Paper by the Netherlands – A Multilateral Instrument for European resilience and Value-chain Autonomy

Proposal for a comprehensive approach to coordinating targeted finance to reinforce the EU's open strategic autonomy

Introduction

- The Netherlands believes rapid developments on the world stage compel the EU to reduce high-risk strategic dependencies to strengthen European resilience and its open strategic autonomy. Where those developments confront us with attestable resilience and autonomy externalities, we should work together to enable our industries to counter those externalities by developing necessary capabilities they do not (sufficiently) provide. That means creating market activity insufficiently present or altogether absent, inasmuch warranted to protect ourselves from undue foreign influence infringing on the EU's autonomy. In the view of the Netherlands, that means certain well-targeted State aid should be approved in earnest under the conditions presently set out, within the purview of a new, dedicated Multilateral Instrument for European Resilience and Value-chain Autonomy (MINERVA). Conversely, aid should not be approved if, even accounting for flanking measures, no sufficiently viable business case is foreseen, or too little strategic benefit is expected for the EU as a whole. This ensures creating the right economic circumstances for necessary industrial and technological capabilities to be attained in the EU, while remaining true to the European belief that state aid should only be provided restrictively and under well-defined criteria and circumstances. Any aid granted should benefit the EU as a whole. Further details can be found in the explanatory notes accompanying this document.

1. Proposal for targeted measures to mitigate high-risk strategic dependencies

- Fast-evolving dynamics on the global stage require the EU to bolster its open strategic autonomy in order to address strategic contingencies it increasingly faces as a result of third country leveraging of vulnerabilities vis-à-vis the EU.
- Crucially, this requires developing and sustaining minimum level of strategic technological and industrial capabilities in value-chains, or parts thereof, essential for the EU's economic resilience, which are currently insufficiently provided by European undertakings or trusted third-country partners. This more granular approach differs from the more generic (production) level targets often set on a sectoral level.
- A **Multilateral Instrument for European Resilience and Value-chain Autonomy (MINERVA)**, involving the European Commission and all Member States collectively, would enable us to commonly identify capability gaps in specific (parts of) value chains, the addressing of which could require State aid.

<u>1.1 Identifying relevant autonomy issues</u>

- Firstly, we should identify, at EU level, **high-risk EU capability gaps in strategically relevant value chains**, which are dependencies third countries can leverage to infringe on

the EU's autonomous decision-making and sovereignty, as well as opportunities to create positions in strategic value chains to deter foreign powers from infringements on our autonomy.

- As such, any State aid should be preceded by an **evidence-based and targeted approach**, relying on two sets of parameters:
    - First, **value-chain parameters** to identify (parts of) value chains important for European resilience and security. These are:
        1. Economic damage and spillover effects;
        2. Exploitability of willingness to pay in the event of supply security issues;
        3. National security risks;
        4. Contribution to scaling up military production.
    - Two, **capability gap parameters** to identify capability gaps *within* those value chains for which the EU lacks sufficient capabilities, or secure access to such capabilities, for its economic resilience and security. These are:
        1. Limited availability of short-term alternative suppliers;
        2. Limited availability of short-term alternative end products or components;
        3. Limited possibilities of stockpiling;
        4. High barriers to entry for scaling of production (economic and/or technical);
        5. Technical and legal capacity to leverage chain positions for geopolitical purposes;
        6. Asymmetry in interdependence and the relationship with the third country in which there is market concentration;
        7. Comparative disadvantage of harm suffered by the EU/EU target country vis-à-vis the costs incurred by the leveraging third country.
- Filling out these parameters **filters out high-risk strategic dependencies** for which use of State aid could be justified, subject to a per-case analysis with precision on the level of individual value chains or parts thereof. The Netherlands offers a developed framework to substantiate the analysis of the parameters above. These factors are all relevant for setting adequate minimum capability levels at European level as well. Crucially, this enables us to take our policy and financial interventions beyond an abstract, sectoral approach towards a tailor-made, evidence-based approach.

1.2 Consensus on minimum capability levels

- Secondly, to fill these gaps, we must set **minimum capability levels at EU level,** focusing on **high-risk strategic dependencies in specific (parts of) value chains**. These are the levels policy intervention should achieve, thus demarcating the extent of the capability gap. Reaching and maintaining them requires a combined policy approach, including deepening of the internal market and capital markets union, trade policy, and mobilising investments. Public investments often are a crucial part of this mix.
- Sustaining minimum capability levels entails sufficiently diversifying access to crucial capabilities and technologies, so as to avert economic security risks as a result of access denial. As such, said access – either from EU-suppliers or trusted third-country partners

with whom the EU has concluded a free trade or customs union agreement – should explicitly be taken into account in the capability gap analysis (*see capability gap parameters above*). Given that minimum capability levels are to be set for capability gaps identified in accordance with the above-mentioned methodology, there is an **established market failure where minimum capability levels are not yet reached**.

- In some cases, the EU's capability gaps are well-known. Wherever so, we may draw on the analysis already conducted, such as within the ambit of established EU instruments, like the Critical Raw Materials Act, with MINERVA properly connecting State aid with established policy objectives. However, in case capability gaps are revealed at short notice, after the adoption of MINERVA, setting the right capability levels requires broad consensus between to be reached **with involvement of various Commission DG's and Member States being extra important for rapidly setting a capability level for a newly discovered capability gap.**
- In both cases, **the Commission may take the initiative to propose and set minimum levels**, calling in stakeholders, drawing upon its own experiences, and consulting Member States. At all times, a clear view should be maintained to attracting capabilities through trusted third-country partners as a potential solution next to solutions which are developed on the internal market itself.

1.3 The potential of State aid

- Thirdly, a tailor-made, multilateral instrument allows for rapid, streamlined mobilisation of necessary investments the EU presently needs to reinforce its open strategic autonomy. To that end, Member States, in co-operation with the European Commission, should undertake joint assessments and **create the right conditions for State aid to be effective** for the EU to become more strategically autonomous. Such conditions may require pursuing necessary **flanking policy measures**, such as regulatory measures and trade measures as may be warranted on a case-by-case basis. Such measures may be crucial for this type of aid to be effective.
- **Any aid granted should benefit the EU as a whole**, by securing strategic capabilities accessible to a wide, cross-Member State industrial and economic base. As such, the Instrument should form the analytical basis and approval methodology to find out *if* State aid is the right answer in the given case; and if so, what interventions are needed to realise a strategic benefit with granting that aid. This entails a thoughtful analysis of a given potential business case – accounting for necessary flanking measures – as well as a strategic benefit for the EU as a whole. Absence of either should preclude granting State aid under the denominator of strategic autonomy.
- On the basis of the above analysis, State aid may be used to fill those capability gaps and attain minimum capability levels, while effectively mitigating risks to the internal market and taking trusted third-country capabilities into account. This is corroborated by the fact that for the target value chains (or parts thereof), there is **no or next to no capability on the EU market**. Therefore, where the Commission and Member States together carefully find such a gap and can create right circumstances to fill it, a significantly more expedient approval trajectory may be adopted.

2. Necessity of a new, dedicated instrument: MINERVA

- The Netherlands believes **the introduction of a dedicated State aid mechanism is justified** for identifying capability gaps and creating the right conditions for State aid to help filling those gaps, so to contribute to the EU's open strategic autonomy while avoiding unnecessary State aid. While the Netherlands recognises other State aid instruments, such as CISAF and IPCEI, may collaterally contribute to strengthening the EU's economic resilience and open strategic autonomy, the Netherlands notes only a dedicated, new instrument is capable of effectively addressing high-risk strategic dependencies while preventing unnecessary distortion of the level playing field on the internal market.
- Firstly, strengthening the EU's value-chain autonomy is an inherently different objective than that for which existing instruments were designed, such as innovation, competitiveness, or the green transition. Consequentially, a State aid instrument addressing economic resilience requires a **dedicated problem analysis** and a **different analytical framework**.
- Secondly, a State aid instrument addressing high-risk strategic dependencies must be conditioned for that specific purpose. This entails **creating the right conditions for State aid to help fill capability gaps**, so to contribute to the EU's open strategic autonomy while avoiding unnecessary State aid. This enables an evidence-based approach which the Netherlands has consistently held is necessary.
- Thirdly, strengthening economic resilience and value-chain autonomy may require different types of State aid interventions, with **a European point of view and the right procedural backing**: to identify capability gaps, define minimum capability levels and ascertain whether a specific aid measure effectively addresses a capability gap for the EU as a whole.
- Effectively, MINERVA may present a **solution for geopolitically and strategically relevant projects** which may have been unable to attract (necessary) public financing, coherently flanked by other necessary policy interventions.
- For these reasons, State **aid approval for value-chain resilience should be granted only based on MINERVA**. Among other things, this ensures approval for aid for that specific purpose is granted only under the right conditions and with the proper guarantees in place to ensure there is no fragmentation of State aid rules in different sectors.
- By extension of the above, with the introduction of MINERVA, **existing aid frameworks can return to their respective primary purposes,** such as the green transition. To that end, we call on the Commission to sharpen those existing aid frameworks, so to realign them to principally serve their primary purpose.

3. Member State involvement

- **Member State involvement is indispensable in four specific aspects in aid approval on the level of individual aid cases**. As such, only a governance structure with roles for both the Commission, including its various DGs involved, and Member State can thus ensure the right approach integrating state aid and other policy interventions.
    - Firstly, Member States possess knowledge and insights into their industries vital for accurately and timely identifying any high-risk strategic dependency. This may

include highly sensitive and classified information. Thus, **strategic issues can only be identified commonly**.

- Secondly, casuistic experience has demonstrated a need for **a forum to bring key information to the table** confidentially and in a structured fashion, ensuring access to all relevant data and intelligence as much as possible in a confidential manner.
- Thirdly**, broad consensus is required to find the right way forward** to address specific high-risk dependency problems, such as setting the right minimum capability levels for the right value chains, thereby accepting compatibility with the internal market of certain aid measures. This is particularly so in case strategic caps reveal themselves at short notice through Member State casuistic experience, after adoption of MINERVA, precluding the opportunity to set minimum capability levels in advance at the time of adopting the instrument.
- Fourthly, aid approval for strategic autonomy requires **maximisation of pan-European compatibility of capabilities** to be developed with state aid. To that end, Member States must have the opportunity to confirm such compatibility, confirming such EU-wide strategic benefit.

- As such, the Netherlands considers Member State involvement a pre-requisite in two, specifically limited steps in the approval trajectory (see also below on the functioning of MINERVA):
    1. **Clearing the way for aid approval by co-establishing a market failure** by first reaching consensus with the Commission DG's responsible that there is a capability gap and commonly establishing sufficient expectation that a particular aid measure proposed may help reaching or maintaining a minimum capability level. From there, DG COMP may **safely presume a pre-determined market failure and little to no distortion of the internal** market, both of which may meaningfully accelerate aid approval as well.
    2. **Verifying *ex post* that the aid measure secures capabilities for the EU as a whole**, confirming the aid conditions are tailored such for those capabilities to reach beyond merely a limited number of Member States.
- For all other matters, the State aid approval trajectory should **remain fully the responsibility of the Commission** given its exclusive competence on State aid.
- For these reasons, the Netherlands believes the new instrument proposed should be **based on point e) of Article 107(3) TFEU**. This legal basis is uniquely positioned to serve the designed instrument and can be relied on by a Commission proposal and a Council decision. By way of alternative, the Netherlands sees a limited option that point b) could be used.

4. Relation with other policy instruments

- Various sectoral instruments cover parts of critical strategic value chains, including the NZIA, the Chips Act (including its recast) and the Critical Raw Materials Act (including its proposed revisions).

- Firstly, each of these instruments is based on a specific sectoral problem analysis, but **not on an overarching evidence-based framework** for addressing strategic capability gaps principally irrespective of the nominal sector the value chain pertains to. As such, MINERVA offers a coherent, integral and interlocking framework.
- Secondly, **these instruments do not constitute State aid instruments**. As such, national aid measures depend on specific State aid instruments for approval or approval directly under the TFEU. Here, the MINERVA instrument plugs an important gap.
- Thirdly, the relevant policy instruments, to varying degrees, **serve more and other policy objectives in relation to the specific sectors they address**, such as competitiveness and the green transition. As such, their scope partially covers value chains not necessarily containing capability gaps and partially leave out value chains that may contain them.

5. Functioning of MINERVA

- A focus on high-risk capability gaps, a combined approach of resolving them and a more pronounced role and responsibility for Member States, in cooperation with the Commission, are all pre-requisites for effective, expedient and non-distorting use of State aid. Therefore, the new aid instrument the Netherlands proposed should be based on the following key components.
- A pre-requisite for effective use of any State aid is a methodologically sound **identification of relevant value chains and high-risk capability gaps within those value chains** at the EU level by the Commission. The necessity to include a certain value chain in the aid instrument should be determined beforehand using the above-mentioned **value-chain risk parameters** and **capability gap parameters**. Any aid should fill capability gaps within those value chains.
- Next, the instrument should be designed so to only approve aid measures that fill those capability gaps. This entails at least the following:
- First, setting **minimum capability levels proposed and set by the Commission, consulting Member States in the process**. These minimum levels should account for diversification and trusted third countries.
- Second, the pinpointing of **specific projects or activities** within a value chain by a Member State that may help to increase supply and/or access for the EU considered as a whole, based on local opportunities, up to the EU's defined minimum capability level.
- Third, a preliminary consultation requirement for the initiating Member State to ensure a **sufficiently substantial number of Member States** confirming whether the specified project or activity addresses a capability gap.
- Fourth, a **necessity and proportionality assessment**. This assessment entails demonstrating that alternative policy instruments and different aid instruments do not suffice to build capabilities is necessary. Furthermore, a proportionality assessment should include an **assessment of the (long-term) economic viability and business case of the project**. Crucially, this assessment should be conducted not only in light of current market circumstances, but also for **flanking measures** the EU may needs to take in order to **create the long-term economic viability required**. Targeting finance to fill capability

gaps may meaningfully accelerate the assessment of aid, since the existence of such a gap confirms there is little to no market activity by EU undertakings to be distorted in the first place, and points to a clear, pre-determined market failure.

- Fifth, a **centralised coordination mechanism** in which the Commission, together with a committee of all Member States, assess initiatives to grant aid to a project or activity is capable of effectively attaining the relevant EU's minimum capability level and ensuring strategic benefits for the EU as a whole.
- Sixth, a series of **generic, minimum requirements** for approving any aid, at least insofar precluding aid with ancillary conditions that may disproportionally favour the initiating Member State and aid covering operating costs.
- Finally, a **fixed duration of the instrument**, five years in principle, to be extended only after due evaluation.