Foreign subsidies and public procurement

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Foreign subsidies and public procurement

ABSTRACT

The EU has helped shape an international economic system based on openness and fair competition. Over the past few years, the benefits of this approach have come under pressure from foreign trade practices which undermine the principle of reciprocal treatment. In particular, this is the case with subsidies granted by non-EU governments and protected public procurement markets. This in-depth analysis reviews the state of play of EU policy action on foreign subsidies and in public procurement markets and identifies gaps in existing EU instruments. The analysis shows that the EU took the initiative with: (i) the completed FDI screening and trade defence reforms; (ii) the proposal for an International Procurement Instrument; and (iii) the proposal for a Regulation targeting the distortive effects of foreign subsidies. In addition, the EU is taking the lead at the multilateral level, promoting coordinated action in the WTO, G7, G20, OECD, and GAMS fora.
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# List of abbreviations

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<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>AB</td>
<td>WTO Appellate Body</td>
</tr>
<tr>
<td>AD/CDVs</td>
<td>Antidumping and Countervailing Duties</td>
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<tr>
<td>AMS</td>
<td>Aggregate Measures of Support</td>
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<tr>
<td>ASCM</td>
<td>WTO Agreement on Subsidies and Countervailing Measures</td>
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<tr>
<td>ASEAN</td>
<td>Association of South East Asian Nations</td>
</tr>
<tr>
<td>BCS</td>
<td>Business Confidence Survey</td>
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<td>B2B</td>
<td>Business to Business</td>
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<td>EC</td>
<td>European Commission</td>
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<td>EU</td>
<td>European Union</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>GAMS</td>
<td>Government/Authorities Meeting in Semiconductors</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>GNP</td>
<td>Gross National Product</td>
</tr>
<tr>
<td>GPA</td>
<td>Government Procurement Agreement</td>
</tr>
<tr>
<td>GPL</td>
<td>Government Procurement Law of China</td>
</tr>
<tr>
<td>IPI</td>
<td>International Procurement Instrument</td>
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<tr>
<td>LDCs</td>
<td>Least-developed countries</td>
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<tr>
<td>M&amp;A</td>
<td>Mergers and Acquisitions</td>
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<tr>
<td>MFN</td>
<td>Most-Favoured Nation Principle</td>
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<tr>
<td>MS</td>
<td>Member State</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<tr>
<td>RTAs</td>
<td>Regional Trade Agreements</td>
</tr>
<tr>
<td>SCM</td>
<td>WTO Agreement on Subsidies and Countervailing Measures</td>
</tr>
<tr>
<td>SDR</td>
<td>Special Drawing Rights</td>
</tr>
<tr>
<td>SDT</td>
<td>Special and Differential Treatment and Other Special Measures</td>
</tr>
<tr>
<td>SMEs</td>
<td>Small and medium-sized enterprises</td>
</tr>
<tr>
<td>TDI</td>
<td>Trade Defence Instrument</td>
</tr>
<tr>
<td>TFEU</td>
<td>Treaty on the Functioning of the European Union</td>
</tr>
<tr>
<td>TTC</td>
<td>Trade Technology Council</td>
</tr>
<tr>
<td>UNCTAD</td>
<td>United Nations Conference on Trade and Development</td>
</tr>
<tr>
<td>US</td>
<td>United States of America</td>
</tr>
<tr>
<td>UK</td>
<td>United Kingdom of Great Britain and Northern Ireland</td>
</tr>
<tr>
<td>WTO</td>
<td>World Trade Organization</td>
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</table>
Introduction

The EU is, along with the US and China, one of three main global economic players. Building on its key role in world trade, the EU has helped shape a global trade system based on openness and fair competition in all markets. While openness largely benefits EU businesses and workers by providing business opportunities abroad and inward investment, it also requires control over potentially damaging foreign trade practices, such as distortive subsidies for companies operating in the private or public procurement markets.

Subsidies are a powerful tool that governments can use to support domestic firms. While the use of subsidies can be justified by the presence of market inefficiencies, by potential welfare gains from economies of scale or by unexpected economic downturns, it can also be motivated by the desire of governments to create ‘national champions’. In this case, subsidised firms can benefit from unreasonable competitive advantages, with detrimental effects for the economy.

Section 1 introduces the fact that many EU firms compete against highly subsidised foreign rivals in their home market. At the same time, EU firms are often confronted with difficulties in gaining access to foreign public procurement markets, where competition can also be highly distorted by subsidies on top of de jure restrictions. As a result, unsubsidised EU companies suffer an unfair disadvantage, for different reasons, in both private EU markets and EU and foreign public procurement markets.

Section 2 shows that the EU already has a well-diversified toolset to tackle these geo-economic challenges. However, while all tools are interrelated and ultimately help to create a level playing field both domestically and internationally, they have different purposes and some of these tools require an update to be fit for today’s global trading system, as noted by Commission’s White Paper on foreign subsidies of June 2020.¹ This is the case of existing EU trade defence, investment screening, antitrust, merger control and state aid rules which do not directly address the issue of potentially distortive foreign subsidies: in fact, these rules do not include any specific provision assessing how concentrations are financed or assessing whether a subsidy granted by a non-EU country could be deemed as distortive.

The EU has therefore taken three specific policy actions:

I. Updating trade toolsets: The Regulation establishing a framework for screening of FDIs defines the scope of investment screening in the EU establishing EU-wide principles, communications, rules and procedures to be followed by national schemes. In compliance with the rules set by the World Trade Organization, the EU also introduced a set of three main trade defence instruments: anti-dumping, anti-subsidy, and safeguards.

II. Reviewing the EU public procurement framework: Currently, Article 69 of Directive 2014/24/EU allows a contractor to reject an offer where the explanations provided by a bidder do not sufficiently account for an abnormally low price. However, there is no corresponding provision pertaining to third country subsidies. In these cases, the only possible action is to demonstrate that a foreign subsidy impedes the viability of the offer and the bidder’s capacity to execute the contract at the (abnormally low) price offered. To address this, the proposal on an International Procurement Instrument (IPI), as presented by the Commission in 2012 and amended in January 2016, encourages the reciprocal opening of public procurement markets. In accordance with the amended proposal of 2016, the proposed mechanism introduces an investigation process by the Commission that can lead to the imposition of a price adjustment measure on tenders submitted by economic operators originating from the third country.

¹ European Commission (2020). White paper on levelling the playing field as regards foreign subsidies
concerned, while the initial proposal of 2012 provided for the exclusion of these tenders and/or the application of a mandatory price penalty.

III. **Regulating foreign subsidies that have a distorting impact on the EU’s internal market:** The proposed Regulation on foreign subsidies distorting the internal market introduces the concept of ‘foreign subsidy’, describes circumstances where this kind of subsidy could exist and suggests tools to assess whether a foreign subsidy is distorting of the competitive conditions of the EU Single Market. Moreover, the proposed Regulation outlines a set of measures to remedy the distortions caused by foreign subsidies, for instance licensing or granting access on fair terms to R&D results and infrastructures realised through such subsidies, dissolving concentrations, refraining from investments.

Finally, Section 3 shows that **the EU is also working to address gaps at the multilateral level.** The Government Procurement Agreement (GPA) is a plurilateral agreement within the framework of the WTO establishing rules for open, fair and transparent competition in government procurement. However, these rules only apply to covered entities purchasing listed goods and services exceeding a threshold value covered by the agreement, and the overall efficacy is hampered by the absence of key market players, such as China. There has been meaningful progress in integrating almost all BRIC countries, but ongoing negotiations with China have so far been limited to lower workable thresholds than those under the GPA.

Negotiations are ongoing on the modernisation of the WTO Agreement on Subsidies and Countervailing Measures (ASCM). The EU, US, and Japan put forward proposals to address chronic low compliance with subsidy notification requirements, as well as the expansion of the list of prohibited subsidies. **However, the core problem remains that some countries, such as China, enjoy a developing member status** granting Special and Differential Treatment and Other Special Measures (SDT) in WTO agreements. The EU, US, and Japan have repeatedly called for a revision of the current definition of developing country, which they deem outdated and distorting. Finally, the EU is also active at the relevant G7, G20, OECD, and GAMS fora to push for a coordinated effort on the modernisation of rules on subsidies and public procurement.

1. **Foreign subsidies and economic activities**

This chapter provides a classification of different types of subsidies and it analyses their economic importance.

1.1 **A classification of third country subsidies**

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. This rough definition indicates that subsidies can take different forms and pursue a wide variety of policy goals. Nevertheless, several researchers have attempted to provide a system for classifying subsidies. According to Steenblik (2003), the different typologies of subsidies can be organised around the dimensions shown in table 1: purpose, type of recipient and type of instrument used to deliver the subsidy.

**A first dimension along which subsidies can be classified relates to their purpose.** General subsidies are granted to all firms disregarding the sector in which they operate. For example, countries can provide a credit support to all firms in order to sustain their R&D investments. Countries may also decide to grant subsidies to firms that only operate in certain sectors which may face stronger worldwide competition (Steenblik, 2003). For example, subsidies have been extensively used by governments in the agricultural sector with the aim of sustaining productivity and achieving the technical efficiency required to operate internationally (Kumbhakar and Lien, 2010). Similarly, subsidies have been granted by several countries worldwide to sustain fishing fleets and even to support the fossil fuel industry (Kotchen, 2021; UNCTAD,
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While in some cases the provision of subsidies to firms may result in an increase of consumer welfare as market inefficiencies are corrected, often governments may decide to provide subsidies and grant further aid to firms that operate in sectors considered to be of strategic importance. This is often done with the purpose of creating national champions which are able to maintain a dominant presence in the home market and a competitive share in the world market, often to the detriment of a healthy level of competition (OECD, 2009).

Table 1: Classification of subsidies

<table>
<thead>
<tr>
<th>Purpose</th>
<th>Type of recipient</th>
<th>Type of instrument used</th>
</tr>
</thead>
<tbody>
<tr>
<td>General</td>
<td>Consumer</td>
<td>Grant and other direct payment</td>
</tr>
<tr>
<td>Sector-specific</td>
<td>Domestic firm</td>
<td>Tariffs and quantitative restrictions on imports</td>
</tr>
<tr>
<td></td>
<td>International firm</td>
<td>Tax concessions</td>
</tr>
<tr>
<td></td>
<td>State-owned enterprise</td>
<td>Credit support</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Direct provision of goods or services</td>
</tr>
</tbody>
</table>

Source: Author’s elaboration

A second relevant dimension regards the type of recipient of the subsidy. Indeed, governments may decide to grant subsidies to consumers or to firms. Consumer subsidies are typically used to stimulate the use of new technologies. For example, feed-in-tariffs and tax rebates associated with the consumption of certain products or services have been extensively used in the energy sector in Europe and the US to promote the adoption of solar and wind technologies (Chemama et al., 2019). While consumer subsidies also benefit firms due to an increase in the demand for specific products or services, governments can directly help firms expand their production though production subsidies which partially offset the production costs or losses of firms. (Steenblik, 2003). Within the broad category of subsidies granted to firms, an important distinction should be made between those firms that operate only within their home country, those that also operate internationally, and state-owned enterprises (SOE) which may or may not be active at the international level. The latter group have privileges that privately owned competitors do not generally enjoy and they are often heavily subsidised (OECD, 2011). This results in SOEs having strong competitive advantages over rivals even if these are not necessarily based on better performance or superior efficiency (OECD, 2011).

The type of instrument used is another very important dimension along which subsidies can be organised (Steenblik, 2003). The most common type of subsidy is a grant and other direct forms of payment. Grants usually take the form of a time-limited payment to allow a certain firm or a set of firms to sustain certain investments or to cover losses (Steenblik, 2007). Other direct payments are usually linked to the production volume or prices. One common example is the deficiency payment which consists in a monetary transfer that compensates for the difference between a target price for a good and the market price (OECD, 2000).

Governments can also sustain firms indirectly by raising trade barriers such as tariffs or quantitative restrictions on imports or by adopting non-tariff barriers such as quotas, import licensing, sanitary regulations and prohibitions (WTO, WEBa). This will have the effect of raising the price of the good above the actual market price and increase domestic firms’ turnover (Steenblik, 2007). Tax concessions are another common type of subsidy; these can take multiple forms such as a tax exemption when the tax is not paid, a tax credit which reduces a tax otherwise due and a tax deferral which delays the payment of a tax (WTO, 2006). Governments can also support firms by providing credit at a lower interest rate than offered on the financial market, by postponing the repayment of a loan or by requiring less collateral to back up a loan (WTO, 2006). They can further support firms by guaranteeing loans taken through commercial banks which allows firms to obtain more favourable conditions in terms of interest rates (Steenblik, 2007).
Finally, governments can sustain firms without the use of financial instruments but simply through the provision of goods or services other than general infrastructure (Steenblik, 2003).

Disregarding the specific characteristics that different subsidies have, the evidence indicates that most subsidies generally have spillover effects on global trade (Hoekman and Nelson, 2020). This means that while governments grant subsidies with the intention of sustaining their consumers or firms, intended or unintended consequences can occur in foreign markets. Governments can then react by limiting inward foreign direct investment (FDI) or mergers and acquisitions (M&A) by firms that are suspected to have benefited from foreign subsidies or by also adopting export support measures to create a more balanced playing field (Dawar, 2020). Instead, in markets that are open to foreign competitors, the risk of creating an uneven playing field increases, thus putting additional pressure on domestic firms (Steenblik, 2003).

The EU is one of the most open markets to international competition with one of the lowest import tariff averages and one of the most predictable and transparent business environments for foreign investors. Clearly, when one market is open to international competition and the other is not, firms based in the former market are at a competitive disadvantage. One market that typifies this unbalance is the public procurement market. Public procurement accounts for on average 13% to 20% of GDP worldwide, with global expenditure in procurement estimated at nearly USD 9.5 trillion (World Bank, 2020). In the EU public procurement represents 13.3% of GDP, around EUR 2 trillion per year (European Commission, 2021b). While the EU promotes the openness of public procurement to foreign firms and it has committed to increase the ease of accessing public procurement for an increasing set of goods and services, many EU firms are confronted with difficulties in gaining access to non-EU countries’ public procurement markets (European Commission, 2021b). In particular, many countries still adopt de jure preferences in domestic government procurement laws and policies, such as ‘buy national’ provisions (European Parliament, 2017). In addition, access to public procurement is also affected by de facto obstacles such as linguistic, cultural, legal, and administrative barriers (European Parliament, 2017). Despite challenges in comparing the openness of public procurement across different countries due to a lack of data, a European Commission study has highlighted that while the EU has a rather high level of openness to foreign competition in public procurement, other countries such as the US are more closed (European Commission, 2010). More recently, also Cernat and Kutlina-Dimitrova (2020) have shown that EU openness in public procurement is the highest, although the EUR 50 billion worth of public contracts awarded to foreign firms in 2017 only accounts for 2.5% of the EU market.

1.2 Economic importance of foreign subsidies

The deep and long-lasting impacts that subsidies can have on the economy, the environment, and the distribution of income in both society and trade have been extensively investigated (Steenblik, 2007). From a theoretical point of view, when subsidies are introduced in competitive markets, they lead to an economic welfare loss. However, when markets are not competitive there are instances where governments may actually improve economic welfare by introducing certain forms of subsidisation (WTO, 2006). The two most notable situations in which the introduction of subsidies can improve economic welfare arise when an industry is characterised by large economies of scale or when market externalities arise from firms or consumers being able to fully capture the benefits of production or consumption (Pigou, 1920).

For economies of scale, the government can intervene with subsidies to help firms to bear large and fixed cost of entry, such as investments in expensive equipment. In this case, the intervention of the government can be justified by the fact that without subsidies, firms may not be able to sustain the initial costs which will lead them to not produce at all, with resulting loss of economic welfare (WTO, 2006). For example, the public utilities sector is usually characterised by large investments in infrastructure which
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may deter entry. Governments may thus decide to grant subsidies to allow more firms to enter the market and overall increase the level of competition. Likewise, in the presence of market externalities, subsidies may improve economic welfare as the quantity of the good produced or consumed will actually be less than what would be socially optimal (Arrow, 1962). For example, when firms invest in R&D, such investments generate knowledge that cannot be fully appropriated by those who generated it, as knowledge can be utilised also by others. This results in the well-known problem of private underinvestment by firms which justifies government intervention.

However, subsidies have been extensively used by governments in markets that are characterised neither by substantial economies of scale nor by market externalities (Hoekman and Nelson, 2020). Export subsidies, for example, are used to foster the competitive advantage of key industries in the international market. Domestic exporters directly benefit from the subsidy while foreign firms have to compete with lower prices which may force some of them to exit the market (WTO, 2006). Furthermore, if the country introducing the subsidy additionally prevents re-imports, domestic consumers don’t benefit from the welfare gain because they cannot source at a lower price from the international market (Evenett, 2019).

Clearly, subsidies are not the only policy intervention at the disposal of governments. Following the global recession in 2008 and the recent COVID-19 pandemic, governments have adopted multiple policy measures to sustain the economy. To assess the recession of 2008, Evenett (2019) accessed the Global Trade Alert database, one of the databases with most comprehensive coverage of policy interventions affecting cross-border commerce. By 2013, thousands of discriminatory policy interventions affected over 70% of world export and by 2017 many firms were still competing against bailed out and highly subsidised foreign rivals in their home market.

**Figure 1:** Evolution of subsidy measures

![Evolution of subsidy measures (2009-2017)](image)

Source: Author’s elaboration based on [Global Trade Alert](#)

With specific reference to subsidies, the evidence indicates that subsidies made up more than 52% of all measures related to trade and implemented by governments worldwide between 2009 and the end of 2017 (Evenett, 2019). Most of these measures were intended to provide macroeconomic stimuli to the depressed economy slowly recovering from the 2008 economic crisis. However, it is noteworthy that many subsidies remained in place long after the world economy recovered which seems to contradict the temporary nature of the stimulus needed (Hoekman and Nelson, 2020). More importantly, as noted by Evenett (2019), while 30% of the increases in import tariffs and almost 50% of harmful public procurement acts that were implemented worldwide had been annulled by 2017, less than 25% of subsidies (both domestic and export-related) that were introduced have been removed. This suggests
that governments have been generally much more lenient towards subsidies as measures to stimulate the economy and less willing to remove them once the economy has overcome the crisis.

Unfortunately, a more in-depth analysis at the country level on the role played by foreign subsidies in international economic activities is difficult for three main reasons: (i) general lack of data available on the various types of subsidies registered in national accounts, (ii) major differences in coverage of the different subsidy types and (iii) different methods of calculation and classification across industries and countries (Steenblik, 2003). The IMF for example collects data on the share of national expenditure allocated to subsidies but it does not differentiate between the recipient of the subsidy and thus includes all monetary transfers to private and public firms, grants to foreign governments, international organisations, and other government units and social security, social assistance benefits, and employer social benefits. Besides the reasons highlighted above, the lack of data on subsidies granted to firms follows from the application of the WTO Agreement on Subsidies and Countervailing Measures which prohibits subsidies if these are contingent, in law or in fact, on export performance, or on the use of domestic over imported goods. Nonetheless, anecdotal evidence exists of certain countries still heavily subsidising certain industries and this has led to complaints from affected countries. For example, the US, Japan and the EU have raised concerns about China’s subsidisation of the steel industry (Matano, 2021).

2 EU’s existing toolset and plans of action

This Section assesses the different tools that the EU has at its disposal to deal with the challenges presented in Section 1, as well as the initiatives taken to modernise and complement them.

2.1 EU competition policy

The EU competition policy framework is based on three main pillars: antitrust (i.e. cartels and abuse of dominance), merger control and state aid.

2.1.1 Antitrust and merger control

Articles 101 and 102 of the TFEU, and their equivalents under MS laws, prohibit agreements or concerted practices of undertakings which (by object or effect): restrict, distort, or prevent competition; and lead to abuses of dominant positions by undertakings. In particular, Articles 101 and 102 of TFEU define those type of agreements and concerted practices that are likely to be prohibited, such as those agreements which directly or indirectly fix purchase or selling prices or any other trading conditions.

The main legislative text providing the framework for merger control is the EC Merger Regulation (Regulation No 139/2004) on the control of concentrations between undertakings and the Implementing Regulation concerning procedural issues related to the notification of mergers. The Merger Regulation defines what is a ‘concentration’ for the purposes of EU law, setting the economic thresholds (i.e. turnover of the undertakings involved) for a concentration to have EU dimension and the procedures for the Commission to assess whether a concentration would significantly impede effective competition in the common market.

However, existing EU antitrust and merger control rules do not directly address the issue of potentially distortive foreign subsidies. As observed by the European Commission in its recent proposed Regulation (COM/2021/223) on foreign subsidies distorting the internal market, the EU antitrust rules prohibiting agreements (or concerted practices of undertakings) and abuses of dominant positions having the object or effect of distorting competition in the internal market, do not include any specific

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2 Further information on the EU merger control framework is available at: [https://ec.europa.eu/competition-policy/mergers/legislation_en](https://ec.europa.eu/competition-policy/mergers/legislation_en)
provision assessing how concentrations are financed. In fact, the European Commission (2021e) acknowledged these gaps in EU antitrust and merger control rules. In its proposed Regulation on foreign subsidies distorting the internal market, the European Commission introduces a new threshold for a new instrument that would complement the existing legislative framework. A detailed discussion on the proposed Regulation is presented in Section 2.5.

2.1.2 State aid

The basic principles of European state aid control are laid down in Articles 107 to 109 TFEU. The purpose of the general prohibition of state aid is to prevent distortive state intervention in EU cross-border competition within the internal market. It is intended to prevent individual MS, driven by economic or political interests that run counter to the objective of the internal market, from favouring individual companies or sectors of the economy and thus threatening to distort competition in the EU through harmful subsidy races.

In practice, to avoid court challenges, MS need to notify the EC of any measure that could potentially fall under state aid rules. The Commission then judges whether the measure is acceptable or not, weighing the likely impact on the internal market also in light of the possible exemptions. If the state aid measure is deemed unlawful, the EC and national courts enforce the judgment, resulting in a total or partial payback of the aid depending on the conditions.

Since traditional state aid control is directed exclusively towards EU MSs, both in terms of procedure and jurisdiction, it does not cover competition-distorting subsidies from third countries and, thus, cannot work beyond the internal market (Böheim et al., 2021). The European Commission started to address the issue with the White Paper on foreign subsidies (COM(2020) 253 final) and a the proposal for a new Regulation (COM(2021) 223 final), which are examined in section 2.6.

2.2 EU trade defence rules and anti-subsidy action

The EU’s commitment to open markets and free trade holds as long as fair competition is maintained between foreign and EU producers. Therefore, the EU has a set of three main trade defence instruments, in compliance with the rules set by the World Trade Organization: anti-dumping, anti-subsidy, and safeguards.

According to European Commission (2020d), the imposition by the EU of anti-dumping and anti-subsidy duties reduced on average unfair imports by 80 % in 2019 on the previous year. Moreover, within the new measures imposed in 2020 (an increase of ten measures compared to 2019) the Commission countervailed, for the first time, subsidies granted by one country (China) to manufacturing plants based in another country (Egypt) and exporting to the EU (see Section 2.2.2). This element of novelty in the Commission’s practice shows the Commission’s awareness of the issue of foreign subsidies discussed in this paper, together with the power to adapt its enforcement. Table 2 below breaks down the TDI in force in the EU in 2020.

\[3\] At the same time, EU state aid law respects the fact that subsidies are sometimes needed to compensate for market failures or to pursue politically desirable goals that the market cannot achieve without state measures. The prohibition is therefore supplemented by a reservation of permission by the Commission which can be granted upon individual notification of state aid by EU MSs or through general exemptions provided by either sectoral block exemption regulations or specific horizontal state aid frameworks on activities that are justified by reasons of general economic development e.g. public support of R&D&I, SMEs or regional development (Böheim and Friesenbichler, 2016; Cremer, 2016).
Table 2: Number of EU trade defence measures in force

<table>
<thead>
<tr>
<th></th>
<th>Anti-dumping</th>
<th>Anti-subsidy</th>
<th>Safeguards</th>
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<tbody>
<tr>
<td>Anti-dumping</td>
<td>99</td>
<td>18</td>
<td>3</td>
</tr>
<tr>
<td>Anti-subsidy</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Safeguards</td>
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Source: Author's elaboration based on European Commission (2021F)

2.2.1 Anti-dumping

As defined by the Commission, dumping occurs when manufacturers from a non-EU country sell goods in the EU below the sales prices in their domestic market or below the cost of production. In compliance with the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (1994), the EU’s anti-dumping Regulation sets up the legal framework for the Commission to investigate and impose measures against dumping.

Anti-dumping measures are normally duties on imports of products from certain countries, and these duties can be fixed, variable or a percentage of the total value (ad-valorem). In 2017, the EU updated its anti-dumping legislation: previously, the dumping margin was calculated by comparing the domestic prices in the exporting country with the export prices for the goods under investigation. The modernisation introduced in 2017 allows anti-dumping investigations to consider not only prices and costs of the exporting country, but also the likelihood of severe market distortions due to state intervention in the exporting economy. In cases where a market contains several firms operating under the ownership, control or guidance of the state, prices and costs can be distorted and, in such instances, other types of benchmarks are performed. For example, looking at corresponding costs of production and sale in an appropriate representative country with a similar level of economic development as the exporting country.

2.2.2 Anti-subsidy

The Commission’s definition of ‘subsidy’ corresponds to the definition of the WTO discussed in Section 1.1, i.e. a ‘financial contribution by a government, or agent of a government, that confers a benefit on its recipients’ (WTO’s ASCM). As described in Section 2.1.2, subsidies by MSs may promote growth, jobs, and social policies, and are strictly regulated under the EU competition policy framework. However, unfair and unregulated subsidies from third countries can severely damage the EU market and create unfair competition: hence, in compliance with the WTO’s ASCM, the EU Regulation 2016/1037 on protection against subsidised imports establishes rules for imposing countervailing measures to tackle third country subsidies. The possible countervailing measures currently available at EU level are: a percentage increase of the price of the goods object of the investigation; an increase of the price of the goods of a fixed amount per unit; the application to the goods of a minimum import price; and ‘price undertaking’ where the exporter commits to sell the product under investigation above a minimum price. If this commitment is accepted by the Commission, a duty is not imposed.

Notably, on one hand EU state aid control is directed exclusively towards EU MSs, on the other hand, the Regulation 2016/1037 only covers the trade of goods, not addressing investments and services made possible by foreign subsidies. This legislative gap is even more concerning in light of the global trade practices in recent years, such as the creation of Chinese overseas Economic and Trade Cooperation Zones: these have the purpose of gaining access to raw materials, transferring production (excess) capacities and making use of the benefits of trade agreements signed by the host country with third countries, as highlighted in the Commission 39th Annual Report on the EU’s Anti-Dumping, Anti-Subsidy and Safeguard activities and the Use of Trade Defence Instruments by Third Countries targeting the EU in 2020. In fact, the EU’s anti-subsidy cases initiated in the last ten-year period have seen a marked increase in comparison to the previous ten years: notably, China accounted for 14 (44 %) out of 32 cases initiated.
Notably, for the first time, in 2020 the Commission imposed countervailing duties on this type of cross-border financial support: the investigations showed that Chinese-owned companies operated from a Special Economic Zone in the territory of Egypt and were provided with subsidies by the governments concerned, benefitting from exports to the EU. These subsidies created additional capacity and opened new channels for export of subsidised products to the EU, causing injury to EU companies producing the same products.

2.2.3 Safeguards

Safeguards may be adopted by the Commission when imports of a certain product in a specific EU industry are increasing in an ‘unforeseen, sharp and sudden’ manner which threatens to severely affect EU producers. In these circumstances, it is expected that EU producers need some ‘buffer time’ to adapt to the new trade conditions in their market: this buffer is allowed to the industry affected by the sudden increase in imports, under the obligation that the industry restructures in line with the new reality.

In compliance with the WTO’s Agreement on Safeguards, the EU Regulation 2015/478 on common rules for imports provides the Commission with the necessary tools to set up safeguard procedures. However, it should be noticed that safeguards have rarely been used to date as a TDI: as displayed in Table 2, at the end of 2020, only three of the trade defence measures in force in the EU were safeguards.

2.3 EU FDI Screening framework

The EU Regulation establishing a framework for the screening of FDIs entered into force in April 2019 and started applying from October 2020 (Regulation (EU) 2019/452). The new framework aims to coordinate FDI screening between MSs and the Commission, allowing for an effective mechanism that preserves a welcoming environment for foreign investments.

The policy debate originated from the perceived weakening of EU principles of reciprocal treatment, as it appeared from mid-2010s data (Grieger, 2019). In 2016, Chinese FDI flows into the EU reached a record high of EUR 35 billion (Hanemann and Huotari, 2017), while the flow of EU FDIs into China continued to decline. The new wave of Chinese FDI targeted the acquisition of assets in key strategic sectors, such as energy infrastructures and cutting-edge technologies (Grieger, 2017). While some were delayed and others were withdrawn, with Chinese FDIs in Europe falling during COVID-19 at a 10-year low in 2020 (Kratz et al, 2021), the nature of Chinese FDIs sparked a debate over the ability of EU countries to assess the national security viability of FDI flows.

Prior to the 2019 Regulation, the EU had no formal coordination mechanism for FDI screening. National schemes were absent in 12 countries, as shown in Figure 2, and varied greatly both in terms of scope (thresholds, sectors, country of origin) and design (ex-ante, ex-post, type of controller) (European Commission, 2018b). Since then, most countries have updated their national schemes, with 14 countries changing theirs in 2020 alone (Kratz et al, 2021). Among those previously without, the Czech Republic and Slovakia have already notified their new schemes to the EC, while other countries are in the process of doing so (European Commission, WEBc).
Outside of the EU, most major market players, including Australia, Canada, China, Japan, and the US, have a long tradition of formal FDI screening mechanisms (Bath, 2012). All frameworks are based on a broad security concept and allow for extensive discretion by decision-making bodies. While the latter characteristic is often the object of criticism because of the uncertainty it creates, the room for manoeuvre allows for negotiated arrangements, and full rejection sentences are extremely rare (Grieger, 2017).

In March 2019, after a two-year policy debate, the EU translated its own mechanism into law. The new EU framework does not establish a new EU-wide scheme, nor does it aim to harmonise national ones. In fact, investment screening remains subject mainly to national law. The Regulation, however, sets up a series of measures to help MS coordination at the EU level (European Commission, WEBa). In particular, it: defines the scope of FDI screening in the EU; establishes EU-wide principles to be followed by national mechanisms; sets out clear timing, transparency rules, and procedures for cooperation and coordination; creates a formal and secure communication mechanism through fixed contact points; and it provides a clear and regularly updated overview of national schemes.

In terms of scope, the regulation applies to any FDI in the EU, excluding portfolio investments. Given that screening is considered a restriction on free movement of capital, it is only allowed as an exception on grounds of security or public order concerns. This includes areas such as critical infrastructure (energy, transport, water, communication, and elections), advanced technology and dual use items, supply of critical inputs, sensitive information and data, and the media (Hanemann et al, 2019). Under the new regulation, MSs can maintain their individual screening mechanisms and are not obliged to create new ones. Nevertheless, several key principles now need to be followed across the EU by countries that have established national systems (Regulation 2019/452): transparency of rules and procedures; non-discrimination among foreign investors; confidentiality of information exchanged; the possibility of recourse against screening decisions; and measures to identify and prevent circumvention by foreign investors.
Procedurally, the MSs where the investment takes place can start a formal investigation, under its national scheme, that must be notified to the European Commission. In case the MS where the investment takes place does not take action, other MSs or the Commission can then request further information or provide comments, following which the Commission can issue a non-binding opinion. The MS where the investment takes place must take into account all inputs received and, in case it decides to trigger the screening mechanism, it can then authorise, authorise with conditionality, or block the investment. The assessment needs to determine whether a foreign acquisition of EU assets is likely to affect security or public order within its target market. Possible elements taken into account include the track record of the investor, the risk that it engages in illegal activities, and whether it is directly or indirectly controlled by a foreign government. The details of the assessment are then left to national legislation.

In parallel with such provisions, the Commission has taken a series of complementary actions. Internally, a group of 27 experts from all MS authorities was established to regularly discuss trends, issues, and best practices connected to FDI screening (European Commission, WEBb). Externally, the regulation encourages cooperation with third-countries and international organisations, such as the OECD (OECD, WEB).

2.4  Public procurement framework and reform

This section provides an overview of the existing EU legislative framework on public procurement, describing the Proposal for an IPI. The reform aims to incentivise EU trading partners to ensure reciprocity and a global playing field in the access to third-country public procurement markets by EU businesses.

2.4.1  The existing public procurement framework

The existing EU legislative framework on public procurement consists of several legislative and non-legislative instruments. Public procurement in the EU is subject to the basic principles of transparency, equal treatment and non-discrimination under the Treaties. EU public procurement directives established minimum harmonised public procurement rules which are transposed into national legislation and apply to tenders whose monetary value exceeds a certain amount, while tenders below the set thresholds are regulated by national laws. The four minimum harmonisation directives which regulate public contracts, utilities, concessions, and defence and security procurement respectively as well as access to review procedures offer public buyers across the EU flexibility to purchase goods, services and works and to tailor their procurements to their own needs.

According to the Commission Guidance for third country bidders, the directives offer the possibility to award contracts based on the Best Price-Quality Ratio and allow buyers to choose the most appropriate and effective procurement procedure. They also offer the choice of quality requirements to intro-

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duce in the tender documents; mechanisms to ensure compliance with environmental, social and labour obligations; freedom in preparing the tender process by engaging with the market and relevant stakeholders. The directives furthermore equip buyers with instruments to deal with bids, which are abnormally low in price; and determine which third country bidders enjoy secured access to the EU procurement market. According to Article 25 of the Directive 2014/24/EU, contracting authorities shall accord to the works, supplies, services and economic operators from third countries signatories of international trade agreements no less favourable than the treatment accorded to the works, supplies, services and economic operators of the Union. No further guarantee is provided to economic operators from third countries, which do not have any agreement providing for the opening of the EU procurement market or whose goods, services and works are not covered by such an agreement.

**The Directive 2014/24/EU, however, does not offer any specific rules regarding the participation of economic operators benefiting from foreign subsidies.** Article 69 allows a contracting authority to reject an offer where the explanations provided by a bidder do not sufficiently account for an abnormally low price. If it is found that subsidies (state aid) from EU MSs are the cause of that price, the tender may under additional conditions be rejected on that ground alone. However, there is no corresponding provision pertaining to third country subsidies. To justify a rejection of a grant of foreign subsidies, as part of an overall assessment it needs to be demonstrated that the foreign subsidies impede the viability of the offer and the bidder’s capacity to execute the contract at the (abnormally low) price offered.

Furthermore, the relationships between public buyers and third country bidders are governed by the Agreement on Government Procurement (GPA) or Bilateral Free Trade Agreements (FTAs) which provide access to the procurement market (see Section 3.1). In light of the discriminatory measures preventing EU businesses from accessing procurement markets in third countries, the Commission proposed the IPI. In June 2021, the Council proposed certain key amendments to the Commission proposal under the auspices of the Portuguese Presidency and, following this breakthrough, the European Parliament restarted its discussions on this initiative in September 2021.

**2.4.2 The proposal on an International Procurement Instrument (IPI)**

The IPI is a proposal that aims at regulating access to the EU’s public procurement markets as a means of encouraging the reciprocal opening of public procurement markets from foreign entities. The updated 2016 IPI proposal lays down a centralised Commission directed process, by which non-reciprocating states could be penalised by price penalties on a tender for an EU procurement. This applies to tenders that are not subject to the EU’s international procurement commitments under the WTO GPA and other Regional Trade Agreements (RTAs) (Dawar, 2017). Among them are Brazil, China, India, Russia, Turkey, and the US. While it is true that the proposed IPI deals with reciprocity of market access, and not distortions of the procurement processes in the internal market arising from foreign subsidies, this instrument aims to complement the proposed Regulation on foreign subsidies distorting the internal market.11

**Proposal for an IPI (2012)**

In the context of the negotiations on a revised GPA and bilateral negotiations in 2012, the European Commission put forward a first proposal for an IPI. This initiative was based on the premise that the EU

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10 At present, 20 parties are part of the GPA: the EU with regard to its 28 Member States; Armenia; Australia; Canada; Chinese Taipei; Hong Kong (China); Iceland; Israel; Japan; Liechtenstein; Montenegro; Moldova; Norway; New Zealand; South Korea; Singapore; Switzerland; Ukraine; United States; and the Netherlands (with respect to Aruba).

lacked leverage in international negotiations with its trading partners. The 2012 IPI Proposal made a distinction between ‘covered procurement’, which corresponds to the EU’s international commitments in the field of public procurement including market access commitments, and ‘non-covered procurement’,\(^{12}\) which is not subject to the EU commitments.

However, during the negotiations, 18 MSs expressed reservations to the initial proposal and believed that measures to restrict access to the EU market for goods and services originating in certain third countries were not the appropriate tool for encouraging these countries to open up. Instead, most MSs considered that the IPI in its current form may be interpreted as a protectionist measure, and feared escalating trade protectionist measures by the EU’s trading partners (Titievskaja, 2020). It was also pointed that optional nature of the decentralised pillar might result in diverse patterns of use, in particular considering the margin of error caused by contracting authorities/entities applying the restrictive measures, which threatened to fragment the internal market. Finally, some MSs were also concerned about a potential disproportionate increase in the administrative burden on both businesses and contracting authorities and entities (Dawar, 2017).

Amended Proposal (2016)

This led the Commission to put forth a revised proposal in 2016, largely reflecting the European Parliament position and its set of amendments voted in January 2014. The possibility of closing, even temporarily, the EU procurement market was removed in the amended proposal. Only the centralised procedure was maintained in the amended proposal with shortened time of country investigations. A further provision was added regarding the obligation for the Commission to make publicly available in a report the main findings of the investigation. In the event of unsatisfactory results following the consultation with the third country concerned, the Commission should take appropriate action. This was limited to imposing price adjustment measures (or ‘price penalties’) on any tender for an EU procurement originating in a country that does not offer the EU reciprocity in access to its procurement markets (Article 8). Price adjustment measures could be imposed by contracting authorities and entities to tenders where more than 50 % of the total value was made of goods and/or services originating in a third country adopting or maintaining restrictive and/or discriminatory procurement measures or practices (Article 11). The revised proposal imposed a very high threshold for any adjustment measure to be taken – i.e. only apply to contracts with an estimated value of EUR 5 million or more. Price adjustment measures should also specify a penalty of up to 20 % on the price of the tenders (Article 8 (2)).

The Commission should determine the contracting authorities or entities or categories of contracting authorities or entities, listed by MS, whose procurement is concerned by the measure, based on a list drafted by the MSs (article 9). Unlike the 2012 IPI proposal, the temporality of such price adjustment measures was clarified in the amended proposal as the Commission could decide to withdraw the price adjustment measure or suspend its application for a period of time if the country concerned takes satisfactory remedial or corrective actions.

Taking up the European Parliament’s amendments voted in 2014 on the initial proposal, the amended proposal exempted SMEs established in the EU and engaged in substantive business operations entailing a direct and effective link with the economy of at least one MS from the application of the IPI (Article 5). Nor would price adjustment measures be applied to bidders and products originating from developing countries subject to GSP+ treatment, in accordance with the EU trade and development policy. Another

\(^{12}\) For this latter category, the initial proposal included two different procedures – i.e. a decentralised procedure, whereby Member States’ contracting authorities and entities would be allowed to exclude a tender after seeking the Commission’s approval, and a centralised procedure, with the Commission playing a central role in the investigation process of the third country concerned, and where appropriate, the imposition of temporary restrictive measures.
important element of the proposal is the approach to take measures targeting territories at regional or local level, thus avoiding applying discriminatory measures to the third country as a whole. It was also clarified that the instrument will apply to all procurement and concessions covered by the 2014 procurement and concession Directives and that MSs and their contracting authorities and entities may not apply restrictive measures beyond those provided by the Regulation.

Nevertheless, the overall efficiency of the proposed IPI was still questioned on whether it would provide sufficient leverage for a third country to remove barriers to participation in its procurement (Djaghe, WEB). A concern raised by Business Europe was also that the instrument should ensure that bidders from locked-up third countries heavily relying on subsidies do not distort the EU’s public procurement market. Indeed, EU companies face increasingly unfair competition from State-Owned Enterprises (SOEs), in EU procurement markets. In this respect, Business Europe recommended to develop specific provisions on SOEs in the IPI. Furthermore, the periods of the investigation and consultation procedures were still considered lengthy and not adapted to the reality of procurement timelines (Business Europe, 2020a). It was also argued that, in the long term, the application of price adjustment measures to products originating both, from the third country targeted and from the EU, could impact negatively these European companies with international supply chains. (Friton, 2017, and Business Europe, 2020a). As a result, 14 MSs maintained their reservations on the amended proposal for an IPI and discussions were put on hold.

Latest developments on the IPI proposal

Following the European Council held on March 2019 and October 2020 and after several years of deadlock on this matter, the Council, under the auspices of the Portuguese Presidency, reached a common position on the IPI and proposed key changes to the legislative text in June 2021. Overall, the approach of this latest proposal is to limit or exclude, on a case-by-case basis, access to EU public procurement markets for businesses from countries that apply discriminatory restrictions vis-à-vis EU businesses.

Notably, the procedures for investigations and consultations by the Commission have been further clarified. Whereas under the 2016 amended proposal, the investigation and consultation procedures could take up to 27 months in total the Council’s position proposes that investigations and consultations shall be concluded within a period of 9 months after the date of initiation (article 4). Upon conclusion of the investigation and consultations where the Commission finds that third country measures or practices against Union economic operators, good or services exist, two types of IPI measures could be implemented (Article 5): the imposition of a score adjustment measure on tenders submitted by economic operators originating from the third country concerned; or, under exceptional situations, the exclusion of tenders submitted by economic operators originating in that third country, or a combination of the two IPI measures. It should be noted that, under this proposal, the score adjustment measure would apply for the purpose of the evaluation and ranking of the tenders, but it should not affect the price due to be paid under the contract to be concluded with the successful tenderer. Furthermore, differentiated thresholds have been proposed by the Council: IPI measures may apply to procurement procedures with an estimated value which should be equal or above EUR 15 million net of value-added tax for works and concessions, and equal to or above EUR 5 million net of value-added tax for goods and services. This would allow for wider coverage of contracts by the IPI, which was deemed to potentially increase the efficiency of the leverage of the instrument (Renda et al, 2013). Finally, the percentage value of the adjustment could be up to 40% of the evaluation score of the tender.

Consequences of the IPI on MSs procurement

One important aspect is that the sole legal basis chosen for the IPI is Article 207 of the TFEU on the common commercial policy, entailing the EU’s exclusive competence over the matter. A consequence of
this choice was recalled in recital 18 of the 2016 amended proposal, stating that once the IPI would be adopted, MSs and/or their contracting authorities and entities should not be able to restrict the access of third country goods or services to their tendering procedures by any other measure than those ones provided for in this Regulation. This was reflected in Article 1(5) of the 2016 amended proposal, which prohibited MSs and their contracting authorities and entities to apply restrictive measures towards foreign bidders beyond those provided for in the Regulation.

However, while Article 207 of the TFEU remains the sole legal basis of the latest proposed Regulation, the abovementioned provisions have been proposed to be deleted by the Council. Therefore, outside the scope of the Regulation, the Council has proposed that the MSs and/or their contracting authorities and entities may still exclude economic operators from third countries, which do not have any agreement providing for the opening of the EU procurement market or whose goods, services and works are not covered by such an agreement, from accessing their procurement procedures, as indicated in the 2019 Commission Guidance on the participation of third-country bidders and goods in the EU procurement market.

Additionally, in cases within the scope of the Regulation, Article 8 of the Council proposal still provides for the possibility of MSs’ contracting authorities and entities not to apply, on an exceptional basis and only to a limited extent, IPI measures with respect to a procurement procedure. This is restricted to situations where there are only tenders from economic operators originating in the country subject to an IPI measure, or only such tenders meet the tender requirements; when it is justified for overriding reasons relating to the public interest; or when the application of an IPI measure would lead to a disproportionate increase in the price or costs of the contract that would render its execution economically unviable.

**Position of the European Parliament**

On 2 June 2021, the Council agreed on the amended proposal for an IPI. This breakthrough allowed the EP Committee on International Trade (INTA Committee) to re-launch works on the dossier on the basis of a new draft report presented by the Rapporteur. On 1st of September, INTA Committee discussed a second draft report on the IPI proposal (European Parliament, INTA Committee, 2021). Proposed amendments to the Commission proposal remain important in this second draft report which welcomes anyhow the significant departure from the logic of the 2016 amended proposal and the enhanced practicability brought to the instrument.

### 2.5 Third country subsidies to undertakings: gaps in EU rules

As highlighted by several policy papers, notably in the Commission’s White Paper on foreign subsidies of June 2020 and the recent proposed Regulation (COM/2021/223) on foreign subsidies distorting the internal market, the **EU state aid framework** applies only where an EU MS grants financial support to an undertaking or a group of undertakings, giving rise to an advantage that distorts competition and affects trade between MSs: **no comparable regime is in place for state support granted by non-EU countries**, even when the equivalent of certain subsidies granted by third countries would constitute illegal state aid if granted by an EU MS.

Moreover, as observed by European Parliamentary Research Service (2021), the EU trade defence rules based on the WTO rules (described in Section 2.2) allow duties or other countervailing measures to be taken when subsidised goods are imported into the Single Market, but not when subsidies take the

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13 Articles 107 to 109 of the Treaty on the Functioning of the European Union (TFEU), as detailed in Section 2.2.

14 This is for instance the case of China, as evidenced by the European Court of Auditors in the report ‘The EU’s response to China’s state-driven investment strategy’, Review 03 (2020).
form of subsidised investments, acquisitions or bids in procurement procedures or when they concern services and the financial flows. In fact, neither services, nor business decisions by externally subsidised companies in the EU are covered, as long as trade in goods is not concerned. In particular, European Parliamentary Research Service (2021) notes that the issue of third country subsidies is increasingly becoming of strategic importance as cross-border M&A flows into EU high-technology sector have grown over recent years (European Commission, 2017b). According to European Commission (2021d), 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.

2.5.1 White Paper: Proposal for Regulation

In light of the legislative gaps highlighted above, on 17 June 2020, the European Commission published a White Paper dealing with the distortive effects caused by foreign subsidies in the Single Market, presenting several options for future legislations. The White Paper considers that since there are no EU and international instruments to address this type of distortions, there is a regulatory gap, in particular where foreign subsidies take the form of financial flows facilitating acquisitions of EU undertakings or where they support the operation of an undertaking in the EU. The same applies where foreign subsidies distort public procurement procedures or where foreign subsidies provide a benefit when it comes to access to EU financial support.

The White Paper, therefore, proposes solutions and calls for new tools for addressing this regulatory gap. It puts forward several approaches, in particular envisaging three ‘modules’: a general market scrutiny instrument to capture all possible market situations in which foreign subsidies may cause distortions in the Single Market (Module 1); an approach to tackle foreign subsidies facilitating the acquisition of EU companies (Module 2); and a proposed legal instrument to address foreign subsidies in EU public procurement procedures (Module 3).

2.5.2 The Commission’s proposed Regulation on foreign subsidies distorting the internal market

Despite the review of EU trade defence instruments (the so-called ‘EU modernisation of TDI’ of 2017), alongside multilateral political efforts at WTO level to update the WTO rules, the European Commission’s communication of 18 February 2021 on the ‘Trade Policy Review’ underlines the inappropriateness of the ASCM to tackle the commercial behaviour of state-owned enterprises, such as:

- the lack of rules against practices forcing companies to transfer innovation and technology to the state or to their competitors (forced technology transfers); and
- the lack of rules to ensure that domestic regulation is transparent and pro-competition.

Therefore, such gaps in EU and WTO rules and the lack of foreseeable amendments to the ASCM, find a preliminary answer in the proposed Regulation on foreign subsidies distorting the internal market. Firstly, the Regulation introduces the concept of ‘foreign subsidy’, describing those circumstances where this kind of subsidy could exist and suggesting indicators to assess whether a foreign subsidy is distortive of the competitive conditions of the EU Single Market.

Namely, the proposed Regulation states that ‘a foreign subsidy exists where a third country provides a financial contribution which confers a benefit to an undertaking engaging in an economic activity in the internal market and which is limited, in law or in fact, to an individual undertaking or industry or to sev-

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eral undertakings or industries’. More specifically, a ‘financial contribution’ provided by non-EU public authorities (central governments, other government authorities, public entities) includes: the 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, debt to equity swaps or rescheduling; the foregoing of revenue that is otherwise due; and the provision of goods or services or the purchase of goods and services.

To assess whether such financial contributions could create distortions on the internal market, as a general threshold, the foreign subsidy is unlikely to distort the internal market if its total amount is below EUR 5 million over any consecutive period of three fiscal years. This amount differs from the threshold proposed in the White Paper, which was aligned with the de minimis threshold established by EU state aid rules. Notably, the proposed Regulation also identifies four categories of foreign subsidies which are more likely to be deemed distortive.

Where distortive effects are established, the proposed Regulation provides for a ‘balancing test’, between ‘negative effects of a foreign subsidy in terms of distortion on the internal market’ and ‘positive effects on the development of the relevant economic activity’ (Article 5 of the proposed Regulation). This test is aligned to the balancing test that is applied to the assessment of compatibility of state aid under Article 107(3)(c) TFEU: if positive effects of a foreign subsidy outweigh its negative effects, the balancing test may eventually lead to the conclusion that no redressive measures (Article 6 of the proposed Regulation) should be imposed (Cleary Gottlieb (2021). This approach differs from the White Paper that referred to an ‘EU interest test’, a concept derived from EU trade policy which included the assessment of EU public policy objectives (e.g., jobs, environmental protection, digital transformation, security, or public safety). Consistently with the approaches outlined in the White Paper, the proposed Regulation envisages three ‘tools’ to tackle distortive foreign subsidies: a market investigation tool that the Commission may use on its own initiative (ex officio) in those market situations where the Commission suspects that a distortive foreign subsidy affects the internal market (Chapter 2 of the Proposed Regulation); an ex-ante notification and approval by the Commission of concentrations potentially distortive of the internal market, due to foreign subsidies (Chapter 3 of the Proposed Regulation); and an ex-ante notification to the contracting authority and approval by the Commission of participation of subsidised bidders in public procurement in the EU when foreign subsidies enable an undertaking to submit a tender that is unduly advantageous in relation to the works, supplies or services concerned (Chapter 4 of the proposed Regulation).

Chapter 2: Ex officio review of foreign subsidies

Chapter 2 proposes the establishment of a general market scrutiny instrument to capture all possible market situations in which foreign subsidies may cause distortions in the Single Market. Information on these market situations could stem from market operators or MSs. With this instrument, the Commission will exercise its enforcement powers upon any element it considers relevant indicating the granting of a foreign subsidy to a beneficiary active in the EU. In this sense, the proposed Regulation differs from the White Paper: enforcement will be an exclusive responsibility of the Commission (this applies to all the three tools), and it will not be shared with national competition authorities.

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16 EUR 200 000 granted over a consecutive period of three years
17 Foreign subsidies granted to distressed undertaking, foreign subsidies in the form of an unlimited guarantee for debts, foreign subsidies directly facilitating a concentration, foreign subsidies enabling an undertaking to submit an unduly advantageous tender.
A case would start with a preliminary review to examine whether there is a foreign subsidy that may distort the internal market. If there is no concern, because either there is no foreign subsidy, or there are no indications of a distortion in the internal market, the Commission would close the case. If there is evidence tending to show that a foreign subsidy may distort the proper functioning of the internal market, an in-depth investigation would follow, during which the Commission would need to confirm its preliminary finding that there is a foreign subsidy that distorts the internal market. At the end of that in-depth investigation, if confirmed that the proper functioning of the internal market may have been or may be distorted through the foreign subsidy, the Commission may impose measures to redress those distortions in the internal market (‘decision with redressive measures’). Similarly to the reasons to dismiss a preliminary review, an investigation would be closed with a ‘no objection’ decision if the existence of a foreign subsidy is not confirmed or if, after the balancing test, a distortion on the internal market is outweighed by positive effects on the development of the relevant economic activity.

The proposed Regulation states that this tool has a broad material scope and would allow distortive foreign subsidies in all market situations to be addressed: this includes the possibility to review acquisitions facilitated by foreign subsidies and market behaviour by a subsidised bidder in public procurement, when these subsidies are not captured by the turnover threshold outlined in Chapters 2 and 3 of the proposed Regulation.

**Chapter 3: Concentrations**

Chapter 3 is intended to specifically address distortions caused by foreign subsidies facilitating the acquisition of EU companies. This instrument aims to ensure that foreign subsidies do not confer an unfair benefit on their recipients when acquiring (stakes in) EU companies, either directly by linking a subsidy to a given acquisition or indirectly by de facto increasing the financial strength of the acquirer, which in turn would facilitate an acquisition. This tool provides for a compulsory notification mechanism and an ex-ante review by the Commission of concentrations above certain thresholds, in parallel with the existing competition law-based merger control and foreign investment review proceedings (Cleary Gottlieb (2021)).

Concentrations will trigger a notification obligation (Article 19) if two cumulative thresholds are met (Article 18): the acquired undertaking – or at least one of the merging entities, or the joint venture or one of the parents of a joint venture – is established in the EU and generates a turnover in the EU of at least EUR 500 million; and the undertaking concerned (or the joint venture and its parents) received from third countries an aggregate financial contribution in the three calendar years prior to notification of more than EUR 50 million. These thresholds differ from the proposals of the White Paper. Namely: the turnover threshold is higher in the proposed Regulation (EUR 500 million against EUR 100 million in the White Paper); and the financial contributions that are expected in the coming year (or that are not yet paid to the undertaking) are not taken into account in the thresholds of the proposed Regulation.

The notifications would therefore focus on the potentially problematic acquisitions, namely where a financial contribution from a third-country authority facilitates an acquisition. Buyers would not be able to close a transaction for 25 working days after filing a complete notification (as for the procedures of the EU Merger Regulation). Notably, as observed by Cleary Gottlieb (2021), the proposed Regulation refers to a ‘financial contribution’ received from a third country, which arguably is a broader standard than a ‘foreign subsidy’. This would imply that financial contributions received from foreign governments

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18 Article 6 of the Proposed Regulation outlines the full list of structural and behavioural measures.
on market terms may also in principle trigger a notification obligation (Cleary Gottlieb (2021). Under this instrument, the Commission would ex ante review planned acquisitions involving possible foreign subsidies under a compulsory notification mechanism: notably, the Commission has exclusive jurisdiction to investigate the effects of subsidies on concentrations, under a centralised ‘one-stop-shop’ system, similar to that of the EU Merger Regulation.

As outlined in Chapter 1, the review process would happen in two steps: a preliminary review phase and, where relevant, an in-depth investigation. If the Commission has, on the basis of a preliminary review, sufficient evidence that the acquiring company benefits from foreign subsidies facilitating the acquisition, it would be able to launch an in-depth investigation. If, at the end of the investigation, the Commission finds that an acquisition is facilitated by foreign subsidies and distorts the internal market, it would have either to accept suitable commitments (which effectively remedy the distortion) by the notifying party or, as a last resort, prohibit the acquisition. To ensure effective implementation of this tool, the Commission would also have the right to ex officio review an acquisition which should have been notified by the acquirer but was not, including after it is completed. This review could ultimately result in the prohibition of the acquisition or, if it is already completed, in its unwinding.

Chapter 4: Foreign subsidies in EU public procurement procedures

Chapter 4 addresses foreign subsidies that could have a harmful effect on the conduct of EU public procurement procedures. Foreign subsidies may enable bidders to gain an unfair advantage, for example, by submitting bids below market price or even below cost, allowing them to obtain public procurement contracts that they would otherwise not have obtained. A review specifically dedicated to distortions in public procurement would aim to preserve the level playing field in that specific area.

This instrument ensures that foreign subsidies can be addressed in individual public procurement procedures, by requiring EU public buyers to exclude from public procurement procedures those economic operators that have received distortive foreign subsidies. Therefore, economic operators participating in public procurement procedures (where the estimated value of the public tender is equal or greater than EUR 250 million) would have to notify to the contracting authority when submitting their bid whether they, including any of their consortium members, or subcontractors and suppliers have received a financial contribution within the last three years preceding the participation in the procedure. Contrary to the White Paper and following the same approach of Chapter 3 on concentrations, the Proposed Regulation does not provide for an obligation to notify prospective foreign subsidies that the company is expected to receive during the term of the public procurement contract. Moreover, the proposed Regulation does not set any threshold concerning the amount of foreign financial contributions: therefore, any foreign contribution shall be notified to the contracting authority if the value of the tender amounts to at least EUR 250 million.

Along the lines of the abovementioned approach of preliminary review and in-depth investigation, if the Commission confirms that, after an investigation, the economic operator has received a foreign subsidy distorting the public procurement procedure, it will exclude this economic operator from the ongoing procurement procedure. As for the other tools, the Commission could either dismiss the findings of the preliminary review (i.e. not confirming the existence of a foreign subsidy), or impose commitments to address effects of the foreign subsidy.

3 EU’s international commitments and action

This section describes the existing international obligations on market access and the multilateral policy initiatives initiated by the EU on public procurement and subsidies.
3.1 The Government Procurement Agreement (‘GPA’)

As noted by the Commission’s White Paper, the legislative instrument ensuring that foreign subsidies are addressed in public procurement procedures will be defined in accordance with the GPA. Indeed, at the multilateral level, the GPA applies to procurement procedures opened by economic operators established in the 21 signatory states of the Agreement.

Overall, the GPA establishes a framework of rights and obligations among its parties with respect to their national laws, regulations, procedures and practices in the area of public procurement. Parties to the Agreement are required to accord to products, services and suppliers of any other party to the Agreement treatment ‘no less favourable’ than they give to their domestic ones (Article III:1(a)). Furthermore, parties may not discriminate among goods, services and suppliers of other Parties (Article III:1(b)). In addition, each party needs to ensure that its entities do not treat domestic suppliers differently on the basis of a greater or lesser degree of foreign affiliation or ownership as well as to ensure that its entities do not discriminate against domestic suppliers because their good or service is produced in the territory of another party (Article III:2).

The GPA, which was revised in March 2012, is composed of two parts: the text of the Agreement and parties’ and market access schedules of commitments. However, these rules only apply to procurement of goods and services by covered entities, as listed in each party’s coverage schedules in Appendix I to the Agreement. Goods and services procured must be of minimum estimated value equal to or exceeding the relevant threshold values specified in a party’s annexes to Appendix I. Table 3 below presents the thresholds applied by most parties to the GPA.

Table 3: Thresholds applied by most GPA parties, in Special Drawing Rights (SDR)

<table>
<thead>
<tr>
<th>Party</th>
<th>ANNEX 1 (Central Government Entities)</th>
<th>ANNEX 2 (Sub-central Government Entities)</th>
<th>ANNEX 3 (Other Entities)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Goods and services</td>
<td>Construction services</td>
<td>Goods and services</td>
</tr>
<tr>
<td>Thresholds applied by most Parties</td>
<td>130 000</td>
<td>5 000 000</td>
<td>200 000</td>
</tr>
</tbody>
</table>

Source: e-GPA portal

On the relation and interaction between the GPA and the proposed Regulation on foreign subsidies distorting the internal market, it is noted in the Commission’s White Paper on foreign subsidies of June 2020 that only public procurements exceeding the specified threshold values indicated in each party’s coverage schedules are covered by the new legislative instrument. Concerning the tendering procedures and the award of contracts, the existing provision of the GPA merely requires procuring entities that have received a tender abnormally lower than other tenders to ask the tenderer to ensure that it complies with the conditions of participation and be capable of fulfilling the terms of the contract (Article 19). SDR is not a currency but an international reserve asset created by the IMF to supplement official reserves. A basket of currencies defines the SDR: the US dollar, Euro, Chinese Yuan, Japanese Yen, and the British Pound.

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19 SDR is not a currency but an international reserve asset created by the IMF to supplement official reserves. A basket of currencies defines the SDR: the US dollar, Euro, Chinese Yuan, Japanese Yen, and the British Pound.
XIII: 4). In this respect, the European Commission (2021b) suggested that the GPA should be reviewed to include specific rules for dealing with distortive foreign subsidies.

Widely used in WTO Agreements, the 2012 GPA Agreement also incorporates Special and Differential Treatment and Other Special Measures (SDT) for developing countries. As such, an acceding developing country can negotiate transitional measures in the form of ‘a price preference programme’, ‘an offset’; ‘the phased-in addition of specific entities and sectors’; ‘a threshold that is higher than permanent threshold’; and ‘a delayed application of any specific obligation’ in the Agreement (Article V.3-7). These measures also include providing technical assistance to the developing country (Article V.8).

Currently, 11 WTO Members are negotiating accession to the GPA. Despite repeated efforts, the absence under the GPA of emerging countries remains a major problem. China applied to join the GPA in 2007 and has since submitted sixteen revised offers of GPA coverage, with the latest offer being circulated in October 2019. In a 2020 report on China’s compliance with its WTO commitments, the U.S. Trade Representative (USTR, 2021) reported progress in several areas, including thresholds, coverage at the sub-central level of government, entity coverage, and services coverage. Nevertheless, it also concluded that the offer remained ‘far from acceptable to the United States and other GPA parties’. The 2020 GPA Committee Report (WTO Committee on Government Procurement, 2020) also described the offer as ‘a comprehensive and ambitious one that was already on the whole commensurate with those of GPA Parties’.

The fact remains that while the EU procurement market is accessible to foreign companies, such as those from China, European businesses are subject to discriminatory measures in public procurement markets in China. One persistent issue for European bidders is the preferential market access to domestic products in China, referred to as ‘Buy national policy’. This follows the application of Article 10 of the Government Procurement Law of China (GPL) which requires government entities to procure only domestic goods, construction and services, except when they are not available in China or, if available, cannot be procured on ‘reasonable commercial terms’, or are for use outside China. Another problem specific to the field of public procurement is, as expressed by the EU Chamber of Commerce in China, the imposition by some local governments of unfair and unreasonable bidding requirements to exclude or restrict market competition to foreign businesses, despite initiatives to reform the public procurement system in China (EU Chamber of Commerce in China, 2020). Significant protectionist requirements that restrict access to Chinese public procurement markets also relate to imposing technology transfers, including industrial property rights, other intellectual property rights and undisclosed information, as a condition for the award of public contracts or local content requirements (Business Europe, 2020b; European Commission 2018c). As a result, in 2020, the EU Chamber of Commerce in China’s Business Confidence Survey (BCS) registered that 44% of European companies reported missing business opportunities due to market access restrictions, such as barriers to government procurement processes (EU Chamber of Commerce in China, 2021).

Moreover, given that state-owned enterprises (SOEs) conduct most of Chinese procurement, one of the key points in the negotiations is their coverage in its market access offer to join the GPA. Against this background, it is important to emphasise the distorted impact that the participation of SOEs can have. In particular, the use of much lower prices than normal in the Chinese SOEs bids may cause distortions.

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20 The European Commission made this suggestion in the Impact Assessment accompanying the proposal for a foreign subsidy Regulation, noting that the GPA does not address the question of foreign subsidies.
21 Note that the status of ‘developing countries’ is not strictly defined in WTO Law as it is largely subject to ‘self-declarations’.
22 In this regard, see for example the EU case at the WTO against China on the Transfer of Technology where the EU outlined at least 17 laws through which China imposes technology transfer, Case DS549; https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds549_e.htm
of the EU procurement procedures of the internal market. One striking example was the award of the EUR 420 million ‘Pelješac bridge’ project in Croatia to one of the largest Chinese SOE. The controversy revolved around the abnormally low bidding price offered by the Chinese SOE – a price more than 36% below the European tenderers – and the fact that this major construction contract was co-financed by the EU at 85% (European Commission, 2017c). Although European co-bidders lodged a complaint for violation of the EU competition rules, alleging that the bid which was backed up by Chinese state aid constituted a case of dumping (Blockmans & Hu, 2019), their challenges were dismissed by the Croatian State Commission for Supervision of Public Procurement Procedure. Therefore, the accession of China to the GPA should happen as soon as possible as suggested in a report by Business Europe on the relations between the EU and China.

3.2 Possible contributions to a level playing field in global trade within the WTO framework

At multilateral level, the WTO Agreement on Subsidies and Countervailing Measures (ASCM) was adopted in 1995 and is an integral part of the WTO system, thus binding all its Members. This section will examine possible contributions to a level playing field within the WTO framework.

3.2.1 WTO Agreement on Subsidies and Countervailing Measures (ASCM)

First, the ASCM includes a broad definition of ‘subsidy’. Indeed, in order for a subsidy to exist, there must be a financial contribution by a government or any public body within the territory of a Member and a benefit conferred thereby (Article 1). The ASCM established two types of subsidies:

1. Prohibited subsidies under the narrow scope of Article 3 because they are designed to directly affect trade and thus are most likely to have adverse effects on the interests of other Members., i.e.: Export subsidies’, which are subsidies that are contingent, in law or in fact, on the recipient’s export performance. An illustrative list of export subsidies is set out at Annex I to the ASCM; and ‘local content subsidies’, which are subsidies whether solely or as one of several other conditions, upon the use of domestic over imported goods.

2. Actionable subsidies, which are subsidies that are not prohibited but are subject to a challenge, either through multilateral dispute settlement or through countervailing action, in the event that they cause adverse effects to the interests of another Member according to Article 5.

Second, the ASCM contains important notification and surveillance procedures. Indeed, transparency rules of subsidies require members to notify all specific subsidies, as defined in Article 2 of the Agreement, at all levels of government and covering all goods, including agriculture, to the SCM Committee pursuant to Article 25.2 of the ASCM. It is a requisite that the notification’s content is sufficiently specific to enable other Members to evaluate the trade effects and to understand the operation of notified subsidy programmes, which is notably provided by an obligation towards Members to include statistical data permitting an assessment of the trade effects of a subsidy in their notification (Article 25.3). Exempt from this requirement are non-specific subsidies i.e., subsidies not covered by Article 3 of the ASCM and not limited, in law or in fact, to specific sectors, industries, or regions, etc.

Members shall also inform the Committee in the event there are no measures in their territories requiring notification. In addition, according to Article 25.8 of the Agreement, any Member may, at any time, make a written request for information on the nature and extent of any subsidy granted or maintained by another Member, or for an explanation of the reasons for which a specific measure has been considered as not subject to the requirement of notification. Pursuant to Article 25.9, Members so requested shall provide such information as quickly as possible and in a comprehensive manner, and shall be ready, upon request, to provide additional information to the requesting Member. They shall
provide sufficient details to enable the other Member to assess their compliance with the terms of this Agreement. Furthermore, any Member which considers that any measure of another Member having the effects of a subsidy has not been duly notified may bring the matter to the attention of such other Member. If the alleged subsidy is not thereafter notified promptly, such Member may itself bring the alleged subsidy in question to the notice of the Committee (Article 25.10).

However, in practice, the ‘chronic’ low compliance with the fundamental transparency obligation of subsidy notification requirements was considered to constitute ‘a serious problem in the proper functioning of the Agreement’, as expressed by the chair of the Committee in October 2020 (WTO Committee on Subsidies and Countervailing Measures, 2020a). A background note prepared by the WTO Secretariat (2019) observes that between 1995 and 2017, the number of members that have failed to make a notification rose sharply as WTO membership has increased. As of 27 April 2021, 80 WTO members have still not submitted their 2019 notifications, while 67 had not yet submitted subsidy notifications for 2017, and 57 members have still not submitted subsidy notifications for 2015 (WTO Committee on Subsidies and Countervailing Measures, 2021).

The lack of transparency and low compliance with the obligation to notify subsidies under the ASCM was also raised in the Commission’s White Paper. Due to this very low level of notification of subsidies by WTO Members, the total amount of subsidies is likely underestimated. Therefore, it is also very difficult to obtain reliable and accurate data on the total amount of foreign subsidies affecting the EU internal market, as identified by the European Commission (2021b). In particular, developing countries fail to comply with this transparency and notification requirement. Some developing countries also raised concerns with respect to strict deadlines. To address this issue, the US put forward a formal proposal concerning the submission of requests for information under Article 25.8 of the ASCM and the submission of answers under Article 25.9, which should take the form of a written procedure. According to the proposal, requested Members should provide written answers as quickly as possible and in a comprehensive manner, within 60 days after the receipt of a written request. Follow-up questions should then be answered within 30 days. Finally, any outstanding requests would stay on the agenda of the Committee until answered (WTO Committee on Subsidies and Countervailing Measures, 2020b). This proposal was notably supported by the EU, commenting that ‘a written question and answer process under Articles 25.8 and 25.9 would enhance the transparency provisions in the Agreement which was very important especially in light of the fact that the subsidy notification exercise was not giving a full picture of subsidies granted’ (WTO Committee on Subsidies and Countervailing Measures, 2020a). In contrast, China considered that this proposal would ‘impose newly-added substantial obligations on Members’ and ‘would pose challenges to many developing countries facing capacity constraints increasing their workload and distracting their focus on preparing the notifications’ (WTO Committee on Subsidies and Countervailing Measures, 2020a).

Possible contributions to a level playing field in global trade also take place in the wider context of the prospects for the WTO reform. The EU has, through its concept paper for the WTO modernisation, offered concrete proposals for WTO Member to improve compliance with their notification obligations under the ASCM, and overall to address inadequacies in the ASCM. These proposals aim to (i) involve the WTO Secretariat (WTO Negotiating Group on Rules, 2015a) in regularly monitoring compliance with notification obligations and reporting back to Members, through a streamlined system detailed by the EU (WTO Negotiating Group on Rules, 2015b). It is argued that the proposed mechanism would not entail any increases in the notification burden of Members granting subsidies, which are particularly important for developing countries, nor requires any changes in the ASCM.

It (ii) also sets out a number of incentives for improving WTO Members’ compliance with their notifications obligations (WTO Negotiating Group on Rules, 2015a). The advanced options include that duly notified subsidies would be presumed to be non-actionable or more difficult to act against. Conversely,
there would be a rebuttable presumption according to which failure to notify subsidies would lead those subsidies to be presumed as automatically in breach of WTO disciplines and therefore actionable under the provisions of Part II or Part III of the ASCM. The need for strong incentives to notify subsidies was also emphasised in the Joint Statement of the Trilateral Meeting of the EU, the US, and Japan of 14 January 2020. The trilateral group tabled to render prohibited any non-notified subsidies that were counter-notified by another Member, unless the subsidising Member provides the required information in writing within set timeframes. Other proposals of the US–EU–Japan trilateral group submitted to the WTO with other WTO Members also include the establishment of a Working Group to enhance notification compliance (WTO General Council for Trade in Goods, 2021).

3.2.2 New types of prohibited subsidies to be added to the ASCM

The ASCM provides two routes of remedies to challenge other Members’ foreign subsidies – the WTO dispute settlement and countervailing duty action, in the event that subsidies cause adverse effects to the interests of another Member. Adverse effects caused by subsidies may be of three types under Article 5 of the ASCM: (i) injury to a domestic industry of another Member caused by subsidised imports in the territory of the complaining Member, which is the sole basis for countervailing action; (ii) nullification or impairment of benefits under the GATT 1994; and (iii) serious prejudice to the interests of another Member.

The imposition of a countervailing measure by a Member is then subject to compliance with the strict conditions and substantive or procedural requirements detailed in Part V of the Agreement. An investigation shall be initiated if the application includes sufficient evidence of the existence of a subsidy and, injury to a domestic industry, and a causal link between the subsidised imports and the alleged injury. A failure to respect Part V can be taken to a dispute settlement and may be the basis for the invalidation of the measure. The demonstration of adverse effects stemming from subsidisation remains difficult in some cases. The ineffectiveness of WTO remedies for harmful subsidies is indeed one argument for the reform of subsidy rules (Siqi and Winquan, 2020).

In the context of the US–EU–Japan trilateral initiative, it was acknowledged that the current list of prohibited subsidies provided in Article 3.1 of ASCM is insufficient to tackle market and trade distorting subsidisation that exist in certain jurisdictions and that new types of unconditionally prohibited subsidies need to be added to the ASCM. Thus, the proposal first suggested adding a new type of ‘unconditionally prohibited subsidies’, which would include: unlimited guarantees; subsidies to an insolvent or ailing enterprise in the absence of a credible restructuring plan; subsidies to enterprises unable to obtain long-term financing or investment from independent commercial sources operating in sectors or industries in overcapacity; and certain direct forgiveness of debt.

Second, to address the difficulty of demonstrating adverse effects caused by actionable subsidies, the US–EU–Japan trilateral group tabled four types of ‘conditionally prohibited subsidies’, including but not limited to subsidies that are excessively large; prop up uncompetitive firms and prevent their exit from the market; create massive manufacturing capacity, without private commercial participation; and lower input prices domestically in comparison to prices of the same goods when destined for export. Additionality, the proposal argued that these types of subsidies have such a harmful impact that a reversal of the burden of proof is justified, so that the subsidising Member must demonstrate that there are no serious negative trade or capacity effects and that there is effective transparency about the subsidy in question. Conversely, China and other developing members support a reform proposal that seeks greater recognition of the role of subsidies in pursuing legitimate social and development goals (WTO, 2019b). A second broader proposal for WTO reforms was, for example outlined by China in a 2019 document and circulated at the WTO General Council (WTO, 2019a). Key issues and comparison of the trilateral group’s positions versus China’s position are highlighted in the table below:
Table 4: Key differences between the proposals by the US–EU–Japan and China

<table>
<thead>
<tr>
<th>Trilateral group</th>
<th>Key issues</th>
<th>China</th>
</tr>
</thead>
<tbody>
<tr>
<td>Issue</td>
<td>Industrial subsidies</td>
<td>Non-issue</td>
</tr>
<tr>
<td>Non-issue</td>
<td>Misuse of AD and CVDs</td>
<td>Issue</td>
</tr>
<tr>
<td>Non-issue</td>
<td>Aggregate measure of support subsidies in agriculture</td>
<td>Issue</td>
</tr>
<tr>
<td>Issue</td>
<td>SOEs and national champions</td>
<td>Non-issue</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Key policy recommendations</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>Expand list of prohibited subsidies</td>
<td>No</td>
</tr>
<tr>
<td>Yes</td>
<td>Reverse ASCM burden of proof for very large subsidies</td>
<td>No</td>
</tr>
<tr>
<td>Yes</td>
<td>New clause of serious prejudice to interests of WTO members for subsidies that distort capacity</td>
<td>No</td>
</tr>
<tr>
<td>Yes</td>
<td>Stronger subsidy notification incentives</td>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
<td>Expand list of non-actionable subsidies</td>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
<td>Eliminate developed countries’ AMS entitlements for agricultural subsidies</td>
<td>Yes</td>
</tr>
<tr>
<td>EU and Japan support China’s position; US opposed</td>
<td>End the AB appointment blockage</td>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
<td>Improve trade remedies rules</td>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
<td>Improve rules on security exception to prevent misuse</td>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
<td>Tightening rule on unilateral measures inconsistent with WTO rules</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Source: Draper et al. (2020).

3.2.3 Advanced WTO members claiming developing country status

A specific feature of the ASCM is to acknowledge that subsidies may play an important role in economic development programmes of developing countries. The Agreement recognises three categories of developing country Members that all benefit from a more favourable treatment: LDCs, Members with a GNP per capita of less than USD 1000 per year which are listed in Annex VII to the Agreement, and other developing countries. The lower a Member’s level of development, the more favourable the treatment it receives with respect to subsidies disciplines. As such, with regard to prohibited subsidies, LDCs are exempted from the prohibition on export subsidies and other developing countries have an eight-year period to phase them out their export subsidies. In addition, LDCs have eight years to phase out import-substitution subsidies while other developing countries have five years to eliminate them. Developing countries also receive preferential treatment if their exports are subject to countervailing duty investigations. Claiming the developing country status, China opted out of the eight-year transitional period to implement the prohibition of paragraph 1(b) of Article 3 relating to subsidies contingent. However, with regards to the notification requirement under Article 25 of the ASCM, China’s subsidies are often notified with years of delay (Hu, 2019).

In the EU Concept Paper on WTO Modernisation, the European Commission supported reforms of the Special and Differential Treatment and Other Special Measures (SDT) provisions in future WTO agreements. The EU argued that the current distinction between development and developing countries no longer reflected economic reality as some developing countries now rank among the world’s top trading nations. The US–EU–Japan Trilateral Trade Ministerial Cooperation also called on advanced
WTO members that claim developing country status to undertake full commitments to ongoing and future WTO negotiations. While China’s developing member status is openly challenged by several WTO Members, the country has repeatedly reiterated its attachment to its identity as a developing country within the WTO framework. The European Commission, as well as European businesses, support the idea that China can no longer be regarded as a developing country. At the July 2020 meeting of the WTO General Council, China recalled that in an international organisation with developed and developing Members, non-reciprocity was a means and a principle to realise equity, and argued that reclassification of WTO members was not a way out. China as well as other developing members also pointed out that the current practice of self-designation of developing country members was the most pragmatic means of applying the SDT (WTO, 2019b).

### 3.3 Other major international fora to control subsidies

Other international fora such as the G7, G20, the Global Forum of Steel Excess Capacity (GFSEC) facilitated by the OECD, and the Governments/Authorities’ Meeting on Semiconductors (GAMS) have also been acting to strengthen control over subsidies and their impact on market distortions. Following up on the discussions from the Charlevoix G7 Summit in June 2018, in May 2021, the **G7 Trade Ministers called for the start of negotiations to develop stronger international rules** on market-distorting industrial subsidies and trade-distorting actions by state-owned enterprises. The objective is to continue to tackle unfair practices that force companies to transfer technology to the state or to competitors.

The OECD has been active in identifying and estimating the value of government support that benefit particular sectors of the economy since the 1980s. In March 2021, the **OECD Steel Committee** expressed the need to accelerate their work on a subsidies database as steel market conditions have rapidly deteriorated as a result of the COVID-19 crisis. The pandemic had accelerated the decline in global trade of steel. Government subsidies and other support measures and interventions also led to distortions in steel trade flows and contributed to trade tensions. Committee members agreed to resume collecting subsidy data on the world’s largest steel producing jurisdictions, including those where recent data on increasing production has raised concerns about potential government support. This marks a further step towards improving transparency about support measures and will feed into future work examining the impact of these measures on global steel markets.

On 26 October 2020, a ministerial meeting of the Global Forum on Steel Excess Capacity (GFSEC) co-organised by the Forum’s Co-Chairs – the EU and the Republic of Korea – and facilitated by the OECD took place. The 29 Ministers and senior government officials from GFSEC members discussed, inter alia, the detrimental impact of excess capacity on the steel industry generated by market-distorting subsidies. Such measures distort competition by sustaining uneconomic plants or by encouraging investment in additional steelmaking capacity that would not otherwise be built. Recognising the challenges facing their steel industries, the participants at the meeting jointly recommended that G20 Leaders consider to: firmly maintaining the problem of excess capacity on the G20 agenda; promoting

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24 G7 Trade Ministers’ Communiqué, 28 May 2021. Available at: https://www.g7uk.org/g7-trade-ministers-communique/.

25 The **OECD Steel Committee** has 25 members (Austria, Belgium, Canada, the Czech Republic, Finland, France, Germany, Hungary, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, Poland, Portugal, the Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, the UK, the US and the EU).

26 Statement by Mr Ulf Zumkley, Chairman of the OECD Steel Committee, 89th session of the Steel Committee, 18-19 and 22-23 March 2021. Available at: https://www.oecd.org/industry/ind/89-oecd-steel-chair-statement.htm.

27 The meeting was held virtually due to the ongoing COVID-19 global pandemic.
the GFSEC principles in tackling the problem; and supporting the GFSEC as a multilateral way forward, which is open to all G20 and interested OECD members.28

The Governments/Authorities’ Meeting on Semiconductors (GAMS) was established by the US, Japan, Korea, and the European Commission to promote growth of the global semiconductor market. It has maintained its commitment to increasing transparency through regular sharing of information and analysis and assessment of subsidies and other forms of government support. It acknowledges that this is vital to promoting alignment with the principles of the Guidelines and WTO rules, and to avoid non-market-based support that can lead to excess capacity, creating unfair competitive conditions, hindering innovation, and undermining the efficiency of global value chains.29

More recently at bilateral level, as part of the first Trade Technology Council (TTC) meeting in September 2021, the EU and the US have expressed intention to share information on non-market distorting policies in order to increase the efficiency of their domestic measures and to develop strategies for responding to such practices. The categories covered by the statement include market-distorting industrial subsidies, discriminatory treatment of foreign companies, and any other form of support of anti-competitive government supports given to SOEs and other businesses (European Commission, WEBd).

4 Conclusions

This in-depth analysis presented a comprehensive overview on the EU geo-economic context, legal framework, and reform process on foreign subsidies and public procurement.

Section 1 of the paper defined what subsidies are, their importance, and how they may create an uneven playing field. The wide reliance of government subsidies worldwide puts pressure on EU companies, unduly affecting their competitiveness vis-à-vis third-country companies both abroad and within the EU. The EU is one of the largest and most open economies, making it particularly vulnerable to unfair competition. Moreover, EU openness is often not matched by equal openness in other markets, particularly in the case of public procurement. This lack of reciprocity represents a burden for EU competitiveness and strategic autonomy, which in the long run may reduce the benefits and endanger the sustainability of continued open markets.

Section 2 presented the existing toolset within the EU legal framework. The analysis of EU competition rules showed that subsidies granted by non-EU governments to companies active in the EU fall outside state aid control, antitrust and merger control rules. To address this, the analysis focused on three main initiatives.

- **Trade defence and FDI screening instruments (i):** Anti-dumping and anti-subsidy measures were modernised in 2017, in line with WTO requirements. The recently adopted EU framework for FDI screening aims to prevent hostile acquisitions of strategic assets while preserving a welcoming environment for foreign investments.

- **The Proposal for an IPI (ii),** whose negotiations have been recently relaunched following the agreement reached by the Council on its position regarding the Commission proposal, is based on the premise that further regulating access to the EU’s public procurement markets would encourage the reciprocal opening of public procurement markets from foreign entities.

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The proposed Regulation on foreign subsidies distorting the internal market (iii) is the first piece of legislation describing the concept of ‘foreign subsidy’. It identifies the categories of subsidy which are more likely to distort competition, the criteria to assess their distortive impact on the internal market and the set of remedies and measures to tackle these subsidies and to restore fair and competitive markets.

Section 3 looked at EU involvement at the international level. The WTO Agreement on Government Procurement established a framework for reciprocity and non-discrimination in the area of public procurement, but its effectiveness is limited by the fact that several countries, including China, are still not subject to its obligations. The WTO Agreement on Subsidies and Countervailing Measures suffers from chronic low compliance. Consequently, the EU repeatedly proposed ways to modernise the WTO system, including the scope of the current agreements, the way countries negotiate and obtain access, and the current definition of a developing country. Finally, the EU is also taking the lead on modernising rules on subsidies and public procurement in the relevant G7, G20, OECD, and GAMS fora.
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5.2 Legislation


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5.3 Websites


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