RESPONSE OF CLIFFORD CHANCE LLP TO THE WHITE PAPER ON LEVELLING THE PLAYING FIELD AS REGARDS FOREIGN SUBSIDIES

Clifford Chance LLP welcomes the opportunity to respond to the White Paper on levelling the playing field as regards foreign subsidies. Our comments below are based on the substantial experience of our lawyers of advising on EU State aid and WTO laws for a diverse range of clients, and across a large number of jurisdictions. However, the comments below do not necessarily represent the views of every Clifford Chance lawyer, nor do they purport to represent the views of our clients.

QUESTIONS RELATING TO THE THREE MODULES - GENERAL QUESTIONS

Q1. Do you think there is a need for new legal instruments to address distortions of the internal market arising from subsidies granted by non-EU authorities ('foreign subsidies')?

No.

Please explain and also add examples of past distortions arising from foreign subsidies.

1. We recognise that foreign subsidies have, in some cases, caused some distortions to the EU's internal market and that the regime proposed by the White Paper is seeking to address a legitimate problem. However, our view is that the proposals are not the most appropriate way to address that problem and that they risk having substantial adverse and unintended consequences. In particular, we have four fundamental concerns.

2. First, the regime would mean that EU law recognises the right of EU member states to grant market-distorting subsidies that are in the interests of the EU (as verified through the State aid approval process), but not the right of foreign jurisdictions to grant market-distorting subsidies that are in their own interests, unless they also serve a "public policy interest recognised by the EU", as only those meeting a test for being in the EU interest would escape redressive measures. Foreign states may have public policy interests that are different to those of the EU, but are still legitimate. For example, in developing countries subsidies may play an important role in nurturing domestic businesses that and facilitating the transition to a developed market economy (as implicitly recognised by the preferential treatment for developing countries if the WTO Agreement on Subsidies and Countervailing Measures (**ASCM**)), and this may necessitate support to sectors and industries that need no support within the EU. This point raises issues of international comity that are best resolved through bilateral or multilateral international agreements, not the unilateral introduction of powers to impose redressive measures.

3. Second, the logical consequence of the point above is that if the EU introduces powers to impose remedies on businesses that have received such subsidies from foreign public bodies, foreign governments are likely to introduce their own powers to impose remedies on businesses that have received lawful State aid from EU public bodies. Any benefit in the form of less unfair competition for EU businesses with activities focused in the EU would be outweighed by the harm to EU businesses with activities outside the EU and the economic impact of increased barriers to global trade and foreign investment.

4. Third, the regime would inevitably act to deter some foreign investment into the EU, and into EU-based businesses. Given the very substantial and varied benefits of foreign investment for the EU, the proposals should be the subject of a careful and rigorous impact assessment that balances the likely loss of those benefits against the putative harm cause by foreign subsidies.

5. Fourth, the regime risks being ineffective and discouraging foreign countries from opening up their markets, again to the detriment of EU businesses with activities outside the EU. As the White Paper notes, foreign governments can grant advantages to businesses not only through subsidies but also through "selective market opening, licensing and other investment restrictions". As the proposed regime would not catch these advantages, because the resulting monopoly profits do not amount to a financial contribution by a government, it would create incentives for foreign governments to rely more heavily on protectionist measures of this sort.

Q2 Do you think the framework presented in the White Paper adequately addresses the distortions caused by foreign subsidies in the internal market?

Other.

Please explain.

6. Please see our responses below in respect of the individual Modules.

QUESTIONS RELATING TO MODULE 1

Q1 Do you consider that Module 1 appropriately addresses distortions of the internal market through foreign subsidies when granted to undertakings in the EU?

No.

Please explain.

7. For the reasons set out above in response to question 1 of the general questions, we do not consider that the unilateral introduction of powers to impose redressive measures on recipients of foreign subsidies is an appropriate way to address concerns about the impact of foreign subsidies on the internal market. We also have some doubts regarding the Commission's assertion that there is a gap in WTO law concerning "foreign subsidies" that necessitates the introduction of the proposed regime.[1]

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1 The Commission considers that the ASCM only covers subsidised imports of goods and consequently does not apply to 'trade in services' and to 'investment' (i.e., firms establishing in the EU and producing goods/providing services from within the EU) (page 10 of the White Paper). However, with regard to 'investment', while it may be argued that the SCM Agreement does not cover 'investment' as it requires (for non-prohibited subsidies, only) that the subsidies be 'specific to an enterprise or industry or group of enterprises/industries within the jurisdiction of the granting authority', that provision can also be read as not referring solely to 'territorial' jurisdiction. In addition, with regard to trade in services, while it is true that the GATS lacks (for the moment) a specific discipline on subsidies, it is also true that other GATS provisions may provide a remedy (even if partial) to the issue of foreign subsidies, in particular the national treatment obligation in Article XVII, which prohibits WTO members (that have undertaken specific commitments) from discriminating against like services/service suppliers of other WTO Members - arguably, independently of where those services/service suppliers are located.

8. If, however, the Commission does proceed with these proposals, we submit that they should be refined in various respects, as set out in our responses to the questions below.

9. In this respect, one over-arching point is that the White Paper is silent as to how the Commission proposes to design the regime in compliance with its obligations under international law. It seems to us inevitable that foreign (or foreign-owned) businesses would be affected differently by the proposed legislation than like businesses from the EU, and in several respects (outlined below) this differential treatment may be less favourable. Accordingly, to the extent the regime applies to services sectors and modes of supply within the scope of the EU's GATS commitments, it is at risk of violating the EU's national treatment obligation under Article XVII of the GATS. In addition, to the extent the regime limited investments in sectors in which mode 3 commitments have been undertaken by the EU under GATS, the regime could also violate the EU's market access commitments under the Article XVI of the GATS. Similar issues would arise under services, investment and government procurement chapters of Free Trade Agreements, where the EU has committed to market access, national treatment and MFN disciplines.

10. In addition, the broad definition of a "foreign subsidy" in the White Paper (including "foreign subsidies granted to an undertaking established in a third country", where "third country" does not appear to exclude the subsidising country), would mean that the proposed regime would apply to some subsidies that clearly fall within the scope of the ASCM, and would therefore be in breach of Article 32.1 ASCM and go beyond what is necessary because of the gap in WTO law.

11. We recognise that it may be possible to formulate elements of the regime in a manner that is consistent with the EU's international obligations, either on the basis that they would not in fact be discriminatory, because the EU has in place equivalent rules for subsidies granted by its own Member States; or under applicable exceptions such as Article XIV(c) of the GATS.

12. However, whether this is the case will, in our view, be finely balanced and ultimately rest on a complex analysis of the equivalency of the regime with internal market rules. Consequently, it will be important to structure the regime in a way that ensures that the different treatment of businesses in receipt of foreign subsidies is no less favourable than those that receive subsidies from EU member states under the EU State aid rules. There are various aspects of the regime proposed by the White Paper that would appear to afford less favourable treatment to recipients of foreign subsidies, including the following:

    (a) The possibility that the legitimate interests of the granting State can justify a subsidy granted to a recipient of EU State aid, but may not suffice to justify a subsidy granted by a foreign public body (see our response to Question 4 below).

    (b) The availability of block exemptions and advance clearance for recipients of State aid, which are not envisaged by the White Paper to be available to recipients of foreign subsidies. This suggests that one clear principle should be that any subsidy that would have been block exempted or cleared as compatible with the internal market if it had been granted by an EU member state, must also be accepted as incapable of distorting the internal market when granted by a foreign public body.

(c) The difference in the scope of redressive measures that can be imposed. Again, this suggests a principle that no redressive measure should be capable of causing a financial loss to the recipient that is greater than the value of the subsidy received.

(d) The procedural process, which places the burden and cost of compliance and responding to the investigation on the recipient rather than (as is the case under the EU State aid rules) the granting government.

(e) If Module 2 is implemented, recipients of foreign subsidies would be subject to mandatory filing and standstill obligations and the possibility of having their acquisitions of other businesses prohibited, whereas recipients of unlawful State aid face no such obligations or risks.

13. In addition, we consider that, to further minimise inconsistent treatment between recipients of subsidies from EU member states and recipients of subsidies from foreign governments, the Commission should consider applying the concepts developed under EU State aid law for the purposes of defining which foreign subsidies fall within the scope of the proposed regime, rather than those developed under the WTO rules, i.e. a selective advantage granted through State resources, rather than a financial contribution that confers benefit. That would also have the advantage of allowing the Commission to rely on the considerable body of EU case law and decisional practice that has developed those concepts, which is much greater in volume and detail than the case law dealing with the WTO concepts.

Q2 Do you agree with the procedural set-up presented in the White Paper, i.e., 2- step investigation procedure, the fact-finding tools of the competent authority, etc.? (See section 4.1.5. of the White Paper)

Other.

Please explain.

14. We agree that if the proposals are implemented, a two-step procedure is appropriate and that the relevant authority will need suitable powers of investigation. However, as with other areas of EU law, these powers should be subject to the defence of State compulsion, such that no penalty can be imposed if an alleged recipient cannot provide the relevant information without infringing a legal prohibition of a foreign country.

15. As regards the possibility of "fact finding visits" to the premises of alleged recipients, we do not agree that such powers should be available to relevant authorities, even if subject to a right of consent for the foreign government that granted the alleged subsidy, as the Commission has no equivalent power (under Regulation 2015/1589) when investigating the alleged grant of unlawful State aid (see our comments in response to Question 1 above regarding the need for consistency between the proposed regime and the State aid regime).

16. It will also be important that alleged recipients of foreign subsidies are accorded appropriate due process. In this respect, a key difference between investigations under the proposed regime and State aid investigations would be that the procedure is between the Commission and the recipient of the alleged subsidy, not the State that granted it.

In addition, an obligation to make a "redressive payment" to an EU member state (rather than recoupment by the granting foreign State) is likely to be indistinguishable from a (quasi-) criminal financial penalty for the purposes of the Charter of Fundamental Rights of the EU. Consequently, it will be important that the investigative procedure affords recipients of alleged subsidies full rights of defence, including all the rights available to businesses that are subject to investigations under Articles 101 and 102 TFEU.

17. Finally, the White Paper does not envisage any possibility for businesses to obtain advance clearance from the relevant authority before making a significant investment in the EU. Unless such a mechanism exists, there will be a significant risk, in our view, that beneficial foreign investment is deterred because investors cannot obtain comfort that redressive measures will not subsequently be imposed on them if they proceed with an investment.

Q3 Do you agree with the substantive assessment criteria (section 4.1.3) and the list of redressive measures (section 4.1.6) presented in the White Paper?

No.

Please explain.

18. The Commission's justification for imposing remedies on recipients of foreign subsidies that are different to the repayment obligation that applies to recipients of incompatible State aid is not, in our view, coherent. The fact that "it may be difficult in practice to establish that the foreign subsidy is actually and irreversibly paid back to the third country" seems to us to be an irrelevant consideration, given that it would be equally difficult to establish that the third country has not granted a further subsidy to compensate for the financial loss caused by whatever redressive measure is imposed on the recipient.

19. Moreover, the fact that the effect of the proposed redressive measures would be to enrich the EU institutions and EU member states at the expense of foreign governments suggests that it would greatly increase the risk that foreign states introduce "retaliatory" regimes to State aid received by EU businesses.

20. Our view, therefore, is that the default remedy should be the same as under the EU State aid regime, i.e. repayment to the granting government, with interest. It would in fact be simple to verify that the relevant funds have in fact been transferred, and any concerns that a repayment has been reversed could be dealt with in the same was as any other foreign subsidy, or by providing for the possibility of alternative redressive measures (such as a bar on participation in public procurement procedures or access to EU grant funding) in the event that it is established that a repayment has been effectively reversed.

21. In addition, if national authorities are empowered to investigate subsidies and impose redressive measures, the exact role of the Commission would have to be clarified, e.g. whether the Commission will have powers to issue binding opinions on the appropriate remedy, in light of the potential link between the EU interests that are identified by the Commission (for which it will have exclusive competence) and the remedies that may be most appropriate in light of those EU interests.

Q4 Do you consider it useful to include an EU interest test for public policy objectives (section 4.1.4) and what should, in your view, be included as criteria in this test?

Other.

Please explain.

22. As explained in our response to question 1 the Module 1 questions, we consider that a recipient of a foreign subsidy must not be subject to redressive measures if the same subsidy would have been cleared as compatible with the internal market, had it been granted by an EU member state. Such a principle would, in our view, be a necessary (albeit perhaps not sufficient) requirement for compliance with the EU's obligations under international law.

23. However, for the reasons set out in response to question 1 of the general questions, we also consider that the test should go further, and take account of the legitimate interests that a foreign government may have when granting a subsidy. Such legitimate interests could include, for example, digital transformation, protection of the environment, the development of economic activities in respect of which there is a market failure in the country in question (even if not in the EU), or the protection of a country's domestic businesses from the economic impact of a pandemic. The White Paper appears to suggest that such interests could form part of the EU interest test, as a "public policy objective recognised by the EU", but it is unclear whether this would extend to public policy objectives that are legitimate for a particular foreign country to pursue – e.g. because of its level of development – but which are not pursued by the EU. We submit that it should, and that there should be clear guidelines that set out:

(a) the types of public policy objectives that are "recognised by the EU" as being legitimate (even if not pursued by the EU);

(b) how the Commission will assess the "positive impact that the investment might have within the EU";

(c) the role that State aid guidelines of the Commission will have in such an assessment; and

(d) how public policy objectives and positive impacts will be weighed against each other and the identified distortions to the internal market.

Q5 **Do you think that Module 1 should also cover subsidised acquisitions (e.g. the ones below the threshold set under Module 2)? (section 4.1.2)**

No.

Please explain.

24. For the reasons set out in response to the Module 2 questions, we disagree that the introduction of a mandatory filing regime for businesses in receipt of financial contributions from foreign governments is desirable. For the same reasons, the introduction of powers to impose redressive measures on below-threshold transactions is even less desirable. Creating possibilities for deals to be prohibited and unwound after they have closed will harm legal certainty and deter investment.

25. If such powers are introduced, then there ought to be a mechanism for businesses to obtain advance clearance from the relevant authority before making an acquisition (i.e. a voluntary filing regime). Unless such a mechanism exists, there will be a significant risk, in our view, that beneficial foreign investment is deterred because investors cannot obtain comfort that redressive measures will not subsequently be imposed on them if they proceed with an acquisition. However, the need for legal certainty that an investment will not be unwound would mean that such a voluntary filing system could be overwhelmed with filings unless it is also subject to some minimum jurisdictional thresholds below which the relevant authority would have no jurisdiction to review a transaction.

26. Indeed, if powers to impose redressive measures on mergers are introduced, we consider the optimal procedural regime – i.e. the one that would minimise deterrence of desirable foreign investment - to be one in which:

(a) there are no mandatory filing obligations at all;

(b) the relevant authority can only impose redressive measures on transactions meeting certain thresholds (see our responses to the Module 2 questions for our views on the appropriate thresholds); and

(c) a voluntary filing mechanism exists that allows businesses to obtain advance clearance of a transaction if they so desire.

Q6 Do you think there should be a minimum (de minimis) threshold for the investigation of foreign subsidies under Module 1 and if so, do you agree with the way it is presented in the White Paper (section 4.1.3)?

Yes.

Please explain.

27. A de minimis threshold is vital to minimise excessive burdens on foreign investors. In line with the principle outlined in our responses to the questions above – that a subsidy should not result in redressive measures if it would have been exempt or found to be compatible with the internal market had it been granted by an EU member state – we consider that a threshold that is aligned with the State aid de minimis block exemption would be appropriate.

Q7 Do you agree that the enforcement responsibility under Module 1 should be shared between the Commission and Member States (section 4.1.7)?

No.

Please explain.

28. It seems to us that it would be highly undesirable to have multiple national authorities investigating the same foreign subsidy in parallel. Unlike antitrust investigations (where the infringing conduct may take place in different ways in different jurisdictions) all national authorities would ultimately be investigating the same foreign subsidy, creating inefficient duplication and the risk of conflicting approaches to the same facts and substantive issues.

29. Moreover, if national authorities are unable to apply the EU interest test (as is proposed) even greater inefficiency would be introduced, as the Commission would also need to investigate the same facts for the purposes of deciding whether the EU interest test is met.

30. We therefore submit that, in the first instance, the Commission should assume exclusive jurisdiction over all foreign subsidies, or, alternatively, over those involving a recipient that is active in two or more EU member states. Jurisdiction could then be extended to national authorities in the future if there is evidence that this would result in more effective enforcement.

QUESTION RELATING TO MODULE 2

Q1. Do you consider that Module 2 appropriately addresses distortions of the internal market through foreign subsidies that facilitate the acquisition of undertakings established in the EU (EU targets)?

No.

Please explain.

31. The points set out in our response to question 1 of the general questions are equally applicable to the Module 2 proposals.

32. We also have a number of reservations that are specific to Module 2, which are set out in response to the questions below.

33. However, our over-arching concern is that the proposals in this area are not founded on robust evidence that subsidised acquisitions cause economic harm of a magnitude that merits the imposition of filing burdens and bidding disadvantages on foreign investors.

34. In particular, the perceived problem that Module 2 seeks to address is that subsidised acquisitions "may distort the level playing field with regard to investment opportunities in the internal market", as where a subsidised acquirer outbids competitors for the acquisition of a target, it "distorts the allocation of capital and undermines the possible benefits of the acquisition for example in terms of efficiency gains". This implicitly assumes that subsidies affect markets for corporate control in the same way as they do markets for goods and services. We question that assumption, for two reasons:

   (a) unlike a subsidised provider of goods and services, a subsidised bidder does not necessarily obtain any advantage from their subsidy, they merely deny another bidder the potential opportunity to create efficiencies. However, a number of economic studies suggest that mergers often create no, or minimal, efficiencies, even when the parties are active in the same sector. It is striking to us that the White Paper offers no empirical economic evidence of the harm that may be caused by such distortions in investment opportunities, or the magnitude of such harm; and

   (b) any such harm is offset, and potentially outweighed, by the benefits for the EU economy that arise when sellers of EU businesses are able to secure higher prices, e.g. benefits in the form of increased incentives to innovate and invest in their businesses.

35. It seems to us that any steps to inhibit subsidised acquisitions should be taken only on the basis of rigorous economic studies demonstrating that they give rise to net negative effects. At minimum, any new regime should be limited to the most obvious and egregious types of transaction, with a view to further expansion of the regime once its benefits have been established.

36. The lack of any economic analysis of the effects of subsidised acquisitions makes it even less justifiable that this form of subsidy is treated (as it is in the White Paper) as inherently likely to cause "serious harm" to the internal market and therefore "normally considered to distort the internal market" (this also applies to the treatment of such subsidies under Module 1).

Q2 Do you agree with the procedural set-up for Module 2, i.e. ex ante obligatory notification system, 2-step investigation procedure, the fact-finding tools of the competent authority, etc.? (See section 4.2.5 of the White Paper)

No.

Please explain.

37. While we agree that a two-step procedure is appropriate, and suitable fact-finding powers would be necessary, we do not agree that the test for opening a second phase investigation should be that there is "sufficient evidence tending to show that the acquiring company could have benefitted from foreign subsidies facilitating the acquisition". The test for a second phase should instead mirror the overall substantive test, i.e. there should be sufficient evidence tending to show that (i) the acquiring company could have benefitted from foreign subsidies facilitating the acquisition; (ii) that the acquisition could significantly distort the internal market; and (iii) the acquisition is not in the EU interest.

38. As regards the type of filing regime, our view is that an ex-ante obligatory notification system is not the most appropriate procedural option. In particular, the usual justification for mandatory filing obligations – that in the absence of such obligations harmful transactions would go undetected – does not appear to apply to a significant extent. If the concern is that other bidders for a target business are denied an efficient investment opportunity, then those aggrieved bidders can be relied on to report their concerns to the Commission.

39. In contrast, the benefits of a voluntary filing system are particularly pronounced for a regime to address subsidised acquisitions, as the proportion of investments in EU business that would give rise to concerns meriting a detailed investigation is likely to be a very small and – as the Commission will be aware – designing clear and objective mandatory filing thresholds that focus only on the transactions most likely to be problematic is difficult.

40. Similarly, the typical justifications for a standstill obligation (prohibiting implementation prior to clearance) are less applicable in the context of the proposed regime. Under merger control regimes, standstill obligations may (arguably) prevent competitive harm arising during the review process and guard against the possibility that an alternative buyer cannot be found in the event that the target is required to be divested. However, those considerations do not apply to the proposed regime:

(a) the proposed regime does not target anticompetitive effects (the competitive effects of subsidies being already addressed in reviews under the EU Merger Regulation);

(b) subsidised buyers have no inherent incentive to deteriorate the target's competitive activities;

(c) even if the Commission were to require the target to be divested, a subsequent purchaser would not be prevented from achieving efficiencies by the target's prior ownership by a subsidised investor; and

(d) there should be no concern that an alternative buyer could be found, given that the theory of harm is founded on the attractiveness of the target as an investment opportunity for other bidders.

41. Finally, if a Module 2 filing regime is introduced, it will be important to minimise inefficient duplication and overlap with merger control and foreign investment filings that are required. For example, where a transaction would be subject to both a Module 2 filing and an EU Merger Regulation filing, it should be possible (at the parties' discretion) to notify under both procedures using a common filing form, with the same case team.

Q3 Do you agree with the scope of Module 2 (section 4.2.2) in terms of:

definition of acquisition;

No.

definition and thresholds of the EU target (4.2.2.3);

No.

definition of potentially subsidised acquisition.

No.

Please explain. As regards thresholds, please provide your views on appropriate thresholds.

<u>Definition of an acquisition</u>

42. We agree that the EUMR concept of decisive influence is sufficiently objective and well-understood to form the basis for filing obligations under the proposed regime. In addition, it is of direct relevance to the theory of harm that the Commission is seeking to address: if a subsidised investor acquires decisive influence, it will be able to prevent another investor from integrating with the target in a way that creates efficiencies, but if no decisive influence is acquired, it will remain possible for another investor to achieve those efficiencies.

43. For the same reason, we do not see any merit in either a shareholding threshold or a threshold based on the concept of material influence. If some lower test for control is used, it should be clearly and objectively defined – through detailed guidance - by

reference to the specific veto rights that could allow a minority investor to prevent an acquisition of corporate control by another investor. The test for material influence that derives from the UK merger control regime (or its German counterpart, the test for competitively significant influence) is inappropriate for this purpose, as it catches investments that do not deny other investors the opportunity to acquire corporate control and, through the use of that control, achieve integrative efficiencies.

44. Moreover, non-controlling minority investments are a favoured investment strategy of many Sovereign Wealth Fund investors, which have been a vital source of foreign investment into the EU in recent years. It is therefore of particular importance that they are not deterred unnecessarily.

<u>Definition and thresholds of the EU target</u>

45. We favour the use of a quantitative turnover threshold, for which the established principles set out in the Commission's Jurisdictional Notice could be applied. A threshold based on EU-wide target turnover of €100 million would, in our view, be appropriate, as it aligns with the threshold below which a party's activities are considered not to have an EU dimension under the EUMR.

46. With regard to qualitative thresholds, the White Paper appears to suggest that mandatory filing obligations could be based on whether the target company has "critical assets" or "low turnover but high growth or technology development prospects, which may be of particular economic or strategic interest". While we favour any criteria that limit the scope of filing obligations to particular sectors, rather than being generally applicable, the relevant sectors and activities of interest would need to be carefully and precisely defined. Moreover, numerous EU member states now have foreign investment and national security screening regimes that apply where the target has activities involving critical infrastructure or of "economic or strategic interest", such that targeting these activities in a subsidy filing regime would risk duplicative, overlapping and inconsistent assessments. Similarly, a transaction value threshold gives rise to various difficulties, with which the Commission will be familiar from its deliberations over whether to introduce such a threshold under the EUMR.

<u>Definition of a potentially subsidised acquisition</u>

47. The focus on financial contributions from a foreign government will catch an excessively wide range of businesses, both EU-based and foreign, as it includes those that have made sales or purchases of goods or services to/from a foreign government in the past three years in excess of a given value, irrespective of whether those transactions were on market terms. This approach itself risks distorting investment opportunities in the internal market, as businesses with activities outside the EU will find themselves at a disadvantage when bidding for assets against those that do not have mandatory filing and standstill obligations.

48. This is another reason why a voluntary filing regime would be more appropriate (see our response to question 2 above). Under a voluntary filing regime, the jurisdictional test could be set by reference to whether there was a foreign subsidy (not just a financial contribution) without giving rise to the concerns regarding risk or error or circumvention that are identified in the White Paper (section 4.2.2.2). It would also make it possible to define the quantitative threshold by reference to the amount of the

actual subsidy (rather than the much larger amount of a "financial contribution") as a proportion of the acquisition price.

Q4 Do you consider that Module 2 should include a notification obligation for all acquisitions of EU targets or only for potentially subsidised acquisitions (section 4.2.2.2)?

Other.

Please explain.

49. As explained in response to questions 2 and 3, we consider that Module 2, if implemented, should have no mandatory filing obligations and that a voluntary filing regime is much more appropriate to the specific objectives of the proposed regime.

50. However, if mandatory filing obligations are imposed we do not see any benefit in extending those obligations to all acquisitions of EU targets, irrespective of whether the buyer has had any financial contribution from a foreign government.

Q5 Do you agree with the substantive assessment criteria under Module 2 (section 4.2.3) and the list of redressive measures (section 4.2.6) presented in the White Paper?

No.

Please explain.

51. The substantive assessment criteria for Module 2 are broadly the same as those proposed for Module 1, despite the theory of harm that they are seeking to address being very different from subsidies that distort markets for the supply of goods and services (see our response to question 1 of the Module 2 questions above). When measured against that theory of harm – that subsidised acquisitions may foreclose other investors from efficient investment opportunities – many of the listed criteria seem to us to be inappropriate. In particular, we have the following observations:

   (a) The criteria fail to address a key question, which is whether there were any alternative bidders that would have been capable of achieving efficiencies had they acquired the target instead, e.g. because the alternative investor has overlapping or complementary activities. It is stated that the existence of competing offers is "one aspect of the assessment" but is "not determinative". Our view is that, if a business sale has been appropriately advertised and there were no competing offers from trade buyers (i.e. buyers with businesses in the same sector or area of activities as the target that are therefore capable of achieving transaction efficiencies), that is conclusive proof that no other investor has been foreclosed from an efficient investment opportunity.

   (b) The criteria suggest that "outbidding in acquisitions" is a negative factor, despite the fact that the relevant authority will in practice only be reviewing transactions in which the subsidised investor made the highest bid. A more relevant factor would be whether the subsidised bidder is itself able to achieve significant efficiencies that would justify the purchase price that it is paying.

(c) Some of the criteria seem to focus instead on the competitive effects of the transaction, which are not relevant, e.g. cases where the target is active in a concentrated market. It is not clear to us how the concentrated nature of the target's market makes it any more likely that an alternative bidder would have been able to achieve significant efficiencies (as opposed to anticompetitive price increases).

(d) The fact that an acquirer has special or exclusive rights in its domestic market seems to us to be irrelevant to the question of whether acquisitions made by it foreclose other investors of efficient investment opportunities.

52. We also consider that the strict approach towards subsidies that directly facilitate an acquisition is unjustified. The White Paper states that such subsidies will "normally be considered to distort the internal market" due to the "serious harm they cause to the level playing field for investments". However, in the absence of empirical economic evidence (of which the White Paper presents none), such serious harm should not be assumed - see further our response to question 1 of the Module 2 questions above.

53. As regards remedies, the White Paper indicates that the "focus of commitments is likely to be on structural remedies". Again, the fact that the concern relates to investment opportunities, not restrictions of competition, militates against remedies that require a total divestment of the target. In contrast to merger control cases, allowing a subsidised acquirer to retain a minority interest does not risk undermining the purpose of the regime, provided suitable restrictions are placed on the interest to ensure that it cannot be used to inhibit an acquisition of control, and the resulting achievement of efficiencies, by an alternative investor.

Q6 Do you consider it useful to include an EU interest test for public policy objectives (section 4.2.4) and what should, in your view, be included as criteria in this test?

Other.

Please explain.

54. Please refer to our response to question 4 of the Module 1 questions, which is equally applicable to this question.

Q7 Do you agree that the enforcement responsibility under Module 2 should be for the Commission (section 4.2.7)?

Yes.

Please explain.

55. We agree that, in the absence of sufficient experience to determine how many acquisitions would prove to be negatively affected by foreign subsidies, a centralised system at EU level would be the most suitable option. It would lead to lower overall enforcement costs, both for public authorities and companies, and increased legal certainty. Such a system would avoid the need for investors to deal with several Member State authorities at the same time and the duplication of 27 similar merger screening regimes.

56. The precise role of members states in the Commission's review process would have to be clarified (e.g. whether it would be similar to the one assumed during EU merger control review or broader).

QUESTIONS RELATING TO MODULE 3

Q1 Do you think there is a need to address specifically distortions caused by foreign subsidies in the specific context of public procurement procedures?

No.

Please explain.

57. For the reasons set out above in response to question 1 of the general questions, we do not consider that the unilateral introduction of powers to impose redressive measures on recipients of foreign subsidies is an appropriate way to address concerns about the impact of foreign subsidies on the internal market.

58. In addition, the considerations regarding compliance with the EU's international treaty obligations that are set out in our response to question 1 of the Module 1 questions are equally applicable here. In particular, Article IV of the Revised Government Procurement Agreement also imposes limitations on the EU's ability to impose restrictions on foreign participation in covered public procurements.

59. If, however, the Commission does proceed with the Module 3 proposals, we submit that they should be refined in various respects, as set out in our responses to the questions below.

Q2 Do you think the framework proposed for public procurement in the White Paper appropriately addresses the distortions caused by foreign subsidies in public procurement procedures?

No.

Please explain.

60. In our view, if the Module 1 proposals are implemented, it is not <u>necessary</u> or <u>desirable</u> to have a specific regime for public procurement procedures.

61. The Module 3 proposals are not necessary because the relevant authorities with responsibility for investigating subsidies can do so at any time, before or after a public procurement procedure and if necessary would be able to impose redressive measures that prevent the recipient's participation in future public tenders, as well as redressive payments and other measures, which in combination should suffice to deter subsidised participation in public tenders. As noted in the White Paper, the current public procurement framework has operated to date without any specific exclusion ground for the recipients of State aid that is incompatible with EU rules, which also suggests that a procurement-specific regime for foreign subsidies is not necessary.

62. To the extent that subsidised participation in tenders is not deterred in some (likely isolated) instances, the harm caused to competing bidders by allowing a subsidised bidder to win and perform the contract would be much less than the harm that would be caused to contracting authorities and to the public purse by disadvantaging foreign bidders and requiring contracting authorities to delay contract awards. In particular, these include the following harms:

(a) Delays: The White Paper envisages that contracting authorities would be prevented from awarding a contract to an allegedly-subsidised bidder while that bidder is being investigated by a supervisory authority with subsidy enforcement powers. Delays in the award of potentially-important public contracts could have substantial adverse impacts on the delivery of public services that should be avoided if at all possible, particularly when urgent or business critical contracts are at stake. While the White Paper pays lip service to this point by referring to the need to minimise delays, the proposed timeframe of almost four months for an in-depth investigation would in practice cause very substantial disruption. Moreover, subsidy investigations will inevitably be complex (e.g. involving considerations of specificity and advantage in the context of third country economies) and time-consuming – even simple State aid clearances typically take around five months – so it seems to us unlikely that a supervisory authority would be able to come to any definitive conclusion on the presence of market-distorting subsidies within that timeframe.

Such delays would also open up additional opportunities for the winning bid to be challenged by losing tenderers (whether subsidised or non-subsidised). Effectively the conduct of two procedures (rather than just one) and multiple authorities (rather than just the contracting authority) would be open to scrutiny by tenderers' lawyers, and any inconsistencies or subjectivities in decision making can be seized upon as discriminatory. This will particularly be the case in respect of the contracting authority's final decision on whether the subsidy distorts competition for the tender, and even more so if that decision leads to an exclusion from future tenders. In our view, there is a significant risk that contracting authorities may struggle with the complexity of such decisions, so increasing the risk of challenges, both by aggrieved underbidders or by the allegedly-subsidised winning bidder. If the Module 3 proposals are implemented, it will be very important that the envisaged "uniform methodology" for determining distortion is very precise.

(b) Higher costs to the public purse: A regime that delays the award of contracts to potentially-subsidised bidders and creates additional compliance costs for those bidders will inevitably deter some from participating, even if they have not received market-distorting subsidies, and would have submitted the most economically advantageous bid.

Moreover, such a regime would incentivise contracting authorities to avoid, wherever possible, identifying as the winner of a procurement procedure any bidder that has potentially received financial contributions from a foreign government. While we recognise that the EU procurement rules are designed to minimise the exclusion of bidders on subjective grounds, they cannot completely eliminate it from happening in practice. The result would be that contracts are not awarded to foreign (or foreign-linked) bidders that tender the most economically advantageous bids, even where those bidders are subsequently revealed by a supervisory authority not to have received market-distorting subsidies.

63. Public procurement processes may be a useful opportunity to gather information from businesses that have received financial contributions from foreign governments, which could be used by supervisory authorities to inform their enforcement under Module 1 - that in itself should suffice to deter the participation of bidders that actually have received market-distorting subsidies. However, in light of the considerations above, we see no merit in requiring contract awards to be suspended (or unwound) in the event of an investigation or adverse finding by a supervisory authority.

Q3 Do you consider the foreseen interplay between the contracting authorities and the supervisory authorities adequate e.g. as regards determination of whether the foreign subsidy distorts the relevant public procurement procedure?

No.

Please explain.

64. Please see our response to Question 2 above.

Q4 Do you think other issues should be addressed in the context of public procurement and foreign subsidies than those contained in this White Paper?

No.

QUESTIONS RELATING TO THE INTERPLAY BETWEEN MODULES 1, 2 AND 3

Q1. Do you consider that

a. Module 1 should operate as stand-alone module

No.

b. Module 2 should operate as stand-alone module

No.

c. Module 3 should operate as stand-alone module

No.

d. Modules 1, 2 and 3 should be combined and operate together?

Yes.

Please explain.

65. Given that investigations under each of the Modules would involve substantially the same substantive issues, it makes sense to us for them to be operated in a coherent and joined-up way. It would be important to minimise regulatory burdens on business

operating in the EU and that any review mechanisms are efficient and cost effective for both for businesses and the relevant supervisory authorities.

Clifford Chance LLP
September 2020