

The European Commission Adopts White Paper on Foreign Subsidies – A Trend Towards Protectionism on a Global Level?

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As State aid measures granted by EU Member States continue to surge in the aftermath of the COVID-19 outbreak and ongoing pandemic, the European Commission (“Commission”) has turned to subsidies coming from non-EU countries.

On 17 June, the Commission announced that it had adopted a [consultative White Paper](#) which sets out proposed new legal tools to deal with the distortive effects caused by foreign subsidies in the European Single Market. With this, it opened a public consultation seeking input from stakeholders on the proposals set out in the White Paper. The public consultation will be open until 23 September 2020.

With the benefit of some distance since the issuance of this White Paper, we assess the proposal and the responses to it.

EU rationale

Whilst the EU’s economy grows increasingly linked to the rest of the world, there is a corresponding need to formulate tools to ensure that foreign subsidies do not distort the EU market. This EU control of course is already performed by the Commission when it comes to subsidies by EU Member States through the EU State aid rules. At the same time, however, subsidies granted by non-EU countries, however large their negative impact on competition within the Single Market, fall outside the scope of EU State aid control or any other form of efficient EU control until now.

In the face of foreign subsidies facilitating acquisitions of EU companies, distorting investment decisions or trade policies or even negatively affecting public procurement, there was a clear need to fill the regulatory gap for which existing trade defence rules do very little and to level the playing field for all those that operate on the EU market.

Proposed White Paper “Modules”

The White Paper, which is a long-awaited and well-received initiative, proposes a number of solutions and tools called “Modules” for this purpose. There are three Modules which are detailed in the White Paper, each tackling three distinctive issues which the Commission has identified as being potentially negatively impacted by foreign subsidies. These are: (i) the EU internal market generally; (ii) acquisitions of EU companies; and (iii) public procurement procedures.

Module 1: ex post control of foreign subsidies distorting the EU internal market

Module 1 is a general instrument which aims to address foreign subsidies that cause distortions in the internal market and are provided to a beneficiary that is either established or, so long as the activity is not covered by the EU trade defence instrument, active in the EU. This instrument would allow a supervisory authority, either a national authority or the Commission (the latter did not want to decide on this point at this stage), to conduct a preliminary review and in-depth investigation if there are elements that indicate that a non-EU government is granting foreign subsidies to a beneficiary in the EU. The competent supervisory authority could impose fines and periodic penalty payments for failure to supply the information requested or for supplying incomplete, incorrect or misleading information. In those circumstances the authority could make decisions on the basis of the available information alone which could be detrimental to the concerned beneficiary. If a distortion through a foreign subsidy is confirmed, the supervisory authority may impose “redressive measures”. A possible distortion to the EU would need to be weighed against any possible positive impacts stemming from the foreign subsidy.

Module 2: ex ante control of foreign subsidies facilitating EU acquisitions

Module 2, which can be used as an alternative to or cumulatively with Module 1, specifically aims to address distortions caused by foreign subsidies which would facilitate the acquisitions of EU companies. A supervisory authority would conduct an *ex ante* review of the planned acquisition by way of a compulsory notification mechanism, which would be in parallel and in addition to the existing prior EU (or national) merger notification system. The White Paper provides the possibility of opening an *ex officio* investigation of an acquisition in the event the prior notification procedure is circumvented however it fails to specify what the outcome or sanctions of such an investigation could be and whether the unwinding of an acquisition could be possible (as the United States can do under its CFIUS process). The competent supervisory authority could also start an administrative procedure for violation of procedural rules resulting in fines with sufficient deterrent effect for procedural infringement. This Module also provides for a two-step review with a preliminary review and in-depth investigation where necessary, which is modelled on the EU State aid procedure. If the supervisory authority concludes that the foreign subsidies facilitate an acquisition and thereby distort the internal market, there would be two options: (a) accept commitments which adequately redress the distortion, or (b) prohibit the acquisition. This Module may include thresholds above which the assessment would be carried out.

With regard to the ‘redressive measures’ which are considered in the White Paper, normal EU State aid rules dictate that unlawful (not notified) and incompatible (not exempted) aid must be recovered by the Member State that granted it. As this may be difficult to enforce with regard to non-EU countries, the Commission considers both structural and behavioural alternatives ranging from divestment of certain assets, prohibition of certain investments, licensing on fair, reasonable and non-discriminatory terms, redressive payments etc.

Module 3: foreign subsidies distorting EU public procurement procedures

Module 3 addresses public procurement procedures and aims to exclude bidders that have received foreign subsidies that are deemed distortive. Here too, there would be a notification procedure whereby bidders would have to notify the contracting authority when submitting a bid where they received a financial contribution within the last three years preceding the participation in the procedure. After conducting a completeness assessment, the contracting authority would send the notification to a supervisory authority who would conduct a preliminary review and in-depth review where necessary to establish the existence of a foreign subsidy. If the reviews reveal the existence of a foreign subsidy, the contracting authority would assess whether the subsidy has distorted the public procurement procedure and if so, exclude the bidder from the process.

Foreign subsidies and EU funding

The White Paper also tackles foreign subsidies in the context of EU funding to ensure that funding is competed for on an equal playing field. For this to be effective financial institutions such as the European Investment Bank and European Bank for Reconstruction and Development would need to mirror the approach to foreign subsidies.

Comments

This is an ambitious European project that has become even more important in the aftermath of the COVID-19 outbreak where subsidies will play an increasingly important role globally in order to counter the devastating effects of the pandemic. It also could protect European companies from takeovers from economic giants like China who may see an opportunity in Europe's weakness to penetrate the EU market further. The Commission has defended this initiative stating that it is purely about levelling the playing field and certainly "*not about scaring off foreign investment*" since the White Paper focuses on unfair foreign subsidies even if they are granted to European companies. Some commentators remain sceptical, however, in light of the complexity of the issues, not least due to the lack of enforcement power against third-party states, the risk of disproportionate administrative burdens and the potential need for other authorities to adopt similar systems for them to be effective.

The measures in the White Paper have the potential, however, to create increased uncertainty and place additional burdens on foreign investors in the EU beyond the existing EU merger control and FDI obligations, resulting in three separate notification procedures and additional red tape. The White Paper also has many ambiguities and raises many questions, such as:

- how will the reviews be handled under Module 2 in the context of already tight deadlines for merger review?
- how will the timelines of transactions be affected by the additional tools and procedures, and how can this be done with no real enforcement power?
- how will foreign subsidies actually be detected if cash flows from government to company are difficult to identify?
- how will this interventionist approach be perceived by the Member States?
- how will interested third parties will be heard?

There are also those concerned about the constant surveillance market operators will be under, the threat of an investigation being commenced at any time within the time limitation of ten years, and the threat of sanctions which may even be retroactive.

It will be most interesting to see the outcome of the public consultation and our Brussels team is available to assist with responses to the consultation.

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National Law Review, Volume X, Number 234

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