ANTI-COERCION INSTRUMENT (ACI)

What is it?

The Anti-Coercion Instrument (ACI) aims to deter and counteract coercive actions by third countries. The EU Commission considers that practices by non-EU countries which seek to influence the EU and/or its member states not to take, or withdraw particular policy measures, should be defined as economic coercion. Thus, the ACI instrument aims to act against these practices by imposing countervailing measures. The measures include but are not limited to the suspension of tariff concessions, imposition of customs duties and restrictions on the importation of goods, access to EU's public procurement, and suspensions in trade in services and trade-related aspects of intellectual property rights (IPRs). As demonstrated by the EU sanctions on Russia, other non-conventional measures can also be taken.

Legal basis – Article 207 of the TFEU confirm and specify EU competencies in the scope of the common commercial policy.

Subsidiarity – As indicated in Article 3(1)(e) of the TFEU, the principle of subsidiarity does not arise. This means a member state cannot put in place a national legislation to cover economic coercion.

Proportionality – The European Commission thinks there should be proportionality in the EU's response to coercion. This proportionality might be difficult to assess due to the variety of damages included in the regulation.

Can the EU act?

While it is obvious that WTO rules have consequences for the ACI, it is equally obvious that the Commission intends to defend actions that are inconsistent with its WTO obligations under national security exceptions in Art. XXI. This is a self-declaratory process that allows for more flexibility, but it does not mean that anything can be declared as a national security exception. There will have to be established that significant coercion has occurred and that it has violated or threatened to violate the national security of the EU. Equally, many of the FTAs that the EU have signed will have consequences for the activation of the ACI against an FTA partner country. Limitations on the suspension of trade in services and IPR apply to ACI and the Updated Enforcement Regulation.

How will it work?

The Commission will establish a process for activating an ex officio investigation into possible coercion. Then the Commission will pursue diplomatic efforts to eliminate the coercive practice. Based on these consultations, the Commission will decide to propose introducing (or not) a measure against another country. The Council will decide by negative Qualified Majority Voting. Measures will terminate or be withdrawn once the coercion has ended. After termination, the Commission will evaluate the Union response measure.

What is the potential impact of ACI?

The EU's anti-dumping cases offer some insight about the volumes of trade that could be affected by the ACI. Another way to estimate the amount of trade, investment, or procurement affected by the EU's anti-coercion mechanism is to look at the existing trade measures against the EU. This is indicative as the scale of the ACI will be proportional to the coercion in a like-for-like framework.

INTERNATIONAL PROCUREMENT INSTRUMENT (IPI)

What is it?

The International Procurement Instrument (IPI) will allow the EU to, on a case-by-case basis, limit or exclude access to its public procurement markets. It will be a discretionary process, where the EU might use IPI to restrict access to its procurement market for companies from countries that apply discriminatory restrictions against EU businesses. The IPI has two types of measures: score adjustments, which are penalties that procurement authorities have to apply to a company subject to the IPI; and the exclusion of tenders from a third country and sector subject to the IPI.

Legal basis – Article 207 of the Treaty on the Functioning of the European Union.

Subsidiarity – International trade falls under the exclusive competence of the European Union. The implementation of IPI will be done by procurement authorities which are national or regional.

Proportionality – The proposal needs sufficient leverage to become an effective tool to gain market access abroad. However, lowering competition within the EU may lead to higher costs for procurement authorities.

Can the EU act?

The EU cannot implement the IPI against countries with whom it has signed international agreements to access each other's public procurement markets. This includes countries which are members of the WTO Government Procurement Agreement which covers countries like Canada, Japan, the United States, and the United Kingdom, and EU bilateral trade agreements that include relevant provisions on public procurement.

How will it work?

The European Commission will be responsible for starting an investigation in case of an alleged trade barrier against EU companies in procurement markets outside the EU. The Commission will invite the country concerned to start consultations to remedy the situation in case the existence of the trade barrier is confirmed. As a last resort, after consultations with EU member states, the Commission could apply measures restricting the access from the third country concerned to the European procurement market. As long as there is no opposition by Qualified Majority Voting from the European Council, the Commission will be able to launch IPI as an implementing act.

What is the potential impact of IPI?

There has been a steady rise in the number of protectionist measures imposed by countries on their procurement markets. The IPI aims at tackling these barriers by leveraging access to the EU own public procurement market as a negotiating tool. Countries which may be subject to IPI are China, Russia or Turkey. The implementation of IPI could lead to retaliation from these countries which could impact sectors such as railway or medical technologies where EU companies are leading suppliers to foreign procurement markets.

CARBON BORDER ADJUSTMENT MECHANISM (CBAM)

What is it?

The Carbon Border Adjustment Mechanism (CBAM) aims to ensure that the price of imported goods reflects their carbon content to help fight climate change. It will take the form of a levy on imported products. The affected products are classified in five different groups: cement electricity, fertilisers, iron and steel, and aluminium. The importers must buy CBAM allowances corresponding with the level of embedded carbon in the CBAM product. The calculated embedded carbon in a product will be based on a mathematical formula for direct emissions.

Legal basis – Articles 191-193 of the TFEU confirm and specify EU competencies in climate change.
Subsidiarity – Climate change is a trans-boundary challenge and requires EU action.
Proportionality – The proposed product coverage of CBAM is framed by the sectors and emissions covered by the EU ETS.

Can the EU act?

Other countries could file complaints at the WTO accusing CBAM of being inconsistent with WTO obligations. These complaints can be in reference to CBAM discriminating against similar products from different countries depending on the extent and quality of a country's climate actions. Moreover, countries could complain that by linking CBAM and the EU ETS, free allowance under the EU ETS may represent a subsidy that distorts international trade.

How will it work?

CBAM will take the form of a regulation for uniform and direct application and enforcement throughout the EU, but certain tasks related to implementation and enforcement will be conferred to authorities in charge of climate and customs in member states.

1. Product Coverage

The proposal lists the product codes for the covered goods, classified under: Cement, Fertilizers, Electricity, Iron and Steel, and Aluminium

2. Declaration Responsibility

Importers of CBAM goods must be authorised by a competent authority or pay a fine. CBAM declarations need to be submitted annually.

3. Declaration Methodology

The importer can either declare the calculated embedded carbon in a product or they can rely on default values supplied by the Commission

4. Final CBAM Levy

Importer will buy CBAM allowances corresponding with the level of embedded carbon in the imported CBAM product and will not have to pay twice if an amount is already paid in the country of origin

What is the potential impact of CBAM?

The amount of EU imports that could be subject to the CBAM is around €60 billion, representing 3% of EU's total imports in 2019. The EU buys CBAM goods from a variety of countries (Russia, China, UK, Turkey, Ukraine) as can be seen in the map below. The EU is one of the largest global importers of these products, and CBAM would affect 11% of global imports of these products. Goods affected by the CBAM are also used as inputs in the production of other goods produced and consumed in Europe, which would increase costs for EU importers.

EU IMPORTS OF CBAM GOODS (MILLION EUROS, 2019)

FOREIGN SUBSIDY INSTRUMENT (FSI)

What is it?

The Foreign Subsidy Instrument (FSI) aims to fill the regulatory gap in EU policy to address the distortive effects of foreign subsidies in the EU internal market. It is a legal tool based on a discretionary process which targets foreign subsidies in two key areas: mergers and acquisitions (M&As) and public procurement. It also includes a catch-all category for other market situations. The FSI will give the EU Commission the power to investigate subsidies granted by non-EU public authorities to companies which operate under the EU territory and that may have an adverse effect on the EU market. If the EU Commission decides that the foreign subsidy should be remedied and if the undertaking does not voluntarily offer commitments, the Commission shall impose redressive measures, such as reducing their market presence, refraining from certain investments or repayment of the foreign subsidy.

Legal basis – Articles 207 and 114 of the TFEU confirm and specify EU common commercial policies for the functioning of the internal market.

Subsidiarity – Since subsidies impact the internal market, Article 114 argues that measures must be at the EU level.

Proportionality – The burden is imposed on companies engaged in economic activity that receive large financial contributions. Although all foreign subsidies can be investigated.

Can the EU act?

At the multilateral level, the Foreign Subsidy Regulation is consistent with WTO rules, both the GATT and the Agreement on Subsidies and Countervailing Measures (ASCM). The limitation of the ASCM agreement is that it only covers trade in goods, and the GATS does not develop the concern on the distortive effects of subsidies in trade in services.

How will it work?

FSI will take the form of a regulation for uniform and direct application and enforcement throughout the EU. The FSI regulation considers the need to revise the instrument five years after its entry into force.

1. Preliminary Examinations

The EU Commission, either on its on initiative, or on being notified, can examine a financial contribution, to conclude if it constitutes a foreign subsidy.

2. In-depth Investigation

If there is sufficient evidence, then an in-depth investigation is initiated. At this stage, the undertaking can also offer commitments to remedy the situation.

3. Market Investigation

If there is evidence of a subsidy in a particular sector, a market investigation is initiated into the sector and the type of economic activity distorted by the subsidy.

4. Redressive Measures

If the Commission decides that the foreign subsidy should be remedied it will import redressive measures, if the undertaking does not offer committments.

What is the potential impact of FSI?

The economic sectors that are heavily impacted by foreign subsidies include semiconductors, aluminium, iron and steel, chemicals, biodiesel, electronics, and wood and paper. Across countries, China has the potential to be the most affected by the FSI. Retaliation against the FSI may arise as the EU kick-starts a more assertive industrial policy, providing subsidies to industries such as microelectronics and semiconductors.

CORPORATE SUSTAINABILITY DUE DILIGENCE (CSDD)

What is it?

The proposed Corporate Sustainability Due Diligence (CSDD) Directive aims to identify, prevent, mitigate, and end adverse human rights and environmental impacts in companies' operations, subsidiaries, and value chains. The Directive requests companies to integrate due diligence to account for actual and potential adverse human rights and environmental impacts. The Directive applies directly to large EU companies (500 employees, €150 million turnover) and non-EU companies (€150 million turnover) as well as smaller EU companies (250 employees, €40 million turnover) and non-EU companies (€40 million turnover) in high-risk sectors such as manufacturing, agriculture, and minerals. SMEs that are part of the supply chain of a larger company that needs to comply with the Directive will be impacted indirectly as they fall within the scope of the new rules. Companies will need to integrate due diligence into their business practices; identify actual or potential adverse human rights and environmental impacts; and take appropriate measures to prevent and mitigate these impacts.

Legal basis – Article 50 and Article 114 of the TFEU provide the EU with the competence to act to avoid fragmentation of the EU single market.

Subsidiarity – Member state's regulation and private sector effort are insufficient to match the scale of the challenge.

Proportionality – SMEs are excluded from the direct application of the new rules although in practice SMEs which are part of supply chains will have to comply.

Can the EU act?

The Directive is likely to be compatible with the WTO rules and the bilateral and regional trade agreements of the EU. However, the EU should design a due diligence process that is transparent and meets the highest standards of accountability. Other EU due diligence regulations have passed that test.

How will it work?

Companies, member states, national agencies and national courts will be involved in the management of the system.

1. Integration of Due Diligence

Business will need to integrate due diligence, identify adverse effects, and take measure to prevent or eliminate these effects.

2. Supervision

Member states are responsible for supervising the new rules and will be able to impose fines in case of non-compliance.

3. Directors' responsability

Company's Directors are responsible for establishing and overseeing the due diligence actions as part of their duty of care.

4. Legal actions

Victims can make a civil liability claim before national courts for damages that could have been avoided with appropriate due diligence measures.

What is the potential impact of CSDD?

The European Commission estimates that this Directive will directly impact 11,700 European companies and 4,000 non-European companies. These companies will face compliance costs and transition costs. It is estimated that EU businesses will need to spend €760 million a year and €220 million one-off costs to set up the new processes, which corresponds to €84,000 per firm during the first year. These costs will be larger in sectors with complex supply chains and may lead to retaliation from non-EU countries.

LEVEL PLAYING FIELD IN THE EU-UK TRADE AND COOPERATION AGREEMENT

What is it?

The Level Playing Field (LPF) provisions under the EU-UK Trade and Cooperation Agreement (TCA) establish rules to safeguard fair competition between EU and UK businesses. LPF is a trade policy term that refers to a set of common rules to prevent businesses in one country undercutting their rivals in the other country. The provisions commit both parties to upholding high standards of protection on labour and social standards, environmental protection, the fight against climate change – including carbon pricing – and tax transparency. It also contains principles on state aid to prevent either side from granting unfair, trade-distorting subsidies. The LPF is designed to manage the divergence of standards between the EU and the UK and pertain to future standards rather than existing ones.

Legal basis, Subsidiarity, and Proportionality – The LPF falls under the EU-UK Trade and Cooperation Agreement (TCA), which is treated as the basis.

Can the EU act?

The main criticism voiced against EU LPF provisions in general relates to enforcement. In order to trigger a LPF related dispute under the EU-UK Trade and Cooperation Agreement, the alleged breach should provide an unfair advantage to an economic operator. This means that the breach should be substantive, which reduces the likelihood that the dispute settlement procedures under an LPF provision will be triggered in the case of the EU and UK. The agreement is very detailed about processes to be followed in case of a breach.

How will it work?

LPF includes chapters on subsidies, competition policy, taxation, labour and social standards, and the environment and climate.

Labour and social standards

- Both parties commit not to lower the overall level of labour and social protection – such as fundamental rights, fair working conditions, and health, safety, and employment standards – in a way that impacts trade or investment.

Environmental standards

- Both parties commit not to lower the overall level of environmental protection – such as industrial emissions, air emissions and air quality, natural and biodiversity conservation, waste management – in a way that impacts trade or investment.

Subsidies

- The agreement provides a common set of principles as to how subsidies should be controlled, which ones should be prohibited, and the establishment of an independent authority that provides oversight.

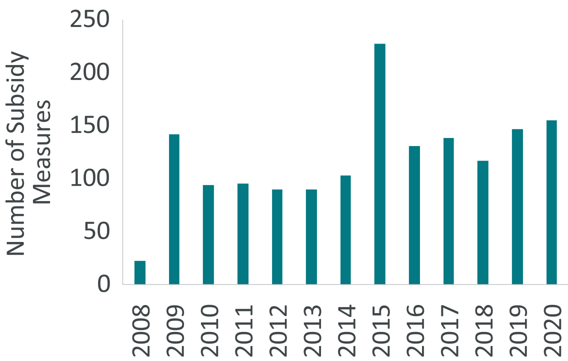
Competition and Taxation

- The agreement sets out common principles for both. However neither of the commitments are enforceable.

What is the potential impact of LPF?

The LPF is more targeted at trade in goods than services, affecting sectors such as manufacturing, automotive, minerals, and raw materials. These are significant volumes of trade as the EU and the UK economies are highly integrated. Trade in goods between the EU and the UK was €514 billion in 2019: EU exports to the UK represented €320 billion, while UK exports to the EU were €194 billion. The LPF also has the potential to play a larger role in subsidies to certain sectors (see figure below), enforceable labour standards, and carbon pricing rules.

Number of new subsidy measures implemented by the EU and the UK affecting each other (2008-2020)



UPDATED ENFORCEMENT REGULATION FOR TRADE DISPUTES (ER)

What is it?

The amendments to the Enforcement Regulation for Trade Disputes (ER) will grant the EU the right to action in response to a measure maintained by a third party, and when the dispute settlement is blocked for non-cooperative reasons by this third party. This regulation will empower the European Commission to adopt countermeasures when there is a failure to implement a panel in the WTO because of paralysis in the Appellate Body or when a similar situation arises under other international trade agreements. When the EU resorts to the Enforcement Regulation, the Commission will make a proposal for what countermeasures to take. Before the countermeasures are approved by member states, the targeted country will be consulted. However, when it comes to services and Intellectual Property Rights (IPRs), international conventions and multilateral and bilateral agreements that the EU has concluded will limit the EU's ability to act.

Legal basis – Articles 133 and 308 of the Treaty of establishing the European Community, confirm and specify competencies in the area of common commercial policy. Article 207 of the TFEU specify the competency in the ability to act in the fields of services and IPR.

Subsidiarity – The commercial policy requires action at the EU level. Yet there are service sectors that are regulated at the national or regional level.

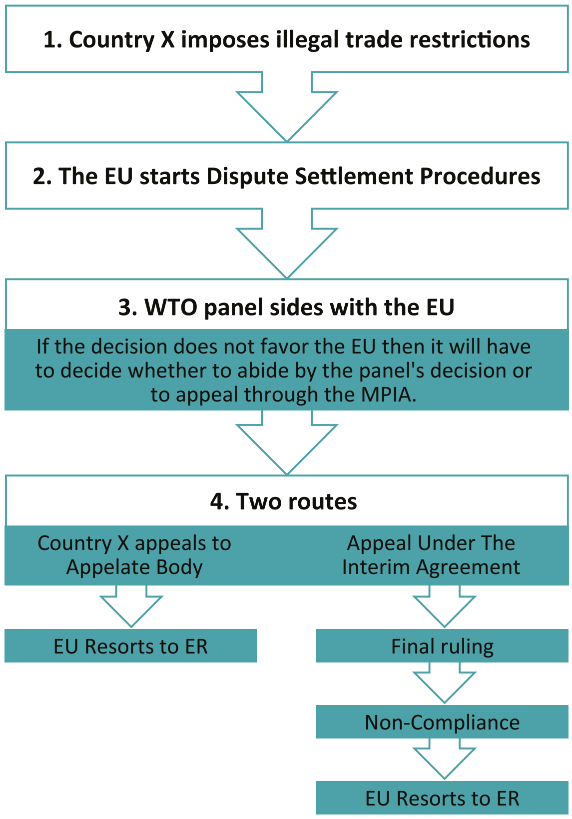
Proportionality – The EU will only act as a response to a trade dispute. The response will be similar to the harm sustained by the EU economy.

Can the EU act?

It is possible that other countries would challenge the incompatibility of the ER with the EU obligations under the WTO rules that determine the procedures for the Dispute Settlement Understanding (DSU), and that establishes the rules for redressive action. However, the ER should be seen as the last resource after a multiple-step process within the available dispute settlement mechanisms. Either within the WTO or FTAs. Undoubtedly, for the EU the greatest challenge will arise in ongoing and future cases in which the third party does not adhere to the Multiparty Interim Appeal Arbitration Agreement (MPIA). In addition, another major complexity will be inclusion of the ER as a resolution mechanism for cases involving the GATS or the TRIPS agreement.

How will it work?

The following chart exemplifies the pathway for EU regulation within the WTO framework.



What is the potential impact of the ER?

The amount of EU imports affected by the regulation will depend on two factors:

1. The number of dispute cases stuck in a gridlock at the Appellate Body and cases where there is no compliance with the ruling of the MPIA.
2. The amount of EU trade and investment impaired by the trade measures of the country against which the complaint has been lodged.

DEFORESTATION INITIATIVE

What is it?

In November 2021, the European Commission proposed a new regulation on deforestation-free products. The proposed new rules would guarantee that the products that EU citizens buy, use, and consume on the EU market do not contribute to global deforestation and forest degradation and would target six commodities: coffee, cocoa, cattle, palm oil, soy, and wood, as well as derived products including leather, oil cakes and chocolate. The proposal must be approved by the European Parliament and the Council.

Legal basis – Article 191 of the Treaty on the Functioning of the European Union.

Subsidiarity – Action at Union level would prevent adverse impact on the functioning of the internal market and on trade aspects.

Proportionality – the European Commission argues that monetised benefits would clearly offset costs.

Can the EU act?

General exceptions are foreseen in WTO legislation allowing unilateral trade restrictions under Article XX of the GATT and Article XXI of the GATS. Specific provisions aim to protect the adoption or enforcement of necessary measures to protect human, animal, plant life or health (XX.b GATT and XIV.b GATS) relating to the conservation of exhaustible natural resources (XX.g GATT). However, some of the measures that the EU could take could be considered discriminatory based on MFN, national treatment clauses or due to the imposition of additional non-tariff restrictions. As a result, any due diligence process implemented by the EU should be transparent and live up to the highest standards of accountability. If they do, measures are likely to be WTO compliant.

How will it work?

The new proposal by the European Commission would set mandatory due diligence rules for companies placing relevant commodities on the EU market and would include a benchmarking system used by the European Commission to assess countries and their level of risk of deforestation and forest degradation driven by the commodities. More specifically, the processes under the new proposed regulation would work as follows.

1. Reporting

Companies would report to national authorities that the products they place on the EU market conform with the rules.

2. Digital System

A digital system would provide authorities in member states with the relevant information about the commodities, such as geographic coordinates and country of production.

3. Benchmarking/Inspections

The benchmarking system by the European Commission would then determine the deforestation risk. In addition, the authorities in Member states will carry out inspections.

4. Penalities

Ranging from fines, confiscation of relevant commodities and products, confiscation of revenues, suspension or prohibition of economic activities, exclusion from public procurement processes.

What is the potential impact of the Deforestation Initiative?

Overall, the new rules are expected to reduce greenhouse gas emissions and biodiversity loss and are expected to have a positive impact on local communities, including indigenous peoples. The European Commission expects that producers implementing more sustainable production practices will gain share in the EU market and see increased competitiveness compared to operators sourcing from 'high-risk' countries. The related costs would result from the complexity of supply chains and setting up of related due diligence systems.