



THE EUROPEAN COMMISSION PROPOSES A NEW INSTRUMENT TO ADDRESS FOREIGN SUBSIDIES DISTORTING THE INTERNAL MARKET

By *CAROLE MACZKOVICS*
Avocat/Advocaat
Partner
DALDEWOLF

The Commission proposed, on 5 May 2021, a [brand new instrument](#) mimicking the EU State aid discipline, allowing it to scrutinise foreign subsidies distorting the internal market. On that basis, the Commission would be empowered to block large public procurements or concentrations with a company that has received foreign subsidies distorting the internal market, or at least, to remedy such distortive effects. The Commission would also be entitled to investigate any other market transaction involving such a company and have the distortions remedied. Stakeholders may [comment](#) on the proposal until mid-July to feed in the coming legislative debate.

I. Introduction

On 5 May 2021, the European Commission (Commission) has adopted a [proposal](#) for a ‘Regulation on foreign subsidies distorting the internal market’. This proposal follows the adoption of a [White Paper](#) in June 2020 and a consultation process with stakeholders. It is part of the actions set out for a [New Industrial Strategy](#) issued by the Commission in March 2020, aiming to help the EU’s industry in its transition towards climate neutrality and digital leadership while ensuring its competitiveness in times of ‘moving geopolitical plates and increasing global competition’. It is a response to the European Council’s call of March 2019 for a comprehensive and long-term EU industrial policy Strategy along with an integrated approach for a deeper and stronger single market, notably in the aftermath of the aborted fusion between Alstom and Siemens aimed at counterweighing the largest rail rolling stock manufacturer worldwide, the Chinese CRRC.

In the [White Paper](#), it is recognised that openness to trade and investments is ‘part of the economy’s resilience’, but it is said to be challenged by unfair practices. While the EU already has a State aid control mechanism regarding advantages granted by EU Member States, foreign subsidies are not subject to any comparable discipline. According to the Commission, potential market distortions may arise due to foreign subsidies, as they provide an advantage to the beneficiaries over undertakings engaged in an economic activity in the EU without subsidies.

As explained by the Commission in its [press release](#), the aim of the proposed regulation is to fill the legislative gap in EU competition, trade and public procurement rules, that currently do not allow the EU to take action when foreign subsidies cause distortions in the internal market. In its proposal, the Commission borrows State aid law concepts and procedures to build up this brand new instrument.

II. Blocking or removing the distorting effects of a transaction with a foreign State sponsored undertaking

A. The proposed tools at a glance

The new instrument consists of three tools to be used by the Commission:

- 1) A notification-based tool to investigate concentrations where the target undertaking established in the Union generates at least €500 million of turnover in the EU and where the undertaking concerned received from third countries a financial contribution of €50 million or more in the three years prior to the notification;
- 2) A notification-based tool to investigate public procurement procedures where the estimated value of that public procurement is equal or greater than €250 million and where the candidate or the tenderer, as well as its main subcontractors or suppliers (ie representing more than 30% of the estimated contract value) received foreign subsidies in the three years prior to the submission of the tender or request to participate in the public procurement procedure;
- 3) A general tool to investigate *ex officio* all other market situations, including smaller concentrations and smaller public procurement procedures or for instance, public

procurement procedures in the defence sector. This tool would be left to the discretion of the Commission.

B. Insight into the proposed tools

1) Notifiable concentrations

Notifiable concentrations would have to be notified prior to their implementation and following the conclusion of the agreement, the announcement of the public bid, or the acquisition of a controlling interest.

The responsibility to notify the transaction lies with the parties to the merger or the parties acquiring (joint) control. In the event of failure to notify, the Commission would not be bound by any time limits for its review and fines not exceeding 10% of the aggregate turnover of the undertaking concerned may be imposed.

On pain of invalidity or fines, notifications would have a suspensive effect on the transaction. It is proposed that a notifiable concentration may not be implemented before:

- it has been declared not to distort the internal market,
- 25 working days elapsed from complete notification, or
- when the Commission initiates an in-depth investigation within that period, 90 working days as possibly extended with an additional period of 15 working days when the undertakings concerned offer commitments to remedy the distortion on the internal market.

Following an in-depth investigation, the Commission would be able to adopt

- a decision with commitments,
- a no objection decision, or
- a decision prohibiting a concentration, where it finds that a foreign subsidy distorts the internal market.

2) Notifiable public procurement procedures

The responsibility to notify the transaction would lie with the undertaking having received the foreign subsidy. This responsibility extends to the main subcontractors or suppliers (ie representing more than 30% of the estimated contract value). On pain of not being awarded the contract or fines, the notification of foreign subsidy received over the past three years (or declaration of absence thereof), would have to be made to the contracting authority or entity, that will transfer the notification to the Commission.

The contract would not be awarded to a notifying undertaking before:

- the foreign subsidy has been declared not to distort the internal market,
- 60 days elapsed from complete notification, or
- when the Commission initiates an in-depth investigation within that period, 200 days after receipt of the notification.

Following an in-depth investigation, the Commission would adopt:

- a decision with commitments, in which case the contract may be awarded to the economic operator having notified receipt of foreign subsidy,
- a no objection decision, or
- a decision prohibiting the award of the contract, where it finds that a foreign subsidy distorts the internal market. In such a case, the contract may be awarded to the next best tender without relaunching the whole tender process.

3) *Ex officio* investigations

The Commission would be entitled to examine, on its own initiative, information from any source regarding alleged distortive foreign subsidies. Information could be submitted by competitors to

the beneficiary, but the proposal does not provide for any specific complaint procedure and they would not be given any specific status in the investigation neither.

The Commission would also be able to conduct a market investigation in case of suspicions of distortive foreign subsidies in a particular sector, for a particular type of economic activity or based on a particular subsidy instrument. The results of such market investigation could be published and used by the Commission to launch an *ex officio* investigation in any market transaction.

III. Existence of a distortive foreign subsidy

A foreign subsidy would be deemed to exist where (i) a third country (including any public or private entity whose actions can be attributed to the third country) (ii) provides a financial contribution (including the foregoing of revenues) (iii) which confers a benefit to an undertaking engaging in an economic activity in the internal market (iv) and which is limited, in law or in fact, to an individual undertaking or industry or to several undertakings or industries.

It would be deemed to distort the internal market (i) if it is liable to improve the competitive position of the undertaking concerned in the internal market and (ii) where, in doing so, it actually or potentially negatively affects competition on the internal market. The Commission suggests several indicators that may demonstrate whether a subsidy could have a distortive effect on the internal market: (i) the amount and (ii) the nature of the subsidy; (iii) the situation of the undertaking and the markets concerned; (iv) the level of economic activity of the undertaking concerned on the internal market; (v) the purpose and conditions attached to the foreign subsidy as well as its use on the internal market.

The proposal lists the categories of foreign subsidies that are most likely to distort the internal market as foreign subsidies granted (i) to an ailing undertaking, that is likely to go out of business in the short or medium term without any subsidy; (ii) in the form of an unlimited guarantee for debts or liabilities of the undertaking, meaning without any limitation as to the amount or the duration of such guarantee; (iii) directly facilitating a concentration; (iv) enabling an undertaking to submit an unduly advantageous tender, on the basis of which the undertaking would be awarded the public contract.

However, foreign subsidies below €5 million over any consecutive period of three fiscal years would not be considered as distortive.

The Commission would have to make a balancing test between the negative effects of the foreign subsidy and the positive impact it might have on the economic activity concerned, and take such balancing into account when deciding on redressive measures or accepting commitments.

IV. General procedural rules

The new instrument would be exclusively enforced by the Commission. The undertakings having received foreign subsidies would be the addressee of the Commission's decisions, contrary to State aid control where the procedure is engaged between the Commission and EU Member States.

A. Preliminary review of the foreign subsidy

The Commission would first proceed to a preliminary review where it seeks whether the financial contribution granted to an undertaking is to be considered as a foreign subsidy and whether it distorts the internal market. In so doing, it can request information from the undertaking itself, from other undertakings or associations of undertakings, from Member States and even from the concerned third country. Officials authorised by the Commission to conduct an inspection would be given large investigating powers, such as entering the premises and land of the undertaking, even outside the EU, provided in this latter case that the undertaking has given its prior consent and the third country has agreed to the inspection. In case of a lack of cooperation or incorrect information, the Commission would nonetheless be able to take a decision on the basis of the facts available. Fines and periodic penalty payments could be imposed on undertakings that supplied misleading, incorrect or incomplete information, whether intentionally or negligently or refused to submit to inspections within the EU.

In order to restore competition in the internal market where necessary and to prevent irreparable harm, the Commission would be given the power to adopt interim measures where (i) there would be indications that a financial contribution constitutes a foreign subsidy and distorts the internal market; and (ii) there would be a serious risk of substantial and irreparable damage to competition

on the internal market. It could also order those measures where a concentration would have been implemented in breach of the prior notification obligation or in breach of a decision with commitments.

Where the Commission considers that an undertaking has received distortive foreign subsidy, it would adopt a decision to initiate an in-depth investigation, and invite interested parties to express their views, otherwise, it would close its investigation.

B. In-depth investigation in a foreign subsidy

After its in-depth investigation, if the Commission finds that a foreign subsidy distorts the internal market, it would be able to adopt a decision imposing redressive measures or accepting commitments offered by the beneficiary, both solutions being a remedy to the distortion. Reporting and transparency reports may also be required.

The redressive measures or commitments could consist of reducing the market presence of the undertaking, divestments, repayment of the foreign subsidy including the interest rate, etc.

Failure to comply with a Commission decision imposing interim or redressive measures or accepting commitments may lead to the imposition of fines of up to 10% of the aggregate turnover of the undertaking concerned in the preceding year or periodic penalty payments of up to 5% of its daily aggregate turnover.

C. Time limits to the Commission's action

The Commission would be limited in time to act on this matter. Regarding the in-depth investigation it might want to conduct, the Commission would have ten years to proceed, starting the day on which the subsidies were received. It would have three years to impose fines and periodic penalty payments for infringements under the Regulation. The period would start the day on which the infringement took place or, in case of continuing or repeated infringements, on the day on which it ceases. The Commission would have powers to enforce its decisions for five years starting the day it would take a decision.

V. Approximation of laws in the internal market and implementation of the common commercial policy

The proposal is based on Articles 114 (internal dimension) and 207 (external dimension) of the Treaty on the Functioning of the European Union (TFEU).

Article 114(1) TFEU relates to the adoption through the ordinary legislative procedure of measures for the approximation of laws of the Member States which have as their object the establishment or the functioning of the internal market.

The proposal also relies on Article 207 TFEU. This provision governs the EU's trade policy, and more specifically the scope of the Union's common commercial policy. The first paragraph provides that the common commercial policy is based on uniform principles, particularly with regard to 'measures to protect trade such as those to be taken in the event of dumping or subsidies'. The proposal therefore falls within the scope of the second paragraph of Article 207 TFEU which provides 'for the adoption of measures defining the framework for implementing the common commercial policy', in accordance with the ordinary legislative procedure.

VI. Next steps

A. Ordinary legislative procedure

The proposal has been submitted in accordance with the ordinary legislative procedure, meaning that the Commission has sent the draft to all the national parliaments and submitted it to the European Parliament and Council for examination. These institutions have the possibility to bring amendments to the initial text of the Commission before final adoption.

B. Stakeholders consultation

The Commission's proposal is open for feedback from 7 May 2021 to 22 July 2021 (midnight Brussels time). Feedback may be provided by any stakeholder [here](#) and will be summarised by the Commission and presented to the European Parliament and Council with the aim of feeding into the legislative debate.

C. Transitional provisions

On the basis of proposed transitional provisions, the Regulation would have a retroactive effect in specific situations.

The Regulation would be applicable as from 6 months after its entry into force, but the Commission would be entitled to investigate foreign subsidies granted up to ten years prior to that date, provided that those subsidies would still have a distortive effect on the internal market.

The Regulation would also apply to foreign subsidies granted up to three years prior to its date of application, if the contributions were granted to an undertaking notifying a concentration or financial contributions in the context of a public procurement procedure pursuant to the Regulation.

On the other hand, the Regulation would not apply to concentrations for which an agreement was concluded, a public bid was announced, or a controlling interest was acquired before the date of application of the Regulation. The same would go for public procurement procedures initiated before the application of the Regulation.

VII. Conclusions

The proposal creates a new instrument to allow the Commission scrutinise subsidies granted by non-EU countries to undertakings active in the EU. The tools proposed are capable to suspend and even block large concentrations and public procurements. They would further give the Commission a large margin of discretion to address distortions in the internal market caused by foreign subsidies in any market situations. The proposal relies on a set of enforcement powers granted to the Commission that, combined with the possibility to adopt decisions on the basis of 'available facts' and the validity risks on the transactions, may prove disciplining.

This instrument is largely built upon EU State aid control. Therefore, some concepts the application of which might be considered as unclear or uncertain, may eventually follow an interpretation that is comparable to the one of the EU Courts in State aid cases.

This proposal is of interest to many stakeholders. Besides undertakings benefitting from public advantages outside the EU, that would be the first concerned by the new instrument, EU undertakings engaging in M&A activities or contracting authorities and entities for large or important contracts may wish to give their feedback on the proposal and once adopted, as possibly amended, they may need to factor in this instrument in their processes. The retroactive effect of the proposed Regulation may already call undertakings to take account of past and coming sponsor by non-EU countries in their envisaged growth strategy in the EU.

This newsletter does not constitute any legal advice and merely provides for an update on current developments in fields where our lawyers can be of assistance to interested parties. For any information, please contact Carole Maczkovics, EU State aid & regulatory partner (cmk@daldewolf.com).