

C L I F F O R D
C H A N C E



TRADE IN 2023: TRENDS TO WATCH



— THOUGHT LEADERSHIP

MARCH 2023



TRADE IN 2023: TRENDS TO WATCH

Global trade was buffeted in 2022 by numerous headwinds. There is now a growing threat of fragmentation as countries onshore critical supply chains and incentivise investment amidst geopolitical and economic tensions over Russia's invasion of Ukraine and escalating tensions between the US and China over trade and domestic subsidies. In addition to macroeconomic concerns, businesses also face increased regulatory oversight from governments on issues as diverse as digital sovereignty, carbon emissions and transfer of intellectual property.

2023 is likely to be a crucial year in establishing the course of global trade policy for the coming decade, with radical changes to domestic rules on permitted state subsidies, supply chain regulations, cross-border data transfers, environmental-related tariffs and foreign investments possible in many jurisdictions. Questions also remain over the future of multilateral trade architecture, with proposals for ambitious trade agreements and WTO reform at critical junctures in the coming months. Here are seven trends for businesses and governments to consider in 2023.



Green incentives and competing subsidies

The fragmentation of the international trading system appears to be accelerating with a developing confrontation between the US and the EU on the issue of subsidies for green technology. The United States' USD 370 billion Inflation Reduction Act (IRA), effective from 2023, includes various incentives designed to reverse China-bound investment flows back to the US and support green industry in the US, especially in critical sectors such as batteries. These incentives, coupled with the energy-exporting strength of the US dollar, are making continued investment in Europe difficult for many manufacturers. EU Member States are divided as to Brussels' response, with the historic North-South divide on state intervention further complicated by Germany and France's alignment on the need to pursue their joint industrial interests over maintaining the EU's existing rigid State aid rules (between them, Germany and France account for 77% of the EUR 672 billion of EU approved state subsidies in response to Russia's invasion of Ukraine).

The European Commission's response to the Inflation Reduction Act is the EUR 250 billion Green Deal Industrial Plan (Green Plan), which is an attempt to find a balance between the US's broad industrial policies and the concerns of smaller, less wealthy Member States, although it remains to be seen if the Green Plan will be sufficient to keep green investments in the EU. The Green Plan aims to make use of existing EU support programmes (such as the RePowerEU plan to reduce dependence on Russian fossil fuels) to distribute funds for green manufacturing, while proposing only limited reforms to State aid rules. It is unclear, however, whether a partial alignment between Washington, D.C. and Brussels on industrial policy is enough to stave off the threat of an EU-initiated trade war over what it perceives are discriminatory subsidies for US manufacturers. The key elements of the IRA and the Green Plan, and potential pitfalls, include:

- **The IRA provides significant tax credits to consumers of US-manufactured green technology, including Electric Vehicles (EVs).** The IRA includes several tax incentives for end-users based on US-Mexico-Canada local content manufacturing requirements. These include a USD 7,500 "clean vehicle tax credit" for purchases of EVs containing battery components manufactured or assembled in North America and using critical minerals extracted or processed there. The WTO Agreement on Subsidies and Countervailing Measures (ASCM) (and the GATT 1994) generally prohibit the use of

subsidies that are contingent on the use of domestic content. Several foreign car manufacturers, including South Korea's Hyundai, have already committed future investment to the US in order to benefit from such subsidies. The EU, China and South Korea are all openly considering initiating disputes against the US before the WTO's Dispute Settlement Body.

- **The Green Plan focuses on a wide distribution of funding for clean tech and new green standards but is unlikely to provide for local content-based subsidies.** The Green Plan proposes to amend existing EU State aid rules to extend existing permissible subsidies (including under programmes such as RePowerEU) to a wider group of industries, as well as increasing the threshold amount of funding required for a mandatory Commission investigation. However, the proposals do not include local content requirements. This is consistent with the EU's arguments that the US Congress should allow EU components to contribute to the IRA's local content requirements. Rather than adopting potentially WTO inconsistent subsidies, the Commission hopes to adopt new EU standards to incentivise the growth of EU-based industries. These standards are likely to give a competitive advantage to EU products. There is a risk that exporters may view such regulations as WTO non-complaint where applied to certification programmes, such as EU net-zero emission requirements.
- **Much of the Green Plan's competitiveness relies on removing existing regulatory barriers.** The Green Plan includes certain proposed legal changes that could transform the regulatory landscape for many green technologies. One of the key pillars of the Green Plan is "a predictable and simplified regulatory environment", brought about by later regulations, including a Net-Zero Industry Act. This envisages fast-tracked construction permits for production facilities in any EU Member State, targeting obvious growth sectors such as carbon capture, heat pumps, solar and batteries. The Commission also wants Member States to reduce administrative burdens for investors by introducing a "one-stop-shop" for all permitting procedures, potentially resolving the myriad of national regulations faced by green technology manufacturers operating across separate Member States.
- **Both initiatives focus on supply chain security measures.** Green technology industries face particular difficulties in guaranteeing the raw materials needed to develop new products, in particular lithium for batteries. We expect to see supplementary supply chain security measures built into new EU standards, including requirements for recycling of raw materials and use of bio-substitutes for extracted minerals, as part of a follow-up 'Critical Raw Materials Act'. These types of measures tie into existing sustainability proposals, such as the EU regulatory framework for batteries, and aim to reduce costs for EU manufacturers while maintaining high quality standards. Under the IRA, US subsidies cover up to USD 45/kw hour of the production costs of batteries while also offering support for the purchase of raw materials. Half of the USD 7,500 clean vehicle tax credit is dependent on certified extraction and processing of raw materials in North America. WTO Members may seek to challenge such measures where they discriminate in favour of domestic buyers of raw materials sourced in the US.

The extent to which the US and EU approaches to interventionist industrial policies align is likely to be settled in Q2 2023 across a series of crucial EU Council summits and US-EU Trade and Technology Council meetings (where the EU is pressing for changes to the IRA that would allow EU manufacturers to benefit from the same subsidies as US competitors).

Trade tensions over China, the WTO and EU/US industrial policy

The IRA and the EU's proposed Green Plan response are just two elements of a growing economic confrontation between the US and China, one of the few areas of consistency between the Biden Administration and its predecessor.

The current US National Security Strategy, published in October 2022, terms China as a competitor and commits to competing responsibly with China, on a global basis, in the technological and economic domains. The US' allegations of intellectual property violations

by China, a key element of the Trump Administration's foreign policy, remains at the heart of US-China relations, with the National Security Strategy emphasising that, under existing Chinese trade practices, US innovators are not rewarded for their risk-taking.

2023 is likely to see rising tensions in relation to the following key trade issues:

- **Continuation of WTO non-compliant tariffs:** Despite removing Trump-era section 232 tariffs on imported steel (25%) and aluminium (10%) from allies Canada and the EU, and having four separate WTO panels rule such tariffs inconsistent with WTO obligations, the Biden Administration has maintained the same tariffs on China. US Trade Representative Katherine Tai confirmed that the US remains "committed to preserving U.S. national security by ensuring the long-term viability of our steel and aluminium industries, and we do not intend to remove the Section 232 duties." The US also took the controversial step on 26 January 2023 of appealing the four rulings to the now-defunct WTO Appellate Body, which cannot review the appeals as the US has blocked the appointment of new Appellate Body Members since 2018. This allows the US to maintain both its measures on China and its arguments on the validity of trade restrictions for national security reasons, despite a WTO panel ruling in China's favour. It also prevents China from imposing retaliatory tariffs in a manner that is WTO-compliant. This policy is likely to further harm US-China trade relations.
- **The 'Chip Wars' intensify:** The US is presently focused on advancing green technology manufacturing at home and reshoring supply chains from Asia, both policies which are likely to adversely impact China. However, it has also adopted measures which are directly aimed at preventing China from advancing its high-tech computing sector. This includes sweeping export controls in the form of the Foreign Direct Product Rule on the sale of semiconductor chips made anywhere in the world with US tools and will restrict foreign firms, including those in the EU and Taiwan, from selling their advanced microprocessor chips, chip-making equipment and software containing US technology to companies in mainland China. US measures also prevent certain Chinese firms placed on an "Entity List" from importing US technology without a special licence from the US Department of Commerce. If such firms cannot be investigated by US officials, they will remain on the Entity List indefinitely. The US has also banned US persons from supporting the development or production of chips at listed Chinese companies. YMTC, one of China's largest memory chip and 3-D NAND manufacturers, may have to exit the growing 3-D chip market as a result of the ban, causing supply chain issues for downstream manufacturers in Taiwan and elsewhere. By the end of 2022, China's chip imports were already falling by double-digit percentage points per month as a result of US measures. These measures may have unforeseen trade impacts on US allies. Advanced lithographic equipment can no longer be supplied to or produced in China. US consumer goods giants such as Apple and Tesla will also be impacted, as the cost of high-grade memory chips increases due to changed supply chains. So far, China's response has been to become more self-reliant, with President Xi Jinping promising more government intervention to "carry out indigenous and leading scientific and technological research [in order to] win the battle in key core technologies." This may only play into the hands of those demanding increased tariffs on Chinese technology imports.
- **Increased trade disputes over US and EU industrial policy:** In December 2022, China filed a rare request for dispute settlement consultations against the US over its chip export control measures. This follows a ruling in its favour in its 2019 complaint concerning the US's imposition of section 232 tariffs on Chinese steel and aluminium imports. Initiating further complaints before the WTO's Dispute Settlement Body in respect of the IRA and other US subsidies raises difficulties for China, as its domestic government support programmes are often the target of anti-dumping investigations and related WTO litigation by other Members. Recent EU statements, for example, have sought to compare the targeted subsidies of the IRA and the EU's Green Plan with so-called "massive subsidies, not only [to] the clean-tech sector but in general", provided to Chinese exports by Beijing. Chinese government rhetoric on the IRA, however, is unusually direct, stating that the IRA is causing serious damage to global

trade and investment in green industries and confirming that a formal challenge is within its right as a WTO Member. While more accustomed to being a respondent in WTO disputes, it is expected that China will initiate several complaints in the coming year should trade tensions with the US (and now the EU) continue to escalate.

The rise of European digital sovereignty

3

This year we are likely to see numerous measures aimed at increasing digital sovereignty, predominantly focused on data localisation and local content requirements for data technology service providers, particularly in the cloud computing sector. France's presidency of the EU Council for the first half of 2022 added real impetus to its ambitions to expand its domestic "Cloud de Confiance" (Trusted Cloud Strategy) across EU Member States. Together with earlier initiatives, the Trusted Cloud Strategy means that cloud service providers operating in France must deliver all aspects of their services from within the EU (including even technical support). A resulting French governmental certification programme, "SecNumCloud", is intended to ensure that public cloud services are not subject to the US Cloud Act, which requires cloud service providers, wherever based, to disclose data to US intelligence agencies unless a bilateral data agreement is in place.

In yet another example of growing Paris-Brussels alignment, the EU Commission appears to be following suit. The proposed EU Data Act is the chief element of the plans of influential Commissioner for Internal Markets, Thierry Breton, and competition chief, Margrethe Vestager, to apply the same principles of data sovereignty to the sharing of, and access to, data across all EU Member States. The Act remains under negotiation but EU Members are agreed on the fundamental issues, including the need to remove technical barriers to use of data by EU customers on different cloud service provider platforms. This requires adoption of the Act's rules on "functional equivalence", obliging service providers to maintain, for similar functionalities, a "minimum level of functionality in the environment of a new data processing service after the switching process [... meaning that] the destination service will deliver the same output at the same performance and with the same level of security, operational resilience and quality of service¹." Effectively, functional equivalence will require some form of co-operation between service providers where a customer wishes to switch its data to a new platform. Opponents of the proposed wording, including portions of the European Parliament, say that it will obstruct innovation and competition amongst service providers, as well as damaging the value of a unique platform's intellectual property. It remains to be seen whether the final form of the Act will be WTO-compliant, especially where its functional equivalence requirements for specific traded software, and differing treatment of EU and non-EU products, may constitute a breach of various WTO agreements, including the WTO Agreement on Technical Barriers to Trade.

There are further concerns that France's Trusted Cloud Strategy and its proposed EU-wide counterpart, the Cybersecurity Cloud Services scheme, could breach several EU WTO obligations, including market access, national treatment and Most-Favoured Nation commitments under the General Agreement on Trade in Services and the EU's market access commitments under the WTO Government Procurement Agreement. The SecNumCloud certification process may also be de facto discriminatory, as only a handful of firms, all French, have been certified to date. As the exporting country most likely to be impacted by French/EU measures, the US may consider initiating a WTO dispute in defence of cloud computing software and service providers. However, the US' own US GovCloud and Federal Risk and Authorisation Management programmes also aim to enforce data localisation requirements in US public contracts for cloud services.

The Act follows the passing of 2022's three major EU laws on data, the Data Governance Act, the Digital Markets Act and the Digital Services Act. A fourth technology standards proposal, the Artificial Intelligence Act (governing the development and use of AI products), is expected to be agreed in 2023. The impact of these and similar measures implemented by China and others on global data flows and trade in services will be a key issue for the technology sector in 2023.

1. Recital 72, Czech Presidency Third Compromise Text (8 December 2022)

UK-EU trade reset

The arrival of Rishi Sunak as UK Prime Minister in October 2022 appears to have coincided with a marked change in the negotiation stance of both the UK and the EU over the contentious and ongoing obstacles to implementation of the Northern Ireland Protocol (Protocol), particularly on customs arrangements and the role of the European Court of Justice (ECJ) in determining legal disputes arising from the UK's alleged failure to conduct the necessary checks on goods arriving in Northern Ireland (NI) from Great Britain (GB). As at the date of publication, London and Brussels have agreed in principle the Windsor Framework which seeks to establish a revised framework for implementing the Protocol. It is proposed that the key elements of the Windsor Framework will come into effect in October 2023, with fresh meat and dairy labelling requirements required by October 2024.

- **Green Lane/Red Lane for customs checks on NI-bound goods:** The Windsor Framework involves some changes to both EU and UK customs processes, necessitating a change to EU regulations. At its core, the Windsor Framework imposes new labelling requirements for goods shipped from GB to NI certified as for "Not for EU" consumption and shipped via the "UK Trader Scheme" certification program, requiring only one digital certificate per delivery vehicle rather than per load. This "green-lane" procedure will necessitate trade monitoring and data-sharing obligations on the part of the UK but will remove all other customs declarations. Goods destined for the Republic of Ireland market (and, by extension, the EU) will be subject to a "red lane" review, encompassing normal EU customs and sanitary and phytosanitary (SPS) controls.

The Windsor Framework includes several other changes to the original Protocol, set out in detail in the UK Government's [explanatory document](#):

- **Simplified customs rules on GB-NI trade in parcels, pets and pharmaceuticals:** No customs declarations will now be required for parcels sent from GB to consumers in NI with limited information sharing requirements imposed on parcel operators. This will be a huge boost to online shopping, as retailers will no longer have to fill out complex customs declarations. It will also allow pets to be moved into NI without need for pet passports and micro-chipping. Finally, there will be no checks on UK regulated drugs, which will be available in NI without EU regulatory labelling. This new regime will be policed by delivery companies sharing commercial data with the UK's tax authority, HMRC, within the digital data-sharing framework agreed with the EU.
- **UK tax control over NI:** One of the key difficulties in implementing the original Protocol was Articles 8 and 10's imposition of EU rules on VAT and State aid in NI. For example, the Protocol had caused concerns that Westminster could not extend its proposed freeport scheme to NI. The Windsor Framework will allow for increased UK control of VAT (including on green technology such as solar panels) and excise tax on alcohol in NI. It also affirms the tests for determining whether any UK subsidies have a genuine and material link to NI's trade with the EU, and may therefore be subject to EU State aid rules, principles that are already in place under the EU-UK Trade and Cooperation Agreement.
- **A UK veto on application of new EU rules having a significant impact on NI citizens (the "Stormont Brake"):** The amended Article 13 of the Protocol will provide the UK Government with a veto over the application of any new EU trade rules to NI where 30 Members of the Northern Ireland Assembly (from at least two political parties) issue a petition concerning a "significantly different" new rule that has a "significant impact specific to everyday life". Any EU rule subject to the Stormont Brake may only be imposed where jointly agreed by the EU and UK and any dispute as to implementation is subject to state-state arbitration rather than the jurisdiction of the ECJ. It is important to note that only parties involved in the power-sharing institutions in NI may refer an EU regulation to the UK Government for triggering the Stormont Brake. EU officials have described the procedure as "only used as a matter of last resort".
- **Acceptance of UK SPS standards for certain goods:** The Windsor Framework removes the prior block on imports of certain plants and seeds from GB into NI, where these may have posed a "high risk" to EU Members. There will now be no SPS checks on seed potatoes and trees and shrubs of 11 different plant species coming into NI, so long as imports are labelled "for use in the UK only".

- **No UK/EU dual regulatory framework:** Three years on from the UK's withdrawal from the EU, there are now several goods sold in GB that do not meet EU regulatory requirements, mainly processed meat and raw fish products. This has resulted in NI supermarkets struggling to import certain foodstuff from the rest of the UK, as they may not pass EU SPS controls where potentially destined for the EU market in Ireland. Although the "green-lane" procedure will likely reduce these difficulties, the EU refused to accept any "optionality" in importers being allowed to accept either EU or UK standards.
- **The ECJ will remain the "sole and ultimate arbiter of EU law" applicable in NI but its jurisdiction will be limited:** The question of the ECJ's role in the Protocol is one of the controversial issues for unionists in NI and the EU maintained its long-standing position on the Court's role in the Windsor Framework. However, since EU law no longer applies to "green-lane" goods (subject to UK law and UK courts), although it would govern the process by which such goods are defined, the EU anticipates that only 3% of all EU regulations now apply in NI. Further, under the new Articles 6(2) and 13, any dispute as to the operation of the Protocol may only be resolved by bilateral negotiations and arbitration. This includes disputes as to the parties' joint obligation to establish and maintain specific arrangements for the movement of goods within the UK's internal market (e.g., the "green-lane" proposal).

Finally, the Windsor Framework paves the way for negotiations for the UK to re-access EU research and collaboration programs, most importantly the EUR 96 billion Horizon Europe fund. The UK had been excluded from all EU research grants as a result of the EU's initiation of a formal dispute over the Protocol. A key issue in any negotiations are the financial terms on which the UK would re-enter the program.

Trade deals and WTO reform amidst a year of fragmentation

5

With increased industrial interventionism likely from the US and the EU, onshoring of critical technology manufacturing and a US-led strategy to disrupt China's role in global supply chains, 2023 appears to offer little hope for advocates of a more stable global trading environment. However, for those with aligned interests and a willingness to engage in compromise, this year we may see the first shoots of a return to ambitious bilateral and small-member-group trade deals. Large plurilaterals, particularly in an era of tension over industrial subsidies, are unlikely to feature, nor is a UK-US free trade agreement (politically impossible for the Biden Administration in the face of continuing Brexit-related difficulties in Northern Ireland). Potential agreements to keep an eye on include:

- **EU-Mercosur trade agreement:** A deal that has waxed and waned in popularity in recent years, both in EU Member States and major Mercosur economies such as Brazil and Argentina, sees its do-or-die moment in 2023. German Chancellor Olaf Scholz's recent trip to Argentina has added impetus to the process to create a combined market of approximately 780 million people (crucially, South American meat exports are excluded). Difficulties in closing a deal include the upcoming Argentinian elections in October 2023 and the EU's demands for commitments to protect the Amazon rainforest.
- **EU-Singapore digital trade agreement:** Following on the heels of the UK's digital trade agreement with Singapore, the EU hopes to finalise a similar deal with the commercially influential city-state, focusing on the facilitation of trade in semiconductors, data flows and digital public services. A deal with Singapore would follow similar agreements with Japan and South Korea, and lay the foundation for the EU's version of an "Asian pivot", amidst renewed efforts to negotiate market access issues with Australia and India.
- **Continuing discussions on reform of the WTO:** 2022's 12th WTO Ministerial Conference promised significant movement on various deadlocked issues by the time of the planned 13th Ministerial Conference in February 2024 (MC13) but, six months on, there is little evidence to suggest that the key issues will be resolved in time. Ongoing negotiations include: (i) efforts to obtain the necessary two-thirds approval of the WTO Membership on the Agreement on Fisheries Subsidies; (ii) finding a permanent solution

6

to the present moratorium on applying customs duties to electronic commerce transmissions; and (iii) preparing draft reform proposals to secure a fully functioning Dispute Settlement Body by MC13 (including proposals for re-establishing a working Appellate Body). WTO Director General, Ngozi Okonjo-Iweala, has already made statements implying that dispute settlement reform may not be achievable until 2025 at the earliest. The US is currently leading a third round of talks with more than 70 WTO Members on establishing a revamped dispute settlement system, including alternatives to WTO Panel arbitration, such as mediation. Although WTO Panels continue to hear complaints by Members, 24 WTO disputes are effectively in limbo and unresolved due to Members making appeals to a non-functioning Appellate Body, allowing respondent Members to maintain the complained-of measures indefinitely. Expect pressure for concrete proposals to resolve the impasse to mount by the end of 2023.

Connecting Climate Action Priorities with Supply Chain Needs

2023 will see the entry into force of a plethora of EU and Member State regulations aimed at addressing climate action, human rights and green industrialisation concerns. Many of the new regulations form part of the EU's "Fit for 55" package of proposals, intended to ensure EU policies are consistent with its stated obligation to reduce net greenhouse gas emissions by 55% by 2030. As the EU goes it alone on several ambitious projects, most notably implementation of its Carbon Border Adjustment Mechanism (CBAM) that effectively taxes imports of certain carbon-intensive industrial raw materials from outside the EU, there is a danger of regulatory divergence with the rest of the World. This could give rise to so-called "carbon clubs", whereby states join together to recognise the equivalence of their domestic emissions reduction mechanisms, but implement levies on imports of carbon-intensive products from those countries outside the club. There is also a risk that different clubs will apply differential rates. Newly effective regulations in 2023 include:

- EU Carbon Border Adjustment Mechanism:** CBAM, covered in detail in a separate Clifford Chance briefing, is expected to take effect from 1 October 2023. The measure requires that importers of certain products purchase EU carbon emission certificates in an amount equal to the price paid by EU producers of the same product under the EU's revised Emission Trading Scheme (ETS), minus any charges paid under the exporters domestic emissions programs (if any). This border levy aims to prevent so-called "carbon leakage", whereby EU producers may move production of carbon-intensive products to countries with less burdensome emission regulations, and then export the finished goods back into the EU. From 2023, importers will be obliged to report the emissions information on imports of cement, iron and steel, aluminium, fertilizers, electricity and hydrogen. A percentage of the applicable ETS carbon price will then be charged on a phased-in basis, rising from 2.5% in 2026 to 100% in 2034. The range of products covered by CBAM is expected to align with those covered by the ETS from 2030. These include refined products such as paper, acids and even emissions produced by commercial aviation when entering EU airspace. The European Parliament and Council of the EU have reached a provisional political agreement on implementation of the proposed CBAM regulation but require individual EU Member State sign-off and changes to other regulations before it can take effect. We expect the final CBAM regulation text to be of critical importance to the global manufacturing and construction sectors in 2023.
- New technical requirements for imported batteries:** The Council of the EU has agreed a draft framework for negotiations with the European Parliament to implement the Commission's proposed regulation on batteries and waste batteries. This will require manufacturers of batteries (the majority being outside the EU) to incorporate certain design features that improve the recycling of batteries at the expiry of their useful lifetime. The proposals include a mandatory "battery passport" for all batteries on the EU market (setting out all applicable sustainability and lifecycle information), as well as recycled content requirements for all new batteries. The proposals are consistent with the EU's general aims of developing a circular economy in Europe, supporting a just

transition for existing labour markets. This is likely to significantly impact imports of batteries into the EU, further incentivising a growth in EU production. Recent EV battery production facilities developed by Tesla, CATL, Northvolt, LG Chem and others stand to benefit from the anticipated regulation.

- **EU Single Market Emergency Instrument:** 2023 will see negotiations between the European Parliament, Council and Member States on the Commission's 2022 proposals to ensure the supply of strategically important goods through regulating and monitoring supply chains. The proposals include Member States having power to obtain sensitive business information from companies involved in the supply of certain critical goods, allowing the Commission to escalate a series of responses in times of crisis, which may include climate emergencies. If the Commission determines that a significant supply incident is occurring, it may require Member States to build up strategic reserves of certain goods. Intra-EU export bans will be prohibited as part of the SMEI proposals as a way of preventing Members from holding medical equipment within closed borders, as happened during the early stages of the COVID-19 crisis. The most controversial element of the SMEI proposals, however, is the power given to the Commission to force a certain manufacturer to prioritise orders intended for EU citizens over those to be exported outside the EU. The same provision is set out in the EU Chips Act and guarantees a certain quantity of Single Market supply in times of crises. Non-compliance by exporters would be penalised by potentially ruinous fines of 1.5% of turnover. Member States are said to be critical of the proposals, with many seeing the reporting obligations as overly burdensome amidst concerns that national governments do not lose all control of critical goods in an emergency. Larger states such as France are supportive of the measure and we expect a draft regulation in the first half of 2023.
- **Germany/EU Supply-Chain Directives:** The much heralded German Supply Chain Due Diligence Act entered into force on 1 January 2023, requiring all firms that supply German companies employing more than 3,000 employees to report all ESG data relevant to their supplied goods. Companies that fail to provide the necessary information will be barred from being part of a German public procurement bid for up to three years. The EU is set to follow Germany's example, with negotiations ongoing between the Parliament and Council on a proposed Corporate Sustainability Due Diligence Directive, which will impose reporting obligations on all companies with an EU turnover of more than EUR 150 million. A lower threshold of EUR 40 million is anticipated for suppliers involved in the export/ production of certain high-risk goods, including textiles, agricultural raw materials, minerals, metals, etc. Firms that do not comply with the regulation may be subject to significant civil claims brought by Member State authorities.

A new era of Trade Defence and Strategic Autonomy

Last year saw the European Commission adopt a radical departure in trade policy towards even greater regulation of imports and inward investment, proposing new forms of trade countermeasures and defences, such as: (i) an anti-coercion instrument to counter the use of trade barriers by other states; (ii) constraints on suppliers from countries engaging in restrictive or discriminatory procurement practices from participating in EU public procurement; and (iii) the now-adopted EU Foreign Subsidies Regulation, which grants the Commission powers to review (and, if necessary, impose redressive measures on) companies engaged in large M&A and public procurement activities in the EU that have received contributions from foreign governments. 2023 may see further steps by the EU to implement its "open strategic autonomy" strategy, as the Foreign Subsidies Regulation begins to bite, while the Commission's more ambitious projects (such as the anti-coercion instrument) continue to be negotiated by Member States. The trend, however, is for greater defence of EU Member interests beyond traditional trade defence mechanisms such as anti-dumping duties, countervailing measures and safeguards.



- **Foreign Subsidy Regulation:** The FSR entered into force on 12 January 2023 and will apply to all applicable M&A (termed "concentrations" by the EU) and procurement activities from 12 July 2023. The key takeaway for impacted companies is the notification obligation to the Commission in the following circumstances:
 - Where the target EU company has an EU turnover of at least EUR 500 million and financial contributions from a foreign government were at least EUR 50 million;
 - Where the company is involved in an EU public procurement procedure with value of at least EUR 250 million and financial contributions from a foreign government were at least EUR 4 million.

If a company falls within the above categories, the transaction must be notified, and the Commission will conduct a review, during the course of which the transaction cannot be concluded. Where identified subsidies are deemed distortive and not outweighed by positive economic impact, the Commission's redressive powers are significant, including the ability to block the proposed acquisition, force a divestment from certain assets or prohibit the award of a public contract to the subsidised bidder. The first notifications may be issued in late 2023, although it is unlikely that we will see the results of a Commission investigation until 2024 at the earliest. Although the WTO's ASCM does not address foreign subsidies in support of investments and procurement bids, etc., and Article 44(9) of the FSR prohibits any investigation that would be contrary to the EU's obligations under international agreements, there will be intense scrutiny from WTO Members of the Commission's use of its powers, potentially resulting in retaliatory actions.

- **Anti-coercion:** The proposed instrument would provide the Commission with the power to adopt countermeasures against imports from a State that has applied economic pressure to one or more EU Members. An example of the type of situation the proposal was designed to protect against is China's de facto embargo on Lithuanian exports following the opening of a Taiwanese "liaison office" in Vilnius in 2021. The Council of the EU, however, has rejected the Commission's proposed role as unilateral enforcer of the mechanism, meaning a majority of EU Members must now agree that coercive actions are being taken by a foreign State and must consider the interests of EU Members, companies and consumers prior to adopting any countermeasure. Although the revised proposals are significantly weaker than those originally put forward by the Commission, EU Members have agreed that "the EU has a right to defend itself [...] when becoming a target of economic intimidation". While we may not see a final regulation in 2023, expect a strong response from other WTO Members in due course.



CONTACTS



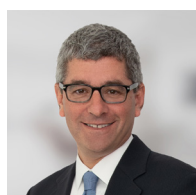
Jessica Gladstone
Partner
London
T: +44 207006 5953
E: jessica.gladstone@cliffordchance.com



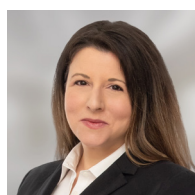
Thomas Voland
Partner
Dusseldorf
T: +49 211 4355 5642
E: thomas.voland@cliffordchance.com



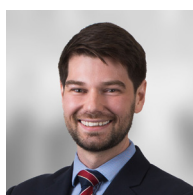
Michelle Williams
Partner
Washington DC
T: +1 202 912 5011
E: michelle.williams@cliffordchance.com



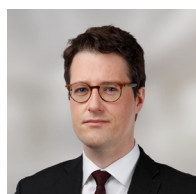
Joshua Berman
Partner
Washington DC
T: +1 202 912 5174
E: joshua.berman@cliffordchance.com



Renée Latour
Partner
Washington DC
T: +1 202 912 5509
E: renee.latour@cliffordchance.com



Jeremy Stewart
Senior Associate
London
T: +44 207006 4502
E: jeremy.stewart@cliffordchance.com



Kieran John McCarthy
Senior Associate
London
T: +44 207006 1374
E: kieranjohn.mccarthy@cliffordchance.com



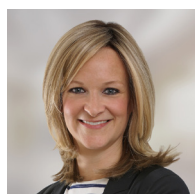
Jonathan Price
Senior Associate
London
T: +44 207006 2286
E: jonathan.price@cliffordchance.com



Holly Bauer
Associate
Washington DC
T: +1 202 912 5132
E: holly.bauer@cliffordchance.com



Phillip Souta
Head of UK Public Policy
London
T: +44 207006 1097
E: phillip.souta@cliffordchance.com



Gail Orton
Head of EU Public Policy
Paris
T: +33 1 4405 2429
E: gail.orton@cliffordchance.com



Roland Scarlett
Lawyer
London
T: +44 207006 2191
E: roland.scarlett@cliffordchance.com

CLIFFORD CHANCE

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Clifford Chance, 10 Upper Bank Street, London, E14 5JJ

© Clifford Chance 2023

Clifford Chance LLP is a limited liability partnership registered in England and Wales under number OC323571

Registered office: 10 Upper Bank Street, London, E14 5JJ

We use the word 'partner' to refer to a member of Clifford Chance LLP, or an employee or consultant with equivalent standing and qualifications

If you do not wish to receive further information from Clifford Chance about events or legal developments which we believe may be of interest to you, please either send an email to nomorecontact@cliffordchance.com or by post at Clifford Chance LLP, 10 Upper Bank Street, Canary Wharf, London E14 5JJ

Abu Dhabi • Amsterdam • Barcelona • Beijing • Brussels • Bucharest • Casablanca • Delhi • Dubai • Düsseldorf • Frankfurt • Hong Kong • Istanbul • London • Luxembourg • Madrid • Milan • Munich • Newcastle • New York • Paris • Perth • Prague • Rome • São Paulo • Shanghai • Singapore • Sydney • Tokyo • Warsaw • Washington, D.C.

Clifford Chance has a co-operation agreement with Abuhimmed Alsheikh Alhagbani Law Firm in Riyadh.

Clifford Chance has a best friends relationship with Redcliffe Partners in Ukraine.