

# THE EU HAS ISSUED ITS WHITE PAPER ON LEVEL PLAYING FIELD RULES DESIGNED TO TACKLE FOREIGN SUBSIDIES. WILL JAPANESE FIRMS SUFFER?

31 August 2020 | Insight  
Legal Briefings - By **Joel Rheuben**

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As [recently reported](#) in the Nikkei Shimbun, on 17 June 2020, the European Commission issued its “[White Paper on levelling the playing field as regards foreign subsidies](#)” (**White Paper**). The White Paper considers possible options and new legal instruments for the Commission to address distortions in the European Union internal market which result from subsidies and other support provided to companies by foreign governments.

## WHAT IS THE WHITE PAPER?

The White Paper is the outcome of several years’ of discussions within the Commission on addressing a perceived enforcement gap in EU competition and trade law. On the competition law side, although the EU has a legal framework governing subsidies provided by EU member states (the [State Aid rules](#)), it currently has no similar rules relating to subsidies from non-EU governments. On the trade law side, EU anti-dumping rules only cover imports into the EU, and not support to companies already doing business in the EU.

The White Paper considers three possible “modules” to address this gap:

A general ex-post tool to investigate and possibly take measures against foreign subsidies provided to beneficiaries established or active in the EU. This would be similar to the Commission's powers to investigate cartels and other breaches of competition law, but unlike competition law investigations, the Commission would be able to take into account whether the subsidised activity has a potentially positive impact in the EU that outweighs any distortions it creates (e.g. the creation of jobs, climate change and protection of the environment, digital transformation, as well as security and public order).

A mandatory mechanism for prior notification of foreign subsidies facilitating the acquisitions of EU companies. This notification mechanism would operate separately from, but in parallel with, the current EU merger control process, as well as national-level foreign investment screening regimes.

A mandatory mechanism for prior notification of foreign subsidies in the context of public procurement procedures.

All three proposals would give the Commission unprecedented powers to scrutinise foreign government financial policies.

## **HOW WILL THE WHITE PAPER AFFECT JAPANESE COMPANIES?**

Although the White Paper is careful not to explicitly make reference to any particular foreign government, much of the commentary surrounding the White Paper suggests that inward investment from China is a key driver for the proposals. The White Paper comes within the context of tighter foreign investment restrictions within the EU ([please see our article from last month](#)), as well as ongoing discussions about [reforming EU merger control rules](#) to better take into account competitive pressure from major non-EU companies, including SOEs. The latter follows the Commission's controversial prohibition of the merger between Siemens' and Alstom's high-speed rail businesses last year, in which the parties unsuccessfully argued that a "European champion" was needed to compete with Chinese trainmakers. It is notable that the Chinese mission to the EU responded quickly to the White Paper, stating that the EU should refrain from taking "protectionist measures".

Nevertheless, the Commission's proposals are wide enough to also have potential implications for private Japanese companies doing business in the EU.

The White Paper defines "subsidies" provided by foreign governments expansively to include not only direct grants of money, but also preferential financing, loan guarantees, tax rebates, and the provision of goods and services, and to include subsidies both aimed at specific investments in the EU, as well as provided more generally. The experience of several decades of State Aid decisions also suggests that the scope of "subsidy" is likely to be treated quite widely.

Accordingly, any eventual mechanisms to deal with foreign subsidies could apply to a range of government support that is commonly received by Japanese companies investing overseas. This could include the provision of low-cost loans and other financial support by export credit agencies, or co-equity investments by government-sponsored investment funds or incorporated administrative agencies.

It is also worth noting that the White Paper envisions setting the threshold at which subsidies could be reviewed at a low level – a total over EUR 200,000 over three consecutive years – meaning that practically all government support would be reviewable.

The White Paper acknowledges the difficulties of identifying and quantifying government support, particularly from governments with opaque budgets and administrative structures. At least initially, Japanese companies may make “easy targets” for review, given Japan’s relatively transparent fiscal rules, and Japanese companies’ willingness to comply with overseas government investigations. It is sometimes suggested that these factors account for a disproportionate representation of Japanese companies in global cartel investigations.

### **WHAT SHOULD JAPANESE COMPANIES CONSIDER?**

If subsidies are found to have distorting effects on competition, the White Paper proposes potential remedies including repayments to foreign governments, redressive payments to EU governments, divestment of assets, or prohibitions on investments. In the long term, some Japanese companies may be more reluctant to accept subsidies aimed at EU investments if this could impact certainty about their ability to hold onto those investments.

If the prior notification module is introduced, Japanese companies will also need to take into account the potential need for additional regulatory filings when negotiating conditions precedent in purchase agreements. As noted above, notification may be required for subsidies of only EUR 200,000, whereas the EU merger control thresholds are based on existing EU turnover of hundreds of millions of Euros. Moreover, the White Paper proposes that prior notification would be required for acquisitions of “material interests” in EU companies, a lower standard than the “control” test under the EU merger control rules. This means that prior notification could be required in many cases where merger control filings are not, adding to complexity for purchasers.

At the same time, private Japanese companies that do not receive government subsidies could become more attractive in competitive bid situations, particularly compared with SOEs. This is a trend that we are already seeing as a result of tightening foreign investment regulation.

It is finally worth noting that as the UK is now no longer a part of the EU, UK government support provided to Japanese companies with key European operations in the UK could potentially qualify as “foreign subsidies” for the purposes of the White Paper’s proposed mechanisms. The UK and EU have yet to reach an agreement on whether [the UK’s post-Brexit State Aid rules](#) will align with those of the EU.

## WHAT HAPPENS NEXT?

Although a substantial development, the White Paper still represents the beginning of a legislative process, and it is not certain whether or to what extent the Commission's proposals will be adopted.

The Commission is currently holding a [public consultation](#) on the proposals, which is open to comments until 23 September 2020. The Commission is likely to then publish legislative proposals in the course of 2021.

For more details, please see our full briefing [here](#).

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**GRAEME PRESTON**  
REGIONAL HEAD OF  
PRACTICE -  
CORPORATE, TOKYO  
+81 3 5412 5485  
Graeme.Preston@hsf.com



**KYRIAKOS  
FOUTOUKAKOS**  
EMEA REGIONAL  
HEAD OF PRACTICE -  
COMPETITION,  
REGULATION AND  
TRADE, BRUSSELS  
+44 7920 455 155  
Kyriakos.Fountoukakos@hsf.com



**KRISTIEN  
GEEURICKX**  
PROFESSIONAL  
SUPPORT  
CONSULTANT,  
LONDON  
+44 20 7466 2544  
Kristien.Geeurickx@hsf.com



**JOEL RHEUBEN**  
SENIOR ASSOCIATE  
(ENGLAND AND  
WALES, AUSTRALIA),  
TOKYO  
+81 3 5412 5480  
joel.rheuben@hsf.com