

# How do PTAs Address “Competitive Neutrality” between State and Private Owned Enterprises?

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**Abstract:** States-owned enterprises (SOEs) have for long used as and are likely to remain an important instrument in any government’s toolbox for a variety of economic, public and societal goals. However, the significant extent of state ownership among the world’s top companies raises the issue of its impact on international trade and global competition. We address the question of how multilateral and preferential trade agreements (PTAs) discipline SOEs with a view to guaranteeing the level playing field between such entities and private enterprises, while, at the same time, allowing governments to provide support to SOEs that deal with market failures and provide public goods. The argument is developed in three main parts. The first briefly outlines the reasons why SOEs are disciplined by a number of international legal instruments. The second assesses how WTO agreements deal with the potential trade effects of SOEs and highlights the main shortcomings of the multilateral trade discipline. The third part analyses the chapters on SOEs of the Transpacific Trade Partnership (TTP) and the EU-Vietnam FTA (EUVFTA), which represent, respectively, for the US and the EU, the PTAs endowed with the most advanced provisions on the matter. We will conclude with some concise remarks.

*Keywords:* PTAs, SOEs, POEs, competitive neutrality

The research question addressed in our paper is expressed above in a straightforward and beguilingly way, which, however, hides its true complexity. One of the reasons of such complexity has to do with the interplay between the use of SOEs by governments to pursue a variety of political and societal goals, the magnitude of state ownership among the world’s top companies and the potential trade/competitive distortions the favorable treatment SOEs may be benefit from may cause.

## 1. Why state ownership?

Often governments have created and invested in SOEs because markets were imperfect or unable to accomplish critical societal needs such as effectively mobilizing capital or building enabling infrastructure for economic development *e.g.* a nationwide electricity grid or water system. Particularly, the OECD and World Bank have set out a range of commonly stated reasons for state-ownership [1] Government traditionally resort to SOEs might:

- Provide public goods (*e.g.* national defense and public parks) and merit goods (*e.g.*

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public health and education), both of which benefit all individuals within a society and where collective payment through tax may be preferred to users paying individually.)

- Improve labor relations, particularly in 'strategic' sectors.

- Limit private and foreign control in the domestic economy.

- Generate public funds. For instance, the state could invest in certain sectors and control entry in order to impose monopoly prices and then use the resulting SOE revenues as income.

- Increase access to public services. The state could enforce SOEs to sell certain goods and services at reduced prices to targeted groups as a means of making certain services more affordable for the public good through cross-subsidization.

- Encourage economic development and industrialization through:

- Sustaining sectors of special interest for the economy, and in particular to preserve employment.

- Launching new and emerging industries by channeling capital into SOEs which are, or can become, large enough to achieve economies of scale in sectors where the start-up costs are otherwise significant. This might be seen as an alternative to regulation, especially where there are natural monopolies and oligopolies (e.g. electricity, gas and railways).

- Controlling the decline of sunset industries, with the state receiving ownership stakes as part of enterprise restructuring.

SOEs are likely to remain an important instrument in any government's toolbox for societal and public value creation given the right context.

## 2. SOEs, international trade and competition

From another angle, the vastness of SOEs' print on the international economy is unquestionable. In a trade policy paper prepared for the Organization for Economic Co-operation and Development (OECD), Kowalski

and his collaborators demonstrate that 204 out of the world's 2000 largest publicly listed firms can be identified as SOEs, representing USD 3.6 trillion or 10% of the aggregate of the largest companies [2]. Similarly, in its 2014 World Investment Report, the United Nations Conference on Trade and Development estimates the presence of 550 state-owned transnational corporations accounting for 11% of global foreign direct investment flows [3]. The magnitude of state ownership among the world's top companies raises a question about its impact on the global competition. The triple role of the government as a regulator, regulation enforcer and owner of assets opens a possibility of favorable treatment granted to state-owned enterprises in some cases. These advantages can take the form of, for instance, direct subsidies, concessionary financing, state-backed guarantees, preferential regulatory treatment, exemptions from antitrust enforcement or bankruptcy rules [4]. They may well be justified in a domestic context, for example, to correct market failures, provide public goods, and foster economic development. But if their effects extend beyond borders, they may undermine the benefits from international trade and investment, which are predicated on the basis of non-discrimination and respect for market principles. In other words, it is contended that when states act as commercial actors in the market place, they can potentially distort trade and investment patterns. Furthermore, taking into consideration the effects of globalization on value chains, there is also the risk of altering the competitive conditions in the upstream and downstream sectors.

In order to cope with the potential trade and anticompetitive effects of state ownership in the global market, States and international organizations have developed different tools. By surveying existing regulatory frameworks at the national, bilateral or multilateral level, one may single-out their relative strengths and weaknesses. For example:

(i) National antitrust law can in principle be used to deal with the abuse of dominant position by State-owned enterprises, including in the international context, or to prevent anticompetitive effects associated with merger and acquisition activities of state-owned enterprises. However, traditional antitrust standards apply to profit maximizing firms and are not aimed at preventing subsidies and artificially low prices –except where these are manifestly motivated by predatory strategies [5].

(ii) In the EU, the state interactions with private and state-owned firms alike are governed by a set of special rules in the areas of antitrust, state aid and transparency. [6]

(iii) The OECD promoted a number of regulatory-initiatives, in the usual form of non-binding provisions (i.e. guidelines), aimed to providing States with instruments to counteract such distortion. The most important are the OECD Guidelines on Corporate Governance of SOEs [7], that constitute the first international benchmark to help governments improve the corporate governance of SOEs by providing standards and good practices, as well as guidance on implementation. The Guidelines recommend the maintenance of a level playing field among state-owned and privately owned incorporated enterprises operating on a commercial basis, by listing and elaborating on a number of guiding principles in a number of areas [8]. Capobianco and Christiansen assess that their implementation would go a long way towards addressing competitive issues associated with the distorted incentive structure of SOE management as well as conditions in access to finance, disclosure and cost-coverage of SOEs objectives [9].

(iv) Government procurement regulation at the national and international levels regulates the purchase by governments and SOEs of goods and services, including imports, and thus can be an important element of levelling the playing field between SOEs and POEs [10]. There are public government provisions in the plurilateral Agreement on Government Procurement (GPA), regional trade agreements

like North-Atlantic Free Trade Agreement (NAFTA), bilateral trade agreements like U.S.-Colombia Free Trade Agreement or EU-Mexico Free Trade Agreement, and domestic public procurement policies [11].

(v) Several other provisions of international trade agreements, even if not directly targeting the SOEs, contribute to the efforts in restoring the “level-playing field” distorted by the presence of the two categories of enterprises [12].

### 3. WTO Discipline

A first textual element catches our attention: there is no reference to the term “SOE” in the GATT/WTO texts, but several agreements contain related concepts (e.g. state-trading enterprise, public monopoly, public body, etc.) which may overlap with the status of some SOEs. Hence, several WTO rules may be applicable and relevant to SOEs. From this perspective WTO rules that can be relevant in the context of potentially anti-competitive behavior of modern SOEs can be categorized into four main groups [13].

First, there are the WTO rules that are in principle ownership-neutral and, therefore, discipline some of the trade distorting government policies that may involve SOEs. For example, the national treatment or the most-favored nation principles oblige all WTO Members to treat imports not less favorably than domestic like products or than other like imports, independently of whether the exporter was a POE, an SOE or a government. The Antidumping Agreement authorizes an importing Member to impose antidumping duties on “dumped” imports—whether the dumped imports were produced and exported, or exported, by a private firm or an SOE. Also, subsidies in the goods sector are regulated by the WTO irrespective of whether they are granted to an SOE or a POE [14].

Second, there are the WTO provisions that allow WTO Members to exempt SOEs’ actions from the application of the WTO disciplines.

For instance, Members can specify that their GATS specific commitments apply only to privately owned entities, which may restrict market access or national treatment of foreign SOEs.

Third, specific provisions of the WTO covered agreements explicitly discipline some practices in which so-called State Trading Enterprises (STEs) (GATT, Art. XVII) or monopoly and exclusive service suppliers (as in the case of GATS Art. VIII) [15], some of which can but do not have to be state-owned, can be used by governments as vehicles to influence international trade. This is the case of Art. XVII GATT, whereby Member should notify the operations of State Trading Enterprises (STEs), including Marketing Boards [16]. In essence, STEs should not be accorded favorable government assistance in the form of discriminatory measures and they should act in a general manner consistent with commercial considerations. It is of note that neither STEs nor state trading are clearly defined and this ambiguity seems to represent a handicap in the application of the article [17].

Fourth, WTO Accession Protocols of China and Russia contain certain provisions which specifically refer to state ownership. Importantly, these accession protocols are an integral part of the WTO Agreement. Yet, doubts have been expressed whether even the relatively strong provisions in China's Protocol have sufficiently impeded trade-distorting policies that advantage Chinese SOEs [18].

Overall, each of the above types of WTO disciplines offers provisions that deal with certain aspects of international competition between POEs and SOEs. Yet, the WTO rules which, directly or indirectly, address the behavior of STEs do not address the issue of competitive neutrality comprehensively. In particular:

(i) some of the definitional ambiguities (*e.g.* the very notion of 'STEs' or of State trading) have rendered application of these disciplines uncertain;

(ii) under Art. XVII of the GATT it is not clear whether the non-discrimination principle applicable to STEs includes national treatment as per Art. III GATT [19];

(iii) as mentioned, some provisions allow countries to exempt state-owned enterprises' actions from certain WTO disciplines (*e.g.* in the GATS).

(iv) Most GATT/WTO rules do not include in their scope of application new trade and economic behavioral patterns of SOEs. For example, GATT/WTO does not refer to the behavior of SOEs when acting as FDIs in another country.

(v) With the commercial presence, no possibility to apply AD or CVD measures.

#### 4. "New generation" PTAs and SOEs

In parallel with the economic relevance of SOEs, the negotiation of preferential trade agreements (PTAs) offers an interesting alternative avenue to adopt legal rules that shield free market from various trade distortions. Existing (in force or in a regime of provisional application) [20] and recently signed or just initialed preferential trade agreements and bilateral investment treaties include specific provisions on state-owned enterprises, attempting to fill gaps in existing multilateral provisions. Some explicitly specify that their provisions apply similarly to state-owned enterprises, clarify some of the *definitional lacunae* in the WTO context, or include additional state-owned specific disciplines.

As specifically regards the two major trade polities - the US and the EU- we chose, the TPP [21] and the EUVFTA [22] as equipped with the most advanced provisions on SOEs. Hence, the question arises of how significantly the disciplines provided by such PTAs innovates compared to the multilaterals discipline and to what extent they address the issue of competitive neutrality.

## 5. Main innovations of TPP and EUVFTA

### 5.1. Definition of SOEs

One major novelty of both the agreements under examination is the inclusion of a definition of SOEs setting a clear link between States and such entities. Arguably, defining SOEs was a considerable challenge for TPP and EUVFTA negotiators. In general, there is no consensus on the matter and, depending on the different legal system and tradition, many variations in the key elements of an entity (e.g., ownership of shares, control of the board of directors) or its behavior could be taken into account to capture this concept. Concerns can be raised with both a narrow definition and a broad one. Whereas risks with a narrow definition include chances of eluding the rules by slightly modifying the ownership structure, a broad definition may comprise entities for which states usually wish to maintain a maximum of policy flexibility and autonomy [23].

While the SOE definition included both in Chapter 17 of the TPP and in the Chapter on SOEs of the EUVFTA remain in line with the dual consideration of ownership and control in previous FTAs concluded by the US, they also include interesting innovations. Particularly, they expressly provide that a SOEs is an enterprise that is engaged in commercial activities, in which a Party

(i) Directly owns more than 50 percent of the share capital;

(ii) Controls, through ownership interests, the exercise of more than 50 percent of the voting rights; or

(3) Holds the power to appoint a majority of members of the board of directors or any other equivalent management body; [24] or

(iv) Can exercise control over the strategic decisions of the enterprise [25]. (ONLY EUVFTA)

The notion of power ‘to can exercise control over the strategic decisions of the enterprise’ is not clarified any further in the EUVFTA. The precise confines of such

definition and the extent to which it allows for flexibility introduce an element of legal uncertainty as to the scope of application of the treaty and will have to be clarified through the interpretation.

TPP also limits the notion of “control” to the action of entrusting a non-SOEs to provide “non-commercial assistance” (= subsidies) to SOEs

As mentioned, both the agreements define SOEs as enterprises engaged in “commercial activities”, [26] but a slight difference between the TPP and EVFTA emerges: the TPP includes in its scope of application SOES when engaged “principally” in commercial activities. The EVFTA includes all SOEs but limit its application to their “commercial activities” and adds that where an enterprise “combines commercial and non-commercial activities” (such as carrying out a public service obligation), “only the commercial activities of that enterprise are covered by this Section.”

To conclude the point, the definition of SOE in both the agreements, thus, encapsulates the consideration of effective influence and expressly refers to engagement in commercial activities.

### 5.2. The discipline: An outline

A comparative analysis of the disciplines provided by the two agreements sheds light on the way the intent of addressing the issue of ‘competitive neutrality’, while allowing governments to provide support to SOEs that deal with market failures and provide public goods and services has been materialized.

The most salient elements of such disciplines may be outlined as follows:

First, the TPP is equipped with a more specific and detailed discipline, what clearly emerges looking at the number pages of Chapter 17(21!) and the number and complexity of articles and annexes dealing with SOEs.

Second, the same treaty also includes a complex and dedicated rules on the so-called “non-commercial assistance”, which essentially

cover direct transfers of funds as well as the provision of goods or services other than general infrastructure on terms more favorable than those commercially available to a private enterprise. By contrast, the EUVFTA does not establish for such a complex discipline [27]. The reasons of such striking difference between the two agreements under examination lies in the fact that, contrary to the TPP, the EUVFTA establishes a detailed discipline on subsidies, including also 'WTO+' provisions on subsidies in the service sectors and comprehensive rules on justification echoing the EU endorsement for the reinstatement of 'green light' subsidies during the DDR [28]. However, it must be noted that the notion of 'non-commercial assistance' has a wider scope than the traditional scope of application of the rules on subsidies. In this sense, it may be readily inferred that the TPP goes further in addressing the issue of the 'competitive neutrality' when regulating SOEs.

Third, in regulating SOEs, both the TPP and the EUVFTA extend their scope beyond goods to include services and investment.

Fourth, the Dispute Settlement Procedures of both agreements are applicable to the SOEs chapter (with minor exceptions). In this respect, it is worth recalling that Horn, Mavroidis, and Sapir in their thorough 'anatomy' of EU and US PTAs indicate that the exclusion from the respective dispute settlement mechanisms of a number of "WTO+/WTOx" provisions of such agreements is one of the main causes of their non-enforceability, which, in the end, means lack of immediate relevance [29]. It is of note, for example, that the competition policy chapters of both the TPP and the EUVFTA will not be subject to the respective dispute settlement mechanisms [30].

Fifth, both treaties include detailed provisions on transparency [31]. In fact the elaboration of disciplines with respect to SOEs would remain highly problematic without express requirements imposed on States to publish specific information on these economic actors. For example, Hufbauer pointedly argues

that SOEs 'should present accounts in accordance with international accounting standards just like any private firm, and if they do not, the same negative inferences should apply as for private firms'. He further notes that SOEs should have to disclose 'any debt or equity financed by the government, and any influence by the government or administrative guidance' [32].

Sixth, both make applicable the principles of "acting in accordance of commercial considerations in their purchases or sales of goods or services" [33] and, differently from GATT, specify that the SOEs obligation to act in a non-discriminatory manner includes MFN and National Treatment obligations [34].

### 5.3. Scope and exceptions

Despite the relevance of including considerations pertaining to SOEs' activities in FTA negotiations, one should not be surprised to encounter several carve-outs within the scope of SOE disciplines in the TPP and EUVFTA. It is mainly through the definition of their scope of application and the inclusion of further exceptions that the goal of addressing the issue of 'competitive neutrality' between private and state-owned enterprises, while, at the same time, allowing governments to provide support to SOEs that deal with market failures and provide public goods and services has been materialized in the two treaties.

For instance, while FTAs negotiated by the USA prior to the signature of the TPP do not expressly enunciate the scope of SOE disciplines, Chapter 17 of TPP encompasses a detailed provision in this regard with a considerable number of exclusions. After emphasizing that this chapter generally applies to 'the activities of state-owned enterprises and designated monopolies of a Party that affect trade or investment between Parties within the free trade area', Article 17.2 enumerates several areas that are not included within its scope of application [35]. Furthermore, Article 17.9 provides a possibility for each Party to list

elements to which SOE disciplines shall not apply. States can thus list in their schedule to Annex IV non-conforming activities of SOEs and designated monopolies regarding non-discriminatory treatment and commercial considerations, as well as non-commercial assistance [36]. Annex 17-D is also used by states to list disciplines regarding nondiscriminatory treatment and commercial considerations, courts, and administrative bodies, non-commercial assistance, as well as transparency that do not apply to sub-central entities [37]. This sub-central entities exclusion is set to be renegotiated five years after the entry into force of the agreement [38]. Finally, Article 17.9 mention the application of specific annexes for Singapore (Annex 17-E) and Malaysia (Annex 17-F) [39].

The negotiations on carve-outs from Chapter 17 of the TPP were arguably complicated by hard lines taken by the USA and by SOE-driven economies. Thus, a multitude of exclusions in the TPP to protect countries' specific sensitivities was largely predictable and must be taken into account to balance the acceptance of relatively challenging SOE disciplines by states like Malaysia, Singapore, and Vietnam. Even rather complex in terms of legal drafting – the discipline of SOEs for each of the party of the TPP can be inferred only after considering the annexes dealing with that specific party - the resulting compromise, however, is balanced.

In light of these provisions, one can nonetheless be surprised by the disparity regarding the formulation of exclusions that were advanced by the USA and concerns raised by other States. In fact, it is clear that issues pertaining to financial services were addressed through horizontal exclusions that unambiguously carve-out these aspects from all the SOE disciplines found in Chapter 17. By contrast, other Parties that were mostly concerned with carve-outs regarding their SOEs had to rely on negative lists that could only exclude these issues from specific provisions found in the same chapter.

A similar normative pattern, *i.e.* the explicit exclusion of a number of areas from the discipline on SOE, (as well as designated monopolies and enterprises with special or exclusive rights) is adopted by the EUVFTA [40].

Finally, in addition to the aforementioned exclusions from the scope of SOE disciplines and specific carve-outs, negotiating parties of both the TPP and the EUVFTA sought to allow more flexibility for SOEs that deal with market failures or aim at providing certain goods or services with conditions that the private sector does not match under specific circumstances. As a consequence, Article 17.13 of the TPP provides exceptions to requirements imposed on States with respect to actions in accordance with commercial considerations, non-discriminatory treatment, and non-commercial assistance [41]. Most exceptions included in Article 17.13 relate to the adoption of temporary measures in response to 'a national or global economic emergency' [42], and the 'supply of financial services by a state-owned enterprise pursuant to a government mandate' [43]. Probably the most important exception to non-discriminatory treatment, commercial considerations, non-commercial assistance, transparency, and the activities of the Committee on State-Owned Enterprises and Designated Monopolies is the one provided for smaller SOEs as defined by Article 17.13(5) and Annex 17-A [44]. As such, only SOEs with 'annual revenue derived from the commercial activities of the enterprise above the established threshold of 200 million Special Drawing Rights are to be covered by the principal SOE disciplines. In turn, the Annex to the Chapter lists a wide array of exceptions which, however, mainly address specific concerns of Vietnam only, for example, excluding from the application of the provisions on SOEs 'adoption, enforcement or implementation of the privatization, equitization, restructuring or divestment of assets owned or controlled by the Government of Vietnam'; 'measures by the Government of Vietnam related to the ensuring of economic stability in the territory of

Vietnam'; and 'measures by the Government of Vietnam aiming at development issues in the territory of Vietnam, such as income security and insurance, social security, social welfare, social development, social housing, poverty reduction, public education, public training, public health, and childcare, promoting the welfare and employment of ethnic minorities and people living in disadvantaged areas'; 'the purchase of goods or services of a state-owned enterprise or a designated monopoly from Vietnamese small and medium enterprises as defined by Vietnam's laws and regulations' [45]. Furthermore, the rules on non-discriminatory and commercial considerations and those on 'transparency' shall not apply with respect to explicitly listed enterprises, their subsidiaries and successors, pursuing the same public mandate, engaged in and limited to the activities as described by the same Annex [46].

#### 5.4. *Acting in accordance with commercial considerations*

Beyond the need to clarify the definition of SOEs and areas that are excluded from the scope of disciplines articulated in the TPP and EUVFTA, a core principle of competitive neutrality is the obligation for States to ensure that their SOEs act in accordance with commercial considerations [47].

Understanding the meaning of such an expression arguably requires more than a vague definition. In this respect, some developments that occurred under the auspices of the WTO must be noted. Article XVII of the General Agreement on Tariffs and Trade targets state enterprises' discriminatory activities and links the national treatment obligation to the need for 'state trading enterprises' to act 'solely in accordance with commercial considerations' for its purchases or sales [48]. The meaning of the 'commercial considerations' expression was determined by the Appellate Body as requiring state trading enterprises to act in a manner economically advantageous to its beneficiaries [49]. More specifically, this requirement involves a case-by-case analysis that includes

the scrutiny of different elements of the enterprise and the relevant market. However, given that Article XVII(1) (b) has to be read with the objective of clarifying the non-discrimination obligation contained in XVII(1) (a), the compatibility of state enterprises' activities with commercial considerations is to be addressed only once discriminatory conduct has been found [50].

Here again, the outcomes of the TPP and EUVFTA negotiations pertaining to the obligation of States to ensure that SOEs act in accordance with commercial obligations appears as a relevant innovation. Article 17.4 of the TPP thus provides that '[e]ach Party shall ensure that each of its state-owned enterprises, when engaging in commercial activities: (a) acts in accordance with commercial consideration in its purchase or sale of a good or service, except to fulfill any terms of its public service mandate' [51]. In addition to this requirement, Article 17.1 defines the terms 'commercial considerations' as 'price, quality, availability, marketability, transportations, and other terms and conditions of purchase or sale; or other factors that would normally be taken into in the commercial decisions of a privately owned enterprise in the relevant business or industry' [52]. Art. 4 and 1(f) of the EUVFTA provides to the same effect [53].

It is questionable whether the requirement for States to ensure that SOEs act in accordance with commercial considerations is formulated in a so generic fashion that it may allow Parties to circumvent it by arguing that commercial considerations do not need to be uniquely market driven. The extent to which the definition of 'commercial considerations' allows for such a flexibility remains indeterminate and will have to be clarified through the interpretation of Chapter 17 and the equivalent chapter in the EUVFTA.

#### 5.5. *Courts and administrative bodies*

Aside from requiring States to ensure that their SOEs act in accordance with commercial considerations and accord a non-discriminatory



treatment in their activities are important aspects to discipline SOEs, other elements must be taken into account in order to limit trade distortions caused by these actors' activities. In fact, schemes such as jurisdictional immunities and regulatory favoritism can potentially impact the competition environment between various actors. Overcoming the risk that a foreign SOEs owned by another member might benefit from the immunity from the civil jurisdiction is one of the main concerns in the US. Indeed, under US law, entities incorporated under local law which are directly majority-owned by a foreign state enjoy, at least in principle, almost exactly the same immunity from jurisdiction as the foreign state itself [54]. That's probably the reason why TPP article 17.5 obliges each party to provide its courts with jurisdiction over civil claims against an enterprise owned or controlled through ownership interests by a foreign Government based on a commercial activity carried on its territory.

A second concern dealt with in the TPP (but not in the EVFTA) relates to the risk of regulatory favoritism for SOEs impacting the level playing field between in the market. The OECD Guidelines on Corporate Governance of SOEs, for example, encourages States to allow "efficient redress and an even-handed ruling" for competitors regarding laws, regulations and legal acts in general. TPP Article 17.5.2 obliges Parties to ensure that any administrative bodies regulating SOEs exercise their regulatory discretion in an impartial manner with respect to enterprises that are under their regulatory jurisdiction (including enterprises which are not SOEs). This direction is coherent with the OECD Guidelines on Corporate Governance of State-Owned Enterprises, which encourage countries to allow 'efficient redress and an even-handed ruling' for competitors with regard to general laws and regulations, among others.

#### *5.6. Incorporation of the OECD "Guidelines on Corporate Governance of SOEs"*

The EVFTA invites members ("members shall endeavor") to ensure that SOEs observe

internationally recognized standards of corporate Governance. Even if the binding force of this provision is questionable, this is a signal confirming the trend of giving binding force to soft law provisions prepared by relevant international organizations. For example, a similar provision is included in several economic and cooperation agreements of the European Union which incorporate the principles enshrined in the Paris Declaration on Aid Effectiveness. Transformation of soft law into conventional law is not a rare occurrence [55]. The specific kind of "hardening" of soft law that seems interesting to consider now is peculiar in that, in inserting the soft law provisions in a treaty, (although in a non-mandatory provision), the Parties of the same increase their reciprocal expectations of compliance with the soft provisions.

#### *5.7. TPP Provisions on Non-commercial Assistance*

The express consideration of non-commercial assistance reflecting concerns raised during the negotiations of the TPP emerges as a genuine innovation that was not firmly rooted in FTAs previously signed by the USA and does not find a counterpart even in the latest FTAs negotiated by the EU.

As observed above, Article 17.1 defines 'non-commercial assistance' as 'assistance to a state-owned enterprise by virtue of that state-owned enterprise's government ownership and control'. The definition emphasizes that this concept more specifically concerns direct transfers of funds as well as the provision of goods or services other than general infrastructure on terms more favorable than those commercially available to an enterprise.

The innovation of this article is that the provisions on NCA are applicable to the assistance to an SOE which is an FDI in another Party (17.6.3), to the assistance to an SOE with another SOE (17.6.2) and to the assistance to SOEs through a private company entrusted by the Government (footnote 18 of article 17). As

article 17.6 makes clear that parties shall not cause adverse effects to the interest of other parties with NCA, it is reasonable to conclude that those types of ASSISTANCE/subsidies, when negatively affect third parties, are prohibited. The provisions are also applicable to services providers: indeed, article 17.6.2 b refers to the subsidized SOEs exporting services in another Party (i.e. the GATS mode 1), while the letter c) of the same article covers the adverse effects caused through a “commercial presence” in another party of the service provider.

As with the provisions on subsidies in the service sectors of a number of EU FTAs of new generation [56], the inclusion of provisions on non-commercial assistance pertaining to services provided by SOEs ultimately constitutes a considerable breakthrough as far as service subsidies are concerned. While it has been suggested that Member States of the WTO were unlikely to reach a consensus on major subsidy disciplines for services [57], these provisions codify innovative rules regarding

## 6. Concluding remarks

From the previous analysis some concluding remarks can be advanced.

First, the regulation of SOEs by PTAs has to be placed within the context of the major challenges the multilateral trade systems had to face right after the conclusion of the Uruguay round. According to Renato Ruggero, the then WTO Director General, one of the improvements that the WTO already needed in the immediate aftermath of its own creation was a toolkit to deal with a new agenda of subjects that were not dealt with in the Uruguay Round and that would have constituted a new focus for negotiations for future trade policy, including ‘the objective of international contestability of markets’ [58]. In the mid-90ies, trade theorists started carrying over the concept of contestable markets to the international context. They advocated the international contestability of

markets as a main objective of the multilateral trading community. A key idea was especially emphasized: a market is deemed internationally contestable when the conditions of competition allow unimpaired market access for foreign goods, services, ideas, investments, and business people. This idea placed an original emphasis on market access and presence as a touchstone of future trade policy [59]. An internationally contestable market is one in which ‘the competitive process -- the rivalrous relationship between firms -- is unimpeded by private or public anticompetitive conduct’ [60].

As widely known a number of institutional initiatives and academic works have been prepared to pursue the market contestability objective, mainly in the form of the formulation and implementation of a program of convergence of antitrust policies [61], and it is widely acknowledged that “the introduction of a competition policy into the WTO regime is a necessity if the effectiveness of the international trade regime is to be maintained.”[62] However, although several provisions in the existing WTO agreements indirectly deal with competition matters, a comprehensive agreement on competition policy is yet to take its place in the WTO regimes. Therefore, it comes as no surprise that most of the recent EU and US FTAs include chapters that expressly address competition policy [63]. However, even if private anti-competitive conduct may offset the benefit of liberalization of economy afforded by the removal or reduction of trade barriers and, hence, constitutes a major impediment for the international contestability of markets, as seen, favorable treatment granted to state-owned enterprises may cause similar distortive effects. From such angle, in going significantly further than the WTO rules, the detailed disciplines contained in the TPP and EUVFTA on SOEs are to be praised as a welcome novelty.

A second conclusion is strictly linked to the first. Addressing competitive neutrality between State-owned and private enterprises by means of international trade agreements while

allowing governments to provide support to SOEs that provide public goods and services domestically and deal with market failures is a hard balancing exercise. In fact, disciplining SOEs is not risk-free and may inflict a variety of social costs in the long run if done hastily or on an exaggerated scale. As observed early, SOEs are traditionally used by governments worldwide (also) to accomplish critical societal needs, contribute to making economic regulation consistent with basic necessities of their citizens and regulate market failures: such objectives cannot be dismissed. In the light of the above, one may well understand the importance of the provisions limiting the scope of the applications of both the agreements we have examined as well as the several exceptions they establish. The very rationale of many of such provisions as well as of the TPP Annexes addressing the specific situations of its different parties, is thus to allow enough flexibility for SOEs that deal with market failures or aim at providing certain goods or services with conditions that the private sector does not match under specific circumstances.

Finally, as certain economists admit, '(o)ur understanding of the recent emergence of international trade and investment by state-owned enterprises (...) are still in the early stages of development [64]. So are the policy and legal responses: a deeper understanding of the implications of SOEs trade and investment for the functioning of international markets is indeed needed to help governments to formulate informed and balanced policy and regulatory responses.

## References

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- [2] Kowalski et al., above note 1, at 20. These figures should be regarded seen as conservative for at least two reasons. First, the reported data does not include unlisted state-owned enterprises such as statutory enterprises in, for instance, postal services or utilities. Second, the state might also exert de facto control over a firm even while holding a minority share, for example, through a golden share or any other specific enabling legislation.
- [3] UNCTAD, World Investment Report 2014 – Investing in the SDGs: An Action Plan (New York and Geneva: United Nations, 2014), at 20–21.
- [4] Kowalski et al., above n 1, at 9 and 31–34. See also OECD, State-Owned Enterprises in the Development Process (Paris: OECD Publishing, 2015), at 12–13.
- [5] Capobianco, A and H Christiansen, "Competitive Neutrality and State-Owned Enterprises: Challenges and Policy Options", OECD Corporate Governance Working Papers, No. 1, (Paris, OECD Publishing, 2011).
- [6] Cfr., in particular, Arts. 101, 102, 106, 107-9 of the Treaty of the Functioning of the European Union (TFEU).
- [7] See OECD, Guidelines on Corporate Governance of State-Owned Enterprises, 2015 editions, <http://www.oecd.org/corporate/guidelines-corporate-governance-SOEs.htm>
- [8] These include: Ensuring an Effective Legal and Regulatory Framework; Principles of state Acting as an Owner; Equitable Treatment of Shareholders; Relations with Stakeholders; Transparency and Disclosure; The Responsibilities of the Boards of State-Owned Enterprises.
- [9] Capobianco and Christiansen, above note 5, p. 20 ff.
- [10] Kowalski et al., above n 1, at 40.
- [11] Ibidem, Annex Section 3.6.
- [12] Milhaupt C. J. and W. Zheng, "Beyond Ownership: State Capitalism and the Chinese Firm", in 103 Georgetown Law Journal, 665. See also Kowalski et al., above note 1, at 30. The WTO/GATT and new generation PTAs are not the only international treaties on the matter. For example, several US-participated "Friendship, Navigation and Commerce" (FNC) agreements and the Free Trade Agreements (FTAs) of new

generation dealt with the distortions of the so-called 'State Capitalism' directly targeting the SOEs as well as private enterprises having a privileged position in the market as beneficiary of a specific treatment from their national Governments

- [13] From yet another angle, WTO provisions traditionally address Governments as subject of international law, in their role as regulators of economic activities. As such, several WTO agreements, especially when they provide limitation to the sovereignty of States, may have an impact to the activity of SOEs and PEs, like, for example, Subsidies and Countervailing Measures. In the WTO covered agreements, there are three main exceptions to this rule: article XVII of GATT, article VIII of GATS and article I of the Subsidies and Countervailing Measures Agreement (SCM).
- [14] More in detail, the Subsidies and Countervailing Measures (SCM) Agreement disciplines subsidies in the goods sector involving financial contributions provided by either governments or public bodies which may be SOEs. Yet, when SOEs act as conveyors of subsidies (e.g. providing cheaper inputs to other firms) the application of subsidy disciplines tends to be more complicated. The WTO Agreement also contains special rules concerning tariffs on products traded by import monopolies, or other actions of public monopolies or other public bodies.
- [15] Article VIII of GATS targets only monopoly and exclusive service suppliers; monopolies are then defined in article XVVIII(h), and article I of SCM points out that a subsidy is "a financial contribution by a government or any public body within the territory of a Member". However, the interpretation of the term "public body" by the AB did not help in establishing a clear guide, leaving the solution to case-by-case assessment.
- [16] Article XVII of GATT 1994 targets, together with Members, specific types of enterprises, i.e. "State enterprise" or "any enterprise" that has been granted "formally or in effect, exclusive or special privileges" (paragraph 1(a)) including "Marketing Boards" (interpretative note to paragraph 1); "any enterprise" under the jurisdiction of a contracting party (paragraph 1(c)) and an "import monopoly" (paragraph 4(b)). Of course, the provisions of article XVII are directed to Members, imposing an obligation on Members establishing or maintaining STEs. However, this is the only case where a provision of GATT (and WTO) does not target directly the State or a State-organ, but a different subject.
- [17] On the one hand, Parties have the right to maintain SOEs or enterprises in a privileged position. On the other, these enterprises (STEs) must act consistently with the non-discrimination principle. STEs shall make any purchase in accordance with commercial considerations (XVII:1 a) and b)). For sure, the scope of the provision includes MFN obligation, however with some flexibility (see Ad interpretative note art. XVII). Furthermore, STEs shall not erode or nullify the negotiated tariff schedules (II:4 and XVII:3) and cannot be instruments for members to implement WTO-inconsistent measures, if carried out directly by Government.
- [18] Kowalski et al, above note 1, 38-9.
- [19] In this respect, there are different views in the literature and, so far, AB has taken no view for the purpose of appeal. Indeed, in Korea — Various Measures on Beef, the panel - the finding was not reviewed by the Appellate Body- pointed out that Article XVII.1(a)"establishes the general obligation on state trading enterprises to undertake their activities in accordance with the GATT principles of nondiscrimination. The Panel considers that the general principle of non-discrimination includes at least the provisions of Articles I and III of GATT". However, first, it should be noted that it is not a strict MFN treatment, but, as clarified in the Ad Note to Article XVII:1: "the charging by a state enterprise of different prices for its sales of a product in different markets is not precluded by the provisions of this Article, provided that such different prices are charged for commercial reasons, to meet conditions of supply and demand in export markets". Secondly, the AB report of the mentioned Canada-wheat case, noted the existence of different views in the literature "as to whether, or the extent to which, Article III of the GATT 1994 would also apply to STEs", even if it did "take no view" for purposes of the appeal. See Canada-Wheat, cit., footnote 104, where the AB reported the existence of different views as discussed in W. Davey, "Article XVII GATT: An Overview", in Cottier T. and P. Mavroidis (eds.), *State Trading in the Twenty-First*

- Century, University of Michigan Press, 1998, p. 17, at p. 26.
- [20] SOE disciplines have been present in the US-driven trade law corpus since the North American Free Trade Agreement (NAFTA) and have subsequently been included in FTAs that the USA have signed with Singapore, Chile, Australia, Peru, Colombia, and South Korea. However, the legal framework on SOEs that prevailed before the signature of the TPP was scarce and the TPP appears as a crucial step in SOE rulemaking. As far as the EU is concerned, we note that, as in the case of the WTO Agreements, other new generation EU FTAs, like the EU-Korea and the EU-Singapore FTAs contain provisions which explicitly discipline some practices in which or monopoly and exclusive service suppliers or enterprises with privileged rights, some of which can but do not have to be state-owned, can be used by governments as vehicles to influence international trade.
- [21] After extensive negotiations between 12 states on the shores of the Pacific Ocean (i.e. Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, USA, and Vietnam), the TPP was signed on 4 February 2016. Trans-Pacific Partnership, 4 February 2016, <https://www.mfat.govt.nz/en/about-us/who-we-are/treatymaking-process/trans-pacific-partnership-tpp/text-of-the-trans-pacific-partnership> (visited 21 March 2016) [hereinafter TPP]. See, particularly, Chapter 17 on 'State-Owned Enterprises and Designated Monopolies.
- [22] EU-Vietnam Free Trade Agreement, text made public on 1 February 2016 at: <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1437>; hereinafter: EUVFTA. This is the text resulting at the end of the negotiations conducted by the European Commission. It will be subject to legal revision in order to verify the internal consistency and to ensure that the formulations of the negotiating results are legally sound. It will thereafter be transmitted to the Council of the European Union and to the European Parliament for ratification.
- [23] An example of a narrow definition would thus be to target only SOEs that are wholly owned by a state, while a broad definition could include any enterprise in which the state owns a share. In practice, these two outcomes are both extreme and unlikely. Thus, whenever states seek to define SOEs for the purposes of an FTA, a balancing exercise must be undertaken to target SOEs that act in an anti-competitive manner in economic sectors where market-driven efficiency is preferable. What is more, beyond the consideration of a state's share of ownership in a SOE, another element that can be taken into account when defining SOEs is the control of the state over the enterprise.
- [24] See TPP, Art. 17(1) and EUVFTA, Art.1 of the Chapter on SOEs.
- [25] EUVFTA, Art.1 of the Chapter on SOES. Such notion follow the suggestions included in the OECD Guidelines on Corporate Governance of State-Owned Enterprise, as above note 7.
- [26] To be intended as 'activities which an enterprise undertakes with an orientation toward profit-making and which result in the production of a good or supply of a service that will be sold to a customer in the relevant market in quantities and at prices determined by the enterprise', TPP, Art. 17.1.
- [27] These rules are analysed in detail in Leonardo Borlini and Claudio Dordi, "Deepening International Systems of Subsidy Control: The (Different) Legal Regimes of Subsidies in the EU PTAs" in ESIL Working Papers, Interest Group in International Economic Law 2015, forthcoming.
- [28] See Gary N. Horlick and Peggy A. Clarke, "WTO Subsidies Discipline During and After the Crisis", in INTERNATIONAL LAW IN FINANCIAL REGULATION AND MONETARY AFFAIRS, 307, 316 (Thomas Cottier, John H. Jackson and Rosa M. Lastra eds., 2012)
- [29] Henrik Horn, Petros C. Mavroidis and André Sapir, Beyond the WTO: An Anatomy of the EU and US Preferential Trade Agreements, 33 WORLD ECONOMY, 1565-88, 2010.
- [30] Note that several FTAs signed by the USA prior to the TPP include a provision that specifically concerns dispute settlement in their chapter covering SOE disciplines. However, such provisions primarily intend to exclude from the dispute settlement mechanism a fairly narrow set of requirements that do not specifically concern SOE disciplines. Cfr., e.g., USA-Singapore FTA, Article 12.7; USA-Chile FTA, Article 16.8; USA-Australia FTA, above n 35, Article 14.11; USA-Peru FTA, , Article

- 13.10; USA–Colombia FTA, Article 13.10; USA–South Korea FTA, , Article 16.8.
- [31] See TPP, Art. 17(10) and EUVFTA, Art.6 of the Chapter on SOEs.
- [32] Gary Hufbauer, ‘The Urgent Challenges Posed by State-Owned and Assisted Enterprises (SOEs)’ (19 September 2012), 4, at: <https://servicescoalition.org/summit/2-uncategorised/55-global-services-summit-2012> . See also OECD, Guidelines on Corporate Governance of State-Owned Enterprises, above note 7.
- [33] See TPP, Art. 17(4) and EUVFTA, Art.4 of the Chapter on SOEs.
- [34] See TPP, Art. 17(4) and EUVFTA, Art.4 of the Chapter on SOEs.
- [35] TPP, Chapter 17 does not prevent a state to adopt or shall not apply to the following: regulatory and supervisory measures from a central bank or a monetary authority; regulatory or supervisory measures over financial services suppliers; measures adopted for the purpose of a failing or failed financial institution; a Party’s sovereign wealth fund; a Party’s independent pension fund; government procurement; the provision of goods and services by a SOE to carry out a Party’s governmental functions; and the establishment of the maintaining of a SOE.<sup>58</sup> Article 17.2 also stipulates that some specific provisions of Chapter 17 do not apply to any services supplied in the exercise of governmental authorities and other specific purchases or sales of goods and services by SOE. See, particularly, Art. 17-2(2)-(11).
- [36] Ibid, Art.17.9(1).
- [37] Ibid, Art.17.9(2).
- [38] Ibid, Article 17.14 and Annex 17-C.
- [39] Ibid, Article 17.9(3).
- [40] EUVFTA, Art. 2(3)-(9) of the Chapter on SOEs.
- [41] TPP, above n 6, Article 17.13.
- [42] Ibid, Article 17.13(1).
- [43] Ibid, Article 17.13(2)–(4).
- [44] Ibid, Article 17.13(5).
- [45] EUVFTA, Annex I to the Chapter on SOEs.
- [46] Ibidem.
- [47] When considering other FTAs negotiated by the USA, one can observe that such an obligation has often been limited to designated monopolies. In this regard, Article 1502 of NAFTA provides an obligation for each Party to ensure that any privately owned monopoly designated by a state or government monopoly ‘acts solely in accordance with commercial considerations in its purchase or sale of the monopoly good or service in the relevant market, including with regard to price, quality, availability, marketability, transportation and other terms and conditions of purchase or sale’. See North American Free Trade Agreement, 17 December 1992, 32 I.L.M. 289 (entered into force 1 January 1994),
- [48] Appellate Body Report, Canada - Measures Relating to Exports of Wheat and Treatment of Imported Grain, WT/DS276/AB/R, adopted 27 September 2004, DSR 2004:VI, 2739, para 140.
- [49] Ibid, para 144.
- [50] Ibid, para 145.
- [51] See TPP, Art. 17 (4)
- [52] Ibid, Art. 17 (1)
- [53] EUVFTA, Arts. 4 and 1(f) of the Chapter on SOEs
- [54] See State Immunity and State-Owned Enterprises, Clifford-Chance, 2008, p. 14.
- [55] See, ex multis, T. TREVES, International Law. Achievements and Challenges, 2006, Castellonp. 135,
- [56] Borlini and Dordi, above note 27.
- [57] See generally Pierre Sauve’ and Marta Soprana, ‘Learning by Not Doing: Subsidy Disciplines in Services Trade’, E15 Task Force on Rethinking International Subsidies Disciplines – Think Piece (2015), [http://e15initiative.org/wp-content/uploads/2015/04/E15\\_Subsidies\\_Sauve-and-Soprana\\_final.pdf](http://e15initiative.org/wp-content/uploads/2015/04/E15_Subsidies_Sauve-and-Soprana_final.pdf)
- [58] Thomas J. Schoenbaum, ASIL Insights, Vol. 1(2), 1996. As widely known, the theory of contestable markets was advanced by William J. Baumol, an economist, in 1982. He argued that the optimal form of industrial organization is a perfectly contestable market characterized by costless entry and exit. In such a market the entrant would encounter no obstacles in terms of production techniques or perceived product quality relative to the incumbent. Baumol concedes that in the real world costless market entry and exit is not possible, but improving market contestability should, nevertheless, be an important policy goal. The theory of contestable market holds that ease of entry and exit to markets (without intervening

anticompetitive barriers due to government of private restrictions) leads to efficiency, even if there are only a few firms in an industry, because they will be forced to price their products competitively because of the ease of market entry. See further William J. Baumol, *Contestable Markets: An Uprising in the Theory of Industry Structure*, 72 *American Economics Review* (Mar. 1982).

[59] Schoenbaum, above note 58, p. 2.

[60] Americo Beviglia Zampetti and Pierre Sauve, "Onwards to Singapore: The International Contestability of Markets and the new Trade Agenda," 1 *OECD Trade Directorate* (1995).

[61] Space precludes here to mention but some of the forerunners: John H. Jackson, "Alternative Approaches for Implementing Competition Rules in International Economic Relations," 49 *Aussenwirtschaft* 177 (1994); Ernst-Ulrich Petersmann, "Proposals for Negotiating International Competition Rules in the GATT/WTO World Trade and Legal System" 49 *Aussenwirtschaft* 231 (1994); Michael A. Geist, "Toward a General Agreement on the Regulation of Foreign Direct Investment", 26 *Law and Policy in International Business* 673 (1995); Eleanor Fox and Janusz A. Ordovery, "The Harmonization of Competition and Trade Law", 19 *World Competition* 5 (1995); Thomas J. Schoenbaum, "The Theory of "Contestable

Markets" in *International Trade: A Rationale for "Justifiable" Unilateralism to Combat Restrictive Business Practices?"* 30 *Journal of World Trade* (1996).

[62] Mitsuo Matsushita, Thomas J. Schoenbaum, Petros C. Mavroidis, and Michael Hahn, *The World Trade Organization. Law, Practice, and Policy*, 788 (3<sup>rd</sup> ed. 2015), to whom we refer for an in-depth analysis of the WTO provisions which indirectly deal with competition policy and of the relations between trade policy/law with competition policy.

[63] See Horn, Mavroidis and Sapir, above note 29, p. 1565 ff.

[64] See Max Büge, Matias Egeland, Przemyslaw Kowalski, Monika Sztajerowska, "State-owned Enterprises in the Global Economy: Reason for Concern?", (May, 2013) at: <http://voxeu.org/article/state-owned-enterprises-global-economy-reason-concern>, who add: "International trade and investment by state-owned enterprises could well continue to increase as countries with significant state-owned enterprise sectors grow and become more internationalized, or because of advantages state-owned enterprises may enjoy – even though nascent privatisation programmes in some countries pull in the opposite direction."

## Các thỏa thuận thương mại ưu đãi giải quyết vấn đề “cạnh tranh trung lập” giữa doanh nghiệp tư nhân và doanh nghiệp nhà nước như thế nào?

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**Tóm tắt:** Doanh nghiệp nhà nước từ lâu được Chính phủ sử dụng như là một công cụ quan trọng để thực hiện nhiều mục tiêu kinh tế, công cộng và xã hội. Tuy nhiên, mức độ quan trọng của sở hữu nhà nước ở các công ty hàng đầu trên thế giới có ảnh hưởng đối với thương mại quốc tế và cạnh tranh toàn cầu. Bài nghiên cứu giải quyết câu hỏi liệu các Hiệp định thương mại ưu đãi và đa phương có tác động như thế nào đối với các doanh nghiệp Nhà nước nhằm đảm bảo một sân chơi bình đẳng giữa họ và các doanh nghiệp tư nhân, đồng thời cho phép chính quyền hỗ trợ các doanh nghiệp Nhà nước xử lý

thất bại trên thị trường và cung cấp hàng hóa công. Bài nghiên cứu gồm 3 nội dung chính. Phần thứ nhất tóm tắt một số lý do tại sao các doanh nghiệp Nhà nước trở thành đối tượng xử lý của một số công cụ luật pháp quốc tế. Phần thứ hai đánh giá tác động của các thỏa thuận WTO đến hoạt động kinh doanh tiềm năng của doanh nghiệp Nhà nước và làm rõ những hạn chế của thỏa thuận thương mại đa phương. Phần thứ ba phân tích các nội dung liên quan tới doanh nghiệp Nhà nước dưới ảnh hưởng của TTP và EUVFTA - trong đó đại diện là Mỹ và EU - hai PTAs ưu đãi với những quy định cao nhất về vấn đề này. Bài viết kết luận với một ý kiến đề xuất ngắn gọn.

*Từ khóa:* PTAs, SOEs, POEs, cạnh tranh trung lập.