



RSC 2022/33  
Robert Schuman Centre for Advanced Studies  
Global Governance Programme-469

# WORKING PAPER

**Transcending territoriality:  
Expanding EU State aid control  
through consensus and coercion**

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ISSN 1028-3625

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Published in April 2022 by the European University Institute.

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With the support of the  
Erasmus+ Programme  
of the European Union

The European Commission supports the EUI through the European Union budget. This publication reflects the views only of the author(s), and the Commission cannot be held responsible for any use which may be made of the information contained therein.

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## **1. Abstract**

This paper tells the story of how the EU legal system has managed to transcend its territorial scope of application of its disciplines on subsidies. State aid control can only apply to state aid granted by EU Member States. Financial support granted elsewhere is, by definition, beyond the jurisdiction of the EU. But, in a globalized economy, what happens in other jurisdictions and markets can have repercussions on the EU internal market and its operators. As known, the EU is unique among various international and domestic systems in controlling subsidies. EU stakeholders that are subject to this unique discipline have thus increasingly raised claims of unfair competition and lack of level playing field vis-à-vis their competitors based in jurisdictions where the public financing to economic activities is not kept in check. Complaints have raised new heights in the context of a phase in international relations where multilateralism, and, in particular, its ability to generate global norms, is in crisis. Responsive to these competitiveness concerns, the EU has taken action at two different levels. The first involves the negotiation and conclusion of rules that incorporate subsidy disciplines either multilaterally or preferentially, the second paves the way to the unilateral imposition of remedies on imports or companies that do not abide by certain disciplines. Through this double-level action – this is the argument of this paper - the EU has transcended the ‘territoriality defect’ of its system of State aid control.

## **2. Keywords**

Territoriality – State aid – subsidy – PTAs – unilateral action.

## 1. The ‘territoriality defect’\*

This paper tells the story of a system which, despite a continuous and successful evolution,<sup>1</sup> has increasingly become aware of what, rightly or wrongly, it perceives as a fundamental limitation: its territoriality. State aid control can only apply to state aid granted by EU Member States. Financial support granted elsewhere is, by definition, beyond the jurisdiction of the EU. But, in a globalized economy, what happens in other jurisdictions and markets can have repercussions on the EU internal market and its operators. As known, the EU is unique among various international and domestic systems in controlling subsidies. EU stakeholders that are subject to this unique discipline have thus increasingly raised claims of unfair competition and lack of level playing field vis-à-vis their competitors based in jurisdictions where the public financing to economic activities is not kept in check. Complaints have raised new heights in the context of a phase in international relations where multilateralism, and, in particular, its ability to generate global norms, is in crisis.

Responsive to these competitiveness concerns, the EU has taken action at two different levels. The first involves the negotiation and conclusion of rules that incorporate subsidy disciplines either multilaterally or preferentially, the second paves the way to the unilateral imposition of remedies on imports or companies that do not abide by certain disciplines.<sup>2</sup>

Through this double-level action – this is the argument of this paper - the EU has transcended the ‘territoriality defect’ of its system of State aid control.

The expansion of EU law beyond its borders is in fact not new. There is significant literature that, on both sides of the Atlantic, is highlighting the various ways through which the EU expresses its normative power beyond its borders.<sup>3</sup> Drawing inspiration from this literature, this paper focuses on the specific topic of state aid.<sup>4</sup>

This paper is organized as follows. Part 2 briefly assesses EU state aid control and its unique features. Part 3 evaluates the claim that the EU and in particular EU companies would be put at a disadvantage globally because of the lack of rules comparable to EU subsidy disciplines that would apply to their international competitors. While Part 4 analyses the EU action to

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\* This paper reflects research done at the EUI during my Robert Schuman Senior Research Fellowship (2020-2021). It is forthcoming in Leigh Hancher, Juan Jorge Piernas López (eds), *The Future of EU State Aid Law and Policy: Consolidation and Expansion*, Madrid, EULawLive Press. I want to thank Petros Mavroidis for reading and commenting on a previous draft. As usual all errors belong to the Author..

1 See, e.g., Claus-Dieter Ehlermann, ‘State Aid Control in the European Union: Success or Failure?’, 4, *Fordham International Law Journal* 18, 1994, pp. 1212-1229; Andrea Biondi and Elisabetta Righini, ‘An Evolutionary Theory of State Aid Control’ in Damian Chalmers and Anthony Arnall (eds) *The Oxford Handbook of European Union Law*, Oxford University Press, 2015, pp. 670-690.

2 In the latter case, an interesting question of “equivalence” comes out if the third country does indeed follow international guidelines or in any event adopts norms regulating State support.

3 See, e.g., Marise Cremona and Joanne Scott (eds.) *EU Law Beyond EU Borders: The Extraterritorial Reach of EU Law*, Oxford University Press, 2019; Joanne Scott, ‘The New EU “Extraterritoriality”’, 5, *Common Market Law Review*, 51, 2014, pp. 1343-1380; id., ‘Extraterritoriality and territorial extension in EU law’, *American Journal of Comparative Law*, 62, pp. 87-126; Anu Bradford, *The Brussels Effect: How the European Union Rules the World*, Oxford University Press, 2020; Cedric Ryngaert, ‘Whither Territoriality? The European Union’s Use of Territoriality to Set Norms with Universal Effects’, in Cedric Ryngaert, Erik Molenaar and Sarah Nouwen, *What’s Wrong with International Law? Liber Amicorum A.H.A. Soons*, Brill, 2015, pp. 434-448; Maria Anna Corvaglia and Kevin Li, ‘Extraterritoriality and public procurement regulation in the context of global supply chains’ governance’, 6 *Europe and the World: A Law Review*, 16, pp.1-16. See also Petros Mavroidis and Damien Neven, ‘Some Reflections on the Extra-Territorial Application of Laws: a Law and Economics analysis’ in *Mélanges offerts à Michel Waelbroeck*, Bruxelles, 1999, p. 1297-1325.

4 The topic will be developed in future research.

counter this scenario through negotiations, Part 5 concentrates on the EU acting unilaterally. Part 6 offers few conclusions.

## 2. A brief assessment of a unique system of public spending governance

It is well known that EU State aid control is unique.<sup>5</sup> It is difficult to find similarly developed systems to control subsidies and their negative effects on the market in other jurisdictions. The exceptions have been rare. In the past, and beyond candidate EU Member States, Denmark was allegedly the only EU Member State with a domestic system of state aid control. Things have changed recently with the departure of the UK from the EU. Be it the result of autonomous choice or of a commitment imposed in negotiations (historians will tell us), the UK will soon have its own system of subsidy control (which in various respects borrows from the EU State aid model). Outside of the EU, scrutiny of state subsidies is infrequent, to say the least.<sup>6</sup>

The cornerstone of the EU system is the delegation of power Member States give to the EU Commission to assess and eventually authorize, or object to, their plans of financial support in the economy. Two remarks are needed. First, increasingly the system has developed into a highly sophisticated body of law which channels Member States' financial support towards horizontal objectives of common interest. (We will go back to this important point.) Secondly, the enforcement of the system is also (at least in principle) very effective since it benefits from the highly integrated legal structure of EU law and its remedies.

It should finally be noted that state aid control has always constituted a crucial policy for both the internal market and competition, a policy crucially intertwined with other major EU objectives such as environmental protection, clean energy transition and the fight of climate change.<sup>7</sup> This is the natural reflection that governments can – and do – use State aid as prime policy tool to achieve different objectives.<sup>8</sup>

How can the EU State aid system be assessed? How has it scored against its evolving objectives? For sure, it has certainly helped governments by enabling 'log-rolling' on occasion of difficult decisions,<sup>9</sup> while ensuring a process of harmonization of public spending towards common horizontal objectives at the European level.<sup>10</sup> That being said, there is a broad consensus that, through the years, the system has ensured the smooth working of the internal

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5 Ehlermann, 'State Aid Control in the European Union', *cit.*, p. 1213.

6 See Alan O. Sykes, 'The Questionable Case for Subsidies Regulation: A Comparative Perspective', 2, *Journal of Legal Analysis*, 2, 2010, pp. 473-523. See also Claus-Dieter Ehlermann and Michelle Everson (eds.), *European Competition Law Annual 1999: Selected Issues in the Field of State Aids*, Hart Publishing, 2001.

7 On the policy complexity of State aid and its control, see, e.g., Michelle Cini and Lee McGowan, *Competition Policy in the European Union*, Palgrave Macmillan, 2009, Chapter 7; on the evolution of the objectives of EU State aid control see Juan-Jorge Piernas-Lopez, *The Concept of State Aid under EU Law: From Internal Market to Competition and Beyond*, Oxford University Press, 2015. On the example of State aid as key tool to foster a green revolution, see the very recent Commission's Guidelines on State Aid for Climate, Environmental Protection and Energy, Brussels 21.12.2021, C(2021) 9817 Final.

8 One good place to get this sense is the *State Aid Scoreboard* which the Commission publishes annually. For the latest issue (2020) see [https://ec.europa.eu/competition-policy/state-aid/scoreboard\\_en](https://ec.europa.eu/competition-policy/state-aid/scoreboard_en).

9 David Spector, 'State Aids: Economic Analysis and Practice in the European Union', in Vives (ed), *Competition Policy in the EU: Fifty Years of on From the Treaty of Rome*, Oxford University Press, 2009, pp. 176-202; Bill Bishop, 'From Trade to Tutelage: State Aid and Public Choice in the European Union', Presentation to the Conference to ACE, Copenhagen, 2 December 2005.

10 See, e.g., Michael Blauburger, 'Of "Good" and "Bad" Subsidies: European State Aid Control through Soft and Hard Law', 4, *West European Politics*, 32, 2009, pp. 719-327.



market by controlling competition between Member States (and companies)<sup>11</sup> and, more recently, assisting governments in spending increasingly tighter budgets well.<sup>12</sup>

All in all, the system has certainly evolved significantly from the vision of the model of control of public subsidies sketched in the Spaak Report in the 1950s, turning into a more comprehensive system of governance of public spending, the quintessential example of the positive and deep integration the EU has created among its Member States. Increasingly, however, claims have been aired that this unique and sophisticated system of control of public spending in the economy would constitute a competitive disadvantage for EU businesses.

### **3. Competitive disadvantage? Assessing the claim**

Although critical for the proper functioning of the internal market, EU State aid control would put EU businesses at a competitive disadvantage with their non-EU competitors. There are two aspects to this claim. First, the absence of competition and state aid rules in third markets would limit EU companies' market access in those markets.<sup>13</sup> Similarly, the insufficiency of global laws and the inapplicability of EU State aid control to third countries subsidising companies active in the EU internal market would impair the level playing field within the EU for EU competitors.<sup>14</sup>

As the French and German governments recently put it:

Despite our best efforts, which we must pursue, there is no regulatory global level playing field. And there won't be one any time soon. This puts European companies at a massive disadvantage. When some countries heavily subsidize their own companies, how can companies operating mainly in Europe compete fairly? Of course, we must continue to argue for a fairer and more effective global level playing field, but in the meantime, we need to ensure our companies can actually grow and compete.<sup>15</sup>

These concerns contributed to the emergence of the notion of 'open strategic autonomy' which is at the core of the recent Commission's consultation for *A renewed trade policy for a stronger Europe*.<sup>16</sup> To understand this notion, it may be useful to focus on the *Alstom* –

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11 See, e.g., Biondi and Righini, 'An Evolutionary Theory of State Aid Control', *cit.*

12 Andrea Biondi, 'State Aid, Government Spending and the Virtue of Loyalty' in Patrick J. Birkinshaw and Andrea Biondi (eds.) *Britain Alone!*, Kluwer Law International, 2016, Chapter 15. Fiscal discipline was indeed one of the central innovation of the 2012 Modernization Process. See the Communication from the Commission, *State Aid Modernisation*, 8 May 2012, COM/2012/0209 final.

13 See, e.g., Communication from the Commission, *Global Europe: Competing in the World – A Contribution to the EU's Growth and Jobs Strategy*, Brussels, 4.10.2006, COM(2006) 567 final, para. 3.2.

14 See, e.g., European Commission, White Paper on levelling the playing field as regards foreign subsidies, Brussels, 17.6.2020, COM(2020) 253 Final, para. 2.1. This policy initiative is discussed in section 5 below.

15 *A Franco-German Manifesto for a European industrial policy fit for the 21st Century*, 19 February 2019, available at: [https://www.bmwi.de/Redaktion/DE/Downloads/F/franco-german-manifesto-for-a-european-industrial-policy.pdf?\\_\\_blob=publicationFile&v=2](https://www.bmwi.de/Redaktion/DE/Downloads/F/franco-german-manifesto-for-a-european-industrial-policy.pdf?__blob=publicationFile&v=2) (page 3).

16 See European Commission, Consultation Note, *A Renewed Trade Policy for a Stronger Europe*, Brussels 16.6.2020. For an impromptu commentary see Luca Rubini, "A Delphic oracle?" What does the recent EU Commission's trade policy review mean?", EU Law Live, 24 June 2020, available at: <https://eulawlive.com/op-ed-a-delphic-oracle-what-does-the-recent-eu-commissions-trade-policy-review-mean-by-luca-rubini/>.

*Siemens merger affaire*<sup>17</sup> and the subsequent Franco-German *Industrial Policy Manifesto*,<sup>18</sup> which are analysed in detailed below. Suffice mentioning here that the controversial novelty of this notion resides in the idea of ‘autonomy’, as it is confirmed by its increasing re-branding into ‘strategic sovereignty’.<sup>19</sup> Crucially, this assertively defensive narrative is shaping EU policy making. It is, for example, central in the important Communication on *A New Industrial Strategy for Europe*.<sup>20</sup>

Before addressing the specific competitiveness claims underlined above, where state aid and its regulation are central, it is useful to briefly ponder “unfair competition” narratives.

The fact is that these narratives are inherently unstable and pliable. There is a risk of making easy but unsubstantiated claims, of comparing situations that are not comparable, of looking “at the speck of sawdust in your brother’s eye and pay no attention to the plank in your own eye”.<sup>21</sup> In this regard, it is worth reproducing the words of the late Robert Hudec, one of the true giants in international trade law scholarship,

Complaints about divergent domestic policies usually come to rest on an assertion that the economic or social policy results of that divergence are “wrong” in some sense – wrong enough to justify the application of diplomatic pressure and perhaps coercive economic force as well. The degree and character of these normative starting points are an absolutely critical element in the effort to reconcile the contending policy objectives.

... All nations have a tendency to distort the norms of fairness they apply to other countries. They assume that what they do at home is normal, and natural, and pleasing to God, while at the same time feeling perfectly free to criticize superficially difference practices of others that are in no rational way distinguishable from their own.<sup>22</sup>

These words call for caution, a caution that is much needed when in European policy parlance narratives about ‘autonomy’ and ‘sovereignty’ are gaining centre-stage in policy-making.

This leads us to answer key questions. Does the existence of EU State aid control really put EU players at a competitive disadvantage? What are in particular the elements that generate competitiveness concerns?

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17 Konstantinos Efstathiou and Bruegel, ‘The Alstom-Siemens merger and the need for European Champions’, 11 March 2019, available at: <https://www.bruegel.org/2019/03/the-alstom-siemens-merger-and-the-need-for-european-champions/>.

18 *A Franco-German Manifesto for a European industrial policy fit for the 21st Century*, cit.

19 See, e.g., Susanna Anghel, Strategic Sovereignty for Europe, European Parliamentary Research Services Papers, PE 625.069, September 2020; European Parliament, Directorate General for External Policies, *Workshop: Achieving Strategic Sovereignty for the EU*, PE 653.634, April 2021, with working papers available at: [https://www.europarl.europa.eu/RegData/etudes/STUD/2021/653634/EXPO\\_STU\(2021\)653634\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/STUD/2021/653634/EXPO_STU(2021)653634_EN.pdf). For an initial analysis see Klaudia Majcher, ‘Open strategic autonomy’: towards the geopoliticisation of EU competition law?, Kluwer Competition Law Blog, 20 November 2020, available at <http://competitionlawblog.kluwercompetitionlaw.com/2020/11/20/open-strategic-autonomy-towards-the-geopoliticisation-of-eu-competition-law/>.

20 Communication from the Commission, *A New Industrial Strategy for Europe*, Brussels, 10 March 2020, COM(2020) 102 final, available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52020DC0102>.

21 Matthew’s Gospel, 7:1-5.

22 Jagdish Bhagwati and Robert Hudec (eds), *Fair Trade and Harmonization – Prerequisites for Free Trade?* (MIT Press, 1996), Vol. II, pp. 16 e 17. It is interesting to highlight that Hudec was making these comments while referring to the adoption of unilateral trade remedies of varied nature.

To be sure, complaints do not seem to relate to the *existence* itself of a system of State aid control, which is generally perceived as a key instrument to ensure a level playing field in the internal market.<sup>23</sup> Nor do they focus on the more or less subtle process of *harmonization* of industrial policies across Europe that increasingly the body of secondary law and practice is leading to. These laws are subject to a transparent and quasi-permanent consultation, they are regularly amended and, to a large extent, can be said to represent the concerted best practices in the relevant areas. They also occasionally address global competitiveness concerns. For example, R&D&I aid disciplines include a (never used) “matching clause” (which enables the authorization of higher intensities of State aid if competitors outside the EU have received public support for similar projects),<sup>24</sup> the recent Guidelines on State aid for climate, environmental protection and energy continue to include exceptions for energy intensive sectors particularly exposed to international competition (though, as compared to the previous guidelines, these have been tightened).<sup>25</sup> At the same time, the Commission is asked to be more flexible in applying the incentive effect and the proportionality test in its individual assessment, which is perceived as a potential constraint.<sup>26</sup>

As seen, the main claim refers to the *lack* of any corresponding system of subsidy control in other countries – a misalignment that, almost by itself, would put European business at a disadvantage and that, only to a limited extent, would be addressed by global (read: WTO) disciplines.<sup>27</sup>

Given many limitations (in terms of transparency, data and analysis on foreign subsidization), this claim is difficult to be put to the test. What can, however, be tested is the *implicit* premise of that claim, i.e. that the *substantive disciplines* of EU State aid control would create indeed *significant constraints* in Member States’ State aid decisions. Is this correct?

Certainly, especially if compared to multilateral disciplines, EU State aid disciplines, and the supranational control of the EU Commission, are triggered very easily. It is known that, once a selective advantage granted by the State through state resources is established, the measure is a State aid and is subject to all transparency, procedural and substantive disciplines. In other words, there is no real need to prove any detrimental impact on EU internal trade and competition, these being normally presumed to exist.<sup>28</sup> Hence – so the argument would go – the quasi-automaticity of EU State aid law would significantly interfere with government prerogatives and impact on potential beneficiaries.<sup>29</sup> To be sure, if it qualifies as State aid, a measure is subject to a close scrutiny at the European level but, as noted, stakeholders do not seem to directly criticize the *existence* of such system of control.

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23 Business Europe, *Improving EU Competition and State Aid Policy*, Position Paper, 4<sup>th</sup> September 2019, pp. 9-10.

24 See Framework for State aid for Research and Development and Innovation, 2014, OJ C198/1, para. 92.

25 Guidelines on State aid for climate, environmental protection and energy 2022, Brussels, 21.12.2021 C(2021) 9817 final, Section 4.11.

26 Business Europe, *Improving EU Competition and State Aid Policy*, p. 10.

27 Ibid.

28 This interpretation, advanced by the Commission, was confirmed by the Court of Justice in the famous Judgment in *Philip Morris v Commission* (Case 730/79, ECLI:EU:C:1980:209).

29 See, e.g., Adrien Gireaud and Sylvain Petit, ‘Tax rulings and state aid qualification: should reality matter?’, 2, *European State Aid Law Quarterly*, 16, 2017, pp. 233-242. *Contra*: Jose-Luis Buendia-Sierra and Ben Smulders, ‘The Limited Role of the “Refined Economic Approach” in Achieving the Objectives of State Aid Control: Time for Some Realism’, in ‘EC State aid law-Le Droit des Aides d’Etat dans la CE, Liber Amicorum Francisco Santaolalla Gadea, Kluwer, 2009, pp. 1-26.

Importantly, being caught in the net represents only half of the story. State aid, as defined by Article 107(1) of the TFEU is only in principle “incompatible with the internal market”. As mentioned, through years of practice, soft law and then hard legislation, EU State aid law has developed a hugely significant body of secondary law, regularly updated, which essentially introduces the terms and conditions for giving the green light to public support. The underlying idea is that State aid can and should be channeled to achieve important, common objectives, and that, if there are substantive and procedural guarantees that is what happens, and negative distortions are balanced-out, the measure should be justified and permitted.

We have already noted that these laws already introduce certain – though limited - mechanisms to address competitiveness concerns. But the statistics concerning the measures that are considered ‘compatible with the internal market’ reveal something more significant. The very large majority of State aid in the EU is permitted.<sup>30</sup> For example, a quick perusal to the latest data for the year 2019 published by the Commission in the *2020 State Aid Scoreboard* shows that a staggering 95.5% of all new State aid measures (referring to 36% of all State aid spending) was automatically green-lighted, because they clearly satisfied the conditions of the General Block Exemption Regulation.<sup>31</sup> Though the remaining 4,5% covered notified aid procedures, and accounted for bigger projects amounting to a total of 61.5% of spending, the number of State aid measures eventually prohibited was very small. In 2019, while not objecting to any case, the Commission opened in depth investigations on three large regional investment projects, and two infrastructure projects.<sup>32</sup> and issued four recovery decisions.<sup>33</sup>

Therefore, EU State aid law surely objects to the most pernicious distortions of the market. But so does the WTO by equally and strictly prohibiting certain categories of subsidies.<sup>34</sup> What mostly distinguishes EU State aid disciplines from the corresponding global disciplines is the significant body of justifications for ‘good’ subsidies, which is certainly beneficial for EU businesses.

#### **4. Addressing the ‘territoriality defect’: acting through consensus (trade agreements)**

Whether the competitiveness concerns are real or simply perceived, the EU has traditionally acted in its external trade relations with the goal to extend the reach of EU State aid law. Of course, we are not talking of an extension of the application of EU law itself, of the very same disciplines that apply in the EU. We are rather referring to the very common attempt to influence the regulation of subsidies in the trade agreement through an incorporation of the fundamental principles of EU State aid control. To be sure, in some cases, the action has focused on negotiating and making partners to accept rules substantially equivalent to those applicable within the EU. That has clearly occurred in those cases where the goal of the trade

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30 The narrative prevailing in both sides of the political spectrum in the UK – that EU State aid law would have operated as an obstacle to many domestic policies - was therefore fallacious. See, e.g., addressing the claims of the Labour Party manifesto, Andrew Tarrant and Andrea Biondi, ‘EU State aid law and British assumptions: A reality check’, *Renewal: A Journal of Social Democracy*, 22<sup>nd</sup> September 2017, available at <https://renewal.org.uk/eu-law-is-no-barrier-to-labours-economic-programme/>. Of course, the assessment would be different if the UK wanted to push heavily distorting and protectionist subsidization.

31 European Commission, *State Aid Scoreboard 2020*,

32 European Commission, Commission Staff Working Paper accompanying the Report on Competition Policy 2019, Brussels, 9.7.2020 SWD(2020) 126 final, pp. 30-31.

33 Ibid, p. 34.

34 In particular, subsidies contingent on exports and on the use of local products.

agreement was to set up the legal framework for an approximation to the EU legal regime and thus pave the way to a future accession. In other cases, the influence of the principles of EU State aid law is less clear or more varied.<sup>35</sup> Given the vagaries and several conditions affecting international negotiations, one should not, however, expect to find provisions corresponding to the key elements of the EU state aid regime in every single case. What, however, the learned observer can often discern in EU's trade agreements are some features, at times even language, that are modelled on, or, at the least, reminiscent of EU state aid law. We will soon provide categories and examples of all these trade agreements.

After these few words of introduction, it is now necessary to proceed with order and distinguish two main scenarios: the multilateral and the preferential level.

The **multilateral** level aims at creating rules, even on subsidies, that are applicable to all Member States in an organization which is universal in its vocation. That was the GATT first, created in 1947, and then the WTO, established in 1995. While GATT subsidy rules were extremely minimal, the WTO features a comprehensive discipline of subsidies, which brings both similarities and differences with EU State aid laws. It is known that the EU has pushed for the introduction of significant subsidy disciplines in the global rule-book since the 1970s.<sup>36</sup>

As far as similarities with EU law are concerned, this clearly happens for the notion, the test of specificity, and the idea that certain, legitimate subsidies (environmental, regional, research and development), should be permitted and non-actionable. The specific language and criteria may be different as compared with EU state aid law but the coverage and the underlying principles are essentially the same. There are clearly also important differences which are mostly explained by the different nature of the WTO (vis-à-vis the EU) and the different level and ambition of integration of the two organizations. This is clear for the impact standards (which determine when certain subsidies are prohibited or in any event objectionable) and, most importantly, for the governance system which lacks any element of supranationalism and is essentially centered on peer-control.

Irrespective of similarities and differences, WTO subsidy disciplines are increasingly criticized for their lack of teeth. The issue does not relate to enforcement only, but more generally to the legal standards, too complex and too restrictive, especially as they have emerged from 25 years of practice and jurisprudence (in particular of the Appellate Body).<sup>37</sup> The only real remedy to counter subsidized goods are countervailing duties ("CVDs") which are used by the EU too but are notoriously prone to protectionist use and, more generally, do not tackle all distortion scenarios.<sup>38</sup>

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35 See, e.g., Juan-Jorge Piernas-López, "State aid law beyond the EU" in Leigh Hancher and Juan Jorge Piernas López (eds) *Research Handbook on European State Aid Law*, Elgar, 2021, p. 297.

36 To be more precise, the main focus of EU negotiating efforts for many years was to introduce stricter disciplines on countervailing duties, to constrain their heavy use by the US. See, e.g., Gilbert Winham, *International Trade and the Tokyo Round Negotiation*, Princeton University Press, 1986; Terence Stewart (ed.), *The GATT Uruguay Round: A Negotiating History (1986-1992)*, Kluwer, 1993; Luca Rubini and Jennifer Hawkins (eds.) *What shapes the law? Reflections on the History, law, politics and economics of international and European subsidy disciplines*, European University Institute, 2016.

37 See, e.g., Pramila Crivelli and Luca Rubini, "Flying high in a plane": Appellate Body report, *European communities and certain member states: measures affecting trade in large civil aircraft*, 2, *World Trade Review*, 19, pp. 316-340.

38 This brief assessment should put to rest the exotic narratives Conservative circles developed in concomitance with the trade negotiations with the EU, whereby EU State aid law would have been worthy of all possible negative assessments, while WTO subsidy laws should have been praised for their clarity and soundness. See the author's testimony to the EU Internal Market sub-committee of the UK House of Lords on 12<sup>th</sup> March 2020, available at <https://parliamentlive.tv/Event/Index/09d-6b3ea-de74-4d63-9a75-cdefc511602a>.



It is against this background that many WTO Members, including the EU, have voiced their concerns about the lack of effectiveness of subsidy disciplines in tackling non-market trade-distorting practices (read: China's action) and put forward proposals for strengthening them. This has, most notably, happened in the context of the so-called "Trilateral Initiative" which has gathered the EU, Japan and the US, since late 2017. The only draft text circulated so far (dated January 2020) essentially introduces new types of prohibited subsidies (thus following what can commonly be found in the most recent PTAs and, arguably, also in EU State aid law).

The **preferential** level refers to the variety of trade agreements concluded by the EU with several partners in the European continent and beyond. These trade agreements are called preferential (the common acronym is "PTAs") because they are essentially discriminatory offering certain benefits only to its parties. They thus breach the fundamental Most-Favoured-Nation ("MFN") principle of GATT/WTO law but, under certain conditions, that essentially relate to the ability of the agreement to create trade and enable its participants to further integrate their markets between themselves are permitted (see GATT Article XXIV and GATS Article V).

There are three broad categories of EU PTAs.<sup>39</sup> First, those that are exclusively modelled on WTO subsidy disciplines;<sup>40</sup> secondly, those that significantly elaborate on the WTO platform and include important borrowings from EU State aid law, for example by covering also services and by introducing justifications for 'good' subsidies (in doing so, at times even reproducing the very same language of EU law);<sup>41</sup> thirdly, those PTAs that copy the EU State aid model in view of a close association and even accession to the EU of the trading partner<sup>42</sup>.

Now, apart from the rather limited number of PTAs belonging to the first category, what is interesting is that in all other trade agreements the EU systematically pushes the inclusion of disciplines that, irrespective of the language used, reflect the key principles of EU State aid law. To be sure, one has to make allowances for inevitable variations with the result that it might perhaps be more appropriate to talk of different models. Apart from the PTAs of the third category, which find their justification in a path towards accession, it would therefore be wrong to talk of a take-it-or-leave-it package, or a hard and fast monolithic model. What is evident, however, is that the same basic principles, which in part correspond to those of the international disciplines, are almost always, and increasingly, there, and, importantly, they now go beyond the circle of those countries that can be defined European. The PTAs with *Viet Nam*, *Singapore*, *Japan* and *Mexico* are excellent examples. Those that are currently being negotiated with *Australia* and *New Zealand* may confirm this trend soon.<sup>43</sup>

What are these 'common' elements? They certainly include the definition of subsidy/State aid, its coverage (which encompasses both goods and services), the stricter discipline for certain more troublesome subsidies, the highlighting of the importance of public interest goals

39 For a detailed analysis see Luca Rubini, 'State aid and international trade law' in Leigh Hanchard and Juan Jorge Piernaz Lopez (eds.), *Research Handbook on European State Aid law* (Elgar Publishing, 2021), pp. 103-133; idem, 'Gli accordi di nuova generazione dell'Unione Europea e le innovazioni in materia di aiuti di Stato e imprese pubbliche' in Giovanna Adinolfi (ed.) *Gli accordi preferenziali di nuova generazione dell'Unione Europea* (Giappichelli, 2021) pp. 181-210, idem, 'International agreements' in Kelyn Bacon (ed.), *European Union Law of State Aid*, Oxford University Press, 2017, Chapter 4.

40 Good examples are the *Comprehensive Economic and Trade Agreement* ("CETA") concluded with Canada in 2016.

41 See, e.g., the agreements with Japan (signed in 2018), Singapore (2018), Mexico (2018) and Viet Nam (2020).

42 One can think of the agreements concluded between 2004 and 2016 with the six West-Balkan countries (North Macedonia, Albania, Montenegro, Serbia, Bosnia-Herzegovina, Kosovo).

43 Despite all rhetoric surrounding its negotiation, the *Comprehensive Trade Agreement* concluded with the UK in 2020 follows this trend.

pursued through subsidies, the introduction of exceptions for certain legitimate subsidies (which, in some cases, reproduce verbatim EU law), the strengthening of transparency mechanisms. One wonders whether, against the presence of these common elements and the extension of the geographic coverage of these PTAs, the normative process collectively emerging from the negotiation, drafting and conclusion of these trade agreements reflects the development of a ‘common law’ of subsidies.<sup>44</sup> Each PTA including similar provisions, each policy or law reform initiative reproducing these elements are reinforcing this claim. Through each new PTA including similar provisions, the substantive standards of EU State aid law extend their territorial reach. This is indeed one of the expression of the best examples of EU’s regulatory power at the global level.

## **5. Addressing the ‘territoriality defect’: acting through coercion (unilateral remedies)**

Increasingly, the EU is following another path to address the territoriality limitations of its EU State aid rules. I am not clearly referring to the imposition of CVDs. Not only are these permitted by global rules, but they are in all respects a defensive measure, simply apt at equalizing the negative effects of subsidized imports, while, at least in principle, the foreign subsidy itself remains untouched.

Within the context of globalized economic relations, and the increasing investment and action of Chinese companies in third markets, complaints have been more and more raised about the alleged negative impact caused by China’s subsidies.

Foreign direct investment assisted by government’s support is not a new topic.<sup>45</sup> The dramatic success of China’s economy after its accession to the WTO in 2001 has, however, multiplied claims of unfair competition and allegations that currently available rules – both at the global and EU level – would not suffice in regulating these concerns. In the EU the alarm bell was distinctly heard on occasion of the high-profile *Alstom-Siemens* merger investigation. Famously, the EU Commission rejected the proposed merger because it would have distorted competition within the internal market. Both the French and German governments immediately voiced their concerns, about the alleged myopic approach of the Commission with respect to the global implications of such a decision. In their view, the Commission should have duly taken into account the fact that *Siemens* and *Alstom* have to face the strong competition of Chinese competitors and, in particular, of the *China Railway Rolling Stock Corporation (CRRC)*, a state-owned enterprise allegedly benefiting from significant state support.<sup>46</sup> The key legal issue would be that these support measures would not be subject to any discipline even remotely comparable to that in force in the EU or, in any event, capable of keeping any distortion on international trade and competition in check. This merger decision led to a heated debate about the need to re-direct European industrial policy (suggesting even the possibility of amending EU merger laws with the introduction of a final veto power of EU Commission’s

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44 This is an hypothesis that is currently being explored by the author.

45 See, e.g., Gary Hufbauer, Thomas Moll and Luca Rubini, *Investment Subsidies for Cross-Border M&A: Trends and Policy Implications*, United States Council Foundation, 2008.

46 According to the *Global Trade Alert* database, the CRRC would have received annual subsidies amounting to US dollars 2485 million in 2016, 1653 millions in 2017 and 2063 millions in 2018: [www.globaltradealert.org](http://www.globaltradealert.org) (“Intervention 77444”, “Intervention 77445”).

assessments by Member States) and on the need to adopt measures to specifically tackle the anti-competitive practices of foreign governments.<sup>47</sup>

On 17<sup>th</sup> June 2020, the day after publishing its consultation note for *A Renewed Trade Policy* (which features at its very core the notion of ‘open strategic autonomy’),<sup>48</sup> the Commission presented its *White Paper on Foreign Subsidies*.<sup>49</sup> This consultation document focuses on subsidies granted by foreign governments to companies established or active in the EU internal market. More specifically, the White Paper mostly addresses those subsidies granted to facilitate the acquisition of a EU target or the participation in public procurement procedures in the EU. The Commission suggested the introduction of four different ‘modules’ or tracks to tackle different scenarios. The explicit premise of this proposal for law reform is the alleged regulatory gap: the said distortions would not be tackled by existing international and EU rules (WTO disciplines, EU competition, merger, State aid, trade remedy, public procurement and FDI provisions). Hence, the need for action. Following the public consultation, the EU Commission presented a proposal for Regulation to the European Parliament and the Council which is currently under review and may well see the light in 2022.

Now, this Regulation would in essence ‘extend’ the application of EU State aid laws to subsidies granted *by* foreign countries. More precisely, it would set up a regulatory mechanism – and remedies – that, *mutatis mutandis*, would reflect the key standards of control of EU State aid laws and would simply be aimed at levelling the playing field between European and non-European companies receiving subsidies.<sup>50</sup> Whatever its nature or impact, and irrespective of its legality with WTO laws,<sup>51</sup> what strikes observers is that the EU seems to have chosen to follow a unilateral course of action to address real or perceived asymmetries in subsidy regulation. As noted in the previous section, the EU has traditionally addressed regulatory diversity and asymmetries (*vis-à-vis* the ‘EU standard’) through negotiating and concluding trade agreements. In other words, and accounting for its clear leverage, the EU has always sought to resolve these differences, and address competitiveness concerns, through consensus with the interested parties. Whatever may be the causes and rationale behind its recent proposal, what the EU is doing now is to act unilaterally.<sup>52</sup> For this reason only, this Regulation may become a trade and diplomatic irritant.

Although firmly embedded in the logic of CVDs, which do not address subsidization in itself but simply neutralize some of its negative effects, this new interventionism echoes another development in the EU’s practice of trade remedies. In particular, the EU creatively construed the notion of subsidy under Article 1 of the WTO Agreement on Subsidies and Countervailing Measures in the context of trade remedy investigations to include also so-called ‘transnational subsidies’. The facts refer to the imposition of countervailing duties on products imported from

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47 *A Franco-German Manifesto*, *cit.*, p. 4.

48 European Commission, Consultation note, *A Renewed Trade Policy*, *cit.*

49 European Commission, White paper on levelling the playing field, *cit.*

50 It is particularly significant that the unit responsible for this proposal sits within DG Comp and not DG Trade.

51 It has been suggested that this proposal may well breach the ‘exclusivity clause’ enshrined in Article 32.1 of the WTO Agreement on Subsidies and Countervailing Measures, in addition to raising issues concerning the principle of non-discrimination. See Luca Rubini, ‘I segni dei tempi: unilateralismo o cooperazione? Riflessioni su alcuni sviluppi nella politica commerciale dell’Unione Europea’, 11<sup>th</sup> November 2020, [www.eurojus.it](http://www.eurojus.it).

52 One wonders whether much of the alleged regulatory asymmetries and competitiveness concerns could in fact be directly addressed at the multilateral level, in particular through the possible renegotiation of the EU’s GATS schedules. This perspective was raised to the Author by Petros Mavroidis.



Egypt which used Chinese funds to support the relevant Egyptian producer.<sup>53</sup> Legally speaking, the Commission relied on the International Law Commission's Articles on State Responsibility to impute the Chinese financial contribution to the Egyptian government.<sup>54</sup>

It is interesting to enquire why the EU is on the one hand stretching the current laws and on the other hand suggesting to introduce new legal instruments to tackle Chinese subsidies. There may be various reasons for this. First, it is known that the global trading system, represented by the WTO and its laws, goes through a period of multiple crises, one of which is certainly its inability to update its rule-book (negotiated in the 1980s-early 1990s) to adapt to the current challenges. Secondly, China's emergence as a global trade power, which is best expressed 'through its loans and investments'<sup>55</sup> (the 'Belt and Road' initiative representing the epitome), is increasingly putting strain on the WTO's rule-book for the simple reason that this is based, like the GATT's, on a liberal understanding of the economy, which is quite different from the Chinese one.<sup>56</sup> Thirdly, initiatives are taking place to discuss about the future of the WTO and how to update its disciplines and the EU plays a prominent role in these debates<sup>57</sup> but, perhaps inevitably, talks and proposals are prevailing on action. Finally, the EU has various negotiating and discussion tables with China but agreement on discrete legal commitments, and particularly agreements constraining public spending, is certainly not within easy reach.<sup>58</sup>

All these, and perhaps other, factors are highly likely to have convinced the EU that unilateral action was inevitable.<sup>59</sup> What could not be achieved through consensus will – so it is hoped in Brussels corridors – be achieved through regulatory coercion. This is too an expression of EU's regulatory power, this too would extend the territorial influence of EU-styled law. Being unilateral and coercive, it is, however, also likely to raise frictions.<sup>60</sup> It remains to be seen

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53 See Notice of Initiation of an Anti-Subsidy Proceeding Concerning Imports of Certain Woven and/or Stitched Glass Fibre Fabrics Originating in the People's Republic of China and Egypt, OJ 2019 C 167/11; Notice of initiation of an Anti-Subsidy Proceeding Concerning Imports of Continuous Filament Glass Fibre Products Originating in Egypt, OJ 2019 C 192/30; Notice of Initiation of an Anti-Subsidy Proceeding Concerning Imports of Certain Hot Rolled Stainless Steel Sheets and Coils Originating in the People's Republic of China and Indonesia, OJ 2019 C 342/18.

54 For a commentary see Victor Crochet and Vineet Hedge, 'China's "Going Global" Policy: Transnational subsidies under the WTO SCM Agreement', 4 *Journal of International Economic Law* 23, 2020, pp. 841-863. What is fundamentally incorrect in this approach is the use of (draft) "secondary" rules (i.e. rules pertaining responsibility) to construe "primary" rules (i.e. rules pertaining regulated definitions and conduct). It is the same mistake made by the Appellate Body in the famous *US – AD/CVD* dispute (DS 379). In this respect, see Joost Pauwelyn, "Treaty Interpretation or Activism? Comment on the AB Report on *United States – ADs and CVDs on Certain Products from China*," *World Trade Review*, pp. 235-241.

55 See Anu Bradford, *The Brussels Effect*, *cit.*, p. 24.

56 See Petros Mavroidis and André Sapir, *China and the WTO: Why Multilateralism Still Matters*, Princeton University Press, 2021.

57 See the Commission's 'Concept paper on WTO modernisation', 18<sup>th</sup> September 2018, available at: [https://ec.europa.eu/commission/presscorner/detail/en/IP\\_18\\_5786](https://ec.europa.eu/commission/presscorner/detail/en/IP_18_5786). Together with the US and Japan, the EU has also set up in late 2017 the so-called 'Trilateral initiative', mostly to address 'market-distorting' conducts in global trade. Finally, the EU is also integral part of the 'Ottawa group', spearheaded by Canada, which convenes 15 Members of the WTO. Information available at: [https://www.international.gc.ca/world-monde/international\\_relations-relations\\_internationales/wto-omc/ottawa-group-groupe.aspx?lang=eng](https://www.international.gc.ca/world-monde/international_relations-relations_internationales/wto-omc/ottawa-group-groupe.aspx?lang=eng).

58 The most notable advance is probably the Comprehensive Agreement on Investment, on which China and the EU reached an agreement in principle on 20<sup>th</sup> December 2020.

59 This is also what is happening with the Carbon Border Adjustment Measures ('CBAM') for which the Commission has recently presented a proposal of regulation currently under review of the European Parliament.

60 The policy initiative on foreign subsidies can be contrasted to the 'parallel' initiative on CBAM (see previous note) where the legislative process is showing a much greater awareness to ensure the flexibility of the proposed instrument and the importance of dialogue with the interested parties. In his recent draft report (2021/0214(COD), 21<sup>st</sup> December 2021), Mr Mohammed Chahim, MEP and member of the Committee on the Environment, Public Health and Food Safety, noted that the "CBAM

whether it will represent a blocking – rather than a stepping stone – in the quest for better plurilateral or multilateral rules on state intervention in the market.

## 6. Conclusive remarks

State aids and their control are one of the most controversial issues in international law. This paper has sketched the ways through which the EU has managed to transcend the limits of territoriality and export and, in some cases, even imposed the key tenets of its internal disciplines.<sup>61</sup>

The extension of State aid principles and rules in preferential trade agreements and in the unilateral instruments adopted by the EU is also relevant from another viewpoint. The extension of the regulatory power beyond one's jurisdiction evokes discussions about sovereignty, its expansion and its limits.<sup>62</sup> And true to the basic principles, one's sovereignty finds its main limits into another's sovereignty. The final piece in this jigsaw is constituted of another unilateral instrument the EU is currently contemplating.<sup>63</sup> Increasingly concerned of the economic coercion exercised by third countries - which is defined as an interference "in the legitimate sovereign choices of the Union or a Member State by seeking to prevent or obtain the cessation, modification or adoption of a particular act by the Union or a Member State, by applying or threatening to apply measures affective trade or investment"<sup>64</sup> - the EU is contemplating the introduction of a legal mechanism to tackle it. This instrument would include a progressive action starting with dialogue and, in case of lack of success, ending with the imposition of countermeasures. Given the breadth of the language of the notion of 'economic coercion', it is not possible to exclude that the scenario might even include subsidies and their regulation. What would happen, for example, if a third country would pressurize the EU to remove a remedy introduced under the prospective Regulation on foreign subsidies?

In a world increasingly interdependent, and, at the same time, increasingly turning towards a more unilateral economic order (where sticks are the often preferred to carrots),<sup>65</sup> how can this clash between unilateral actions be settled? The only answer can be: by ensuring that any action stay within the boundaries of the law. Different unilateral policy actions, and their interface, should comply with key tenets of international law, which encompass non-discrimination, necessity, proportionality and transparency.<sup>66</sup>

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should be a system that fosters cooperation rather than confrontation with respect to climate policies and trade".

61 Space does not allow us to explore another path followed by the EU to export EU law, i.e. via the participation in international organizations. For an analysis of a recent example where the key elements of the *Altmark* jurisprudence have been successfully used in WTO litigation see Luca Rubini, 'The Wide and the Narrow Gate: Benchmarking in the SCM Agreement after the *Canada – Renewable Energy / FIT Ruling*, 2, *World Trade Review*, 14, 2015, pp. 211-237.

62 See the seminal observations of John Jackson, 'Sovereignty – Modern: A New Approach to an Outdated Concept', *American Journal of International Law*, 97, 2003, pp. 782-803.

63 Press Release, 'The EU strengthens protection against economic coercion', Brussels 8<sup>th</sup> December 2021, available at: <https://trade.ec.europa.eu/doclib/press/index.cfm?id=2339>.

64 Article 2.1, Proposal for a Regulation on the protection of the Union and its Member States from economic coercion by third countries, Brussels, 8.12.2021, COM(2021) 775 final.

65 Julien Chaisse and Georgios Dimitropoulos, 'Special Economic Zones in International Economic Law: Towards Unilateral Economic Law', 2, *Journal of International Economic Law*, 24, 2021, pp. 229-257.

66 For an initial commentary on the legality of the proposed Anti-coercion instrument see Freya Baetens and Marco Bronckers, 'The EU's Anti-Coercion Instrument: A Big Stick for Big Targers', Ejliltalk.org blog, 19<sup>th</sup> January 2022, available at: <https://www.printfriendly.com/p/g/nujGuW>.

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