such company's conduct, with a focus on transparency in accounting.

Preparation of the proposal

On 17 June 2020, the European Commission adopted a white paper dealing with the distortive effects caused by foreign subsidies in the single market. This laid the foundations for the 2021 draft regulation on the same subject. The white paper presented the rationale for tackling foreign subsidies, including typical examples of situations where they affect the level playing-field in the

internal market. The white paper also analysed the existing legal instruments and the issue of the regulatory gap, listing potential new tools to close it. It tabled three options (modules) aimed at addressing the problems identified: in the single market generally, in acquisitions of EU companies, and during EU public procurement procedures. It also discussed distortive foreign subsidies in the context of EU-funded projects.

The paper was followed by an intensive consultation process aimed at collecting comments on a broad range of aspects from all of the parties concerned: a public consultation, followed by a stakeholder consultation on the inception impact assessment, which outlined various policy options, and targeted consultations with the most relevant stakeholder representatives.[7] A majority of respondents welcomed the proposal and agreed on the need for action.[8] Many stressed the need for proportionate measures not to stifle FDI, and there were some concerns about the administrative burden and consistency of application. The feedback from the targeted consultations was used to generate examples of types of subsidies, sectors affected and distortive effects. These were discussed in the impact assessment and used to shape the proposal.

The Commission carried out an impact assessment setting out four options: i) taking no action (*status quo*); ii) issuing guidance on existing EU legislation; iii) changing existing EU rules; and iv) developing a new legal instrument. The preferred policy option was to create a new legal tool, based on mandatory notification for major acquisitions and public procurement cases, and an *ex officio* system for smaller cases and other market situations not covered by notifications. The impact assessment received a positive opinion (with reservations) from the Regulatory Scrutiny Board.[9] The initial appraisal of the impact assessment by EPRS found that it is transparent and based on solid research. Its shortcomings include lack of presentation of operational objectives and limited monitoring provisions, as well as an undetailed estimate of the proposed regulation's potential negative effects.

The changes the proposal would bring

On 5 May 2021, the Commission published a proposal for a regulation on distortive foreign subsidies, together with the updated industrial strategy. The two were bound together because the Commission considered the regulation to be a key element in delivering on the strategy, the aim being to safeguard a fair and competitive single market, creating the right conditions for EU industry to thrive.

Chapter 1 outlines the general provisions and definitions, including a definition of a foreign subsidy (Article 2). A foreign subsidy is deemed to exist where a *third country* provides a financial contribution beneficial to an undertaking engaging in an economic activity in the internal market. It has to be limited to an individual enterprise of an industry or several industries. The types of financial contribution include i) transfer of funds or liabilities, such as capital injections, grants, loans, loan guarantees, fiscal incentives, setting off of operating losses, compensation for financial burdens imposed by public authorities, debt forgiveness, a debt to equity swap or rescheduling; ii) the foregoing of revenue otherwise due; and iii) the provision or purchase of goods and/or services.

Article 3 specifies the cases in which distortion on the internal markets is deemed to exist: i) when the foreign subsidy is likely to improve the competitive position of the undertaking in the internal market, and (ii) when this actually or potentially affects competition negatively. The Commission is to establish that the subsidy is distortive using indicators such as amount, nature and purpose of the subsidy, situation of the undertaking on the markets concerned, and level of economic activity of the undertaking in the EU. A foreign subsidy amounting to below €5 million over any consecutive period of three fiscal years is considered by the Commission unlikely to be distortive.

Article 4 specifies the subsidies that are most likely to distort the internal market. These include subsidies granted to ailing enterprises, subsidies in the form of an unlimited guarantee for debts or liabilities, subsidies directly facilitating a concentration and those enabling an undertaking to submit an unduly advantageous tender.

Article 5 describes the balancing act that the Commission performs, between the negative effects (distortion) of a foreign subsidy and the positive effects it has on the development of economic activity. If the balancing act deems the negative effects stronger, the Commission may impose redressive measures or accept commitments offered by the undertaking.

These are defined in Article 6 and are far-reaching, with the aim of fully and effectively remedying the distortion caused. They include behavioural measures such as offering access under fair and non-discriminatory conditions to infrastructure that was acquired or supported by the distortive foreign subsidies, or reducing capacity or market share. Undertakings may also be asked to refrain from certain investments or offer licensing of assets acquired or developed with the help of foreign subsidies on fair, reasonable and non-discriminatory terms. They may also be required to publish the results of research and development. Structural measures such as divestment of assets are also included. Furthermore, a concentration of the undertakings that was formed using subsidies may be dissolved. Finally the Commission may require repayment of the foreign subsidy to the non-EU country, at an appropriate interest rate.[10]

The following three chapters (2, 3 and 4) deal with the novel investigative tools and procedures. Chapter 2 outlines the provisions for the own-initiative procedure to be taken by the Commission for the *ex-officio* review. It is a general screening tool, enabling the Commission to investigate markets. The Commission may, on its own initiative, examine information from any source pertaining to alleged distortive foreign subsidies. Under this procedure, the draft regulation also proposes granting the Commission far-reaching powers to gather information as part of a preliminary review of the market. These include information requests and inspections within and outside the EU.[11] Based on the findings of the preliminary review, the Commission may open an in-depth investigation that may lead to redressive measures or to the enterprise in question deciding to make commitments such as to repay the foreign subsidy. There could also be a no-objection decision if the preliminary assessment is not confirmed or the balancing test determines more positive than negative effects. The Commission may also take rapid interim measures if there is a serious risk that a foreign subsidy will cause substantial and irreparable damage to competition on the internal market. If the undertaking refuses to cooperate, the Commission may take a decision on the basis of the information available. If the undertaking supplies incorrect, incomplete or misleading information during the investigation or does not comply with imposed redressive or interim measures, the Commission can impose fines and periodic penalty payments. It may also take a new decision if an undertaking acts contrary to its commitments or it appears that the previous decision was taken based on incomplete, incorrect or misleading information.

Chapter 3 contains provisions on *concentrations* arising as an effect of mergers, acquisitions or the creation of a joint venture. Concentrations fall under the scope of the draft regulation if at least one of the merging parties, or an acquired undertaking, is established in the EU and has a turnover of at least €500 million. Furthermore, the undertakings concerned must have received from third countries an aggregate financial contribution in the three calendar years prior to notification of more than €50 million. The same thresholds apply to joint ventures. Above the thresholds, concentrations are deemed 'notifiable' and must be notified ex-ante to the Commission. The acquirer must notify any financial contribution received from a non-EU government in relation to the concentration. In the absence of a notification, the Commission may request it. While the Commission review is ongoing, the concentration cannot be implemented (suspension obligation).[12] If the Commission initiates an in-depth investigation, there could be three possible outcomes: no objection, a decision with commitments, or a decision prohibiting a concentration. If the Commission finds that a concentration has been implemented and that it distorts the internal market, it may require its dissolution. The fines and periodic penalty payments set out in Chapter 2 also apply to notified concentrations. They can be imposed also for the provision of incorrect or misleading information, for failure to notify or for non-compliance with the suspension obligation or a decision prohibiting a concentration.

Chapter 4 deals with *public procurement notifications*. To be covered by the notification obligation, the value of procurement has to be above €250 million. When submitting a tender or a request to participate in a public procurement procedure, undertakings must notify either the contracting authority or the contracting entity of all foreign financial contributions received in the three years preceding the notification or declare that they had not received any such contributions during the same period. The notification should then be sent to the Commission without delay for review. A bidder under investigation cannot be awarded the contract.[13] In the absence of a notification, the Commission may initiate a preliminary review. Based on its findings, the Commission can decide to launch an in-depth investigation, which may end in a decision with commitments to be made by the bidder. If no commitments are offered or those that are offered are insufficient to remove the distortion, the Commission would adopt a decision prohibiting the award of the contract. If the Commission finds that the undertaking does not benefit from the distortive foreign subsidy, it would take a no-objection decision. Fines and periodic penalty payments can be imposed as set out in Chapter 2 in the event undertakings fail to notify or in the event they provide false or misleading information.

The final three chapters contain information on other procedural and general provisions, notably on the rights of defence (opportunity for enterprises to offer observations) and the protection of professional secrecy.

The proposal concludes with a legislative financial statement. It estimates the budgetary impact of the proposal's adoption to be €90.34 million, to be spent within the 2021-2027 multiannual financial framework. Most of the expenditure would be used for the human resources necessary to implement the new regulation.

Table 2 – A simplified comparison of EU competition law thresholds and the proposed foreign subsidies regulation

Issue	EU competition law	Draft foreign subsidies regulation
Notification duty	Public support exceeding €5 million per undertaking per year	A foreign subsidy amounting to above €5 million over any consecutive period of three fiscal years
Mergers and acquisitions	Notification required when i) a combined worldwide turnover of all the merging firms is over €5 000 million; and ii) EU-wide turnover for each of at least two of the firms is over €250 million	The turnover of the EU target (or at least one of the merging parties) exceeds €500 million and the foreign financial contribution exceeds €50 million over the previous three years
Procurement thresholds	Tenders exceeding €5 350 000 must be published in the Official Journal.	When the estimated value of the procurement in question exceeds €250 million, bidders must notify the subsidies.

Source: Prepared by the author based on European Commission information.

Advisory committees

The European Economic and Social Committee (EESC) adopted its opinion in October 2021 (Rapporteur: Maurizio Mensi, Group III – Diversity Europe, Italy). The Committee supports the proposed regulation but calls for simplifications and more clarity on certain issues such as the types of subsidies that will be given priority, the details of the balancing act and the regime for *ex-officio* investigations in the procurement markets. It also calls for raising the €5 million threshold to avoid minor cases and for the establishment of a helpdesk to facilitate compliance of businesses with the new regulation.

National parliaments

The deadline for national parliaments to submit reasoned opinions on grounds of subsidiarity was 22 July 2021. The Czech Senate drew attention to the potential increases of the administrative burden and considered it unnecessary to strengthen the Commission's decision-making powers. The French Sénat suggested that the Commission give a broader mandate to national authorities (for example, in the monitoring of remedies and commitments), while also claiming that the behavioural remedies should be preferred, and that the €5 million threshold to launch investigation and the €200 million threshold for notification of concentrations are too high and need to be reviewed.

Stakeholder views[14]

BusinessEurope calls the proposal 'a step in the right direction', adding that many of the recommendations of the EU business community, expressed in the context of the white paper, have been taken on board.

The European Trade Union Confederation (ETUC) welcomes the proposal and the Commission's efforts to address unfair practices and the uneven playing-field in relation to foreign subsidies. It calls for more trade mechanisms against distortions of the single market caused by unfair international competition.

AEGIS Europe, a manufacturing industry alliance, broadly supports the draft regulation as a chance to close a major legal gap. However, it considers the €5 million threshold for triggering investigations to be too high (as compared with the internal market State-aid threshold – see Table 2). It also calls for more detail on the involvement of industry in opening investigations, on the application of the balancing test, and for clarifications regarding timelines. AEGIS also calls for more clarity on potential overlaps with WTO subsidies disciplines or countervailing actions.

The American Chamber of Commerce to the EU supports the Commission's efforts to strike a balance between fair competition and open trade when addressing foreign subsidies. It has however cautioned that the proposed mechanisms may impose important additional compliance requirements on already transparent firms, while still not gathering essential information or properly targeting distortive practices. As such, they may unintentionally hamper legitimate investments.

The China Chamber of Commerce to the EU raises concerns that the new regulation, together with the FDI screening instrument and antitrust review in place, could trigger multiple reviews of Chinese investments in Europe, increasing transaction costs and risks and creating uncertainty over timelines and outcomes.

Bruegel senior fellow Alicia García-Herrero argues that the new measure may not be sufficient to improve the level of the playing-field in the single market and eliminate distortions. This is because these distortions are created by dominant, government-related companies in China, which use profits generated on the domestic market (also to the detriment of the Chinese private sector) to subsidise operations abroad and grow their market share. Furthermore, implicit subsidies can be difficult to quantify, as they may originate from lower-interest payments per debt and/or a lower tax burden than one borne by competitors in an enormous market like China's.

Legislative process

In the European Parliament, the file was allocated to the INTA committee, and Christophe Hansen (EPP, Luxembourg) was appointed rapporteur. The draft report was published in December 2021 and the INTA committee adopted its report in April. The European Parliament voted on the report during its May plenary session, with 627 votes for, 8 against and 11 abstentions, setting its negotiating position for trilogue.

The Council adopted its negotiating mandate on 4 May 2022 and intensive trilogue negotiations commenced, concluding with an agreement on 30 June.

The European Parliament negotiators ensured that state-owned companies are included in the scope of the regulation. Furthermore, they successfully insisted that (non-monetary) support measures, that are economically equivalent to a financial contribution, must be considered as a financial contribution. These could include obtaining privileged access to domestic market and granting exceptions to applicable rules.

The MEPs also specifically provided the Member States, enterprises and other interested parties with the possibility to inform the Commission about the potential distortive subsidies. The European Parliament negotiators shortened the timeframe for the Commission to investigate subsidies in public procurement. Furthermore, the time for the Commission to retrospectively investigate subsidies has been shortened from 10 to 5 years. To increase legal certainty and transparency, the MEPs obliged the Commission to issue guidelines on how it assesses the distortive nature of foreign subsidies and to provide more details on the balancing act (evaluating both the market distorting effects of a subsidy and its potential benefits). The MEPs also secured the possibility for companies to approach the Commission and verify if they need to disclose the subsidies granted to them. The MEPs pushed for the requirement that the Commission engage with countries that have repeatedly granted distortive subsidies. The Commission is also obliged to pursue negotiations on subsidies reform at the WTO level. Once multilateral rules are agreed, the EU regulation will become redundant. Parliament negotiators secured an annual reporting obligation for the Commission, defined in more detail the concept of distortive foreign subsidies and expanded the tool kit for redressive measures.

The European Parliament adopted the agreed text at its November 2022 plenary session and the final act was signed on 14 December. The regulation was published in the Official Journal on 23 December 2022 and entered into force on 12 January 2023.

EUROPEAN PARLIAMENT SUPPORTING ANALYSIS

Kramer E., Tackling distortions of foreign subsidies, initial appraisal of a Commission impact assessment, EPRS, European Parliament, July 2021.

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OTHER SOURCES

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ENDNOTES

[1] Data from 2020 shows that the FDI flows to EU countries nosedived during the pandemic by 70 %.

[2] The WTO defines a countervailing measure as: 'Action taken by the importing country, usually in the form of increased duties to offset subsidies given to producers or exporters in the exporting country'.

[3] For the specific issue of China's status as a developing member of the WTO, see a 2019 Centre for European Policy Studies (CEPS) analysis.

[4] 'Market imperfection', also often referred to as 'market failure', occurs when competitive private markets fail to allocate resources efficiently or to deliver socially desirable outcomes.

[5] For a more detailed commentary on the integration of China into the WTO, see this 2019 Bruegel working paper.

[6] However, the subsidy must be specific (limited) to a firm, industry or group of firms or industries. Export subsidies and subsidies based on using domestic goods over imported ones, are specific as well. However, a subsidy that applies generally, such as one helping all SMEs, is not considered specific. Apart from subsidies being specific, there are three other conditions: i) there must be material injury to the EU industry producing similar products; ii) there must be a causal relationship between the subsidised imports and the material injury; and iii) the measure should not cause more harm to the EU economy than the positive effect it causes on the industry affected by the imports.

[7] The inception impact assessment report proposed, among other things, an option that entailed changing the international rules. This was not however included in the impact assessment accompanying the proposal.

[8] The Commission used the feedback from the targeted consultations to provide examples of types of subsidy, sectors affected and tangible distortive effects. These were discussed in the impact assessment and taken into account when shaping the proposal.

[9] The board outlined the following shortcomings to be rectified: '(1) The report does not clearly establish when foreign subsidies are problematic and when they are not; (2) The presentation of policy options is too complex and does not focus on the issues that matter most to the decision makers. The content of the options and their interaction with existing instruments is not sufficiently clear; (3) The report does not clearly explain how an EU interest test would be applied. (4) The report does not present the positive and negative impacts in a balanced way'.

[10] Article 6(6) contains specific details on the repayment of the subsides: 'Where the undertaking concerned proposes to repay the foreign subsidy including an appropriate interest rate, the Commission shall accept such repayment as commitment if it can ascertain that the repayment is transparent and effective, while taking into account the risk of circumvention'.

[11] These can take place providing the undertaking concerned has given its consent and the government of the third country has been officially notified and has agreed to the inspection.

[12] After the Commission receives the complete notification, the concentration shall not be implemented for a period of 25 working days. However, if within these 25 days the Commission opens an in-depth investigation, the concentration cannot be implemented for a period of 90 working days, followed by a further 15 days if the enterprises concerned offer commitments.

[13] The Commission has 60 days for a preliminary review and 200 days to conclude an in-depth analysis.

[14] This section aims to provide a flavour of the debate and is not intended to be an exhaustive account of all different views on the proposal.

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