ALLEN & OVERY LLP

RESPONSE TO THE CONSULTATION ON THE WHITE PAPER ON LEVELLING THE PLAYING FIELD AS REGARDS FOREIGN SUBSIDIES

23 September 2020

1. INTRODUCTION

1.1 We welcome the opportunity to comment on the questions posed in the consultation on the European Commission's White Paper on levelling the playing field as regards foreign subsidies (the **White Paper**). We answer each question in the order that it appears in the consultation questionnaire.

1.2 Allen & Overy LLP (**A&O**) is a global law firm that helps the world's leading businesses to grow, innovate and thrive. We are participating in this consultation exercise to share our views on some of the legal questions arising from the White Paper.

COMMENTS ON MODULE 1

2. Module 1 Question 1: do you consider that Module 1 appropriately addresses distortions of the internal market through foreign subsidies when granted to undertakings in the EU?

2.1 As a law firm, we do not consider that it is appropriate for us to answer this question substantively as the issues raised are primarily related to matters of policy and economics. Our principal concerns, as a law firm, are that the regime is clear, predictable and transparent and provides adequate procedural safeguards in the light of the risk that the proposals, if enacted, may stifle valuable foreign investment in the EU, unduly increase the regulatory burden on investors of all nationalities and potentially negatively affect undertakings established in the EU.

3. Module 1 Question 2: 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)

3.1 We agree that given the proposed content of Module 1 it is appropriate for there to be a 2-step investigation procedure as detailed in section 4.1.5 of the White Paper. However, a number of points should be addressed when drafting the legislation, including the following:

(a) section 4.1.5.1 suggests that an in-depth investigation "may" be initiated if the competent supervisory authority "has the *suspicion* that there is a foreign subsidy that may distort the internal market" (emphasis added). A mere "suspicion" is a very low threshold which is likely to result in most investigations proceeding to the in-depth stage. We would propose that a higher threshold, such as "serious doubts" as provided for in Regulation (EC) 139/2004 for the opening of an in-depth investigation, should be adopted to limit the burden on the competent supervisory authorities and potentially affected undertakings;

(b) the procedure should be prescribed in detail with the shortest possible time limits associated with each step. Doing otherwise would inevitably negatively affect foreign investors' decisions and would likely detrimentally affect undertakings including those established in the EU;

(c) to the extent both national authorities and the European Commission would be competent for enforcing Module 1 (as proposed in section 4.1.7), the substantive and procedural framework (including time-limits, rights of parties concerned, and obligations of the reviewing authorities) would need to be uniform across the EU in order to mitigate the risk of different

approaches being taken by the competent authorities which could lead to forum shopping and seriously negatively impact the internal market;

(d) all undertakings subject to investigation should be immediately informed of an investigation's commencement and able to participate fully in the preliminary review process to ensure the adoption of reasoned and substantiated decisions in accordance with the general principles of transparency and good administration and to safeguard the rights of all undertakings concerned;

(e) the "interested parties" for the purposes of an investigation should be broadly and flexibly defined to ensure that all potentially affected persons can make representations in relation to the subject matter of the investigation. For example, the third State that is, directly or indirectly, implicated, third party entities (including financial institutions) that have provided financing, and consumers' and employees' representatives should be allowed to participate in the proceedings both at the preliminary review stage and during the course of an in-depth investigation. To facilitate this, the competent supervisory authority could, for example, publish a notice giving ten days for "interested parties" to make submissions at both stages of the investigation;

(f) notwithstanding the need to protect the right of consultation/fair hearing of all other parties involved, any information shared by an undertaking taking part in an investigation with a competent supervisory authority should be kept confidential. To ensure that such undertakings are able to participate fully in the investigation information (including through the sharing of commercially sensitive information), safeguards should be provided to protect the information that they have supplied.[1] This is all the more important in light of the fact that relevant information may be subject to strict disclosure regimes under the laws of the third countries concerned;

(g) any fine and periodic penalty payments for failure to provide information in a timely manner should be proportionate and duly take into account the specific legal and factual circumstances that foreign investors may face;

(h) any additional information (the source of which is not an undertaking taking part in an investigation) relied upon by the competent supervisory authorities should be publically available, except where absolutely necessary for reasons of confidentiality. To enable undertakings taking part in an investigation to effectively challenge any conclusions reached by a relevant competent supervisory authority, the information relied upon by it should be made available, at the very least, to the undertaking concerned; and

(i) undertakings concerned should have the possibility to seek recourse against decisions of national authorities and the European Commission. To protect the rule of law, this right should be included in the draft legislation.[2]

4. Module 1 Question 3: 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?

The substantive assessment criteria

4.1 In relation to the substantive assessment criteria in section 4.1.3 of the White Paper, there should be clarity on the precise standard being applied in Module 1. By way of illustration, we are of the view that the test apparently applied in sections 4.1.1 and 4.1.5.1 of the White Paper, which only refers to

[1] See, by way of example in an analogous situation, article 3(4) of Regulation (EU) 2019/452.

[2] See article 3(5) of Regulation (EU) 2019/452.

foreign subsidies that "may" distort the internal market, is too broad as it could technically include any foreign subsidy remotely affecting the EU market. The threshold applied in section 4.1.5.2, which includes "indications of possible or actual distortions *on a scale justifying intervention*" (emphasis added), whilst arguably more reasonable and proportionate, would still leave considerable discretion to the competent supervisory authorities. As a matter of general policy, the standard being applied should be clear, precise and objective. Precisely defining the relevant threshold will be necessary for the fair and consistent operation of Module 1 throughout the internal market, which will be important from the perspective of investors, potentially affected undertakings and the rule of law.

4.2 Relatedly, only distortions that have a "*serious*" effect on the proper functioning of the internal market should be caught. In our view, it would be disproportionate for *all* foreign subsidies that are valued at over €200 000 over a consecutive period of three years[3] to be presumed to have a sufficiently distortive effect on the internal market and potentially be subject to an in-depth investigation and redressive measures. In some circumstances or sectors, a foreign subsidy significantly over €200 000 may have no demonstrable effect.

4.3 Furthermore, where, as is proposed in section 4.1.5.2, "facts available" are used for decision making, the competent supervisory authority should take into consideration that an undertaking concerned may have no access to the information requested by the competent authority or may be prohibited by law or matters of fact from seeking and/or obtaining the requested information. Consequently, any information requests should be required to be reasonable in the light of all of the applicable legal and factual circumstances and a "reasonable excuse" defence should be available where information that is requested cannot be supplied for legitimate reasons. The risk of redressive measures in the context of the enforcement of Module 1 based on "facts available" – despite the genuine impossibility for foreign companies to provide all requested information – may, on its own, have a chilling effect on foreign investments in the European Union.

4.4 Finally, we are of the view that in relation to those factors identified in section 4.1.3.1 of the White Paper, there should be no *presumption* that any particular categories of foreign subsidies create a distortion in the internal market. Rather, whilst it would be appropriate for the legislation to provide an indicative list of foreign subsidies that may be caught, each instance should be assessed on its own merits. For example, it is possible to envisage circumstances where foreign subsidies directly facilitating an acquisition do *not* create distortions in the internal market. Such an example could arise in circumstances where a company in a financially distressed situation is being acquired and only a single non-EU purchaser is interested in completing the acquisition.

The list of redressive measures

4.5 The nature of the redressive measures is principally a question of policy, so our comments are limited to the following:

(a) we agree that it is difficult legally, as well as practically, to foresee how redressive payments to a third country could be accurately calculated and enforced;

(b) as is the case under Regulation (EC) 139/2004, it would be advantageous for undertakings to be able to offer redressive measures (i.e. commitments) in order to preclude an investigation proceeding to the in-depth stage or to avoid the imposition of other redressive measures with a view to expedite the conclusion of an investigation;

(c) redressive measures should be proportionate to and address the distortion specifically, to avoid politicisation, frictions with third States and retaliatory measures on EU companies active in third States' markets; and

[3] €200 000 is the indicative figure given in section 4.1.3 of the White Paper.

(d) it is likely that a ten-year limitation period will impair the ability of undertakings and other interested parties to participate fully in an investigation and defend their position as, for example, records may have been lost or disposed of and relevant personnel may have left their employment. Such a long limitation period is also likely to create considerable uncertainty for investors and undertakings. A limitation period reduced to three years would seem far more reasonable.

5. Module 1 Question 4: 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?

Introduction

5.1 We consider that an EU interest test for public policy objectives should be included in Module 1. Just as with State aid, there may be circumstances when a market distortion is outweighed by other positive objectives such that a foreign subsidy should be allowed.

5.2 Care must be taken to ensure that the test is rigorous, objective and includes precise criteria that are applied in a non-discriminatory and proportionate manner. This is especially important if individual EU Member States will have supervisory authority to enforce Module 1.

5.3 We also consider that there should be a coordination mechanism to ensure that the EU interest test is interpreted in a consistent manner by national supervisory authorities and the European Commission to the extent that the European Commission is not solely responsible for applying the EU interest test.

5.4 Finally, to the greatest possible extent, the outcome of the EU interest test should be predictable and not unduly influenced by the individual views of any one Member State. A clear set of guidelines on the way the competent authorities intend to apply this test should be issued and made public; it should be the subject of public consultation.

The proposed test

5.5 Guidance on the content of the EU interest test criteria can be drawn from the balancing exercise undertaken as part of the State aid compatibility analysis.[4] However, those criteria alone are insufficient given the potential impact of the measures concerned on third States and the relations between the EU, its Member States and third States. We are also of the view that the concept of "EU interest" in the context of this legislative initiative should not be similar to the "EU interest" test used in the context of trade remedy cases, where much discretion is left to the investigating authorities.

5.6 We would rather recommend that the test is applied on the basis of the following three-step review:

(a) Is the economic activity or investment going to have, or has it had, a positive impact on a well-defined objective recognised as a common interest across the EU? A non-exhaustive list of EU-wide benefits could include:

(i) advancing international peace and security;

(ii) furthering the foreign policy objectives of the EU;

(iii) furthering the national security interests of an EU Member State or a number of EU Member States;

(iv) promoting respect for democracy, the rule of law and good governance;

[4] See, *inter alia*, the "Common Principles for an Economic Assessment of the Compatibility of State Aid under Article 87.3" (https://ec.europa.eu/competition/state_aid/reform/economic_assessment_en.pdf).

(v) protecting the environment and promoting resource efficiency;

(vi) achieving carbon neutrality;

(vii) promoting the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;

(viii) promoting the interests of consumers;

(ix) facilitating the development of certain economic activities, such as digital transformation and the development of public infrastructure, and certain sectors, such as the research, development and innovation sector, the social sector and the transport sector;

(x) promoting culture and heritage conservation; and

(xi) enhancing public order, public safety and resilience.

(b) Is it more likely than not that the economic activity or investment has delivered or will deliver the EU-wide benefits?

(c) Are the distortions of competition and effect on trade limited, so that the overall EU-wide benefits are positive?

The first limb of the proposed "EU interest" test

5.7 The first limb of the proposed "EU interest" test at paragraph 5.6(a) above is both *forward and backward looking* to account for the potentially retroactive effect of Module 1.

5.8 The question is framed to *minimise the impact of industrial, trade or foreign policy differences* between the EU Member States in relation to particular entities or jurisdictions for the purposes of the application of the test. The intention is that an objective determination can be made in order to de-politicise the decision-making process.

5.9 The proposed list of factors that constitute an EU public interest is *non-exhaustive* (see sub-paragraphs 5.6(a)(i) – 5.6(a)(xi) above). Common interests change over time and the factors should therefore be flexible. Alternatively, delegated powers could be given to the European Commission to review the list of factors in a transparent manner from time to time.

The second limb of the proposed "EU interest" test

5.10 In respect of the second limb of the proposed "EU interest" test at paragraph 5.6(b), as with the first question, the question is also both *forward and backward looking* to account for the potentially retroactive effect of Module 1.

5.11 A *relatively low threshold* ("more likely than not") has been set. Although the applicable threshold is a matter of policy not law, we consider that it is preferable for a relatively low threshold to be set to minimise the potentially stifling effect on investment in the EU that the proposed new regime may cause. Consideration should be given as to whether, in respect of retroactive assessments, an even lower threshold is applied as, at least initially, the restrictions in Module 1 would not have been in contemplation at the time that the foreign subsidy was granted.

5.12 The analysis underpinning the assessment of the second limb of the proposed "EU interest" test should be based on the *application of sound economic principles and analysis*.

The third limb of the proposed "EU interest" test

5.13 The third limb of the proposed "EU interest" test affords the decision maker some *discretion* as it requires a balancing exercise to be undertaken. However, as with the second question, the conclusions should be based on the *application of sound economic principles and analysis*.

5.14 In a similar manner to considerations in relation to State aid, the overall balancing exercise requires the tracing of the effects of foreign subsidies on the EU internal market and an evaluation of their size in order to engage in a comparative exercise. So, for instance, large negative effects will need to be offset by correspondingly high levels of positive effects. Conversely, if the distortion of the EU internal market is found to be limited, there would be no logical reason to require the evidence of substantial positive effects when applying the EU interest test.

6. Module 1 Question 5: 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)?

6.1 Although the question of whether Module 1 should also cover subsidised acquisitions is ultimately a policy question, it would be strongly preferable for Module 1 to not cover subsidised acquisitions at all to avoid duplication and confusion.

7. Module 1 Question 6: 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)?

7.1 We consider that it is appropriate to include a *de minimis* threshold as there is in the EU State aid rules. This will avoid disproportionate and unnecessary investigations from taking place. The exact threshold is a matter of policy and economics, so we do not comment on that. However, please also see our comments at paragraphs 4.2 and 4.4 above – where the *de minimis* threshold is exceeded, there should not be a presumption that foreign subsidies have a distortive effect. Instead, a case-by-case assessment should be carried out.

8. Module 1 Question 7: do you agree that the enforcement responsibility under Module 1 should be shared between the Commission and Member States (section 4.1.7)?

8.1 We agree that the enforcement responsibility under Module 1 should be shared between the Commission and Member States. However, to ensure that there is no (or limited) procedural overlap, there should be:

(a) clarity in terms of responsibilities as between the different supervisory authorities; and

(b) effective cooperation and coordination between the different supervisory authorities, including the possibility of referral to, or pre-emption by, the European Commission in cases where two or more national supervisory authorities would investigate the same subsidy.

8.2 Furthermore, all challenges should be adjudicated before the EU General Court, irrespective of the supervisory authority concerned to avoid politicisation and to ensure coherence.

8.3 These factors will reduce the administrative burden on the supervisory authorities as well as on affected undertakings and interested parties.

COMMENTS ON MODULE 2

9. Module 2 Question 1: 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)?

9.1 As a law firm, we do not consider that it is appropriate for us to answer this question substantively as the issues raised are primarily related to matters of policy and economics. Our principal concerns, as a law firm, are that the regime is clear, predictable and transparent and provides adequate procedural safeguards in the light of the risk that the proposals, if enacted, may stifle valuable foreign investment in the EU, unduly increase the regulatory burden on investors of all nationalities and potentially negatively affect undertakings established in the EU.

10. Module 2 Question 2: 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)

10.1 We agree that given the proposed content of Module 2 it is appropriate for there to be a 2-step investigation procedure as detailed in section 4.2.5 of the White Paper. However, a number of points should be addressed when drafting the legislation (many of which are in line with our comments on Module 1):

(a) the procedure should be prescribed in detail with the shortest possible time limits associated with each step. Doing otherwise would inevitably negatively affect foreign investors' decisions and would likely detrimentally affect undertakings including those established in the EU. The procedure should also dovetail with applicable merger control and foreign direct investment screening related procedures;

(b) the scope of information to be provided in the notification form should be clearly set out and limited to information necessary for the assessment of the effects of foreign subsidies in the case at hand;

(c) the European Commission should be allowed to waive the standstill period where appropriate. For example, transactions involving financially distressed companies often need to be completed on a highly expedited timetable to avoid an insolvency situation arising;

(d) the threshold to initiate an in-depth investigation should not be satisfied as soon as "there is sufficient evidence *tending* to show that the acquiring company *could* have benefitted from foreign subsidies" (emphasis added). This threshold is too low. A higher threshold should be applied to limit the burden on the competent supervisory authority and undertakings. For example, the threshold could be set at "serious doubts" as provided for in Regulation (EC) 139/2004 for the opening of an in-depth investigation;

(e) all undertakings subject to investigation should be able to participate fully in the preliminary review process to ensure the adoption of reasoned and substantiated decisions in accordance with the general principles of transparency and good administration and to safeguard the rights of all undertakings concerned. They should also be informed immediately upon the competent supervisory authority's commencement of an investigation;

(f) "stakeholders", for the purposes of the first step, should be defined broadly and flexibly to ensure that all potentially affected persons can make representations. For example, the third State that is, directly or indirectly, implicated, third party entities (including financial institutions) that have provided or may provide financing and consumers' and employees'

representatives should be allowed to participate in the proceedings both at the preliminary review stage and during the course of an in-depth investigation. To facilitate this, the competent supervisory authority could, for example, publish a notice giving ten days for "interested parties" to make submissions at both stages of the investigation;

(g) notwithstanding the need to protect the right of consultation/fair hearing of all other parties involved, any information shared by an undertaking taking part in an investigation with a competent supervisory authority should be kept confidential. To ensure that such undertakings are able to participate fully in the investigation (including through the sharing of commercially sensitive information), safeguards should be provided to protect the information that they have supplied.[5] This is all the more important in light of the fact that relevant information may be subject to strict disclosure regimes under the laws of the third countries concerned;

(h) affected undertakings should be subject to safeguards in a scenario where they have no access to the information requested by the competent authority or may be prohibited by law or matters of fact from seeking and/or obtaining the requested information. Any information requests by the competent authority should be required to be reasonable in the light of all of the applicable legal and factual circumstances and a "reasonable excuse" defence should be available where information that is requested cannot be supplied for legitimate reasons;

(i) any additional information (the source of which is not an undertaking taking part in an investigation) relied upon by the competent supervisory authorities should be publically available, except where absolutely necessary for reasons of confidentiality. To enable undertakings taking part in an investigation to effectively challenge any conclusions reached by a relevant competent supervisory authority, the information relied upon by it should be made available, at the very least, to the undertaking concerned; and

(j) undertakings concerned should have the possibility to seek recourse against decisions of the supervisory authority. To protect the rule of law, this right should be expressly included in the draft legislation.[6]

11. Module 2 Question 3: do you agree with the scope of Module 2 (section 4.2.2) in terms of (a) definition of acquisition, (b) definition and thresholds of the EU target (section 4.2.2.3), and (c) definition of potentially subsidised acquisition. Please explain. As regards thresholds, please provide your views on appropriate thresholds.

Definition of Acquisition

11.1 Whatever definition of an "acquisition" is adopted it should be clearly defined to create as much certainty as possible. In that respect, insofar as non-controlling minority shareholdings could be subject to Module 2, we would recommend that this be based on an objective percentage of share capital or voting rights only, and we would advise against a loose criterion based on "material influence" falling short of control within the meaning of Regulation (EC) 139/2004.

Definition and thresholds of the EU target

11.2 We consider that a definition based on a quantitative threshold is preferable, since its application would be clear. A qualitative threshold is likely to result in considerable uncertainty.

[5] See, by way of example in an analogous situation, Regulation 3(4) of Regulation (EU) 2019/452.

[6] See also Regulation 3(5) of Regulation (EU) 2019/452.

Definition of potentially subsidised acquisition

11.3 We agree with the statement in the White Paper that, as a triggering event, these criteria "need to be clearly defined". They should also be straightforward to apply and based on information that is readily ascertainable.

12. Module 2 Question 4: 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)?

12.1 Although this question is ultimately a policy question, we would favour limiting the notification obligation to only potentially subsidised acquisitions so as to limit the burden on the competent supervisory authority and on market participants.

13. Module 2 Question 5: 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?

The substantive assessment criteria

13.1 In relation to the substantive assessment criteria in section 4.2.3 of the White Paper, there should be clarity on the precise legal standard that will be applied and where the burden of proof lies in respect of Module 2. For example, it is unclear whether, when assessing if an acquisition "would" be facilitated by a foreign subsidy, the supervisory authority's decision will be made on the balance of probability or on the basis of some other standard and who shall bear the corresponding burden of proof.

13.2 There should be no *presumption* that any particular categories of foreign subsidies create a distortion in the internal market. Instead, each instance should be assessed on a case-by-case basis. For example, it is possible to envisage circumstances where foreign subsidies directly facilitating an acquisition do *not* create distortions in the internal market. Such an example could arise in circumstances where a company in a financially distressed situation is being acquired and only a single non-EU purchaser is interested in completing the acquisition.

The list of redressive measures

13.3 The nature of the redressive measures is principally a question of policy, so our comments are limited to the following observations:

(a) the remedies imposed under any applicable merger control reviews should be as consistent to the maximum extent possible with those imposed under the subsidy review;

(b) redressive measures should be proportionate to and address specifically the distortion, to avoid politicisation, frictions with third States and retaliatory measures on EU companies active in third States' markets; and

(c) redressive measures could be offered by any undertaking in order to preclude an investigation proceeding to the in-depth stage. As is the case under Regulation (EC) 139/2004, it would be advantageous for undertakings to be able to offer such redressive measures in order to expedite the conclusion of an investigation.

14. Module 2 Question 6: 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?

14.1 Similar considerations apply in relation to Modules 1 and 2 in this respect. So, we refer to our response at paragraphs 5.1-5.14 above.

15. Module 2 Question 7: do you agree that the enforcement responsibility under Module 2 should be for the Commission (section 4.2.7)?

15.1 Although this is ultimately a policy question, so our observations are limited to the following, we would support the Commission having enforcement responsibility on an exclusive basis to ensure that a consistent approach is taken to the application of the rules adopted, to avoid the risk of parallel investigations and to increase legal certainty. This is assuming that the European Commission will be sufficiently resourced to deal with the additional responsibilities conferred.

15.2 In light of its experience in handling State aid cases and merger control reviews and of the necessity to minimise the risk of divergent outcomes of foreign subsidy review and merger control procedures, we would suggest that DG COMP would be best placed to enforce Module 2.

23 September 2020