

Non-paper strengthening the level playing field on the internal market The Netherlands

Introduction

- A policy of open markets, cooperation and a strong and politically independent enforcement of competition has made the EU one of the most prosperous and competitive regions in the world.
- At the same time, one of the challenges faced by the EU is how to maintain a level playing field when economic operators established in a third country increase their presence and activities on the internal market.
- The EU's competition policy and state aid rules have been part of the Treaty since the start and have been essential to provide a level playing field for businesses on the internal market.
- However, EU competitors do not only compete with other EU competitors, but also with economic operators from third countries that do not always play by the same rules. Especially when it comes to state financing and ownership of foreign companies in their home state.
- In order to address the distortive effects of foreign state ownership and state financing in the internal market, the Dutch government has been working on a proposal to strengthen the EU competition framework to form a "sixth" branch to the existing EU competition law.

Problem analysis

- The structure of state-driven economies can lead to distortions in open market economies. Non-regulated state aid benefits and market power in the home market enable cost advantages and surplus profits that have a distorting effect on competition in markets abroad.
- Within the European Union these problems are mostly prevented through application of a state aid framework for financial aid to companies and a stringent competition framework.
- The improper advantages of third-country economic operators, through discriminatory aid benefits and surplus profits, allow these operators to build up market power on the European internal market at the expense of other economic operators. This results into three problems:
 - On the one hand, allocative efficiency on the internal market comes under pressure, as efficient market economy operators are being displaced by less efficient economic operators. This can also be at the expense of the innovative capacity of the European economy;
 - On the other hand, an increased market concentration of unregulated third-country economic operators can lead to abuse of the dominant position in the future. It may be desirable to anticipate this risk. In the past, this anticipated risk was the justification for regulating economic operators with a dominant market position and the establishment of merger control;
 - More strategically, the competitiveness of European economy operators is undermined and with it the ability to develop critical technologies, address societal challenges and maintain high-quality employment.

Possible options for action

- First-best: preserve global competition as much as possible, and harmonize the regulation of state aid and market power on a global level:
 1. A competition framework that regulates potential abuse of dominant position, with equal application for both market economic operators and state-owned economic operators in all (relevant) sectors;
 2. A state aid regime that complies with market conformity and non-discrimination and includes services.
- Second-best: harmonize the regulation of state aid and (monopoly) market power between countries through bilateral trade agreements.

Analysis: Both solutions have the problem that this affects the sovereignty of third countries within their own jurisdictions. Obstacles to these solutions are not expected to diminish in the short or medium term. The WTO has also been unable to reach a consensus between countries. Negotiating bilateral agreements that sufficiently harmonizes the regulation of state aid and market power is not a possibility in many cases.

- Third-best, in line with the Dutch proposal, economic operators with (discriminatory) aid benefits and unregulated market power should be subject to stricter supervision, in order to prevent potentially disruptive behavior.
- More far-reaching and therefore undesirable 'solutions' are to prohibit or severely restrict the economic activities of selected economic operators on the European internal market or to ease merger regulation to facilitate the creation of European champions. However, next to

multilateral constraints this removes too much competitive pressure from European economic operators and is harmful to consumers. That is not proportional to the problems outlined.

- Therefore the third-best solution seems the best available option. Measures like these are a proportional response to concerns relating to the level playing field between EU and non-EU companies. It also allows the EU to remain an interesting destination for FDI.

Level playing field proposal

- The Dutch proposal aims to strengthen the EU competition framework and forms a “sixth” branch to the existing EU competition law and has to be seen as part of our broader perspective on modernizing EU competition policy, whilst recognizing and holding on to the strengths of a stringent and apolitical competition framework.
- The goal of the proposal is to be able to take measures if a company, **irrespective of its nationality**, distorts or threatens to distort the competition within the internal market, because it (1) receives government support **or** (2) has an unregulated dominant position in a third-country market.¹
- If the suspicion exists that a company exhibits certain potentially distortionary behavior (as described below), enabled by government support or excess profits from an unregulated dominant position in its own country, the European Commission may conduct an (ex-ante) investigation into a company’s conduct, with a focus on transparency in accounting.
- Possible measures include transparent and separate bookkeeping between activities on the internal market and elsewhere. Unless these measures provide sufficient certainty that competition will not be distorted in the internal market, certain market behavior will be prohibited:
 1. Supply constraints that are not in line with market conditions;
 2. Price and product differentiation between different market operators on comparable transactions;
 3. Tied selling, whereby additional conditions are imposed with no (apparent) relationship to the transaction;
 4. Wholesale/retail pricing that is not a reflection of market prices and / or production costs;
 5. investments in assets with no apparent business case, i.e. that are insufficiently profitable.
- Most of these constraints are not necessarily new. They are -under circumstances- also imposed on companies that are in a position to distort competition, i.e. merger control of concentrations and competition supervision of economic operators with a dominant position.
- The investigation and enforcement take place in accordance with existing competition practice and can therefore either be initiated by whistleblowers or by independent investigation by the European Commission.
- The proposal also allows for companies to submit themselves ex-ante to an investigation, if they are unsure whether their market behavior would be subject to the scope of this proposal.
- The proposal is also not a comprehensive solution to all the challenges of state-driven (forced) technology transfers, intellectual property and loss of innovation. The proposal mainly addresses the excesses of distortionary behavior on the internal market. With regard to investments and acquisitions, the proposal mainly looks at investments that are simultaneously not sufficiently profitable and enabled by state aid or excess profits on their domestic market.
- State aid won’t be prohibited, but it should be transparent and companies on the internal market must be subject to regular market conditions. The proposal therefore draws on the original provisions on fair and equal competition from the European Coal and Steel Community.
- Competing on comparative advantages between countries and regions will remain possible and is not affected by the proposal.
- The proposal is based on the best elements of competition practice and case law. Specifically, it combines the tools of EU competition law (cartel prohibition, prohibition of abuse of a dominant position, the treatment of state-owned enterprises, state aid and the market economy operator principle) with the aim of ensuring fair competition in the internal market between companies without discrimination.

Additional and more detailed information can be provided upon request. This includes but is not limited to: a legal non-paper, a draft regulation, additional Q&A’s regarding the relationship with other EU initiatives and the functioning of the mechanism.

¹ It applies to both EU- and non-EU companies. In practice most (but not all) companies affected by such measures based on a non-discriminatory adaptation of Union competition framework will be third country companies as Union companies are already subject to stringent rules on competition and state aid.

Annex 1. Flowchart Level playing field proposal

