

## China as a systemic rival and the European toolbox

- March 2019 the European Commission and EEAS produced a communication on the EU-China relations calling China a “systemic rival” and proposing to the European Council a number of recommendations for action.

- Amongst them and of particular interest for the European services industries are actions 5 to 8, namely:

- \* reforming the WTO in particular on subsidies and forced technology transfers

- \* promote reciprocity and open up procurement opportunities in China by adopting the IPI instrument by the end of 2019

- \* ensure that not only price but also high levels of labour and environmental are taken into account

- \* addressing the distortive effects of foreign state ownership and state financing in the internal market

- Not by accident the EU Communication was published hardly three months after the publication of a ground breaking Policy Paper by the BDI, (Bundesverband der Deutschen Industrie) in January 2019 titled “Partner and Systemic Competitor - How to deal with China's State-Controlled Economy ?”

This was in itself remarkable since Germany has always been very reluctant to openly criticize China. Germany was - and still is - the only EU Member State with a positive trade balance with China, partly as a result of export of luxury cars. But then came the acquisition by a Chinese company - the Midea Group - of KUKA, the German jewel of robotics, which acted as an eye opener.

The proposals of the BDI Policy Paper are going in the same direction of the EU Communication but they are broader and more specific.

Of particular interest to us is the German proposal to prevent dumping of services : " So far, there are no effective instruments against dumping in trade in services. There are gaps in both WTO and EU law. Although the EU Commission has made it possible to take labour and environmental standards into account in the methodological renewal of the basic anti-dumping regulation, it is questionable to what extent this can be used to tackle distortions of competition in the increasingly important services sector. The creation of new instruments should be considered here."

- A third element I want to highlight is the "Made in China 2025" strategy promulgated by the State Council of the Peoples Republic of China in May 2015

aiming at becoming global leaders in a number of strategic high-tech sectors, among them marine engineering and high tech ships.

The recent problems of EU dredging majors in obtaining export licenses for high tech vessels is illustrative.

In the light of all this, and there are of course a large number of other references and examples to demonstrate the systemic challenge China poses for the EU and the world at large, I will try to make a critical assessment of the EU toolbox as of today to counter unfair competition by China and preserve our strategic interests.

In 2012 I introduced together with Michel Barnier IPI, the International Procurement Instrument which tried to set the cursor between openness and reciprocity in the EU Public Procurement Market. We are end of 2019 and there is not yet a decision on the proposal.

The original proposal suggested the possibility to restrict market access for third countries not engaging in trade negotiations with the EU.

For 'not covered procurement' which is not subject to EU's international commitments in FTA's and the GPA - Free Trade Agreements and the Government Procurement Agreement of the WTO - we introduced a new procedure to restrict access to the huge EU Public Procurement Market whenever there was a substantial lack of reciprocal opening of public procurement in the originating country.

Two distinct procedures were proposed :

- \* a decentralized one whereby the procuring entity could request the Commission approval in order to exclude a foreign tender because of a lack of substantial reciprocity in market opening between the EU and the country from which the goods and/or services originate.
- \* a centralized procedure where based on Commission investigations the EU could close the EU procurement market or decide a price adjustment measures for third countries in breach of reciprocity.

The idea was to incentivise such third countries to engage in negotiations on opening up their public procurement markets with the EU.

In the European Parliament a majority was found largely respecting the proposal. The Council however never managed to issue an opinion because of

deep Member State divisions between a group of Member States led by France that was in favour and an opposing block led by Germany and comprising the Eastern European countries as they considered the instrument a protectionist measure.

Because of the deadlock, the Commission proposed in January 2016 an amended proposal. The decentralized procedure was dropped and the centralized procedure watered down. It was no longer possible to effectively close the EU procurement market as a result of the investigations and only a price adjustment measure of 20% maximum survived the political slaughterhouse. EuDA in this supported by FIEC and EIC called for complete rejection of the amended proposal. Rightly so. The Commission is still insisting on the IPI instrument being adopted, but up to now to no avail. And I hope my aborted political child will never grow up. It is too little, too late. And its adoption even risks to be counterproductive because it would result in a misguided feeling of relief.

A number of other proposals have been initiated on procurement by DG Grow, the Directorate General of the EU Commission for the internal market and industry.

\* On large procurement biddings in general, the Commission services have informed Member States that they can - on a voluntary basis - submit large tenders for ex ante consultation to the Commission. The threshold is € 700 mio. Some big projects - such as an airport bidding in Sofia - have thus been submitted for scrutiny. It is though not a public proposal to change the legal framework.

\* In the area of energy, there is a specific ex-ante notification system for intergovernmental agreements. They often include derogations to public procurement rules. Decision 2017/684 of the European Parliament and the Council on establishing an information mechanism with regard to intergovernmental agreements and non binding instruments between Member States and third countries in the field of energy makes sure the Commission knows about that before the fact. This is part of the Energy Union to make external energy policy more coherent and is possibly interesting for wind farms.

\* In the current public procurement directives, the general rule is as follows: tenders which are suspiciously low, because of the bidding company may pay low wages, does not comply with social security etc., cannot be excluded right away. But the authority can override a cheaper bid for these reasons and award the contract to a more expensive one. The Directives do not contain a definition

of the concept of abnormally low tender, it is for the Member State and the contracting authorities to determine the method of calculating an anomaly threshold constituting an abnormally low tender. Not very promising if you ask me.

In the area of utilities there is a comparable norm which is however almost never applied in practice. The IPI instrument was partly conceived to remedy this but in its watered down doesn't offer a remedy either.

Concluding, the current EU rules on international procurement are not up to their task as they allow diverging national approaches in the single market. They do also not create leverage to open up third country markets, one of the declared goals of the Directives.

I should open here a parenthesis on the recent 6th revised Chinese offer on GPA that gives market access to dredging services with threshold of 7,5 mio SDR (Special Drawing Rights - more or less the same as Euros). However, the exceptions that apply leave a large leeway for China to effectively discriminate in awarding procurement contracts. There is a general exception with respect to reciprocity, an exception for small and medium enterprises, national security and indirect procurement (meaning procurement on behalf of a not covered entity). As such, these exceptions are not uncommon, but relating to China their hollowing out effect is major. I really wonder whether the EU should consider this offer positively or rather menacing. If accepted it would give China an undisputed entry on our public procurement market without any guarantee of actual reciprocity!

Reciprocity is a buzz word in international trade agreements. But will it create business for our companies on the Chinese market? I doubt it. I am not a believer. The starting point of my reflection is that we should count on our own strengths and procedures, matching openness on third markets, living up to the WTO rule book, to our international engagements, but leaving aside any glimpse of naivety.

What we need to protect our procurement market against unfair competition is a new instrument that effectively tackles the present unsatisfactory market conditions. As I mentioned in the beginning of this brief introduction, also the BDI has come to that conclusion: So far, there are no effective instruments against dumping in trade in services. The creation of new instruments should be considered here".

EuDA has developed such a new instrument and submitted it to the outgoing European Commission. For such an instrument to be effective it should be

robust, ambitious and comprehensive. And above all, the initiative - as in the trade defence instruments in goods - the initiative should be primarily with the industries concerned and the decision taking with the Commission. It should be straightforward and equally addressed at all third countries .

The EU can introduce such an instrument of its own because it has exclusive competence over the common commercial policy and international trade and within this remit acts as a sovereign, as a state so to say. Meaning the EU is the only one to decide and/or act unless it is explicitly prohibited or stipulated as otherwise. Art 207 TFEU puts it uncommonly clearly: "The common commercial policy shall be based on (...) measures to protect trade such as those taken in the event of dumping or subsidies".

Though, for services there is a serious gap as they got less attention in the WTO remit. GATS (the General Agreement on Trade in Services) has no proper sanctioning regime. This gap could be filled by applying the same procedure as under the Trade Defence Instruments which are now only applicable to goods but this can as well apply to services. And this goes for anti-dumping and anti-subsidy procedures, either looking at them independently or combined. It largely depends on whether the burden of proof can be realistically determined.

One can find inspiration from Regulations on unfair pricing practices in maritime transport and air transport, the latter being the subject of a recently adopted Regulation. These Regulations lay down certain procedures on how to respond to unfair pricing practices or the violation of applicable international obligations by certain third country service providers. If they affect the competition and cause injury to Union providers, the EU could investigate and apply repressive duties in order to protect Union service providers from these unfair trade practices and safeguard their interests. More importantly these regulations can provide the basis or layout so to create similar instruments addressing other service sectors than just air and maritime transport, like construction, dredging and services involving contractors.

The initial reaction of the Commission is not outspoken positive and seems to argue that the specific EU rules addressing unfair practices in air and maritime transport services cannot be extended directly to other sectors, but without putting forward a decisive argument. We will have to convince the incoming Commission. We have overriding arguments and strong supporters, not in the least the BDI that has come to exactly the same conclusion.

One last remark. The TDI systems work because industry can put it in motion. When a representative sample of an industrial sector - 15% - hands in a complaint with the Commission, she has to act, investigate and take the

appropriate measures. Such happens. The recent reform of TDI has strengthened the hand of the Commission.

I have no doubt that the incoming Commission will take the defence of the EU interests at heart and that the changing winds of trade will help.