EuDA/ FIEC/ EIC joint Policy Paper

on

Fostering a Level Playing Field in Construction Services

Executive Summary

In over 20 years, China has become the 2nd biggest economy in the world and the world's workshop as well as the largest construction market in the world, ahead of the EU and the United States.
To achieve such results, China developed an economic model of asymmetric relations and unbalanced partnerships, established and controlled through a comprehensive network of State-owned Enterprises, capable of providing cheap financing, dumped prices and mega package economic and political deals.
China's ambitions are threatening EU industries, including construction and dredging.

FIEC, EIC and EuDA call upon the EU Institutions and EU Member States to

- ensure that the general trade principle of "**reciprocity**" is respected in practice;
- ensure that **EU funds cannot be used in the Internal Market by contractors from third countries** which reserve the use of their funds for domestic construction companies only;
- ensure that **"abnormally low tenders" are actually checked and analysed** by the contracting authorities;
- develop efficient **trade defence instruments for services**, in particular in the areas of anti-dumping and anti-subsidies;
- ensure that **Chinese State-owned Enterprises** need to prove that they apply Market Economy Principles, that their prices are not dumped and that they are not benefitting from illegal State subsidies (incl. illegal State aid);
- ensure that **EU State Aid Regulations** uniformly apply to all contractors, including third country contractors, active in the Internal Market;
- open the Chinese construction market for foreign contractors, e.g. by ensuring that **China becomes a GPA signatory on equal terms** with all other GPA participants.
- ensure that the European construction and dredging industries can rely on a **strong European export and project finance institution** to provide long-term finance for construction projects executed by European contractors in third countries, as do our major third country competitors;
- establish, in practice, a real level playing field with China as regards to all **OECD Regulations in connection with State-supported export credits**;
- establish, in practice, a real level playing field with China as regards to **all decisions, recommendations and guidelines of the OECD Development Assistance Committee**;
- declare **Chinese construction companies ineligible for participation in infrastructure tenders financed from EU Official Development Assistance**, especially if such companies are **State-owned**, as long as China does not follow the same official financing rules and practices as its OECD counterparts;
- update the **EIB Procurement Guide** as regards the financing of EIB operations outside the EU and **align with the EU Procurement Directive 2014**, in particular with regard to the **"Most Economically Advantageous Tender"**;
- incorporate into the EIB Procurement Policy **safeguards** similar to those in the World Bank's Standard Procurement Documents in relation to **Environmental, Social, Health and Safety (ESHS)**;
- reconsider the **EC infrastructure funding strategies towards China**, and in particular towards the Belt and Road Initiative, and switch EC investments to the Sub-Saharan African, Mediterranean and Balkan areas also to reduce immigration.

FIEC (European Construction Industry Federation) *represents via its 31 national Member Federations in 27 countries (26 EU & EFTA and Turkey) construction enterprises of all sizes, i.e. craftsmen, small and medium-sized enterprises as well as "global players", carrying out all forms of building and civil engineering activities.*

EIC (European International Contractors) *has as its members construction industry trade associations from fifteen European countries and represents the interests of the European construction industry in all questions related to its international construction activities. In 2017, the international turnover of companies associated with EIC's Member Federations amounted to more than 175 billion €.*

EuDA (European Dredging Association) *and is the official interface between the European dredging industry and the European Institutions. EuDA members employ approximately 25,000 European employees directly "on land and on board of the vessels" and more than 48,300 people indirectly (through the suppliers and services companies). The combined fleet of EuDA's members counts approximately 750 seaworthy EU-flagged vessels.*

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1 Background on the EU and the "China Challenge"

China's economic power and political influence has grown with unprecedented scale, speed and unopposed. In his analysis, "*The Silk Road Trap: How China's Trade Ambitions challenge Europe*", 2019, Prof. Jonathan Holslag stated that despite decades of constructive engagement towards China, Europe has made no significant progress on any of its policy objectives with regard to China[1]. Furthermore, he states that overall, China's economic policy had a negative impact on the economic growth of the European countries.

The European Commission's recently published new strategic outlook on China has called it *"a cooperation partner with whom the EUC has closely aligned objectives, a negotiating partner with whom the EU needs to find a balance of interests, an economic competitor in the pursuit of technological leadership, and* ***a systemic rival*** *promoting alternative models of governance."*[2]

In the recent EU-China Summit, Donald Tusk, President of the European Council, underlined the fact that *"our aim is to focus on achieving a balanced relation, which ensures fair competition and equal market access."*[3] The rebalancing of the economic relationship remains a top objective and priority, nevertheless China is proposing no concrete actions. It is high time for Europe to retake the strategic and economic leadership and take decisive action: "*The future of Europe must not be made in China, it must be made in Europe*".

During the Council Meeting of 21-23 March 2019, the European Council - the EU Member States - came to the conclusion that "*the* ***EU must also safeguard its interests in the light of unfair practices of third countries****, making full use of* ***trade defence instruments*** *and* ***our public procurement rules****, as well as ensuring* ***effective reciprocity for public procurement*** *with third countries. The European Council calls for resuming discussions on the EU's international procurement instrument."* [4]

We therefore welcome the European Council's call for action by the EU and its Member States to ensure *"***fair competition … within the Single Market and globally***, both to protect consumers and to foster economic growth and competitiveness, in line with the long term strategic interests of the Union. We will continue to update our European competition framework to new technological and global market developments. The Commission intends to identify before the end of the year* ***how to fill gaps in EU law in order to address fully the distortive effects of foreign State-ownership and State-aid financing in the Single Market****."*[5]

1.1 Unbalanced Partnership

Since 1995, the European countries agreed on a constructive partnership with China, intending to *"help China in its difficult process of transition"*. In other words, China would temporarily benefit from an asymmetric relationship whereby it can access the EU market without reciprocating the favour, until the transition is completed or self-sustained.

In the 15 years (1995-2010) that followed, China grew into the second biggest economy in the world, became the world's workshop and progressed from a low-income country to an upper-middle income country. This is sufficient proof that **the temporary favours (asymmetric relations) have achieved their goals and should be stopped**.

Since 2008, European countries overall lost over **140 billion euros per year** to China (amounting to 1.4 trillion euros transferred to China in 10 years). Furthermore, this **unbalanced partnership model** was replicated worldwide by China.

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[1] According to Prof. Holslag, the seven policy objectives towards China, which the Member States have put forward via the European institutions, are the following: Rebalancing of the Chinese economy, diminishing of China's dependence on external markets, reducing Europe's trade deficit with China, secure fair treatment for European companies on the Chinese market, level the playing field in exchanging intellectual property, fair competition with China in third markets and work together with China to strengthen global economic governance.

[2] European Commission, 'EU-China – A strategic outlook' (March 2019) https://ec.europa.eu/commission/sites/beta-political/files/communication-eu-china-a-strategic-outlook.pdf

[3] European Council, 'European Council Conclusions, 21-22/03/2019' (March 2019) https://www.consilium.europa.eu/en/meetings/european-council/2019/03/21-22/

[4] European Council, 'European Council Conclusions, 21-22/03/2019' (March 2019) https://data.consilium.europa.eu/doc/document/ST-1-2019-INIT/en/pdf

[5] European Council, 'European Council Conclusions, 21-22/03/2019' (March 2019) https://data.consilium.europa.eu/doc/document/ST-1-2019-INIT/en/pdf

Evolution of China in the World Bank Analytical Classifications

GNI per capita in US$ (Atlas methodology)		1990	1995	1997	2000	2005	2010	2015	2017
CHN	China	*Low income (L)* <= 610	L <= 765	*Lower middle income (LM)* 786-3,125	LM 756-2,995	LM 876-3,465	*Upper middle income (UM)* 3,976-12,275	UM 4,036-12,475	UM 3,896-12,055

World Bank Analytical Classifications (presented in World Development Indicators)

Nevertheless, despite all this impressive progress, China is still officially a developing country because it has not yet crossed the symbolic income threshold of US$ 12,000 per capita to become formally a high-income country.

1.2 China's strategy and the contractors

The overall objective of China's economic policy is **to achieve a state of global oligopoly or monopoly for Chinese companies** involved in 'strategic sectors' (including construction and dredging[6]). All the economic and political instruments of China's economic policy aim at drying out gradually the selected markets from non-Chinese competition.

The countries in these situations have to repay loans they cannot afford and are contractually forced to pay with their natural resources and key economic assets (such as their main national ports, used as collateral guarantee of payment). Moreover, once the Chinese oligopoly or monopoly has been established, these countries face prices much higher than before. "*Many companies are allowed to generate large incomes from virtual monopolies or enjoy cheap funding from State banks*".

This paper is describing the unfair trade practices used by China in the construction and dredging sectors inside and outside as well as concrete proposals by FIEC, EIC and EuDA for the EU Institutions to react effectively.

[6] See "*The Silk Road Trap: How China's Trade Ambitions challenge Europe*", 2019, Prof. Jonathan Holslag.

2 Unfair competition practices and issues inside the EU

2.1 Reciprocity in Market Access for Construction Services

2.1.1 The Agreement on Government Procurement (GPA)

In the 21st century, **public procurement** is arguably the **largest trade sector sheltered from multilateral trade rules**. It is not covered by any multilateral WTO discipline and it is specifically exempted from the WTO obligation to treat foreign and domestic companies equally. The most important international agreement related to public procurement is the **WTO Agreement on Government Procurement (GPA)**, which establishes a set of rules governing the procurement activities of its signatories and provides for market access opportunities. However, the GPA is not mandatory for all the 153 WTO Members but **extends the market access benefits provided by virtue of its national treatment clause only to the Agreement's Parties**.

In terms of scope, it is important to emphasise that the GPA has never provided, or even been envisioned to provide, all-encompassing, universal coverage commitments. In fact, the GPA limits the scope of application of its non-discrimination provisions to "covered procurement" – i.e., purchases of goods and services by governments that are reflected in the various Parties' "coverage" or market access schedules. Hence, there is **no standard or "one-size-fits-all" access to procurement markets of contracting partners**, but rather there are **reciprocal levels of market liberalisation** between the GPA parties.

Regrettably, there has been little to **no progress in widening the GPA membership over the past 25 years**. With the exception of the 13 new EU Member States having accessed the EU since 2004, and thus have become automatic members of the GPA, only seven new signatories with comparably small government procurement markets have signed up to the global government procurement treaty during the first years of the new millennium. By contrast, the BRIC countries (Brazil, Russia, India and, most notably, China), which all belong to the Top 10 global construction markets, still remain outside the ambit of the GPA.

2.1.2 The GPA and the principle of Reciprocity

One of the basic characteristics of the GPA is the principle of reciprocity, i.e. the Parties to the GPA have agreed to insert **significant "reciprocity clauses", both sector- and country-specific, as well as negotiated "notes"** that limit the application of the non-discrimination principle contained in the Agreement in important ways. From the outset, the EU has strictly applied the principle of reciprocity, for instance, the EU has stated in its General Notes and Derogations from the Provisions of Article III of Appendix 1 of the GPA under No.3: *"Until such time as the EC has accepted that the* ***Parties concerned provide access for EC suppliers and service providers to their own markets****, the* ***EC will not extend the benefits of this Agreement*** *to suppliers and service providers of…"* [our emphasis] several other GPA signatories (Document WT/Let/438 dated 11 January 2003).

In March 2012, the GPA Parties completed a comprehensive revision of the Agreement, encompassing both its text and coverage (market access commitments). Under the revised GPA, the schedule of each party contains seven annexes. As regards construction services, the **EU submitted an official note in Annex 6** (Document WT/Let/1050 dated 15 July 2015): *"Procurement by procuring entities covered under Annexes 1, 2 and 3 of any of the construction services covered under this Annex is a covered procurement in regard of a particular Party's provider of service* ***only to the extent that such Party has covered that service under its Annex 6****"* [our emphasis].

2.1.3 The GPA and China

In terms of allowing market access to government procurement markets, the PR China is a particularly striking example of protectionist behaviour. In **China, foreign construction companies** are **prohibited by law from participating in all public tenders** in the construction sector, whilst so-called foreign companies registered as "wholly-foreign owned enterprises" are only allowed to take part in tenders that are financed by non-Chinese authorities, i.e. foreign investors and multilateral institutions. By contrast, participation in the domestically financed government procurement market for foreign construction companies is possible for foreign firms only in the form of Sino-Foreign Joint Ventures, which are subject to a ***de facto*** **discriminatory qualification regime** that puts them at a disadvantage compared to domestic companies. This has resulted in a downward trend concerning the market share of foreign construction companies in the PR China, shrinking from 6 percent before the Chinese accession to the WTO to less than 1 percent today (see EIC Position Paper dated July 2006, http://www.eic-federation.eu/media/uploads/attachment/eic_document_pp_0028_1.pdf).

The European construction industry would therefore welcome an accession of China to the GPA on equal terms with the current level of market access commitments. The China has submitted since the year 2001 six GPA accession offers, but still does not meet the expectations of GPA signatories. The **latest Chinese GPA offer dated December 2014 is still limited** to the procurement of goods, works and services conducted with fiscal funds by State-organs, public institutions and social organisations (approximately 10% of the market). By contrast, it leaves out the procurement of large infrastructure and public utility projects, e.g. power generation and supply, sewage, water supply and public transportation (approximately 90% of the market) completely.

2.1.4 Conclusion on Reciprocity

FIEC, EIC and EuDA believe that Chinese State-owned Enterprises and their subsidiaries should not be allowed to compete for EU-financed public tenders within the EU as long as European contractors are legally prevented from bidding for domestically financed projects in China.

In any case, **FIEC, EIC and EuDA hold the firm opinion that, if the principle of reciprocity governs the relationship between GPA signatories, then *a fortiori* the principle must also apply between the EU and non-GPA members.** Hence, any contracting authority or entity as well as any EU Member State may, under the current "*acquis communautaire*", invoke the principle of reciprocity to decide autonomously not to accept foreign bidders' participation in its tenders when those are not covered by EU commitments under GPA or other international trade agreements. Whilst there is no corresponding obligation and Member States wishing to do so may waive such right, **FIEC, EIC and EuDA oppose the legal assumption promulgated by the European Commission that the European Government Procurement market is generally open to international bidders**.

We are therefore opposed to the current version of the proposed EU Regulation for an International Procurement Instrument (IPI) which intends to erase the possibility for contracting authorities/entities in EU Member States to exclude foreign bidders from third countries (Art. 1 no 5), which have closed their government procurement market for European companies, from their tenders and would therefore weaken (or even abandon) the principle of reciprocity, which is well-established in international trade relations and in particular in the field of government procurement. The International Procurement Instrument (IPI), as currently drafted, will not help with opening third country procurement markets for European companies, but open the European procurement market completely for third country bidders. This is why **we advocate for a robust, ambitious and comprehensive instrument that writes the principle of reciprocity enshrined in the GPA into the IPI Regulation.** What has been proposed so far does not meet these criteria and our expectations.

2.2 Internal EU Market under Threat

The fact that all recent spectacular successes of Chinese construction State-owned Enterprises in public tenders the EU Internal Market are based on unfair competition and abnormally low tenders (surprisingly, none recognised as such by contracting authorities and courts concerned), indicates the **need for a European strategy for defending the EU Internal Markets**, the "*acquis communautaire*" and fundamental principles of the EU.

Sadly enough, the Internal Market has to be protected against its own participants who award such contracts for whatever reason to tenders which should have been rejected for non-respect of EU law. This also means that the EU leaves too many loopholes which can be and are exploited for achieving the intended result, namely the award of (EU-financed) construction contracts to Chinese State-owned Enterprises in consideration for promises of further investment.

2.2.1 Abnormally Low Tender (ALT)

Article 69 of the EU Procurement Directive 2014 (Directive 2014/24/EU) stipulates that contracting authorities may **reject a tender** where the **evidence supplied does not satisfactorily account for the low level of price or costs proposed**, taking into account various criteria. Contracting authorities shall reject the tender, where they have established that the tender is abnormally low because it does not comply with applicable obligations in the fields of environmental, social and labour law established by Union law, national law, collective agreements or by certain international environmental, social and labour law.

The main issue with **abnormally low tenders** is that there is **no definition in the EU legislation**, nor is there a clarifying ruling from the Court of Justice. A tender's price can be considered abnormally low when it is significantly lower than most of or the average of all tenders in the same procurement procedure.

There is unfortunately no undebatable threshold or mechanism to trigger the obligation for a contracting authority to check whether a particularly low offer is an ALT or just a good offer. Therefore, not raising the question whether a tender "appears to be" abnormally low, as the Directive says, becomes the easier option selected by many authorities in the situation. This **mandatory "check-triggering"** should be done in a way that method and results can be presented to and reviewed by courts, if necessary, for instance as recommended by the World Bank. In general, awarding to ALT tends to become, in the end, very expensive for the contracting authority and is therefore economically uninteresting in the medium and long run.

In line with **Article 69 paragraph 4**, where a contracting authority establishes that a tender is abnormally low because the **tenderer has obtained State aid**, the **tender may be rejected on that ground alone** after consultation with the tenderer where the latter is unable to prove, within a sufficient time limit fixed by the contracting authority, that the aid in question was compatible with the internal market within the meaning of **Article 107 TFEU**.

To improve a level playing field in Europe, **EU State Aid Regulations should be applicable to all companies operating in the EU and delivering products and services to the EU**, regardless of the origin of the State subsidies they benefit from. One way forward, for instance, would be that prior to award, **any company, whether EU or third country**, should produce the evidence proving that their tenders/ prices are **free from any form of State subsidy considered illegal under EU law (including under EU State Aid Regulations)**.

2.2.2 Most Economically Advantageous Tender (MEAT)

According to Article 67 paragraphs 1 and 2 of the EU Procurement Directive 2014 (Directive 2014/24/EU), without prejudice to national laws, regulations or administrative provisions concerning the price of certain supplies or the remuneration of certain services, contracting authorities shall base the award of public contracts on the most economically advantageous tender. The most economically advantageous tender from the point of view of the contracting authority shall be identified on the basis of the price or cost, using a cost-effectiveness approach, such as life-cycle costing in accordance with Article 68, and may include the best price-quality ratio, which shall be assessed on the basis of criteria, including qualitative, environmental and/or social aspects, linked to the subject-matter of the public contract in question. In this respect, the **Most Economically Advantageous Tender (MEAT)** is a method of assessment to support public authorities in their selection procedure for public procurement. It was part of a new public procurement package adopted in 2014 by Parliament and the Council. This new package aimed at, amongst others, ensuring that **greater consideration** is given to **social, environmental and innovation criteria other than price alone** by the contracting authorities in their award decision.

In order to ensure the best value for money (rather than the lowest price), the legislation lists 'alternative' criteria:

- quality;
- price or life-cycle costs;
- technical merit (of the work, goods or service, e.g. for construction: proposed staff, equipment, construction method and planning, technical characteristics, etc.);
- aesthetic and functional characteristics;
- accessibility;
- social characteristics;
- environmental characteristics;
- innovative characteristics;
- after-sales service and technical assistance (technical compatibility with other equipment, availability of service and spare parts, operating costs, maintenance costs, etc.);
- delivery conditions such as delivery date, process and period.

Each criterion used must be given a relative weighting, which must be set out in the tender documents. Alternatively, they can be listed in descending order of importance.

However, as long as price alone is considered as one of the forms of MEAT, there is no real incentive to award on the best price-quality ratio (BPQR) favoured by the Directive. There is no efficient limit to abuse.

2.3 Trade Defence Instruments for Services

With a share of over 65% in the world's GDP and still growing, services have become and will continue to be an essential and vital part of the EU's economy. Services also represent a substantial part of EU's exports. It is therefore surprising that, contrary to goods, there are no mechanisms at Member State level, at EU level or at WTO level to effectively tackle and stop unfair trade practices.

"***Unfair competition practices are like coastal erosion****: markets are eroded and lost at a steady pace. Left untackled in the long term, these practices can wear out even the most resilient of companies*."

This is why the European Union has developed counter-schemes aiming at reducing competition distortions on global markets and reinforcing a level playing field. **Anti-dumping and State Aid Regulations** are among these EU level playing field measures. However, **both of these measures have limitations** that in today's context of the economic rise of China, seriously affect the European industries.

Multilateral and **EU Anti-Dumping Regulations only apply to Goods**, leaving the **Services sectors outside the scope of any Trade Defence Instrument**. As for the **State Aid Regulations**, they **do not apply to non-EU companies**, even if they provide heavily subsidised services inside the EU territory.

FIEC, EIC and EuDA hold that it is high time to develop such instruments in the EU to prevent that unfair practices keep damaging the European industry inside its own market and outside when EU funding is used and have recently submitted a "Plan of Action on Protecting the EU-Services Industry" to the highest level of the European Commission..

2.3.1 Legal Framework

Even if no EU commitments are made under the WTO/internationally, the EU can act because it has exclusive competence over the **common commercial policy** – international trade (Treaty on the Functioning of the European Union (TFEU) Article 2(1), 3 and 207).

Meaning the EU is the only one to decide or/and act on issues unless it's explicitly prohibited or stipulated as otherwise.

TFEU Article 2(1): When the Treaties confer on the Union exclusive competence in a specific area, only the Union may legislate and adopt legally binding acts, the Member States being able to do so themselves only if so empowered by the Union or for the implementation of acts of the Union.

TFEU Article 3:

1. *The Union shall have exclusive competence in the following areas:*
   (a) customs union;
   (b) the establishing of the competition rules necessary for the functioning of the internal market;
   (c) monetary policy for the Member States whose currency is the euro;
   (d) the conservation of marine biological resources under the common fisheries policy;
   (e) common commercial policy.
2. ***The Union shall also have exclusive competence for the conclusion of an international agreement*** *when its conclusion is provided for in a legislative act of the Union or is necessary to enable the Union to exercise its internal competence, or insofar as its conclusion may affect common rules or alter their scope.*

TFEU Article 207:

3. *The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy* ***and measures to protect trade such as those to be taken in the event of dumping or subsidies****. The common commercial policy shall be conducted in the context of the principles and objectives of the Union's external action.*

In a way these exclusive powers and incorporation of EU law could be read as the EU being/acting like a sovereign body, in the sense that the EU is the only one to decide or/and act on issues unless it's explicitly prohibited or stipulated as otherwise. The EU has the first and final say over a broad range of issues (falling within its competences). European institutions have the power to override national authorities over policies that are explicitly conferred to the Union or been defined as matters of shared competence between the EU and the Member States.

2.3.2 Anti-Dumping Regulation in the EU

The dumping of services is a typical example of unfair trade practices and can be compared to a commercial attack on a selected market, aiming at temporarily damaging or permanently eliminating competitors to establish and secure a stable market share in this market. This could ultimately lead to de facto monopolies or oligopolies for entire sectors in certain countries, exposed to risks of abuse of dominant position and extortionary prices.

The **EU Anti-Dumping Regulation refers to the WTO legislation** and **only covers the dumping of the price of goods**. This regulation requires proof of dumping as well as evidence of injury to the industry (including threat of injury). With regard to dumping of the price of services, the following vocabulary could be defined as **dumping** occurs when "*the export/import price is lower than the normal value*". The **normal value** of a service can be defined as the "*value of the service sold on the exporter's domestic market for domestic consumption*". The main difficulty is to determine with a fair and transparent methodology the **export price** (*ex-company price of services destined for export*).

Because of the absence of such a legislation at WTO level for services, there is also no such legislation at EU level. Moreover, it has to be noted that China's trade arsenal has evolved far beyond just price dumping and has been further refined with tied financing schemes, mega-package industrial and political deals (combining investments by China with the development of a variety of infrastructures) to close down markets to non-Chinese competition.

There is a **clear legislative gap with regard to tackling unfair trade practices with services**. It is important to equip the EU with instruments that will allow the EU to obtain the information/evidence and counteract with for instance as countervailing duties.

2.3.3 Anti-Subsidies vs State Aid Regulations in the EU

Governments intervene on markets as regulators and fiscal authorities, setting and enforcing the general rules of "*unhindered and fair competition*", but they can also act as market makers, buyers and suppliers. These interventions impact on the functioning of these markets. The taxes and subsidies governments choose to impose change the costs of the concerned businesses and influence the decision making in those businesses. Financial support provided by governments to companies is impacting competition in their domestic and in their export markets. This public support can take many forms, incl. State subsidies and tied financing schemes.

The EU has implemented a 'sanitisation' of its Member States support to their industries by imposing strict State Aid Regulations, however these regulations fail to address the State subsidies provided by non-EU public administrations to companies operating in Europe.

The definition of State aid is quite broad: it is defined as an **advantage** in any form whatsoever conferred on a **selective basis to undertakings** by national public authorities. (excluding subsidies granted to individuals or general measures open to all enterprises).

State aid can affect competition both negatively or positively. Indeed, despite the general prohibition of State aid, in some circumstances government interventions are necessary for a well-functioning and equitable economy. Therefore, the Treaty leaves room for a number of **policy objectives for which State aid can be considered compatible**. The legislation stipulates these **exemptions**.

These regulations have progressively restricted State aid from EU Member States, allowing for less and less distorted competition distortions due to EU Member States' subsidies. Positive EU State aid is typically used to address: market failures (e.g. Maritime Guidelines) and cyclical difficulties (e.g. banks in 2008) or achieve wider social or economic objectives (e.g. regional development, economic stimulation).

Today, more and more competition distortions are caused by third countries' subsidisation of their national companies operating in the EU Internal Market. Indeed, in the case of non-EU State-owned Enterprises (SoEs) it is practically always the case that an abnormally low tender (see 2.1.1 above) is, among others, the result of illegal State aid.

There is an argumentation that EU State aid rules cannot be applied to third country enterprises. However, it is neither convincing nor acceptable, as such illegal State aid directly negatively impacts the procedures and results of EU public procurement. These practices are certainly not less damaging to fair competition in the EU Internal Market because they emanate from third countries. On the contrary, they even create in the EU Single Market a **reverse discrimination** that favours the bidders benefitting from non-EU State aid to the detriment of EU bidders fully compliant with the State Aid Regulations.

Therefore, to improve a level playing field in Europe, EU State Aid Regulations should be applicable to all companies operating in the EU and delivering products and services to the EU, regardless of the origin of the State subsidies they benefit from. One way forward, for instance, would be that prior to award, any company, whether EU or third country, should produce the evidence proving that their tenders/ prices are **free from any form of State subsidy considered illegal under EU law (including under EU State Aid Regulations)**.

In the particular case of non-EU State-owned Enterprises, there are many financial flows of public money crossing from one entity to another, especially with the Chinese State-owned Enterprises fully supported by the Chinese State-owned Banks under full control of Beijing. Unless there is full access to the detail on these flows, it is difficult to assess whether prices are being dumped or whether there is (illegal) State aid.

It is therefore advisable to reverse the burden of proof and request that, to access and operate in the EU territory, such State-owned Enterprises need to prove that they effectively apply Market Economy Principles, that their prices are not dumped and that they are not subsidised. In fact, a mandatory **State Aid Test** should be established to provide the authorities with the necessary and relevant information to confirm the qualification or disqualification from a public procurement tender.

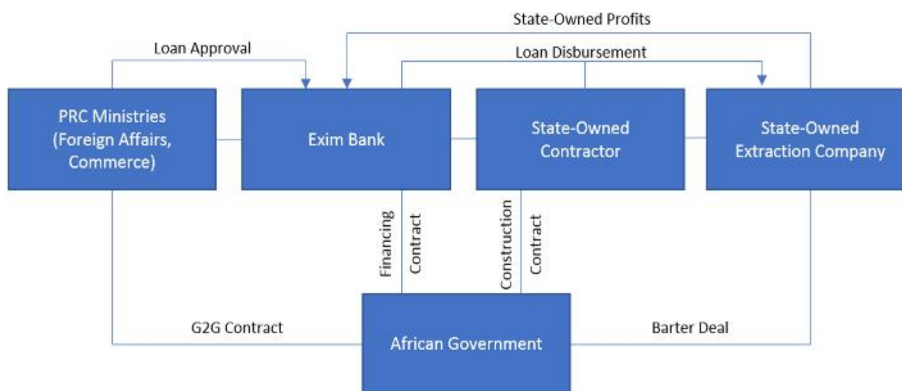
3 Unfair competition practices and issues outside the EU

3.1 Chinese Tied Financing Government-to-Government Infrastructure Deals

Emerging in 1999, the "Going Global" strategy sought to bid farewell to the Mao-era mindset of self-reliance, urging Chinese firms to take advantage of booming world trade to invest in global markets. The first years of "Going Global" coincided with China's 2001 admission to the WTO. From the outset, the "Going Global" strategy was about **nurturing Chinese "dragon heads"** (national champions) to become globally competitive multinational firms. The vast expansion of Chinese State-owned companies in third markets in the last decade was facilitated a sophisticated **State-coordinated subsidy programme** in combination with **exclusive targeted political support by the Chinese government and the Chinese policy banks**, especially China Eximbank.

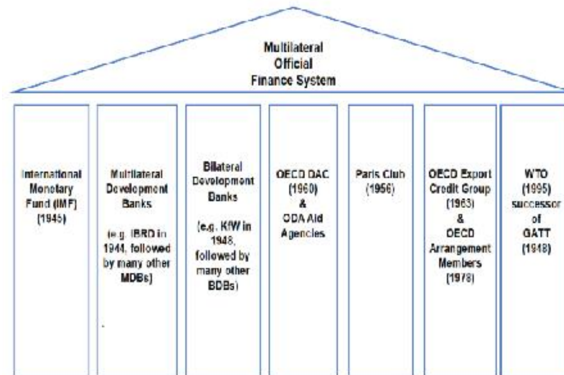
China's State-coordinated engagement in third markets is most obvious in headline-grabbing **tied financing Government-to-Government ("G2G") infrastructure deals** in developing countries, which **often comprises a barter component**. As the graph below illustrates, the Chinese government directly or indirectly intervenes in every step of the model: its Ministries negotiate package deals with governments and are in charge of approving project investment. Partner governments conclude the financing contracts of "G2G" package deals with China Eximbank, while construction and/or extraction contracts and licenses are exclusively negotiated with China's State-owned Enterprises (SoEs) under the supervision of the respective Chinese Ministries. After signing, China Eximbank disburses loans directly to the SoEs, which in turn revert their profits to the bank, allowing for future direct contracting. The model of a "G2G" contract regularly includes tax, tariff and visa exemption, reducing the costs of imported labour, equipment and material. The financing agreement sets the rules of procurement to ensure an execution by Chinese companies via direct contracting and enables a fast mobilisation of funding. The construction contract allows companies to implement their own standards and rules thus reducing compliance costs, while the Barter Deal grants preferential licensing, resource discounts and tax exemptions.

Contrary to the common practice of multilateral and bilateral development banks, which commission comprehensive feasibility and bankability studies before any project approval and disbursement of funds) this process may take several years), the Chinese project cycle does not require thorough project planning and design. Upon initiation by an African government and/or a Chinese state-owned enterprise, G2G contracts get signed within a few months or even weeks, effectuating the disbursement of funds by one of the Chinese policy banks. The contractor to execute the project is quickly established via internal competition for which only Chinese bidders are eligible; construction works can therefore be completed without bureaucratic supervision or compliance issue, thereby reducing the project delivery time substantially .



3.2 Deviation from Multilateral Rules on Development and Export Finance

This above-mentioned model of Tied Financing "G2G" Infrastructure Deals is facilitated by **China's reluctance to adhere to the multilateral financial architecture** displayed in the graph below**.** The global framework includes detailed regulations for development finance, official export credits, financial and technical assistance for countries in debt distress, and debt rescheduling for developing countries to major creditor countries on a multilateral basis rooting in the Paris Club.



7 Pillars of the Multilateral Official Finance System (Mudde, 2018)

Chinese loans to developing countries **do not meet the minimum concessionality levels that the OECD Development Assistance Committee (DAC) applies to tied financing**, which are 50% for Least Developing Countries and 35% for other countries. China would have to use substantial higher subsidy amounts to meet international aid requirements. China continues to ignore the multilateral consensus on export and development finance and, unlike OECD countries, does not yet make a clear distinction between "Official Development Assistance" (ODA) and officially supported export credits. **China's financial loans are highly intransparent** as they do not adhere to OECD DAC.

China's export credit practices include:

- **Minimum risk or market-based premiums** for officially supported export credits adopted by the OECD to comply with WTO regulations **do not apply** to China. China can easily undercut pricing from OECD ECAs and create competitive advantages for Chinese (construction) companies.
- **Minimum interest rates** for officially supported export credits do not apply to Chinese official finance. Neither do relevant OECD minimum interest rates to safeguard the WTO obligation – so-called Commercial Interest Reference Rates (CIRRs).
- **Terms and conditions** of export credits regarding the repayment profile, maximum credit periods, maximum grace periods, maximum support for local costs and minimum down payments (15%) **do not apply** to China.
- China is **not a member of the OECD DAC**. Hence, its 'development loans' lack transparency and are not in line with ODA standards and practices on concessionality.

FIEC, EIC and EuDA call upon the EU Institutions and EU Member States to create a level playing field vis-à-vis China with regard to all obligations determined by the OECD Arrangement on Officially Supported Export Credits. The Arrangement, which was initially created in the 1970s, remains the only detailed international rulebook on officially supported export credits and encourages competition among exporters based on the quality and price of goods and services rather than on the most favourable officially supported financial terms and conditions. Hence, China should be convinced to at least apply the minimum terms and conditions of the so-called "OECD Consensus" for its overseas financing activities in third markets. Furthermore, China should become a member of the "Paris Club" and cease to negotiate debt re-scheduling agreements on a bilateral basis as well as commit to the OECD's environmental, ethical and social due diligence rules in connection with export finance and export credits.

Given that Chinese State-owned Enterprises benefit most from multilaterally or bilaterally financed Official Development Assistance in the infrastructure sector, **China must sign up to all decisions, recommendations and guidelines of the OECD Development Assistance Committee, including debt sustainability, and to also comply with the minimum concessionality levels with respect to tied financing.**

At present, Chinese development loans do not meet the minimum concessionality levels that the OECD DAC applies to tied financing – 50% for Least Developing Countries and 35% for other countries –, meaning that China would have to use substantially higher subsidy amounts to meet international aid requirements. Chinese development loans are a serious threat for debt sustainability in developing countries. To top things off, China asks countries that wish to qualify for a concessional loan to grant some kind of preferential treatment to the project such as: tax-free repatriation of the payments on the loan; relief on import tariffs for inputs; lower income tax.

As long as China does not follow the same official financing rules and practices as its OECD counterparts, the EU Institutions and Member States should declare Chinese companies ineligible for participation in infrastructure tenders financed from EU Official Development Assistance, especially if such companies are State-owned. The EU Institutions and Member States should only untie European Official Development Assistance to other OECD and non-OECD countries on a reciprocal basis. Reciprocity should be fully transparent and verifiable, and it must be ascertained that untied financing is not de facto tied.

The EU and its Member States should also consider creating its own strong European financial institution that can provide long-term credits to the European private sector for international projects. Unlike the U.S., China, Japan, Korea and Turkey, the EU does not have a strong "EU Exim Bank" which can support and improve the international competitiveness of the European industry, in particular in the field of infrastructure.

3.3 Abnormally Low Tenders on EIB-financed infrastructure tenders outside the EU

Whereas the majority of lending by the European Investment Bank (EIB) is attributed to promoters in the EU countries (about 90 percent of the total volume), EIB lending outside Europe is based either on a mandate from the European Union, with an EU Guarantee under Decision No 466/2014/EU (the so-called **External Lending Mandate or "ELM"**), or at its own risk under dedicated facilities managed by the EIB. The External Lending Mandate (ELM) sets out the guidelines and priorities for the bank when lending outside of the EU, except for ACP countries, where the bank operates under the Cotonou agreement. The current ELM, with a fixed ceiling of €27 billion, came into force in July 2014. Its purpose is to provide an EU guarantee to the EIB against losses under financing operations signed over the period 2014-2020 in support of investment projects (loans, loan guarantees and debt capital market instruments) in eligible countries outside the EU. In its external lending operations, the **EIB focuses on vital infrastructure and private sector development** in line with the political goals defined in the EU Agenda for Change and in the Sustainable Development Goals.

EIB Borrowers outside the EU usually select the winning bidder for their infrastructure projects based on the **lowest price** and, as a consequence, have awarded infrastructure projects financed or co-financed with EIB funds to Chinese State-owned Enterprises, e.g. in the context of the EU-Africa Trust Fund. The fact that bid prices offered by Chinese contractors on projects financed by the EIB and other Multilateral Development Banks usually lie below the direct costs indicates that **high profits generated via projects under tied Chinese financing agreements** described above are **"re-invested" to distort competition in international open tender**ing. As a consequence, Chinese contractors gained ground in international open competitive tenders while being cross-financed through subsidies, supported by high returns on G2G contracts. In this context, there have been reports of bidding practices that undermine conventional bidding standards: Several Chinese companies participate in the bidding procedure with differently priced bids. After the closest bid has won, the winning company contracts its Chinese competitors for the execution of project works. This type of behaviour leads to a heavy distortion of competition and to project cost explosion via price undercutting.

The EIB Guide to Procurement stipulates that infrastructure tender evaluations may be based not only on the lowest price of the compliant and technically responsive tender but also on the Most Economically Advantageous Tender (MEAT; see above 2.2.2.), applying several criteria adapted to the contract in question. In practice, however, contracting authorities or "promoters" rarely use their option to purchase infrastructure services on a Value-for-Money basis, but choose the lowest price. This **widespread ignorance towards the MEAT option** can be partly explained by the fact that the EIB Procurement Guide does not give any further advice on how to apply rated-type evaluation criteria. Contrary to the EU Procurement Directives, the **EIB Guide does not comprise a reference to "Abnormally Low Tenders"**.

FIEC, EIC and EuDA hold that the EIB Procurement Guide should be updated as regards the financing of EIB operations outside the EU and should be brought in line with the EU Procurement Directive 2014. The EIB Guide should introduce a provision which authorises the promoter to reject an abnormally low offer if, after a detailed price analysis of its tender price in relation to the contract, scope, proposed methodology, schedule, allocation of risks and responsibilities, the tenderer fails to demonstrate its capability to deliver the contract for the offered price.

In addition, the EIB should incorporate in its Procurement Policies safeguards similar to those in the World Bank's Standard Procurement Documents in relation to Environmental, Social, Health and Safety (ESHS). Last but not least, the EIB Guide should comprise the option for the promoter to include additional sustainability requirements in the tender procedure if they are applied in ways that are consistent with the EIB's core procurement principles.

3.4 Reconsider EC infrastructure funding strategies towards China (BRI)

The EU and China are currently discussing the potential to **further connect Europe and Asia** in the context of the EU-China Connectivity Platform. The EU and China look at ways to create synergies between the EU's approach to connectivity, including the Trans-European Transport Network, and China's Belt and Road Initiative. Meanwhile, the EU and China have reached an agreement under the Connectivity Platform on the Terms of Reference for a **Joint Study** to identify the most sustainable railways-based transport corridors between Europe and China.

Whilst the EU has negotiated with China in this context a commitment to openness, transparency and a level playing field in the area of infrastructure connectivity, as well as mutually beneficial implementation of the EU-China Connectivity Platform projects, recent analysis suggests that these principles are not guaranteed under bilateral initiatives. According to a database established by a Washington-based think-tank, the Center for Strategic and International Studies (CSIS), *"...**out of all contractors participating in Chinese-funded projects within the Reconnecting Asia database, 89 percent are Chinese companies**, 7.6 percent are local companies (companies headquartered in the same country where the project was taking place), and 3.4 percent are foreign companies (non-Chinese companies from a country other than the one where the project was taking place). In comparison, out of the contractors participating in projects funded by the multilateral development banks, 29 percent are Chinese, 40.8 percent are local, and 30.2 percent are foreign"....*[7] This discrepancy challenges the rhetoric that Beijing has used to promote its "Belt and Road Initiative" (BRI) which seeks to build infrastructure to win friends in some 70 countries".

Against that background, FIEC, EIC and EuDA call upon the EU to reconsider the EC infrastructure funding strategies towards China, and in particular towards the Belt and Road Initiative, and to switch EC investments to the Sub-Saharan African, Mediterranean and Balkan areas also to reduce immigration.

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[7] https://www.csis.org/analysis/chinas-belt-and-road-initiative-five-years-later-0

4 Conclusions and Recommendations

In over 20 years, China has become the 2nd biggest economy in the world and the world's workshop as well as the largest construction market in the world, ahead of the EU and the United States. To achieve such results, China developed an economic model of asymmetric relations and unbalanced partnerships, established and controlled through a comprehensive network of State-owned Enterprises, capable of providing cheap financing, dumped prices and mega-package economic and political deals. In this asymmetric relations model, European countries overall lost over **1.4 trillion euros** to China from 2008 to 2018. China's ambitions are threatening EU industries, including construction and dredging. China's overall economic policy objective to achieve global oligopoly or monopoly should be challenged.

- ensure that the general trade principle of "**reciprocity**" is respected in practice;
- ensure that **EU funds cannot be used in the Internal Market by contractors from third countries** which reserve the use of their funds for domestic construction companies only;
- ensure that **"abnormally low tenders" are actually checked and analysed** by the contracting authorities;
- develop efficient **trade defence instruments for services**, in particular in the areas of anti-dumping and anti-subsidies;
- ensure that **Chinese State-owned Enterprises** need to prove that they apply Market Economy Principles, that their prices are not dumped and that they are not benefitting from illegal State subsidies (incl. illegal State aid);
- ensure that **EU State Aid Regulations** uniformly apply to all contractors, including third country contractors, active in the Internal Market;
- open the Chinese construction market for foreign contractors, e.g. by ensuring that **China becomes a GPA signatory on equal terms** with all other GPA participants.
- ensure that the European construction and dredging industries can rely on a **strong European export and project finance institution** to provide long-term finance for construction projects executed by European contractors in third countries, as do our major third country competitors;
- establish, in practice, a real level playing field with China as regards to all **OECD Regulations in connection with State-supported export credits**;
- establish, in practice, a real level playing field with China as regards to **all decisions, recommendations and guidelines of the OECD Development Assistance Committee**;
- declare **Chinese construction companies ineligible for participation in infrastructure tenders financed from EU Official Development Assistance**, especially if such companies are **State-owned**, as long as China does not follow the same official financing rules and practices as its OECD counterparts;
- update the **EIB Procurement Guide** as regards the financing of EIB operations outside the EU and **align with the EU Procurement Directive 2014**, in particular with regard to the **"Most Economically Advantageous Tender"**;
- incorporate into the EIB Procurement Policy **safeguards** similar to those in the World Bank's Standard Procurement Documents in relation to **Environmental, Social, Health and Safety (ESHS)**;
- reconsider the **EC infrastructure funding strategies towards China**, and in particular towards the Belt and Road Initiative, and switch EC investments to the Sub-Saharan African, Mediterranean and Balkan areas also to reduce immigration.

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