

Sponsored by ... a foreign government

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European State Aid Law is a topic known all too well by investment-hungry ports. In the wake of the 'open strategic autonomy' agenda, the EU continues to ramp up its arsenal of instruments to protect the common market against unwanted or even corrosive external influences. The latest tool is a regulation tackling subsidies attributable to states outside the EU, de facto internationalising existing state aid rules.

In the context of recent geopolitical developments and the EU's 'open strategic autonomy' objective, the European Commission (COM) decided to develop more assertive trade defence instruments. One milestone was the promulgation of the Foreign Direct Investment (FDI) Screening Regulation to protect its strategic interests relating, inter alia, to harbours, energy infrastructure, or technology firms (see also BTJ 5/18's *Beware of investors bearing gifts*). The relevance of FDI screening became obvious, for example, in the case of the planned purchase of a minority stake in a container terminal in the Port of Hamburg by COSCO.

Now, a mechanism to police recipients of foreign state subsidies active in the internal market has been agreed upon by the EU's lawmakers: Regulation 2022/2560 on foreign subsidies distorting the internal market (FSR) was officially published on 23 December 2022 (OJ L 330/1) and will apply in essence from 12 July 2023.

Unknown: the magnitude of the problem

The rationale of this regulation is closely related to FDI screening, but it has a different, somewhat shadowy target. While data on FDIs is widely available and (national) investment screening has a long record in practice, data on distortive foreign subsidies are scarce: the regulation is a novelty in the arsenal of trade defence instruments.

The reasons for and objectives of the new legal instrument are evident – in theory.

According to the explanatory memorandum, foreign subsidies appear in some instances to have had a distorting impact on the EU's internal market, creating an uneven playing field for competition. Consequently, the goal of the new regulation is to provide a remedy where the positive contributions do not outweigh the distortive effects of a foreign subsidy. However, as the COM concedes, the empirical foundation for such assumptions is rather slim, as there is still "a general lack of reliable data on subsidies granted by third countries." That means that not even the lawmakers know precisely how big the problem they intend to target is.

A 2020 European Court of Auditors (ECA) report provides at least limited insights. ECA concludes that, with a view to financial data available on China's Belt and Road Initiative (BRI) projects, "BRI projects are mainly financed by Chinese state-owned enterprises, including state-owned policy banks and commercial banks, which benefit from Chinese public financing. Under EU rules, such subsidies, if granted by a Member State, would be treated as state aid. This difference in treatment can distort competition in the EU's internal market and makes it difficult to achieve a level playing field between China and the EU."

Gap analysis

As a novel instrument, the FSR is supposed to fill a gap left open by the existing regulation, particularly the current state aid rules, which only apply to subsidies granted by the EU Member States. The scope of the Agreement on Subsidies and Countervailing Measures, under

the roof of the World Trade Organization (WTO) and its implementation into EU law by Regulation 2016/1037 on protection against subsidised imports from non-EU countries, is limited to subsidised goods only. The EU antitrust rules cover breaches of cartel law and the abuse of a dominant position by undertakings, irrespective of their forms or the way they are financed. The EU merger rules provide a system of prior notification and approval for concentrations but are blind regarding how such concentrations are financed.

Finally, the existing EU legal framework in the field of public procurement does not specifically address distortions to the block's procurement markets caused by foreign subsidies. Provided that foreign bidders have access to the EU procurement market, the current procurement rules empower contracting authorities to reject offers they consider to be abnormally low. However, it is more of a rule than an exception that contracting authorities lack the ability to identify a foreign subsidy, let alone to justify the rejection of such an offer by demonstrating that the foreign subsidy impedes the viability of the offer and the bidder's capacity to execute the contract at the subsidised price offered.

Focus on concentrations and public procurement proceedings

According to Article 3 FSR: "a foreign subsidy shall be deemed to exist where a third country provides, directly or indirectly, a financial contribution which confers

¹ This article represents the author's personal views.



a benefit to an undertaking engaging in an economic activity in the internal market.” A financial contribution may include, among other things, the transfer of funds or liabilities, such as capital injections, grants, loans, loan guarantees, fiscal incentives, debt forgiveness, debt to equity swaps, or the foregoing of revenue that is otherwise due, such as tax exemptions or the granting of special or exclusive rights without adequate remuneration. This enumeration closely resembles the definition of “aid” in current state aid law based on Article 107 I TFEU.

The FSR contains two specific ex ante notification requirements to identify a foreign subsidy. First, in the cases of concentrations, Article 21 confers an obligation to jointly notify the subsidy on the parties of a merger or the parties acquiring joint control of another undertaking. In all other cases, i.e., a classical take-over where one undertaking acquires control of another undertaking, the notification shall be done by the undertaking acquiring control. However, not every concentration needs to be notified. At least one of the merging undertakings, the acquired undertaking or the joint venture, needs to be established in the EU and generate an aggregate turnover in the block of at least €500m. The combined aggregate financial contributions in the three financial years prior to the notification must amount to more than €50m.

Second, in the cases of public procurement procedures, Article 29 obliges the economic operators to notify the contracting authority of all foreign financial contributions. The contracting authority shall transfer the notification to the COM without delay. The notification requirement applies where the estimated total value of that public procurement is equal to or

greater than €250m and the aggregate financial contributions received from a foreign government in the three financial years prior to notification is equal to or exceeds €4.0m.

In addition, the COM possesses extensive investigation rights, according to Article 9 and following, which it can apply ex officio, meaning independent of notification or concentration, and which apply to any market situation.

Good & bad subsidies, as well as remedies

Once a foreign subsidy is detected, the COM assesses its distortive effects on the internal market based on indicators provided by FSR’s Articles 4 and 5.

For instance, a foreign subsidy is deemed most likely to distort the internal market if it directly facilitates a concentration or enables an undertaking to submit an unduly advantageous tender. However, the COM may balance the adverse effects of a foreign subsidy with positive effects on the development of the relevant subsidised economic activity and consider broader positive effects relating to relevant policy objectives.

Article 7 FSR endows the COM with a wide range of options concerning the foreign subsidy ranging from unconditional approval of the subsidy via accepting commitments from the undertaking concerned or the imposition of redressive measures to ultimately ordering

the repayment of the foreign subsidy. The EU’s executive may also prohibit the concentration or the award of the tender.

Strong signal but blunt instrument?

The potential role of the FSR in the port sector should not be underestimated, given the need for major infrastructure investments in many harbours. Investors with a “strategic interest” willing and able to pay above the market price were – and still are – often glorified as ‘saviours.’ They help ports realise projects that are economically not viable (enough) to attract investors with no access to state resources and where subsidies from the respective EU Member State are unavailable.

However, while on its face, the FSR sends a strong signal to states subsidising undertakings active on the internal market, the devil is in the detail: how to acquire the necessary information to prove a foreign subsidy? The practice of WTO dispute settlement proceedings vividly shows how difficult collecting relevant data in foreign countries can be. And, as of today, no guidelines or notification forms exist (the COM announced that such documents would be published in about a year).

While the requirements of the FSR will play a significant role in ports’ administrative proceedings, it remains to be seen whether this significance is mirrored in its effectiveness in preventing distortive foreign subsidies. ■



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