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The Comeback of the China Railway Rolling Stock Corporation and the FSR

Pablo Torres Méndez (College of Europe, Bruges) · Friday, March 15th, 2024

It is often said that one of the greatest things about watching an important character is people wondering when he is going to make his comeback. In 2019, thirteen days after the prohibition of Siemens' proposed acquisition of Alstom was published by the European Commission, Germany and France issued a public Manifesto 'for a European industrial policy fit for the 21st century'. The merger approval would have created a great European leader in rolling stock manufacturing to compete with giants such as China Railway Rolling Stock Corporation (CRRC), Russian CJSC Transmashholding or US GE Transportation, and the driving forces of the European Union questioned to what extent the competition legal framework and state aid rules enabled European undertakings to **successfully compete on the global stage**.

The intergovernmental Manifesto warned: "*Despite our best efforts, which we must pursue, there is no regulatory global level playing field. And there will not be one any time soon. This puts European companies at a massive disadvantage. When some countries heavily subsidise their own companies, how can companies operating mainly in Europe compete fairly?* ***Of course, we must continue to argue for a fairer and more effective global level playing field, but in the meantime, we need to ensure our companies can actually grow and compete***".

How to reasonably deal with those giants' (at least potential) presence in European markets?

When CRRC has become the first-ever undertaking facing an in-depth investigation under the relatively young FSR, attention must be paid to the comeback of this Chinese player.

The Commission's (first) assessment of CRRC's ability to enter European markets

According to the European Commission's assessment in Alstom/Siemens (Case M.8677 – Merger Procedure), CRRC – along with its sister company China Railway Signal & Communication (CRSC) – was not a credible competitor and entry into European markets was unlikely in the foreseeable future.

However, both merging parties considered that CRRC's expansion on the European markets was a feasible possibility because of its aims at exporting production, technology development based on European tech transfers, and, at the time, brand-new EU-compliant platforms designed in accordance with the European Railway Standard TSI. Attention was also paid to China's or

CRRC's '*ambition'* and its "*purported intention to target entry in Europe*".

Nevertheless, the European Commission's analysis concluded that CRRC was not a credible prospective bidder in the European Economic Area (EEA) and would take more than five years to become so. To reach that assessment, the Commission noted that CRRC had never won a tender in the EEA and that its position in specific markets remained marginal. Moreover, in 2019, CRRC's sales were limited in scope, and it did not have any high-speed trains in operation outside of China – projects in Mexico, Myanmar, Libya, Venezuela, and the US were cancelled.

Consequently, the Commission considered that any hypothetical potential entry of Chinese suppliers to the European markets would not be enough to overcome the significant impediment to effective competition that resulted from the merger.

While the Commission did not foresee a potential entry of CRRC into the European markets, no barriers for foreign undertakings actually impeded the access of those suppliers into Europe. On the other hand, the market investigation confirmed (in para 129) that China's insurmountable barriers made the entry of any European player into the Chinese markets impossible because of the rules under which only national undertakings were allowed to bid for rolling stock contracts, the requirement that companies be licensed to bid – under no predefined criteria, and public procurement rules requiring local production.

The Union's plan for action

Once the Siemens/Alstom merger was prohibited, changes in the legal framework were suggested. One of those immediate proposals – included in the Franco-German manifesto of February 2019 – asked for taking into more significant consideration the state control of companies and subsidies for undertakings within the framework of merger control as well as updating merger guidelines to take greater account of competition at the global level. Does this ring a bell to you?

At that time, complaints had been increasingly raised about the potential negative impact on the internal market and the level-playing field caused by third countries' subsidies. Only a year after, in 2020, the Commission presented a *White Paper on levelling the playing field as regards foreign subsidies,* addressing the types of State Aid which needed to be controlled to avoid undermining competitiveness and resulting in "*an uneven playing field in which less efficient operators grow and increase market share at the expense of more efficient operators, […] resulting in costly and often wasteful emulation and lead to subsidy races between public authorities*". The new Regulation on ensuring a level playing field had to target both acquisitions of EU companies ensuring that all companies compete on equal footing to pursue inorganic growth, and EU procurement markets characterised for being largely open to third-country bidders ensuring that EU and non-EU companies compete on equal footing in public procurement procedures in the EU.

In record time, all institutions – including the Council – agreed on the Commission's proposal and the Foreign Subsidies Regulation (FSR) was officially adopted, extending *mutatis mutandis* the application of EU State Aid rules to subsidies granted by third countries. The Regulation was effective on July 12th, 2023, with notification obligations starting five months ago – on October 12th 2023. As Luca Rubini flagged, the EU seemed to have chosen "*to follow a unilateral course of action to address real or perceived asymmetries in subsidy regulation*", while in the past, it was traditionally addressed through negotiations and the conclusion of specific trade agreements. This

was the only possible solution "*in the face of the growing economic imperialism of certain non-EU countries*" as perfectly described by Massimo Merola and Alessandro Cogoni here.

Where does the five-year time period lead us? A particularly important elephant in the room

The Commission was heavily criticised for not considering competition in the worldwide markets in Siemens/Alstom. However, an assessment was made on whether (unfair) competition from the Chinese players would be feasible in the coming years, and the conclusion was that it would actually take them more than five years to enter the European markets. Unfortunately, the Commission erred on this finding. On January 22nd, 2024, strikingly on the fifth anniversary of the merger decision, the contracting authority concerning the Bulgarian procurement procedure for the project 'Bulgaria-Sofia: Railway and tramway locomotives and rolling stock and associated parts' forwarded a notification under Article 29(1) FSR from Chinese CRRC. The (back then) unlikely possibility of CRRC submitting credible bids became a reality, and the parties' arguments came back to life. The comeback of CRRC to the central stage of the European merger control and (now) FSR legal debate is certainly twofold.

First, the merging parties at Siemens/Alstom had a point. It was argued that CRRC is advantaged by a low-cost base due to the financial contributions of its main shareholder, the Chinese state, and increasingly bidding in tenders in different areas of the globe at the time targeting the EEA in particular for expansion, which is now evident with their participation in the Bulgarian tender. While this potential competitive pressure on the identified markets may not have been sufficient to overcome the significant impediment to effective competition that the merger would have created, the question arises as to what extent the Commission was correct to underestimate the foreign threat to European companies which, sooner or later, would come true. Was a European big player needed to compete with giants such as CRRC?

Second, CRRC's participation in the Bulgarian tender is the first in-depth investigation under the Foreign Subsidies Regulation. It concerns a public procurement procedure for a project with a value of EUR 614 million consisting of the provision of twenty electric trains, the maintenance of the rolling stock for fifteen years and staff training. The Commission contends that, based on the information available and the exchanges of information, there are sufficient indications that CRRC received foreign subsidies in accordance with Article 28(1)(b) FSR. That is, it was granted financial contributions in the three years prior to notification greater than EUR 4 million per third country, under the definition laid down in Article 3 FSR. This exists where a third country provides, directly or indirectly, financial contributions conferring a benefit on an undertaking economically active in the internal market.

According to the Commission, CRRC did not provide complete information ("*Despite the request of the Commission to the Notifying Party to list all entities falling under Article 28(1)(b) FSR, the Commission notes that not all entities were listed*").

Notwithstanding this, the Commission's preliminary assessment finds that CRRC was awarded public procurement contracts of more than 7.5 billion, which conferred a benefit, and the company was not able to provide sufficient proof that those contracts were granted on competitive market conditions. Moreover, CRRC was granted government grants of 804 million as of June 30th, 2023, conferring a benefit which is specific to the undertaking. Based on these "*sufficient indications*,"

the Commission considers that those foreign subsidies are liable to improve the competitive position of CRRC in the internal market and, in doing so, "*actually or potentially negatively affect competition in the internal market*". Taking into consideration the fact that CRRC's offer is "*substantially lower than the estimated costs of the contracting authority*" and the offer of the (by coincidence, European) competitor Talgo, one of the largest Spanish manufacturers, the Commission preliminarily concludes that CRRC was granted foreign subsidies that may distort the internal market.

Will those "*sufficient indications*" be enough for the Commission to prohibit the award of the contract or to impose the redressive measures envisaged under Article 7 FSR? Is the Commission addressing the Alstom/Siemens argument of a "*foreign threat*" and a reply to its critics by scapegoating CRRC? How will the balancing test, as defined in Article 6 FSR, be applied to this specific case and for the very first time under the FSR? May the Commission accept any potential commitments offered by the undertaking, or will CRRC directly challenge the Commission's future decision before the General Court? The Commission is getting ready – DG COMP is staffing up to 40 professionals and creating a brand-new Directorate K to ensure the proper enforcement of the FSR.

Conclusion

The initiation of the first in-depth investigation under the FSR is also the story of the comeback of CRRC to the European merger control and state aid legal analysis. As was the case in 2019 with Siemens/Alstom and all those identified as potential competitors, third-party involvement in Commission proceedings will play an essential role in the final decision. This is well described by Lena Hornkohl in her paper, where she flags that third parties might be subject to requests for information, interviews and even inspections under Articles 13(3)(7), 14 and 15 FSR. This is particularly relevant for the present case, for those instances when the Commission considers that the investigated undertaking does not provide sufficient information.

Third parties – surely including Talgo, Siemens and Alstom – as recalled in the Summary Notice, are now invited to submit their comments and views in writing, not later than ten working days from the Notice's date of publication. The information that is provided will immediately allow the Commission to understand better the distortive effects of the Chinese subsidies, their potential implications on the European markets and the possible decision outcomes. While it has been demonstrated that in 2019, the Commission underestimated CRRC's capacity to enter the European markets by rejecting the merging parties' arguments, it now has the possibility to emulate China's "*insurmountable barriers*" and, therefore, foreclose the Chinese player by virtue of the fairest response: the enforcement of a non-discriminatory, objective and predefined legal toolkit.

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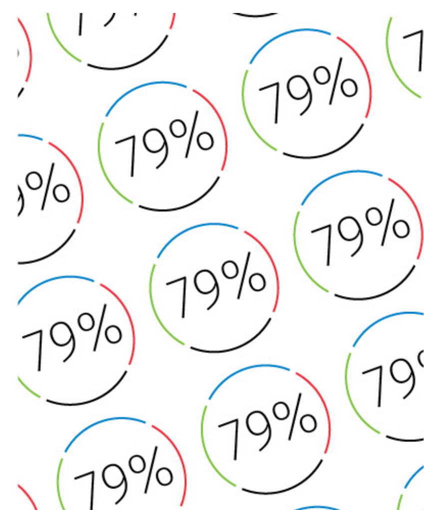

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