

# **THE EU FOREIGN SUBSIDIES REGULATION AND THE WTO AGREEMENTS: COMPLEMENTARITY OR CONFLICT?**

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## ABBREVIATIONS

<b>Commission</b>	European Commission
<b>DSB</b>	Dispute Settlement Body
<b>EU</b>	European Union
<b>FDI</b>	Foreign direct investment
<b>FSR</b>	Regulation 2022/2560 of the European Parliament and of the Council of 14 December on foreign subsidies distorting the internal market
<b>GATS</b>	The General Agreement on Tariffs in Services
<b>GATT</b>	The General Agreement on Tariff and Trade
<b>SCM Agreement</b>	Agreement on Subsidies and Countervailing Measures
<b>TFEU</b>	Treaty of the Functioning of the European Union
<b>VCLT</b>	Vienna Convention on the Law of the Treaties 1969
<b>White Paper</b>	White Paper on levelling the playing field as regards foreign subsidies
<b>WTO</b>	World Trade Organization

## **ABSTRACT**

The Foreign Subsidies Regulation ('FSR') soon to come into force by the EU consider corrective measures to offset the market distortion of foreign financial contributions that benefit European undertakings. According to the EU authorities, the Regulation is in full compliance with and complements the disciplines of, the WTO agreements touching on subsidies and countervailing duties.

However, there are reasons to believe that the relationship between the Regulation and WTO law is more tense than it would first appear. This Thesis aims at assessing the consistency of the FSR with a number of WTO obligations, including those contained in the SCM Agreement and the GATS.

First, I examine whether EU and WTO provisions cover different types of subsidies or, conversely, whether there exist overlaps between the two bodies of rules. On this basis, I then argue that, depending on one's legal interpretation, the corrective measures contemplated under the FSR may be seen as partly contravening Article 32.1 of the SCM Agreement. Further, I take the view that, under certain circumstances, those corrective measures may be applied in a manner inconsistent with the EU's national treatment obligations under Article XVII of the GATS.

# INTRODUCTION

Nowadays foreign subsidies are becoming more and more popular within the European Union ('EU'). This phenomenon appears as a direct or indirect financial contribution by a non-EU country to one or a couple of particular companies or industries in various forms (e.g. interest-free loans, unlimited guarantees, preferential tax treatment, grants, etc).<sup>1</sup> The company active in the Single Market benefits from a such contribution.

According to the European Commission ('**Commission**'), foreign subsidies existence, which may distort the internal EU market, is not regulated by World Trade Organization ('**WTO**') law, in particular by the Agreement on Subsidies and Countervailing Measures ('**SCM Agreement**').<sup>2</sup> To fill this regulatory gap, the Commission implemented the Foreign Subsidies Regulation ('**FSR**') that will come into force on 12 July 2023.<sup>3</sup>

The main purpose of the Thesis is to evaluate whether the FSR is consistent with the EU's obligations under the WTO. This evaluation rests on two alternative hypotheses. On the one hand, the Commission may be correct that the subject matters of the WTO agreements and the FSR do not overlap, such that no normative conflict can arise between them. On the other hand, contrary to the Commission's views, a genuine conflict of norms may arise between certain provisions of the FSR and the obligations contained in a number of WTO covered agreements, particularly the

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<sup>1</sup> 'What is a foreign subsidy?' (European Commission , 8 February 2023) <[https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/europe-fit-digital-age/european-industrial-strategy/foreign-subsidies-regulation\\_en#:~:text=Documents-,What%20is%20a%20foreign%20subsidy%3F,active%20in%20the%20Single%20Market](https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/europe-fit-digital-age/european-industrial-strategy/foreign-subsidies-regulation_en#:~:text=Documents-,What%20is%20a%20foreign%20subsidy%3F,active%20in%20the%20Single%20Market)> accessed 15 June 2023

<sup>2</sup> Agreement on Subsidies and Countervailing Measures 1869 U.N.T.S. 14

<sup>3</sup> Regulation 2022/2560 of the European Parliament and of the Council of 14 December on foreign subsidies distorting the internal market [2022] OJ 2 330/1/

SCM Agreement and the General Agreement on Tariffs in Services (**'GATS'**).<sup>4</sup> Under this latter hypothesis, it would be necessary to assess the extent to which the substantive obligations under the FSR are compatible with those under the WTO agreements.

To develop this analysis, the Thesis will begin by providing an overview of the background of the FSR's implementation, considering such factors as the expansion of cross-border subsidization within the EU, the negative effect of foreign subsidies on local markets, the absence of adequate remedies, and the non-efficiency of existing EU tools. Foreign subsidies regulation in other WTO Member States on the example of the USA also will be taken into account. Moreover, the introductory part will cover a brief summary of the FSR provisions.

Next, the Thesis will turn to the interaction between the FSR and the SCM Agreement. *Firstly*, the scope of each instrument will be identified based on (1) the interpretation of its object and purpose, (2) the ordinary meaning of the 'subsidy', and 'foreign subsidy', and the range of subsidies under consideration as well as the scope of procedures for the investigation of subsidies; and (3) the scope of remedies available under the FSR and the SCM Agreement. *Secondly*, the FSR provisions that overlap with SCM Agreement will be checked for compliance or contravention of respectful norms. Therefore, the analysis will conclude whether the norm conflict between the FSR and SCM Agreement exists and whether their simultaneous application is possible.

Finally, the Thesis will cover the consistency of the FSR provisions that do not overlap with the SCM Agreement to the national treatment principle as the foundation of WTO law.

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<sup>4</sup> GATS: General Agreement on Trade in Services, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, 1869 U.N.T.S. 183, 33 I.L.M. 1167 (1994)

## RESEARCH QUESTION:

### **Is the FSR consistent with the EU's obligations under the WTO?**

Historically, the EU and the WTO were established at almost the same time with the main aim to promote trade across borders.<sup>5</sup> Despite the same purpose, international entities determine different regulations on trade-related issues. However, Article 216 of the Treaty of the Functioning of the European Union ('TFEU') recognizes that international agreements are binding upon the institutions of the Union and on its Member States.<sup>6</sup>

According to Article 32.1 of the SCM Agreement, any specific action against a subsidy of another Member except measures (countervailing measures and withdrawal) prescribed in its provisions is prohibited. At the same time, the EU implemented the FSR, alleging that foreign subsidies are not a subject of the WTO regulation and that the newly implemented tool completely corresponds to actual WTO rules governing subsidies. Additionally, Article 7 of the FSR entitles the EU Member States to take redressive measures against the domestic recipients of foreign subsidies.

If the EU's contention is correct and WTO law does not cover cross-border subsidies, then the scope of obligations under the SCM Agreement and the FSR do not overlap each other. Therefore, the new EU tool addressing the distortive effects of cross-border subsidies is completely legit.

By contrast, if the SCM Agreement scope covers the cross-border subsidies, the overlap between those rules and the FSR may be present. In that case, the issue under consideration is whether the redressive measure available under the FSR are consistent with the WTO law.

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<sup>5</sup> Birgitte Egelund Olsen, Michael Steinicke & Karsten Engsig Sorensen, *WTO Law from a European Perspective* (Wolter Kluwer 2012), p.3

<sup>6</sup> Consolidated version of the Treaty of the Functioning of the European Union [2012] OJ 1 326/4/

Consequently, the research question will consist of two parts such as (1) the existence of the overlap between the FSR and the SCM Agreement and (2) in the event of any overlap if European redressive measures comply with or contravene the SCM Agreement norms.

The scope of the FSR extending to subsidies on services and service providers, which does not overlap any WTO regulation on subsidies, will also be checked on the conformity with the national treatment principle under Article XVII of the GATS.

## CHAPTER II: Introduction to the FSR

### 1. Background of the FSR development

#### *a) On the international level*

Originally, the subsidies were implemented as a form of government financial aid to local businesses in order to promote a social good or an economic policy.<sup>7</sup> By means of direct or indirect contribution, the government is able to support essential industries constituting public interest such as transportation, housing, agriculture, mining, etc.<sup>8</sup> Unlike domestic subsidies, foreign subsidies or cross-border subsidies are ‘*granted to a benefit recipient manufacturing the product at issue outside the country of the granting government.*’<sup>9</sup> Thus, foreign government or foreign company contributes to the undertakings which are based in the territory of another country.

Globalization of cross-border subsidies, especially from China, provoked a number of legal concerns in countries with developed economies.<sup>10</sup> Moreover, the US, the EU, and Japan created the trilateral group to negotiate and represent the proposal to reform foreign subsidies regulation in WTO law in order to prevent the threat to the transatlantic trade relationship.<sup>11</sup> During Trade Policy Review in October 2021, the trilateral group criticized Chinese industrial subsidies as part of the Belt and Road Initiative and recognized such actions as unfair trading practices that affect

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<sup>7</sup> The Investopedia Team, 'Subsidies: Definition, How They Work, Pros and Cons' (*Investopedia*, 12 June 2023) <<https://www.investopedia.com/terms/s/subsidy.asp#:~:text=A%20subsidy%20is%20a%20direct,to%20achieve%20greater%20economic%20efficiency>> accessed 15 June 2023

<sup>8</sup> The Editors of Encyclopaedia Britannica, 'Subsidy' (Britannica, 30 May 2023) <<https://www.britannica.com/money/topic/subsidy>> accessed 15 June 2023

<sup>9</sup> Marc Benitah, *The WTO Law of Subsidies, A Comprehensive Approach* (New edn, Wolters Kluwer 2019), p.605

<sup>10</sup> Victor Crochet and Vineet Hegde, 'China's 'Going Global' Policy: Transnational Production Subsidies Under the WTO SCM Agreement' [2020] 23(4) *Journal of International Economic Law*, p.5 ('**China's 'Going Global' Policy**')

<sup>11</sup> Dylan Gerstel, 'Trade Trilateral Targets China's Industrial Subsidies' (CSIS, 22 January 2020) <<https://www.csis.org/analysis/trade-trilateral-targets-chinas-industrial-subsidies>> accessed 15 June 2023

competition and result in excess capacity.<sup>12</sup> Despite the public discussions and the proposed US Draft of the General Council Decision to rein in non-market economy practices,<sup>13</sup> no amendments to the SCM Agreement were implemented up to this date.<sup>14</sup>

Indeed, some issues were also raised in GATT and WTO case law. In *Canadian Countervailing Duties on Grain Corn from the United States*, the GATT Panel confirmed that foreign subsidies may negatively affect domestic producers, e.g. by the general decline in world market prices.<sup>15</sup>

### ***b) On the EU level***

Although the level of foreign direct investment (**'FDI'**) to the EU is not constant,<sup>16</sup> before the pandemic it accounted for around 31% of global flows.<sup>17</sup> Many inwards in the EU come from third countries such as the US, UK, Switzerland, or Canada.<sup>18</sup> The question of the foreign subsidies application within the EU was first raised in the 1980s, at that time the application was allowed because it did not distort the EU's internal market.<sup>19</sup>

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<sup>12</sup> William Alan Reinsch, 'Crossing the Line: Transnational Subsidy' (CSIS, 14 January 2022) <<https://www.csis.org/analysis/crossing-line-transnational-subsidy>> accessed 15 June 2023 (**'Crossing the Line'**)

<sup>13</sup> Draft of General Council Decision proposed by United States 'The importance of market-oriented conditions to the World Trading System' (20 January 2020) WT/GC/W/796, 20/02/2020

<sup>14</sup> Crossing the Line

<sup>15</sup> *Panel on Canadian Countervailing Duties on Grain Corn from the United States*: Panel Report (21 February 1992) SCM/140 and Corr.1 – 39S/411 [para 5.2.10]

<sup>16</sup> The European Commission, 'White Paper on levelling the playing field as regards foreign subsidies' (17 June 2020) COM(2020) 253 final, p.6 (**'White Paper'**)

<sup>17</sup> OECD, *Global FDI flows slowed down in 2022, but new investment showed modest growth* (April 2023)

<sup>18</sup> Wolters Kluwer, *White Paper 'How will the new EU Foreign Subsidies Regulation work?'* (2023) Introduction by Lena Hornkohl (**'Kluwer White Paper'**)

<sup>19</sup> Commission Decision concerning guarantees of the Land Brandenburg (Germany) for investment projects in Poland [5 June 1996] OJ 2 102; Commission Decision of concerning aid that the Republic of Austria intends to grant under the ERP internationalization scheme [5 June 1996] OJ 2 096; Commission Decision concerning aid that the Republic of Austria intends to grant pursuant to the ERP Eastern Europe programme [5 June 1996] OJ 2 096/

In 2019, the Commission initiated three anti-subsidy investigations, examining Chinese subsidies provided to exporters of glass fiber fabrics and filament glass fiber from Egypt<sup>20</sup> and hot-rolled stainless steel flat products from Indonesia.<sup>21</sup> Based on their results, the EU imposed countervailing measures on China and Egypt.<sup>22</sup>

In 2020, essential concerns regarding foreign subsidies were summarized in a White Paper. The Commission analyzed the law of the WTO and concluded that current international trade rules do not provide appropriate remedies against foreign subsidies.<sup>23</sup> It was also underlined that currently the actual information on granted subsidies is limited due to the lack of transparency and non-compliance with notification obligation.<sup>24</sup> Meanwhile, WTO modernization is crucial for further strengthening the multilateral framework on subsidies and addressing distortions to trade and competition.<sup>25</sup>

In addition, the Commission recognized that tools that have already existed to address distortions caused by foreign subsidies (in particular, trade defense instruments, competition rules, and public procurement rules) are insufficient to prevent unfair competition.<sup>26</sup>

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<sup>20</sup> Commission Implementing Regulation (EU) imposing a definitive countervailing duty and definitively collecting the provisional countervailing duty imposed on imports of continuous filament glass fibre products originating in Egypt, and levying the definitive countervailing duty on the registered imports of continuous filament glass fibre products originating in Egypt [24 June 2020] OJ 2 201/10/

<sup>21</sup> Commission Implementing Regulation (EU) initiating an investigation concerning possible circumvention of the anti-dumping measures imposed by Implementing Regulation (EU) 2020/1408 on imports of certain hot rolled stainless steel sheets and coils originating in Indonesia by imports of certain hot rolled stainless steel sheets and coils consigned from Turkey, whether declared as originating in Turkey or not, and making such imports subject to registration [26 July 2022] OJ 2 198/8/

<sup>22</sup> Crossing the Line

<sup>23</sup> Victor Crochet and Marcus Gustafsson, 'Lawful Remedy or Illegal Response? Resolving the Issue of Foreign Subsidization Under WTO Law' [2021] 20(3) World Trade Review, p.1, 4 ('**Lawful Remedy or Illegal Response**')

<sup>24</sup> White Paper, p.6; 'Subsidies Committee members again cite concerns on lack of transparency' (World Trade Organization , 30 April 2019) <[https://www.wto.org/english/news\\_e/news19\\_e/scm\\_30apr19\\_e.htm](https://www.wto.org/english/news_e/news19_e/scm_30apr19_e.htm)> accessed 15 June 2023

<sup>25</sup> Joint statement of the European Parliament, the Council and the Commission (2021) 2021/0114(COD)

<sup>26</sup> White Paper, p. 9, 10, 13

Based on the alleged regulatory gap, the Commission elaborated instruments for EU Member States' unilateral actions against foreign subsidies to protect the internal market.<sup>27</sup> Moreover, considering the EU's foreign policy toolkits, the EU has the intent to compel other countries to adapt their own rules and standards in compliance with EU instruments (the same way, as General Data Protection Regulation (GDPR) became the new data and privacy gold standard).<sup>28</sup> Therefore, the FSR was developed as a tool that covers a regulatory gap left by available trade instruments<sup>29</sup> and eliminates distortion on the internal market by problematic foreign subsidies.<sup>30</sup>

Nevertheless, the purpose to establish local regulation in other countries according to the EU standard may be not realistic since EU Member States are not the only WTO Members adopting tools concerning foreign subsidies.

### *c) The US experience*

In the United States of America, foreign subsidization is an issue of concern for years. For instance, in his time President Clinton promised to '*provide select US industries with a subsidy above and beyond the protection level needed to counteract foreign subsidies*'.<sup>31</sup>

The same position was supported by President Bush who initiated the implementation of Session 817 on Prohibition on Procurement from Beneficiaries of Foreign Subsidies.<sup>32</sup> Its provisions

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<sup>27</sup> Lawful Remedy or Illegal Response, p.2

<sup>28</sup> Anu Bradford, *The Brussels Effect: How the European Union Rules the World* (Oxford University Press 2020), p.131

<sup>29</sup> Noerr, 'The EU foreign subsidies regulation from the trade perspective' (*NOERR*, 2 March 2023) <<https://www.noerr.com/en/insights/the-eu-foreign-subsidies-regulation-from-the-trade-perspective>> accessed 15 June 2023

<sup>30</sup> Kluwer White Paper

<sup>31</sup> *United States — Continued Dumping and Subsidy Offset Act of 2000*: Report of the Panel (16 September 2002) WT/DS234 [4.143] ('**US — Offset Act (Byrd Amendment)**')

<sup>32</sup> George W. Bush, 'Statement of Administration Policy: HR 1815 - National Defense Authorization Act for Fiscal Year 2006' (The American Presidency Project, 25 May 2005) <<https://www.presidency.ucsb.edu/documents/statement-administration-policy-hr-1815-national-defense-authorization-act-for-fiscal-year>> accessed 15 June 2023

prohibited procurements from entities possibly obtaining foreign country subsidies in order to prevent adverse effects on national defense such as reduction of competition.<sup>33</sup> The US Administration got the right to investigate foreign subsidies and subsidy programs.<sup>34</sup> Since that time, National Defense Authorization Act for Fiscal Year includes these provisions.<sup>35</sup>

Consequently, concerns about the legal regulation of foreign subsidies arose when the number of cross-border subsidies increased. The two main legal issues covered (1) the possibility of a negative impact of foreign subsidies on domestic producers and (2) the absence of appropriate remedies that may be applied in the case of the distortion of the EU's market by foreign subsidies. The tendency to control foreign subsidy holders has been already initiated by the USA before the introduction of the FSR.

## 2. Summary of the FSR provisions

Referring to the FSR as an instrument for the protection of the internal market, the Commission got extensive powers to conduct reviews and investigations of any legal entity whose business operations may distort the intra-European market. Generally, the control is focused on the participation of legal entities, getting subsidies from non-EU Member States (**foreign subsidies**), in definite business activities such as (1) concentrations (mergers) and (2) public procurement procedures. Alternatively, the Commission may initiate an *ex-officio* investigation. Based on the results of investigations, the Commission may impose a number of redressive measures, from fines to the prohibition of concluding transactions (if they are conducted, recognize them as void) or

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<sup>33</sup> *Ibid*

<sup>34</sup> Alloy Magnesium from Canada (Final Results of the Countervailing Duty New Shipper Review), Panel Review No. USA-CDA-2003-1904-02 [73]

<sup>35</sup> For example, National Defense Authorization Act for Fiscal Year 2020 (Public Law 116-92)

participating in public procurement. Concurrently, the Commission may accept commitments offered by the undertaking under investigation.

### *a) General provisions*

The FSR clearly determines what is foreign subsidy and how it may distort the internal market. According to Article 3 (1) of the FSR, a **foreign subsidy** is a financial contribution provided by a third country (both public and private entities),<sup>36</sup> directly or indirectly, which confers a benefit on an undertaking engaging in economic activity in the internal market.

**Financial contribution** is present in a number of situations<sup>37</sup>

- (a) the transfer of funds or liabilities, such as capital injections, grants, loans, loan guarantees, fiscal incentives, the setting off of operating losses, compensation for financial burdens imposed by public authorities, debt forgiveness, debt to equity swaps, or rescheduling;
- (b) the foregoing of revenue such as tax exemptions or the granting of special or exclusive rights without adequate remuneration; or
- (c) the provision of goods or services or the purchase of goods or services.

A **distortion in the internal market** exists if foreign subsidy improves the competitive position of an undertaking in the internal market, which negatively affects competition.<sup>38</sup> In order to establish the level of distortion, a number of indicators should be taken into account such as the amount of subsidy, its nature, size of the company, market or sector, level of evolution of economic activity, and purpose and conditions of the foreign subsidy.<sup>39</sup>

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<sup>36</sup> Article 3(2) of the FSR

<sup>37</sup> *Ibid*, subpara 2

<sup>38</sup> Article 4(1) of the FSR

<sup>39</sup> *Ibid*

It is considered that foreign subsidy is unlikely to distort the internal market if it does **not exceed EUR 4 million** over any consecutive period of three years.<sup>40</sup> The same position applies to foreign subsidy, which aims to cover damage caused by natural disasters or exceptional occurrences.<sup>41</sup>

Assessing every particular merger or participation in public procurement, the Commission applies **the balancing test**. It reflects a balance between the negative effects of a foreign subsidy in terms of distortion in the internal market and the positive effects on the development of the relevant subsidized economic activity in the internal market.<sup>42</sup>

Under Article 7 of the FSR, the Commission is entitled to impose **redressive measures** in order to remedy the actual or potential distortion in the internal market from a foreign subsidy. The Commission may also accept commitments offered by the undertaking under investigation if they comply with requirements of **proportionality and effectivity of the remedy** to the distortion in the internal market.

### ***b) The review of foreign subsidies***

The Commission is getting a mandate to initiate the examination of information from every source including the Member States, a natural or legal person, or an association, regarding alleged foreign subsidies distorting the internal market.<sup>43</sup>

If the risk that foreign subsidy distorting the internal market exists, the Commission may

- request the information under Article 13 of the FSR;
- conduct inspections within and outside the Union under Article 14 of the FSR.<sup>44</sup>

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<sup>40</sup> Article 4(2) of the FSR

<sup>41</sup> Article 4(4) of the FSR

<sup>42</sup> Article 6(1) of the FSR

<sup>43</sup> Article 9(1) of the FSR

<sup>44</sup> Article 10 of the FSR

Based on the preliminary review followed by in-depth investigation the Commission may adopt the decision with the redressive measure.<sup>45</sup>

It is considered that either concentration or participation in the public procurement procedures may distort the internal market.

### *c) Concentrations*

Concerning concentration, only foreign subsidies granted **in the three years prior** to the conclusion of the agreement, the announcement of the public bid, or the acquisition of a controlling interest shall be considered in the assessment.<sup>46</sup>

Criteria for a **concentration to be notifiable**<sup>47</sup>

- 1) turnover of at least one of the merging undertakings, the acquired undertaking or the joint venture is **at least EUR 500 million**; and
- 2) the following undertakings were granted combined aggregate financial contributions of **more than EUR 50 million** from third countries in the three years preceding the conclusion of the agreement, the announcement of the public bid, or the acquisition of a controlling interest:
  - (i) *In the case of an acquisition*, the acquirer or acquirers and the acquired undertaking;
  - (ii) *in the case of a merger*, the merging undertakings;
  - (iii) *in the case of a joint venture*, the undertakings create a joint venture and the joint venture.

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<sup>45</sup> Article 11 of the FSR

<sup>46</sup> Article 19 of the FSR

<sup>47</sup> Article 20(3) of the FSR

A notifiable concentration shall not be implemented before its notification.<sup>48</sup> The Commission may initiate an in-depth investigation that will result in one of the following decisions:<sup>49</sup>

- (a) Decision with commitments;
- (b) No objection decision;
- (c) A decision prohibiting a concentration in the case of distortion of the market.

***d) Public procurement procedure***

Foreign subsidies distorting a public procurement procedure enable an economic operator to submit a tender that is unduly advantageous in relation to the works, supplies, or services concerned.<sup>50</sup>

Foreign financial contribution in a public procurement procedure is considered **notifiable** when:<sup>51</sup>

- 1) the estimated value of that public procurement or framework agreement net of VAT, or specific procurement under the dynamic purchasing system, is equal to or greater than **EUR 250 million**; and
- 2) the economic operator, including its subsidiary companies without commercial autonomy, its holding companies, and, where applicable, its main subcontractors and suppliers involved in the same tender in the public procurement procedure was granted aggregate financial contributions **in the three years prior to notification** or, if applicable, the updated notification, equal to or greater than **EUR 4 million** per third country.

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<sup>48</sup> Article 24(1) of the FSR

<sup>49</sup> Article 25(3,4) of the FSR

<sup>50</sup> Article 27 of the FSR

<sup>51</sup> Article 28(1) of the FSR

After the in-depth investigation of public procurement participants, who have made the notification, the Commission implements an act in the form of

- A decision prohibiting the award of the contract to the economic operator concerned;<sup>52</sup>
- A no-objection decision.<sup>53</sup>

To sum up, the first step of the Commission is to identify if a foreign subsidy exists (it means the presence of both financial contribution and benefit in business activities). The second issue under consideration is whether foreign subsidy improves the competitive position of an undertaking in the internal market. Mainly, for the purposes of merger conduction and public procurement participation. Thus, if the risk of distortion exists the Commission initiates the preliminary review, which may be followed by an in-depth investigation. Adverse effect on the internal market leads to the implication of redressive measures or the adoption of commitments of the undertaking.

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<sup>52</sup> Article 31(2) of the FSR

<sup>53</sup> Article 31(3) of the FSR

## **CHAPTER III:**

### **Potential overlap between the scope of application of the FSR and SCM**

#### **Agreement**

It is clear that conclusions on the compliance or contravention of the FSR to the SCM Agreement may be made only if their scopes correspond to each other or at least partially overlap. To identify the range of the application, we need to interpret the fundamental provisions of both instruments.

At the same time, the connection between them has already been confirmed in the FSR norm. Article 44 (9) of the FSR requires it to be consistent with Article 32.1 of the SCM Agreement. This statement follows the general duty of new instruments to comply with obligations under international agreements.<sup>54</sup>

Therefore, Chapter III will be focused on the interpretation and comparison of the FSR and SCM Agreement scopes, taking into account (1) the object and purpose, and (2) the ordinary meaning of key terms. Based on the main purposes of the instruments as well as the consistency of essential components the overlap may be established.

#### **1. Interpretation of the FSR and SCM Agreement**

Under WTO practice, the issue of interpretation usually arises in the dispute settlement system. According to Article 3.2. of the Dispute Settlement Understanding, the main aim is to clarify provisions of the trade agreement ‘*in accordance with customary rules of interpretation of public*

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<sup>54</sup> White Paper, p.40; Article 216 of the TFEU

*international law*'.<sup>55</sup> Appellate Body refers to rules of interpretation prescribed in Articles 31, 32 of the Vienna Convention on the Law of the Treaties 1969 ('VCLT').<sup>56</sup>

Following the given approach, it is necessary to use general rules of interpretation in order to determine the application scope of the FSR and the SCM Agreement. According to Article 31 of the VCLT, a treaty shall be interpreted '*in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose*'.

Additionally, since WTO law is mandatory for the EU, the Court of Justice established a specific principle to ensure consistency with WTO law.<sup>57</sup> The **principle of consistent interpretation** obliges the Member States to harmonize the interpretation of EU secondary legislation in accordance with WTO law.<sup>58</sup>

### *a) Object and purpose*

*The main aim of the FSR* is declared in Article 1 (2). The Regulation has a clear focus on the contribution to the proper functioning of the internal market by establishing a harmonized framework to address distortions caused, directly or indirectly, by foreign subsidies, with a view to ensuring a level playing field.<sup>59</sup> Its provisions focused on the subsidies granted to an undertaking engaged in economic activity in the internal market.

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<sup>55</sup> Also, confirmed by case law, e.g. *United States — Countervailing Duties on Certain Corrosion-resistant Carbon Steel Flat Products from Germany*: Report of the Appellate Body (28 November 2002) WT/DS213/AB/R, WT/DS213/AB/R/Corr.1 [61-62] ('**US – Carbon Steel**')

<sup>56</sup> WTO Law from a European Perspective, p.65; *European Communities — Customs Classification of Frozen Boneless Chicken Cuts*: Report of the Appellate Body (12 September 2005) WT/DS269/AB/R, WT/DS286/AB/R, [175-176]; *India — Patent Protection for Pharmaceutical and Agricultural Chemical Products*: Report of the Appellate Body (19 December 1997) WT/DS50/AB/R [42]

<sup>57</sup> WTO Law from a European Perspective, p. 107-108

<sup>58</sup> Case C-61/94 *Commission v Germany* (International Dairy Arrangement) [52]; Case C-428/08, *Monsanto Technology*; Case C-245/02, *Anheuser-Busch v Budvar*

<sup>59</sup> Article 1(1) of the FSR

Considering the *object and purpose of the SCM Agreement*, it is necessary to mention that its provisions do not explicitly indicate them.<sup>60</sup> Nevertheless, the WTO case law developed the general approach to their interpretation. One of the most used definitions is mentioned in *Brazil – Aircraft* where the Panel determined that the object and purpose of the SCM Agreement are ‘*to impose multilateral disciplines on subsidies which distort international trade*’.<sup>61</sup> Meantime, any potential trade distortion can be considered only if was caused by ‘subsidies’ *as defined* in the Agreement.<sup>62</sup>

Indeed, both the FSR and SCM Agreement strive to decrease the number of trade distortions provoked by subsidies. In its turn, the adverse effect will lead to remedies application respectively. Therefore, the object and purpose of the documents under the analysis have a lot in common. Since the consistency is maintained, the overlap between the FSR and SCM Agreement is highly possible.

### ***b) Ordinary meaning of ‘foreign subsidy’ and ‘subsidy’. The scope of subsidies under consideration***

It is clear that the object and purpose of both the FSR and the SCM Agreement are directly referring to the subsidy regulation to prevent distortion in the internal market. However, although subsidization is the core element for both agreements, the scope of subsidies under consideration differs in some significant respects.

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<sup>60</sup> *Canada — Measures Affecting the Export of Civilian Aircraft*: Panel Report (14 April 1999) WT/DS70/15 [9.119] (**‘Canada – Aircraft’**)

<sup>61</sup> *Brazil — Export Financing Programme for Aircraft*: Panel Report (14 April 1999) WT/DS46/29 [7.26.] (**‘Brazil — Aircraft’**)

<sup>62</sup> *United States — Measures Treating Export Restraints as Subsidies*: Panel Report (29 June 2001) WT/DS194/4 [8.63.]

On the one hand, the scope of the FSR appears narrower than that of the SCM Agreement, in that the former only covers a specific category of subsidies, namely ‘foreign’ subsidies, whereas the latter does not contain such a specification.

On the other hand, the scope of the FSR is broader than that of the SCM Agreement, in that the former covers foreign subsidies in all industry sectors, whereas the latter only covers subsidies relating to the manufacturing, marketing, and sale of goods. Additionally, procedures for the investigation of subsidies are different.

These differences are examined immediately below.

### **(1) Correlation of definitions of ‘foreign subsidy’ and ‘subsidy’**

In accordance with the FSR, ‘**foreign subsidy**’ shall be deemed to exist where a third country provides, directly or indirectly, a financial contribution that confers a benefit on an undertaking engaging in economic activity in the internal market and which is limited, in law or in fact, to one or more undertakings or industries.<sup>63</sup> The following provisions show that the main criteria for the determination of ‘foreign subsidy’ are: (a) the existence of a financial contribution; (b) the benefit that financial contribution confers to an undertaking or industry within the EU; and (c) the fact that the financial contribution originates from outside the EU.<sup>64</sup>

The SCM Agreement, by contrast, defines just the notion of ‘subsidy’ without any references to the existence of foreign subsidies. According to Article 1.1 (a)(1) of the SCM Agreement, a ‘**subsidy**’ is a financial contribution by a government or any public body within the territory of a WTO Member, including a direct transfer of funds, foregone governmental revenue, providing

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<sup>63</sup> Article 3(1) of the FSR

<sup>64</sup> White Paper, p.46

goods or services, or purchasing goods. Similarly to the FSR definition, the subsidy under WTO law includes two discrete elements such as (a) financial contribution by the government and (b) benefit.<sup>65</sup>

While in the EU the existence of foreign subsidies is enough to evaluate the distortion of the internal market and apply redressive measures, the SCM Agreement established the **specificity requirement** for further application of its provisions, including the access to remedies, on the financial contributions given. According to Article 2 of the SCM Agreement subsidy is specific to an enterprise or industry or group of enterprises or industries **within the jurisdiction of the granting authority**. Hence, remedies under the SCM Agreement are available for subsidy recipients just within the jurisdiction of the granting authority.<sup>66</sup> Meanwhile, there is no clarification on whether jurisdiction covers just one country (where subsidies were made) or the territory of all WTO Members.

Under the initial approach, the jurisdiction is strictly connected to the territory. In the *Lotus case*, the PCIJ determined jurisdiction as ‘*certainly territorial; it cannot be exercised by a State outside its territory*’.<sup>67</sup> Although the first time the Negotiating Group on Subsidies and Countervailing Measures clarified that specificity exists within the territory of a signatory,<sup>68</sup> the provisions were lately amended to subsidy granted ‘*within the territory of the subsidizing country*’.<sup>69</sup> The territorial

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<sup>65</sup> Mitsuo Matsushita and others, *The World Trade Organization* (Oxford University Press 2004), p.268

<sup>66</sup> Lawful Remedy or Illegal Response? p.8

<sup>67</sup> *The Case of the S.S. Lotus (France v Turkey)* (Judgment) 7 September 1927, PCIJ Series A no 10, ICGJ 248 (PCIJ 1927), para. 45.

<sup>68</sup> Note by the Secretariat to Meeting of 6 November 1990 of GATT Negotiating Group on Subsidies and Countervailing Measures (29 November 1990) MTN/GNG/NG10/24, para. 3. (**Note by the Secretariat**)

<sup>69</sup> Multilateral Trade Negotiations the Uruguay Round, ‘Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations’ (20 December 1991) I.2, MTN.TNC/W/FA

approach is also supported in WTO case law.<sup>70</sup> Therefore, until recent times the practice when foreign governments subsidize producers outside of their territory was excluded.<sup>71</sup>

Nevertheless, the judicial practice has changed this approach. In the *US – FSC (Article 21.5 DSU)*, the US recognized ‘*the recipient of a financial contribution need not be within the territory of that Member*’.<sup>72</sup> The same position was also supported in the *Brazil – Aircraft* dispute where the Brazilian Government provided foreign aircraft buyers with financial contributions.<sup>73</sup> Negotiating Group on Subsidies and Countervailing Measures also made the above-mentioned conclusion during its meeting.<sup>74</sup> Consequently, Article 1.1(a)(1) of the SCM Agreement declares the requirement that the government or public body, but not the recipient of financial contribution has to be located within the territory of a WTO Member.<sup>75</sup>

Thus, under the interpretational approach, the phrase ‘*within the territory of a Member*’ should be applied just to ‘*government or public body*’ without consideration of ‘*financial contribution*’.<sup>76</sup> It means that Article does not prescribe the location of the financial contribution recipient and the words ‘*government or any public body within the territory of a Member*’ should be considered as one term.<sup>77</sup> Therefore, Article 1.1 (a) (1) does not require from financial contribution recipient to be located in the same territory as subsidizing Member.<sup>78</sup>

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<sup>70</sup> *United States – Import Prohibition of Certain Shrimp and Shrimp Products*: Appellate Body Report (12 October 1998) WT/DS58/AB/R [133]; *United States – Tax Treatment for ‘Foreign Sales Corporations’*: Panel Report (8 October 1999) WT/DS108/R, at Annex F-3 [108] (‘US — FSC’)

<sup>71</sup> China’s ‘Going Global’ Policy

<sup>72</sup> *US — FSC*, Annex F-55 [103]

<sup>73</sup> *Brazil — Aircraft*, [2.1-2.6] and [4.19-4.20.]

<sup>74</sup> Note by the Secretariat, para. 3

<sup>75</sup> China’s ‘Going Global’ Policy, p.5

<sup>76</sup> Lawful Remedy or Illegal Response? p.6

<sup>77</sup> *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*: Panel Report (22 October 2010) WT/DS379/R [8.67.]

<sup>78</sup> Lawful Remedy or Illegal Response?

The other significant decision from the cross-border subsidy perspective is *US – Washing Machines* where the Appeal Body directly recognized that the subsidy may be granted outside of the jurisdiction of subsidizing Member (even in multiple jurisdictions at the same time when it comes to the international corporation):<sup>79</sup>

*5.297. However, the above-mentioned provisions do not indicate that, for purposes of calculating per-unit subsidization, the subsidized **products should be limited to those produced by the recipient of a subsidy within the jurisdiction of the subsidizing Member.** We do not see any express limitation to this effect in the SCM Agreement. Thus, we consider that a **subsidy may, indeed, be bestowed on the recipient's production outside the jurisdiction of the subsidizing Member.** For instance, if the recipient is a multinational corporation with facilities located in multiple countries, the subsidized products may, depending on the circumstances of the case, include that corporation's production in those multiple countries.*

To sum up, the definition of ‘subsidy’ provided by Article 1.1 of the SCM Agreement does not exclude the possibility to grant subsidies to entities based outside of the subsidizing Member or to the goods produced outside the subsidizing Member.<sup>80</sup> Thus, so-called cross-border or foreign subsidies fall under the definition of a subsidy, consequently, they are regulated with the SCM Agreement.

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<sup>79</sup> *United States — Anti-Dumping and Countervailing Measures on Large Residential Washers from Korea*: Report of Appellate Body (7 September 2016) WT/DS464/AB/R [5.297] [emphasis added]

<sup>80</sup> Lawful Remedy or Illegal Response? p.7

Therefore, the Commission's allegations that foreign subsidies are not covered in the WTO law contradict the declared positions of WTO panels. Being within the subsidy's scope, if given foreign financial contributions lead to the distortion of the internal market, the remedies available under the SCM Agreement may be applied. This conclusion shows that provisions of the FSR are not filling the legislative gap, but cover the same measures as defined in the SCM Agreement.

## **(2) Types of subsidies covered by the FSR and SCM Agreement**

Even though the scope of the FSR is narrower than the one of the SCM Agreement, which covers 'foreign subsidies' as a form of 'subsidy', the European Anti-subsidies Rules cover more industries.

The SCM Agreement is aiming to govern just the subsidies to trade in goods.<sup>81</sup> However, its provisions do not apply to trade in services.<sup>82</sup> The overall WTO panels' interpretation of the SCM Agreement also shows a clear orientation on goods

*'The ASCM is in general drafted to address situations where a WTO Member is subsidizing the production or sale of its own goods'.*<sup>83</sup>

Numerous WTO cases confirm the given approach. The focus on goods starts from the definition of the SCM Agreement's object and purpose as a tool to discipline subsidies on exported goods that can distort international trade.<sup>84</sup> Since SCM Agreement covers just subsidies granted for

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<sup>81</sup> White Paper, p.41

<sup>82</sup> *Ibid*, p.42

<sup>83</sup> WTO, 'Expert Group Meeting on Trade Financing – Note by the Secretariat' (16 March 2004) WT/GC/W/527, p. 21

<sup>84</sup> *Brazil – Aircraft* [7.26]; *Canada – Aircraft* [9.119.]; *United States — Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India*: Appellate Body Report (8 December 2014) WT/DS436/AB/R [73-74] ('US – Carbon Steel')

producing goods, the loophole in the subsidies for providing services exists. The GATS recognizes the problem regarding subsidies granted for providing services.<sup>85</sup> Currently, the only possible way to solve the issue of distorting effects on trade in services is to conclude a negotiation for the adoption of new rules.<sup>86</sup>

Therefore, unlike the subsidies on goods, the WTO law does not regulate subsidies on services. For the purposes of foreign subsidies on services provided in the EU, only the FSR provisions exist since their scope is aiming for all industries where cross-border subsidies may arise. Hence, in the current situation, the FSR fills the gray zone regulation, and its application cannot contravene the WTO law on subsidies.

The FSR and SCM Agreement overlap each other just with respect to foreign subsidies on goods. In this field, the compliance of the EU regulation to WTO law should be checked. Although subsidies on services are not covered by SCM Agreement, their regulation should confirm with fundamental national treatment principle.

### **(3) The scope of procedures for the investigation of subsidies under the FSR and the SCM Agreement**

As was mentioned in Chapter II, Section 2, the FSR reflects the reasonable concerns regarding EU undertakings holding foreign subsidies that showed the intent to conduct the concentrations (mergers) or to participate in public procurement procedures. Hence, the FSR established a clear focus on particular business activities that may distort the internal market. In such occurrences, foreign subsidy recipients come under the Commission's review or investigation which may lead

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<sup>85</sup> Article XVI of the GATS

<sup>86</sup> WTO Law from a European Perspective, p.336

to further imposition of redressive measures. Although the Commission is entitled to arrange *ex officio* reviews of foreign subsidy holders, just further practice will show in what situations the risk of distortion will be considered and if the causal link between the financial contribution and injury will be established.

In its turn, the SCM Agreement is initially focused on the analysis of the provided subsidy's scope and nature. It is crucial to demonstrate the presence of three substantive conditions such as (1) the existence of subsidization, (2) injury, and (3) the causation between the first and the second criteria.<sup>87</sup> The SCM Agreement also clarifies the conditions under which Members may not employ subsidies.<sup>88</sup> Based on the type of distortion, the appropriate type of remedies (e.g. withdrawal of the subsidy or countervailing measures) should be applied. The test illustrates that the distortion of the trade market may be caused by different means. The SCM Agreement is not concentrated on the particular actions, which may affect internal trade.

Hence, the scope of procedures for the investigation of subsidies is considerably broader under the SCM Agreement than under the FSR. Meantime, the SCM Agreement does not exclude that concentration or participation in public procurement procedures may distort the trade.

## **2. Provisional conclusions on the coverage of the FSR and the SCM Agreement**

On the basis of the identified scope of the FSR and the SCM Agreement, it is possible to conclude that their provisions consist of partial overlap. Its presence can be confirmed with three main arguments:

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<sup>87</sup> *US – Carbon Steel* [73-74]

<sup>88</sup> *Ibid*

- 1) Both instruments cover similar objects and purposes even though the SCM Agreement has a wider application;
- 2) The term ‘subsidy’ in the understanding of the SCM Agreement covers the ‘foreign subsidy’ defined in the FSR considering that the subsidy can be granted outside the jurisdiction of the subsidizing Member;
- 3) The scope of procedures for the investigation of subsidies is similar. If subsidies distort the internal market, the remedies available under the instrument should be applied. Despite the fact that the scope of the actions that may distort the internal trade under the SCM Agreement is broader, the distortions caused by concentrations and public procurement procedures referred to in the FSR may be also included in the general range.

Simultaneously, it is known that the SCM Agreement governs just foreign subsidies on goods. Since subsidies granted for providing services are not regulated either by its provisions or by other WTO Agreements, in this case, the FSR is the only regulatory tool.

Therefore, the FSR and the SCM Agreement partially overlap each other with respect to foreign subsidies on goods. This overlap, in particular considering the remedies available under both instruments, will be under further analysis on the consistency of the FSR norms to WTO law.

Although provisions on subsidies on services do not create an overlap they still should be checked on conformity with the essential WTO principle such as the national treatment principle established in Article XVII of the GATS.

## CHAPTER IV:

### **Is the scope of the FSR consistent with WTO law?**

#### **1. Is partial overlap in terms of subsidies on goods comply with commitments under the SCM Agreement?**

As analysis of the previous Chapter illustrates, the FSR provisions partially overlap the SCM Agreement regarding the regulation of foreign subsidies on goods. In accordance with Article 216 of the TFEU, the EU Member States are obliged to perform the commitments under the ratified international agreements. Thus, the FSR as the EU secondary legislative act should correspond to the SCM Agreement provisions.

According to Article 32.1 of the SCM Agreement, no specific action against a subsidy of another Member can be taken except in accordance with the provisions of GATT 1994.<sup>89</sup> In order to identify if the FSR complies with imposed obligation it is necessary to (1) compare remedies prescribed by each of the instruments and (2) interpret Article 32.1 of the SCM Agreement.

#### ***a) Remedies available under the FSR and the SCM Agreement***

##### **(1) Remedies under the FSR**

The remedies that may be imposed to foreign subsidy holders distorting the internal market are determined in Article 7 of the FSR. If the foreign subsidy actually or potentially distorts the internal market, the Commission may<sup>90</sup>

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<sup>89</sup> GATT 1994: General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 187, 33 I.L.M. 1153 (1994)

<sup>90</sup> Article 7(1) of the FSR

- 1) **Impose redressive measures;**
- 2) **Accept commitments** offered by the undertaking under investigation if they fully and effectively remedy the distortion in the internal market.<sup>91</sup> The concerned undertaking is allowed to offer commitments that the Commission can make binding during all three procedures under the FSR.<sup>92</sup>

The remedy should be based on three principles:<sup>93</sup>

- Proportionality;
- Fullness;
- Efficiency.

**Commitments or redressive measures may include**<sup>94</sup>

- (a) offering access under fair, reasonable, and non-discriminatory conditions to infrastructure, including research facilities, production capabilities, or essential facilities, that were acquired or supported by the foreign subsidies distorting the internal market unless such access is already provided for by Union legislation;
- (b) reducing capacity or market presence, including by means of a temporary restriction on commercial activity;
- (c) refraining from certain investments;
- (d) the licensing on fair, reasonable, and non-discriminatory terms of assets acquired or developed with the help of foreign subsidies;

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<sup>91</sup> Article 7(2) of the FSR

<sup>92</sup> Kluwer White Paper, p. 9

<sup>93</sup> Article 7(3) of the FSR

<sup>94</sup> Article 7(4) of the FSR

- (e) the publication of results of research and development;
- (f) the divestment of certain assets;
- (g) requiring the undertakings to dissolve the concentration concerned
- (h) the repayment of the foreign subsidy, including an appropriate interest rate;
- (i) requiring the undertakings concerned to adapt their governance structure.

The Commission may also require periodic reporting regarding the implementation.

## (2) Remedies under the SCM Agreement

Under the SCM Agreement, a WTO Member affected by the subsidies of another Member may choose between two types of procedural tracks such as the multilateral track (Article 4 and Article 7) or the unilateral track (Articles 10-23).<sup>95</sup> Generally, the instrument that should be applied varies on a case-by-case basis.

**The multilateral track** applies with respect to prohibited subsidies and actionable subsidies.

In the case of reasonable doubts that the granted subsidy is prohibited or results in injury to domestic industry, nullification or impairment, or serious prejudice, the Member State may request **consultations** with such other Member.<sup>96</sup> The allegations should be proven with respective evidence.<sup>97</sup> During the consultations, parties either conclude a mutually agreed solution or refer the matter to the Dispute Settlement Body (**‘DSB’**).<sup>98</sup>

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<sup>95</sup> WTO Law from a European Perspective, p.316

<sup>96</sup> Articles 4 (4.1.), 7 (7.1.) of the SCM Agreement

<sup>97</sup> Articles 4 (4.2.), 7 (7.2.) of the SCM Agreement

<sup>98</sup> Articles 4 (4.2.), 7 (7.2.) of the SCM Agreement

If the established Panel found that the subsidy is prohibited, it shall recommend to subsidizing Member to **withdraw the subsidy** without delay, specifying the particular time period.<sup>99</sup> If the subsidy resulted in adverse effects on the interest of another Member, the Member granting or maintaining such subsidy **shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy**.<sup>100</sup>

In the event, the Member State has not taken appropriate steps to remove adverse effects or withdraw the subsidy during a particular period, the DSB shall grant authorization to the complaining Member to take countermeasures.<sup>101</sup>

Alternatively, to countermeasures in accordance with Article 4 or 7 of the SCM Agreement, the Member may impose countervailing measures (**The unilateral track**) under Part V (Articles 10-23) of the SCM Agreement.

Countervailing duties may only be imposed pursuant to investigations initiated.<sup>102</sup> The investigation should be based on the evidence of (a) subsidy and its amount; (b) injury and (c) a causal link between the subsidized imports and the alleged injury.<sup>103</sup> The authorities check all possible information, including of confidential nature.<sup>104</sup> Based on the complete consultations, a Member makes a final determination of the existence and amount of the subsidy (in particular, the amount of the benefit to the recipient), and material injuries caused by subsidies to the domestic market for like products. Afterwards, the Member may impose a **countervailing duty** unless the

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<sup>99</sup> Articles 4 (4.7.) of the SCM Agreement

<sup>100</sup> Articles 7 (7.8.) of the SCM Agreement

<sup>101</sup> Articles 4 (4.10.), 7 (7.9.) of the SCM Agreement

<sup>102</sup> Article 10 of the SCM Agreement

<sup>103</sup> Article 11 (11.2.) of the SCM Agreement

<sup>104</sup> Article 12 (12.4.) of the SCM Agreement

subsidy or subsidies are withdrawn.<sup>105</sup> When countervailing duty is imposed regarding any product, it shall be levied.<sup>106</sup>

Indeed, the remedies available under the SCM Agreement significantly differ from the FSR approach. That concludes non-compliance of provisions on available remedies in EU Regulation and WTO Agreement.

### ***b) The interpretation of Article 32.1 of the SCM Agreement***

Generally, Article 32.1 of the SCM Agreement prohibits any specific action against a subsidy.<sup>107</sup> In the *US–Offset Act case*, the Appellate Body clarified that Article 32.1 of the SCM Agreement restricts unilateral actions of Member States to counter subsidization.<sup>108</sup> Additionally, it was established two types of actions that can be applied

*A response to subsidization must be either in the form of **definitive countervailing duties**, provisional measures, or price undertakings or in the form of **multilaterally sanctioned countermeasures** resulting from resort to the dispute settlement system’.*<sup>109</sup>

Indeed, this statement confirmed the parties’ right under the SCM Agreement to choose between the unilateral track and the multilateral track.<sup>110</sup> In turn, the FSR does not specify two different procedural orders. Although its provisions do not include even countervailing measures, the FSR

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<sup>105</sup> Article 19 (19.1.) of the SCM Agreement

<sup>106</sup> Article 19 (19.3.) of the SCM Agreement

<sup>107</sup> Article 32.1 of the SCM Agreement

<sup>108</sup> *US–Offset Act (Byrd Amendment)* [252]

<sup>109</sup> *Ibid*, para. 273

<sup>110</sup> Features of each of them have already been described in Section 1(b) of the Chapter IV

established number of other unilateral actions in the form of either commitments or redressive measures listed in Article 7(4) of the FSR.

Considering remedies available pursuant to both instruments, the two possible approaches to interpretation may be distinguished.

Under a strict interpretation of Article 32.1 of the SCM Agreement, no actions can be done against cross-border subsidies. Hence, if the subsidies on goods distort the internal market, Member States may just impose countervailing duties or recourse to the DSB. Since redressive measures as per Article 7(4) of the FSR differ from allowed ones, they cannot be applied. Moreover, the norm should be considered inconsistent with the SCM Agreement.

In this context, non-compliance with WTO provisions provokes a conflict of norms. Under the WTO jurisprudence, the norm conflict arises if a party to two treaties is not able to comply with its obligations under both treaties.<sup>111</sup> In *Bananas III* the conflict is defined as

*‘Clashes between obligations ... [which] are **mutually exclusive** in the sense that a Member cannot comply with both obligations at the same time.’<sup>112</sup>*

Considering the WTO approach, all necessary criteria are present in the current situation. As a consequence of the distortion of the internal market by foreign subsidies from non-EU Member States, the EU has to impose remedies under both the FSR and the SCM Agreement, which are different by its nature. Especially taking into account that WTO law excludes the application of

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<sup>111</sup> Erich Vranes, ‘The Definition of ‘Norm Conflict’ in International Law and Legal Theory’ [2016] 17(2) European Journal of International Law, p.1

<sup>112</sup> *European Communities & Regime for the Importation, Sale and Distribution of Bananas*: Panel Report (22 May 1997) WT/DS27/R [7.159] (‘EC — **Bananas III**’)

actions against subsidies non-established by the GATT and the SCM Agreement. Consequently, the performance of obligations under one instrument will immediately entail the violation of the other.

Under a more lenient interpretation of Article 32.1 of the SCM Agreement, WTO Members are allowed to take unilateral actions against subsidies on goods when they cannot be contrasted through the DSB recourse to countervailing measures. Since the SCM Agreement does not determine particular remedies for foreign subsidies, Article 7(4) of the FSR is not inconsistent with WTO law. In the event of the absence of such provisions, the EU will be without remedies against the distortions produced by cross-border subsidies.

Essentially, the SCM Agreement also recognizes the crucial role of Article 32.1. of the SCM Agreement. According to Article 44(9) of the FSR, any actions under the FSR which contradict Article 32.1 of the SCM Agreement should be excluded. In this way, final provisions confirm the obligations to meet the duties recognized by the EU before.

Consequently, the EU would not implement the provisions that primarily contradict Article 32.1 of the SCM Agreement. The redressive measures can be considered as alternative remedies if it's impossible to impose countervailing measures or refer to the DSB.

By way of conclusion, the consistency or the contravention of the FSR provisions to the SCM Agreement will depend on the way of interpretation of the scope of unilateral actions against subsidies on goods distorting the internal market that can be applied by Member States. Under the strict interpretation, the non-compliance is obvious, while a more lenient interpretation may admit new instruments to cover the loophole of remedies for foreign subsidies distorting the EU market.

## 2. Are FSR provisions governing foreign subsidies to service suppliers consistent with the GATS?

As was mentioned before there is no WTO regulation on subsidies for providing services. The FSR is the only applicable tool for investigation initiation and remedies implications against foreign subsidies distorting internal trade. Nevertheless, this fact does not provide the EU with the unlimited capability to interfere in service provider activities. All laws related to trade have to comply with the WTO law. Considering the trade in services, the GATS provisions have to be applicable. In specific, new legislation should not violate an essential principle such as the national treatment principle governed in Article XVII of the GATS.

The statement that the GATS may cover foreign subsidies on services among other things comes up from the definition of trade in services. According to Article 1.2. (c) of the GATS, ‘**trade in services**’ includes the supply of a service by a service supplier of one Member, through commercial presence in the territory of any other Member. In *Mexico – Telecoms*, the Panel defined commercial presence as any type of business or professional establishment in the territory of any other Member.<sup>113</sup> Thus, GATS may be applied to subsidiaries or affiliate companies receiving financial contributions from the parent company based in the territory of the other Member.

Indeed, the scope of national treatment or granted market access may be limited by the Member.<sup>114</sup> The limitations have to be inscribed in a schedule. Specifically, the EU has a consolidated Schedule of specific commitments that introduces the batch of limitations on market access and national

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<sup>113</sup> *Mexico — Measures Affecting Telecommunications Services*: Panel Report (2 April 2004) WT/DS204/9 [7.375.]

<sup>114</sup> *China — Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*: Panel Report (12 August 2009) [7.950.] WT/DS363/R (‘**China – Publications and Audiovisual Products**’)

treatment.<sup>115</sup> Therefore, the scope of the trade in services covers all aspects connected with services provision and service suppliers except specific measures adopted in the EU's Schedule of specific commitments.

At any rate, some service providers subject to the FSR, whose activities comply with the EU's Schedule of specific commitments, are protected by the GATS.

According to Article XVII (1) of GATS, each Member shall accord to services and service suppliers of any other Member **treatment no less favorable** than that it accords to its own like services and service suppliers. Hence, both domestic and foreign service suppliers should get the same level of treatment.

WTO case law shows that in analyzing the violation of Article XVII of GATS generally, the Panel considers (1) the likeliness of services,<sup>116</sup> and (2) the modification of competition conditions.<sup>117</sup> In light of likeliness, there is no need to analyze if 'like services' exist since we are not reviewing a particular situation within a local industry. In fact, the FSR covers all possible undertakings receiving financial contributions from outside of the EU within various industries.

In consideration of the modification of competition conditions, the inappropriate treatment should deprive the foreign service supplier of *any* opportunity to compete with like domestic suppliers. In substance, the examination of 'less favorable treatment' should be based on the analysis of the **effects of a measure on conditions of competition**.<sup>118</sup>

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<sup>115</sup> European Union Schedule of Specific Commitments (7 May 2019) GATS/SC/157

<sup>116</sup> *EC — Bananas III* [7.322.]; *China — Publications and Audiovisual Products* [7.975-7.976.]; *China — Certain Measures Affecting Electronic Payment Services*: Panel Report (16 July 2012) WT/DS413/R [7.697.-7.700]

<sup>117</sup> Article XVII (3) of the GATS; Panel Report, *China — Publications and Audiovisual Products* [7.978-7.979]

<sup>118</sup> *China — Publications and Audiovisual Products* [7.1130-7.1131]; *Korea — Measures Affecting Imports of Fresh, Chilled and Frozen Beef*: Appellate Body Report (11 December 2000) WT/DS161/AB/R, WT/DS169/AB/R [142]

In fact, measures under the FSR may affect the position of foreign subsidy holders, especially, subsidiaries of foreign companies on a market. It is known that the Commission got the exclusive competence to conduct the investigation, get assess all company documentation, and impose redressive measures and fines for non-compliance with the notification requirement.<sup>119</sup> By these means, the EU could skew the conditions of competition to the detriment of foreign service suppliers with a commercial presence in the EU vis-à-vis domestic service suppliers. Therefore, those specific undertakings may become the subject of discriminatory treatment.

On these grounds, there are reasonable concerns that service suppliers, receiving foreign subsidies, will get less favorable treatment than domestic suppliers. The functioning of the first may be complicated by the Commission's actions. Undoubtedly, it will affect undertakings' competitive position.

Therefore, the FSR provisions constitute the risk of unreasonable unequal treatment of undertakings getting foreign subsidies in comparison with other local enterprises. In particular, the interference with normal business operating by investigations, imposition of repressive measures, and fines may have significant adverse effects on the competitive position.

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<sup>119</sup> Article 10, 14(2)(c), 7, 17 of the FSR

## CONCLUSION

The implementation of the FSR resulted from a number of different reasons. *Firstly*, the globalization of cross-border subsidies on the international level caused a negative effect on other Members' internal trade, including domestic competition (e.g. Chinese industry subsidies). *Secondly*, after conducting three investigations concerning the distortion of the internal market by cross-border subsidies, the EU concluded that neither its tools nor WTO Agreements prescribe foreign subsidy regulations. Taking into account the significant inflow of FDI in the EU, the cross-border subsidies undoubtedly may distort the internal market.

The FSR is aimed to cover the regulative loopholes. Mainly, its provisions are focused on the assessment of concentration conductions and participation in public procurement procedures initiated by undertakings receiving financial contributions from non-EU countries. Article 7(4) of the FSR defines a number of redressive measures that may be imposed against foreign subsidies that distort the internal market.

Despite the EU's allegations, the interpretation given in the Thesis shows that foreign subsidies fall under the scope of subsidies determined in the SCM Agreement. Thus, the FSR overlaps the SCM Agreements in terms of subsidies on goods. Nevertheless, the FSR is the only instrument for subsidies on services regulation.

The consistency of the FSR overlap with the SCM Agreement comes into question. On the one hand, Article 32.1 of the SCM Agreement directly prohibits any action against the subsidy of another Member. Hence, Article 7 of the FSR implementing a list of new remedies contravenes the prohibition mentioned above. Non-ability to perform obligations from both instruments simultaneously demonstrates the existence of norms conflict. On the other hand, the SCM

Agreement does not declare any specific remedies against foreign subsidies that distort the internal market. Therefore, redressive measures under the FSR may be considered as unilateral actions within the scope of allowed remedies.

Despite the fact that the FSR does not overlap with any specific WTO Agreement concerning subsidies on services, its provisions should correspond to the main principles declared in WTO law. Article XVII of the GATS guarantees the same level of favorable treatment to all services and service suppliers, either foreign or domestic. The analysis illustrates that measures under the FSR create a discriminatory risk. Once the latest are adopted, foreign services suppliers will get less favorable treatment than domestic suppliers that definitely will affect the competition position.

To conclude the Thesis, the given investigation clearly shows that the new EU Foreign Subsidies Regulation was not implemented in consideration of all WTO provisions applicable to subsidies. Therefore, the high risk that the non-compatibility to WTO law will be stressed at the international level. If the conflict of norms will be proven, the FSR further application will be questioned.

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