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II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 30 October 2001

on the State aid granted by Germany to Graf von Henneberg Porzellan GmbH, Ilmenau

(notified under document number C(2001) 3303)

(Only the German text is authentic)

(Text with EEA relevance)

(2002/865/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 88(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above ⁽¹⁾ and having regard to their comments,

Whereas:

I. PROCEDURE

- (1) By letters dated 16 November 1998 and 24 March 1999, the Commission received complaints from competitors alleging misuse of purported State aid granted to Graf von Henneberg Porzellan GmbH located in Ilmenau, Thuringia.
- (2) Following an information request by the Commission on 6 January 1999, Germany submitted replies on 3 and 25 May 1999. After further information provided by complainants and a meeting between Commission officials and the German authorities on 23 September 1999, the Commission requested on 30 September 1999 that the case be notified. After the Commission had sent a reminder on 9 November 1999, Germany submitted further information, but refused to notify the aid. On 10 November 1999, the case was registered as non-notified aid NN 135/99.

⁽¹⁾ OJ C 272, 23.9.2000, p. 30.

- (3) By letter dated 13 July 2000, the Commission informed Germany that it had initiated the procedure laid down in Article 88(2) of the EC Treaty in respect of the aid. At the same time Germany was enjoined to provide all necessary information and data to allow assessment of whether a number of aid measures complied with the terms of approved aid schemes under which they had allegedly been granted.
- (4) The Commission decision to initiate the procedure was published in the *Official Journal of the European Communities* ⁽²⁾. The Commission invited interested parties to submit comments on the aid. The Commission received comments from an association of the European ceramics industry (Cérame-Unie) and from the undertaking. These comments were forwarded to Germany by letter dated 18 December 2000.
- (5) On 18 September 2000, Germany responded to the information injunction and informed the Commission of further aid measures, which had not been notified before. The Commission posed questions on 13 November 2000. Replies were received on 19 December 2000. A meeting with representatives of the German authorities was held on 9 January 2001. Further questions were sent out on 24 January 2001. Replies were received on 6 March 2001.
- (6) By letter dated 25 April 2001, the Commission informed Germany that it had extended the procedure laid down in Article 88(2) of the EC Treaty to those aid measures which did not comply with the terms of the approved aid schemes under which they had been allegedly awarded as well as to those aid measures of which the Commission had not been informed before.
- (7) The Commission decision to extend the procedure was published in the *Official Journal of the European Communities* ⁽³⁾. The Commission invited interested parties to submit their comments on the aid. The Commission received comments from one of the complainants as well as from the aid recipient. By letters dated 28 and 30 August 2001, these comments were forwarded to Germany, which was given the opportunity to react.
- (8) On 28 June 2001 Germany replied to the extension of the formal investigation procedure submitting extensive information on the relevant aid measures.

II. DETAILED DESCRIPTION OF THE AID

A. The company

- (9) Graf von Henneberg Porzellan GmbH manufactures porcelain dishes and china. It is located in a region eligible for aid under Article 87(3)(a) of the EC Treaty. The following data on its operation correspond to the management reports submitted to the Commission:

(in DEM million)

	1992	1993	1996	1997	1998	1999	2000
Employees	625	563	334	309	296	269	210
Turnover	20,756	11,584	19,417	21,039	18,507	16,840	17,677
Assets	96,891	80,522	17,221	23,780	25,410	26,264	16,843
Operating result	- 32,607	- 14,227	- 2,999	- 2,292	- 3,730	- 1,299	0,024

⁽²⁾ See footnote 1.

⁽³⁾ OJ C 211, 28.7.2001, p. 27.

- (10) The company was created on 1 March 1990 by transforming the *volkseigenen Betrieb* Henneberg Porzellan Ilmenau into a private limited company under the name Graf Von Henneberg Porzellan GmbH (GvH1). It was registered at the Meiningen Local Court on 23 August 1990 under number HRB 327.
- (11) On 23 August 1991, the Treuhandanstalt (THA) privatised GvH1 after an open call for tender by selling it for DEM 7,5 million to Mr Jamalian. The sale was conditional upon payment of the purchase price, though the THA waived this condition on 17 September 1992. On 18 September 1992, Mr Jamalian became sole manager and shareholder of the company.
- (12) On 7 January 1993, the THA revised the privatisation contract, waiving the payment of the purchase price and to certain other obligations agreed upon privatisation. Mr Jamalian agreed to increase the company's capital by DEM 7,5 million. This capital increase never took place.
- (13) On 11 July 1995, GvH1 filed for bankruptcy. By the end of that month the Thuringia Landesentwicklungsgesellschaft (LEG) requested a consultancy firm, Project Management Eschbach (PME), to propose a solution for the company including a state participation. On 17 August 1995, the Meiningen local court initiated bankruptcy proceedings (*Gesamtvollstreckungsverfahren*) and the undertaking became Graf von Henneberg Porzellan in Abwicklung (GvHiA). On 24 August 1995, PME presented its proposals to local authorities and representatives from the State-owned Thuringia Industriebeteiligungs GmbH & Co. KG (TIB), including Mr Frowein, then employee of the TIB. According to Germany, the administrator in bankruptcy continued business activities and sought an investor. Germany states that some potential investors showed interest, but none made an offer. On 30 November 1995, all employment contracts with the workforce were cancelled.
- (14) On 18 December 1995, a new company was created under the same name: Graf von Henneberg Porzellan GmbH (GvH2). GvHiA took over 51 % and the TIB 49 % of the shares. GvH2 was set up with capital of DEM 1 million, of which DEM 0,51 million was contributed by GvHiA and DEM 0,49 million by the TIB. According to Germany, GvH2 was no longer in difficulty. On 1 January 1996, the majority of the workforce of GvHiA was taken over by GvH2. On 8 January 1996, GvH2 acquired the assets⁽⁴⁾ of GvHiA for DEM 8,5 million. The price was fully financed through a loan from the Thuringia Aufbaubank (TAB). This price was indicated in a report by PME, but without any explanation of how it was determined. On 18 January 1996, the company was registered at the Meiningen Local Court under number HRB 3738.
- (15) According to Germany, an investor had been sought since GvH2 was set up, but none was found until 28 August 1998, when all the shares in GvH2 were sold to Mr Frowein for DEM 0,2 million. There is no indication of how this price was determined. After this share deal, Germany refers to the company as GvH3. According to the press, in September 1999 Mr Frowein acquired the shares in Glashütte Schmiedefeld GmbH, a competitor involved in bankruptcy proceedings, and the company with 30 employees became a subsidiary of GvH2/3 producing glass.

B. The restructuring

(a) Restructuring plans for GvH1

- (16) The first plan devised by the THA and adapted by Mr Jamalian stretched from the second half of 1990 to 1993. Its main points were: concentration on the new *Bundesländer* and east European markets; positioning of the trade mark 'Graf von Henneberg' in the low/middle price segment; reduction of costs (personnel, material and energy); improvement of efficiency (training, computerisation, new ordering and distribution system, recycling, reorganisation of stock); improvement of productivity. The plan foresaw investments of DEM 22,259 million, covering of losses of DEM 44,410 million and interest payments of DEM 8,927 million. It was to be financed by credits of some DEM 60 million and amortisation of debt.

⁽⁴⁾ With the exception of some real estate which, according to Germany, was sold.

	(in DEM million)		
	1991	1992	1993
Turnover	20,950	35,540	44,910
Operating result	- 17,929	- 8,525	2,260

- (17) By the end of 1992, GvH1 lost orders from Russia and Iran and faced the failure of an oven, which led to an acute crisis and to a revision of the plan for the period 1993 to 1996. Its key points were: reorganisation of GvH1's structure; reduction of costs, personnel and surface; direct distribution of products and telephone marketing in Germany; design of a new distribution strategy for south European markets. It was pointed out that without new liquidity, insolvency would be unavoidable. The plan was contingent upon a capital contribution of DEM 7,5 million by Mr Jamalian, which never took place.

	(in DEM million)			
	1993	1994	1995	1996
Turnover	14,138	40,865	46,478	49,668
Operating result	1,669	- 0,564	0,928	1,443

(b) *Restructuring plans for GvH2/3*

- (18) Three reports by PME were presented as the first restructuring plan for GvH2. A first report presented several scenarios involving a combined solution for several porcelain manufacturers in Thuringia, though this was not the solution chosen. A part of a second report analysed a model for the continuation of the company. This was given substance in a third report, a cost analysis forecasting results for 1996 to 1997 on the basis of the TIB participation. Its main points were: sale of the assets for DEM 8,5 million; between 317 and 329 employees (plus 8 trainees); outsourcing of mass production of porcelain in 1997; 4 % price increase; reorganisational measures (concentration of production eliminating several areas and reducing surface, saving energy, investments of DEM 4,685 million and repairs). Three possible results for 1996 to 1997 were forecast depending on possible turnover figures.

	(in DEM million)					
	1996			1997		
Turnover	27,869	29,852	31,835	29,927	31,901	33,874
Operating result	- 2,860	- 2,238	- 0,872	- 0,161	0,432	1,197

- (19) Following the takeover by Mr Frowein, the plan was revised. The reasons identified for the failure of previous restructurings were mismanagement, over optimistic forecasts and non-implementation of the restructuring plans. A set of short-term measures were designed for stabilisation: staff cutbacks affecting mainly management positions and creation of a profit centre in charge of logistics. A set of medium-term measures were intended for consolidation: diversification of production, direct distribution, cooperation with porcelain manufacturers and investments of DEM 3 million.

- (20) The revision had foreseen cumulated losses of DEM 0,8 million as at June 1998. However, two months later losses amounted to DEM 3,169 million and no cooperation with other manufacturers had been set up. The plan was again revised, foreseeing moderate growth based on the strengthening of porcelain production for hotels, an increase in production in Germany, the stabilisation of exports and investments of DEM 1,750 million.

(in DEM million)		
	1999	2000
Turnover	22,960	25,488
Operating result	0,352	1,547

C. The financial measures

- (21) The following tables list all the financial measures taken in support of GvH1, GvHiA and GvH2/3. It should be noted that the amounts and dates indicated correspond to the latest information submitted by Germany.

(a) *Financial measures in support of GvH1:*⁽⁵⁾

(in DEM million)				
Measures in support of GvH1				
				Amount
Measures within privatisation				
1	23.8.1991	THA	Takeover of old debts	24,051
2	23.8.1991	THA	Takeover of credit DB Ilmenau	22,690
3	23.8.1991	THA	Takeover of credit DB Ilmenau (Russia)	0,174
Measures after privatisation				
4	9.12.1991	Land	Direct investment grants	6,812
5	17/24.8.1992	HeLaBa	Investment credit (security pool)	10,000
6	13.8.1992	Berliner Industriebank	80 % subsidiary guarantee	
7	4.9.1992	Bayerische Landesbank	Investment credit (security pool)	10,000
8	4.9.1992	Bayerische Landesbank	ERP-loan (security pool)	1,000

⁽⁵⁾ Guarantees relating to credits, the full amount of which is included in the total, have not been included to avoid double counting. The guarantee under measure 10 has been included since the credits to which it relates seem not to be any of those included in the table.

(in DEM million)

Measures in support of GvH1

				Amount
Measures within revision privatisation contract				
9	7.1.1993	THA	Waiver purchase price	7,500
10	XX.10.1991	THA	Guarantee	8,629
11	7.1.1993	THA	Grants	13,871

Other measures

12	23.3.1993	Bayerische Landesbank	Loan (90 % subsidiary guarantee)	15,000
13	28.9.1993	Land	SME grant	5,000
14	28.9.1993	Th. Min. Econ. Transport	Non-reimbursable subsidy for liquidity	
15	16.12.1993	Land	90 % subsidiary guarantee on 10 million.	
16	16.12.1993	Land	90 % subsidiary guarantee on 10 million.	
17	12.1.1994	Bayerische Landesbank	Line of credit (90 % subsidiary guarantee)	10,000
18	2.2.1994	Bayerische Landesbank	Loan (security pool)	8,023
19	24.5.1994	Land	90 % subsidiary guarantee on 15 million.	
20	26.9.1994	HeLaBa	Loan (security pool)	8,530
21	20.10.1994	HeLaBa	Line of credit (90 % subsidiary guarantee)	10,000
22	23.6.1993	Sparkasse Ilmenau	Line of credit (security pool)	3,200
23	14.6.1993	Sparkasse Erfurt	Loan	1,500
24	20.1.1995	TAB	Advance payment for real estate	2,000
25	1991-1995	Land	Investment tax refunds	1,857
26	1992-1995	Federal Ministry of Economy	R & D grant	0,472
27	1992-1995	Federal Labour Office and Land	AFG Measures	2,077
TOTAL				172,386

Measures taken by the THA

- (22) *Measures 1 to 3*: three different debts taken over by the THA: old debts dating from before 1 July 1990 and credits from the Deutsche Bank Ilmenau.
- (23) *Measure 9*: the payment of the purchase price was postponed several times and finally waived upon revision of the privatisation contract.
- (24) *Measure 10*: a guarantee of DEM 8,629 million including interest and a processing fee.
- (25) *Measure 11*: According to Germany these grants were paid in compensation for losses of DEM 17,5 million generated by a loss of orders from Russia and for losses of DEM 26,337 million due to a defective oven. The THA agreed originally to pay DEM 25 million. According to Germany, only DEM 13,871 million were paid out. The outstanding amount was offset against the guarantee above.

Measures taken by the Land of Thuringia

- (26) *Measure 4*: direct investment grants of DEM 6,812 million.
- (27) *Measure 13*: a grant of DEM 5 million.
- (28) *Measures 15, 16 and 19*: 90 % subsidiary guarantees covering credits under measures 12, 17 and 21.
- (29) *Measure 25*: investment tax refunds of DEM 1,7 million.

Measures from State-owned financial entities

- (30) *Measures 5, 20 and 21*: credits from the Hessische Landesbank (HeLaBa).
- (31) *Measure 6*: an 80 % guarantee from the Berliner Industriebank, now Deutsche Ausgleichsbank (DtA), amounting to DEM 7,68 million.
- (32) *Measures 7, 8, 12, 17 and 18*: credits from the Bayerische Landesbank. Measure 12 was an advance financing for the grants under measure 11 expected from the THA.
- (33) *Measures 22 and 23*: credits from the Sparkassen Ilmenau and Erfurt.
- (34) *Measure 24*: an advance payment of DEM 2 million for real estate allegedly worth DEM 4,6 million, which was to be taken over by the Thuringia Finance Ministry. The price was determined by a public real estate agency.

Other measures

- (35) *Measure 14*: a non-reimbursable subsidy for short-term liquidity. Germany states that this subsidy was never granted, consequently its amount has been eliminated from the table above.
- (36) *Measure 26*: grants for R & D from the Federal Ministry of Economic Affairs.

- (37) *Measure 27: grants under a programme for the promotion of employment, Labour Promotions Law (Arbeitsförderungsgesetz, 'AFG').*

Securities

- (38) Credits under measures 5, 7, 8, 18, 20 and 22 were assured within a security pool subscribed by the awarding banks. The following securities were provided: a first, second and third range mortgage on GvH1's real estate valued at DEM 5 million, DEM 16 million and DEM 17,2 million respectively, the 80 % subsidiary guarantee under measure 6 and a mortgage on GvH1's machinery and installations (valued at DEM 2,280 million by an expert). In addition personal guarantees by Mr Jamalian were provided to each bank.

- (39) Credits under measure 12 ⁽⁶⁾ 17 and 21 were assured by State guarantees covering 90 % of the risk of default.

(b) *Claims registered as part of the estate of bankruptcy and financial measures in favour of GvHiA*

- (40) The Bayerische Landesbank registered claims of some DEM 47 million plus cumulated interest.
- (41) The Federal Institute for Special Tasks associated with Unification (the BvS) registered some DEM 1,430 million. According to Germany, DEM 0,942 million as revenue from the sale of real estate (see measure 30 below), DEM 0,4 million as compensation for damages which had been agreed to within the revision of the privatisation contract and interest.
- (42) The Federal Ministry of Economic Affairs registered claims of DEM 0,467 million plus interest (measure 26).
- (43) The HeLaBa registered claims of some DEM 31,707 million. According to Germany this amount consisted of measures 5, 20 and 21 plus interest on arrears.
- (44) The Sparkasse Ilmenau registered its credit under measure 22 plus interest.
- (45) The Sparkasse Erfurt registered claims of some DEM 1,995 million plus interest. The information submitted specified only credits of DEM 1,5 million. It thus seems that a further DEM 0,4 million had been granted to GvH1 by this entity. Germany has provided no explanation for the difference.
- (46) The TAB registered DEM 8,824 million, of which some DEM 2 million corresponded to measure 24 plus interest. According to Germany the remaining amount related to direct investment grants under measure 4, which the TAB registered for the *Land* of Thuringia.
- (47) The Commission further notes that the town of Ilmenau registered claims on taxes from the period 1991 to 1995 of DEM 0,557 million as part of the estate in bankruptcy.
- (48) The information available indicates that the State was the main creditor of GvH1. There is some indication that some of the amounts were collected as part of the bankruptcy proceedings, but, on the basis of the information available to it, the Commission cannot determine the exact amounts collected by the relevant lenders.

⁽⁶⁾ This credit was an advance on the THA grants under measure 11. It was fully made available and does not seem to have been claimed back as the grants were reduced, nor at the end of the two months for which it was awarded. On the contrary, it was prolonged at least six months.

(c) *Financial measures in support of GvHiA* ⁽⁷⁾

				(in DEM million)
Measures in support of GvHiA				Amount
28	00.7.1995	HeLaBa	Loan (50 % guarantee)	2,000
29	00.7.1995	TAB	50 % guarantee on 2 million	
30		BvS	Waiver revenues sale of real estate	0,940
TOTAL				2,940

(49) *Measure 28*: a loan of DEM 2 million which, according to Germany, was paid back on 30 June 1996.

(50) *Measure 29*: the loan referred to in paragraph 49 was guaranteed up to 50 % by the TAB.

(51) *Measure 30*: the privatisation contract, as amended in 1993, provided that certain real estate of GvH1 was to be sold and the price paid to the THA. On this basis, DEM 0,942 million were registered as part of the estate of bankruptcy, presumably 9 % of the proceeds on the sale of real estate not taken over by GvH2. This debt was waived by the BvS within the bankruptcy proceedings.

(d) *Financial measures in support of GvH2/GvH3* ⁽⁸⁾

				(in DEM million)
Measures in support of GvH2/GvH3				Amount
31	18.12.1995	TIB	Participation	0,490
32	4.1.1996	TIB	Shareholder loan	0,500
33	12.2.1996	TAB	Credit (financing purchase price)	8,521
34	26.2.1996	TAB	Credit	3,000
35	19.9.1996	TAB	Investment credit	4,000
36	22.11.1996	Land	Investment grants	5,981
37	15.12.1997	TAB	Credit	2,000
38	15.12.1997	TAB	Credit for loss cover	3,000

⁽⁷⁾ The guarantee under measure 29 has not been included since it relates to the credit under measure 28, which has been fully included.

⁽⁸⁾ the amount of measure 43 has not been included in the total because it relates to credits, the full amount of which has been included in the total.

				(in DEM million)
Measures in support of GvH2/GvH3				Amount
39	1996-1999	Federal Labour Office + <i>Land</i>	AFG measures	2,044
40	1996-1999	<i>Land</i>	Investment allowances	0,090
41	12.8.1999	TAB	Waiver position on credits	
42	1996-2000		Grants	0,215
43	1997-2000	Federal Ministry of Economy	Grants R&D	0,451
			TOTAL	30,292

Measures from State-owned entities

- (52) *Measure 31*: a participation by the TIB in GvH2's initial capital.
- (53) *Measure 32*: a loan from the TIB of DEM 0,5 million. According to Germany the loan was paid back the same month as it was granted, including interest.
- (54) *Measure 33*: a loan from the TAB for the purchase of assets. Germany states that part of this loan was paid back through direct investment grants (measure 36 below).
- (55) *Measures 34, 35, 37 and 38*: credits from the TAB.
- (56) On 27 August 1998, the TAB offered to waive the repayment of DEM 11,467 million against future profits to be generated between 1998 and 2002 (Besserungsschein) capped at DEM 2 million. However, this offer has not yet been accepted and will therefore not be assessed.
- (57) *Measure 41*: the TAB renounced to its position in the list of creditors for credits under measures 33 and 35 to avoid insolvency.

Measures taken by the *Land* of Thuringia

- (58) *Measure 36*: direct investment grants.
- (59) *Measure 40*: investment allowances of DEM 0,090 million granted until 1998. The Commission has not been informed on whether a further DEM 0,023 million, demanded for 1999, have been paid out.

Other measures

- (60) *Measure 39*: GvH2, as legal successor of GvH1, obtained grants of DEM 2 044 million under the AFG programme for the promotion of the employment.
- (61) *Measure 42*: a series of grants awarded from 1996-2000.
- (62) *Measure 43*: grants for R & D awarded from 1997-2000.

D. The market

- (63) Graf von Henneberg GmbH produces china and porcelain dishes for the household sector and for professional use, in particular for hotels and decorators (NACE 26.21). Products are also exported.
- (64) In the relevant economic sector of tableware and decorative porcelain there is intensive trade among Member States. While decorative porcelain is produced throughout Europe, important regional concentrations of tableware producers exist in Northern Bavaria (Germany), Staffordshire (United Kingdom) and the Limousin (France). Next to a plethora of SMEs, there is also a number of large undertakings. The latter include Villeroy & Boch (Germany/Luxembourg), Hutschenreuther and Rosenthal (Germany) and Royal Doulton and Wedgwood (United Kingdom), which account for more than a third of overall production in the Community. The special requirements of the hotel and catering trades have given rise to the 'hotelware' sector, with specially designed hard-wearing ceramics. The United Kingdom, Germany and Italy are the main producing and consuming countries. A close relationship to the final-consumer and the need to compete on design are special features to this very labour-intensive industry, with its enormous array of products. Sales to third countries exceed European imports in value; imports in tonnage are, however, at a higher level than exports mainly due to the extremely low-price imports from China ⁽⁹⁾.
- (65) There is overcapacity in the porcelain industry. Production and consumption both registered continuing growth between 1984 and 1991, but contracted in 1992 and 1993. A recovery expected for 1994 did not occur. The trade balance of the last years was positive, but the share of imports increased markedly, in particular for household china. The growth of exports is not sufficient to offset the increasing competition in the sector. On the contrary, strong competition and overcapacities have been reinforced due to new market entrants from South-East Asia and Eastern European countries, in particular Czech Republic and Hungary, all benefiting from preferential trading arrangements with the Community ⁽¹⁰⁾.

III. GROUNDS FOR INITIATING THE FORMAL INVESTIGATION PROCEDURE

- (66) In its initiation of the formal investigation procedure, the Commission analysed the financial measures in support of GvH1, GvHiA and GvH2 in the light of Article 87(1) of the EC Treaty and Article 61(1) of the EEA Agreement. The Commission considered that the measures constituted aid and seriously doubted their compliance with the common market.
- (67) The Commission also doubted whether a number of aid measures complied with the terms of the approved aid schemes under which they were purportedly granted. The Commission therefore issued an information injunction within the context of the initiation of the formal investigation procedure.

⁽⁹⁾ Data extracted from the website of Cerame-Unie (<http://www.cerameunie.org>).

⁽¹⁰⁾ Panorama of EU Industry 1997, 9 to 20; NACE (Revision 1). See also Commission Decision 1999/157/EC in Case C 35/97, Triptis Porzellan GmbH (OJ L 52, 27.2.1999, p. 48).

- (68) Following the information supplied by Germany after the initiation of the formal investigation procedure, the Commission found that details of numerous measures had not yet been notified. The information submitted also did not dispel the Commission's doubts regarding the compliance of the aid allegedly granted under approved aid schemes with the relevant schemes. Consequently, the Commission extended the formal investigation procedure to cover these measures.

IV. COMMENTS FROM INTERESTED PARTIES

- (69) Within the context of the initiation of the formal investigation procedure, the Commission received comments from an association of the European ceramic industry (Ceramie-Unie) and from GvH3. These comments were forwarded by letter dated 18 December 2000 to Germany, which was thus given the opportunity to react.
- (70) Within the context of the extension of the formal investigation procedure, the Commission received comments from one of the complainants stating that he had not been allowed to make an offer for the assets of GvH1. Comments were also received from the aid recipient. These comments were forwarded to Germany by letters dated 28 and 30 August 2001.

V. COMMENTS FROM GERMANY

- (71) Germany responded to both the initiation and the extension of the formal investigation procedure, pointing out that GvH1 and GvH2 were different undertakings without continuity, which should be treated within different proceedings. Germany further stated that the financial measures in support of GvH1 either did not constitute aid or constituted existing aid. As regards GvH2, Germany stated that it has never been a company in difficulty, hence financial measures in support of it either did not constitute aid or constituted existing aid or should be regarded as *de minimis* aid.
- (72) Germany submitted no reaction to the comments from interested parties received within the context of the initiation of the formal investigation procedure. As regards those received within the context of the extension of the formal investigation procedure, in its responses of 5 and 21 September 2001 Germany supported the information submitted by the undertaking and denied that any competitor had been excluded from the sale.

VI. ASSESSMENT

A. Aid within the meaning of Article 87(1) of the EC Treaty

- (73) Financial assistance deriving from public resources was awarded to GvH1, GvHiA and GvH2/3, giving these entities advantages over their competitors. As the porcelain market is a highly competitive European product market suffering from overcapacity, financial advantages favouring a company in respect to its competitors threaten to distort competition and affect trade between Member States.
- (74) In its extension of the formal investigation procedure, the Commission concluded that measure 1 did not constitute aid. The remaining measures were still regarded as State aid. Germany has not contested the Commission's view expressed in its initiation and extension of the formal investigation procedure that GvH1 and GvHiA were companies in difficulty. Germany insists, however, that part of the measures do not constitute aid. The Commission substantiates its view again below.

- (75) *Measures 9 and 11*: Germany first claimed that these measures were covered by the relevant THA-regime. When the Commission found that they manifestly were not covered by this scheme, Germany alleged that they did not constitute aid. According to Germany, the THA should have been held responsible for the losses generated by the loss of orders from Russia and by those due to a defective oven. In Germany's view, the THA risked incurring higher losses in confronting Mr Jamalian in court, since Mr Jamalian threatened to annul the privatisation contract rather than accepting the revision of the privatisation contract. Germany states that the award of these measures was in line with the behaviour of a private investor.
- (76) The privatisation contract did not provide for any obligation to indemnify for a loss of orders. By the end of 1992 when the orders were lost the privatisation to Mr Jamalian was already effective. There is therefore no justification for the THA being held responsible for those losses, nor for Mr Jamalian annulling the privatisation contract on that basis. As regards the indemnification for a defective oven, the privatisation contract provided that all warranty liabilities would be limited to 10 % of the purchase price and that the THA's liability would expire three months after the discovery of the failure, by 31 December 1992 at the latest. The Commission has not been informed when the failure was discovered or when legal actions against Mr Jamalian were undertaken. No calculations or reports justifying that the amount paid effectively amounted to a fair indemnification have been provided. Finally, the settlement took place after the THA's warranty liability expired and the compensation exceeded the limit provided for in the privatisation contract. Therefore the Commission cannot conclude that these measures do not constitute aid.
- (77) As far as measure 9 is concerned, the waiver of the purchase price was carried out in favour of Mr Jamalian, and the Commission does not therefore consider this aid to GvH1.
- (78) *Measure 10*: this guarantee from the THA was first claimed to fall under the relevant THA-regime. When the Commission established that it was manifestly not covered by this aid scheme, Germany alleged that it did not constitute aid. Germany stated that GvH1's real estate should have allowed the company to obtain liquidity from banks. However, due to unforeseen administrative delays in transmitting property, the real estate was not immediately available free from encumbrances and the THA awarded this guarantee to allow GvH1 obtain liquidity.
- (79) The Commission notes, however, that the privatisation contract did not impose on the THA any obligation to ensure that GvH1 obtained liquidity. Moreover, the THA was not obliged to compensate for administrative delays that were not its responsibility. The Commission notes the lack of a contractual basis for the award of this guarantee and hence cannot verify its purpose or extent. It is moreover noted that the guarantee was made available only when the real estate became available, but no later than 1994. The Commission hence considers that this is an extra advantage in favour of GvH1, not based on any legal obligation, not in line with the aim for which it was purportedly awarded and not reflecting the behaviour of a market economy investor.
- (80) *Measures 5, 7, 12, 17, 18, and 20 to 23 from State-owned banks*: Germany insists that these do not constitute aid. However, as explained in both the initiation and extension of the formal investigation procedure, GvH1 was a company in difficulty and seriously over-indebted. Thus, the Commission cannot conclude that a market economy investor would have provided such financial support even on market conditions. Moreover, the information available indicates that these credits were not granted on market conditions.

- (81) The credits under measures 17, 18, 20 and 21 had a redemption-free period of two years. As shown in the table below, several credits were granted below the reference rate of interest, which, under the Commission notice of 9 September 1997 on the method for setting the reference and discount rates, should be increased by at least 4 % for companies in difficulty⁽¹¹⁾. Hence none of these credits were granted at market rates.

Measure	Rate of interest	Reference rate + 4 %
Measure 5	7,50 %	13,41 %
Measure 7	9,80 %	13,41 %
Measure 8	7,50 %	13,41 %
Measure 12	7,70 %	13,13 %
Measure 17	Unknown for individual loans	10,62 %
Measure 18	7,25 %	10,62 %
Measure 20	8,40 %	11,62 %
Measure 21	8,40 %	11,62 %
Measure 22	9,50 %	13,13 %
Measure 23	Unknown	13,13 %

- (82) Credits under measures 5, 7, 8, 18, 20 and 22 were assured within a security pool described in recital 38. Regarding the securities provided, the Commission notes that the same real estate was subsequently mortgaged for different values, none of which confirmed by an external evaluation. In addition these mortgages were only provided for the HeLaBa. The verified value of machinery and installation is insufficient to constitute an adequate security. Moreover, it is noted that these assets were directly or indirectly financed by aid granted since privatisation. The personal guarantees from Mr Jamalian for an unspecified amount would only enter into force if all other securities could not be enforced. According to Germany, after the sale of the assets of GvH1 to GvH2, the financial entities concerned obtained some DEM 7 million (17 % of the credits). This amount corresponded to part of the TAB loan under measure 33. The Commission considers that the low amount recovered solely evidences the reduced value of the securities provided by a company in difficulty and does not alter the fact that GvH1 obtained an advantage which it would not have obtained from a market economy investor.
- (83) The credits under measures 12, 17 and 21 were assured by a 90 % State guarantee. Therefore 90 % of the risk of default on those credits to a company in difficulty was assumed by the State. The Commission considers that the existence of these guarantees is a decisive element which would lead any bank to award those credits. The remaining risk of default of a seriously over-indebted company was assumed by public banks without provision of any further security. Thus the Commission cannot conclude that public banks acted as market investors.

⁽¹¹⁾ OJ C 273, 9.9.1997, p. 3.

- (84) No information has been provided on the conditions on which the loan under measure 23 was granted. The Commission cannot therefore conclude that it was granted at market rates. This loan was first granted without the provision of any securities, which does not correspond to the behaviour of a market economy investor, particularly in view of the financial situation of the company at that time. At the request of the Sparkasse, on 17 August 1994, the company provided mortgages of DEM 1,6 million. No further information on such mortgages has been provided, and the Commission cannot therefore rule out the possibility that they relate to the same assets already provided within the security pool. The Commission considers that the provision of the mortgage does not alter the fact that the loan was made available to a company in difficulty, on unknown terms and for one year without providing securities. After the bankruptcy proceedings, the Sparkasse recovered DEM 0,75 million. However, as stated above, the mortgage related to assets directly or indirectly financed by State aid for GvH1. A partial recovery within the bankruptcy proceedings does not alter *ex post* the assessment of the credit.
- (85) Taking into account the serious difficulties of the company, the rate of interest and the lack of acceptable private securities, the Commission can only conclude that these credits constituted aid, potentially to their full amount. The amount of State guarantees will not be calculated as new aid to avoid double counting.
- (86) *Measure 24*: the advance payment by the TAB for real estate intended to be acquired by a public entity is claimed not to constitute aid. The Commission however considers, by analogy with the Commission communication on State aid elements in sales of land and buildings by public authorities, that the price for the real estate was not determined by an independent expert⁽¹²⁾. Moreover, the Commission cannot conclude that a market economy investor would have advanced such a large amount to a company on the verge of insolvency, with all its assets already mortgaged, without signing any contract or demanding any collateral. Consequently, the Commission cannot exclude the possibility that this advance payment constitutes aid.
- (87) *Measure 28*: as stated in the initiation of the formal investigation procedure, this loan from a State-owned bank to the bankrupt GvHiA is regarded in full as aid. The Commission considers that no private investor would have awarded a loan to a company in bankruptcy without any securities other than a State guarantee. The fact that this loan was fully repaid including interest does not change this assessment because the company obtained an advantage which it would not have obtained from a market economy investor.
- (88) *Measure 30*: according to Germany, the debt was contested as a non-priority claim by the administrator in bankruptcy. Germany did not appeal against this decision because the administrator in bankruptcy announced that no dividend would be obtained for non-priority claims. The Commission notes, however, that a dividend was in fact obtained for priority claims. Germany has not demonstrated that the presumed costs of appealing would have been higher than the dividend that Germany could have obtained if this claim had been recognised as priority. Neither did Germany consider the possibility of a successful appeal. The Commission cannot therefore conclude that this waiver took place in accordance with the private creditor principle. This amount is thus deemed to be aid.
- (89) Germany argues that GvH2/3 was never a company in difficulty and that several financial measures in support of it do not constitute aid. However, as stated in both the initiation and extension of the formal investigation procedure, GvH2 is regarded as having been a company in difficulties as from the moment of its creation. The Commission refers on this point to its exhaustive analysis in both the initiation and the extension of the formal investigation procedure and would point out that the financial reports available clearly show that GvH2/3 is financially over-indebted and has operated at a loss since its creation despite a discharge of debt and subsequent capital injections from the State. Financial measures in support of it deriving from State resources are therefore still regarded as aid. The Commission would refer here to its assessment of the individual contested measures.

⁽¹²⁾ OJ C 209, 10.7.1997, p. 3.

- (90) *Measures 31 and 32:* Germany submitted reports drawn up by PME, intended to show that GvH2 was not in difficulties at the time of its creation and that the TIB thus behaved as a private investor with the aim of obtaining profits. As already explained, only the report dated 15 December 1995 forecasts the company's results for 1996 and 1997 in the light of the 49 % holding by the TIB. The report's forecasts have been described in previous sections.
- (91) The Commission considers that the forecast turnover figures were not realistic because they were not supported by an appropriate market analysis. Taking into account the previous performance of the company and the fact that the porcelain industry has suffered from overcapacity since 1992, even the turnover figures forecast for the worst-case scenario were not likely to be achieved. In addition, since GvH1 did not undergo successful restructuring, it should have been clear that the ongoing concern would have to undergo a substantial restructuring to operate efficiently. It is unrealistic that such a process would take only two years, and it would necessarily involve a considerable financial commitment from the shareholders. Finally, even the most optimistic results forecast would represent no profit for the State. The Commission cannot therefore conclude that the TIB acted as a market investor.
- (92) *Measures 33-35, 37 and 38 by state-owned banks:* despite Germany's claims, the Commission notes that the financial results of GvH2 show that it was a company in difficulty at the time of the award of these measures. It is highly doubtful that a private investor would provide the company with such financial support, even on market terms. Moreover, as shown in the table below, none of these credits were granted at market rates.

Measure number	Rate of interest	Reference rate + 4 %
Measure 33	5,50 %	10,99 %
Measure 34	5,50 %	10,99 %
Measure 35	7,25 %	11,33 %
Measure 37	8,00 %	9,54 %
Measure 38	6,25 %	9,54 %

- (93) These credits from the TAB were secured against several mortgages on the company's assets. The Commission would point out once again that GvH1's assets were not acquired within an open, transparent and unconditional call for tender. These assets were financed directly by aid and cannot be regarded as private securities. In addition, an evaluation by an expert for 1998 valued the real estate, buildings and installations at DEM 3,560 million, which, in view of the amount of the credits, cannot be regarded as sufficient security. Moreover, the behaviour of the TAB in waiving its position in the list of creditors (measure 41) shows that the provision of such securities was only a formality without any intention of being enforced.
- (94) Taking into account the serious difficulties of the company, the rate of interest and the lack of acceptable private securities, the Commission can only conclude that these credits constituted aid, potentially in their full amount.

- (95) *Measure 41*: a waiver by the TAB of its position in the list of creditors to avoid insolvency. This measure granted an advantage to the company which was not forced to pay these credits back until a later stage and should therefore be regarded as aid. Its amount is not taken into account to avoid double counting.

B. Aid purportedly covered by approved aid schemes

- (96) Part of the aid for GvH1, GvHiA and GvH2/3 was allegedly granted under approved aid schemes. Since the Commission had serious doubts about the compliance of these aid measures with the terms of the schemes under which they had allegedly been granted, it issued an information injunction pursuant to Article 10(3) of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty⁽¹³⁾ to supply all documentation, information and data necessary for their assessment.
- (97) In its extension of the formal investigation procedure, the Commission concluded that according to the information available, measures 2, 3 and 4 complied with the terms of the approved aid schemes under which they had been granted. These measures were consequently regarded as existing aid, which does not need to be reassessed by the Commission. The Commission also stated that, on the basis of the information at its disposal, it could not be concluded that measures 6, 8, 13, 15, 16, 19, 25, 26, 36, 40 and 43 complied with the terms of the schemes under which they had been allegedly granted. This view is partially revised in the light of the information supplied after the extension of the formal investigation procedure.
- (98) *Measure 6*: a guarantee of DEM 7,68 million from the DtA allegedly granted under an approved scheme⁽¹⁴⁾. Despite Germany's claims, the Commission maintains its view that this guarantee exceeds the limit of DEM 1 million provided for in the scheme and does not comply with the rules on the cumulation of aid. The Commission therefore still considers that the guarantee was manifestly not covered by the scheme and falls to be assessed as ad hoc aid.
- (99) *Measure 8*: a loan of DEM 1 million granted under an approved aid scheme⁽¹⁵⁾. The Commission considers that, according to the information available, this loan complied with the conditions of the scheme under which it was granted and thus constitutes existing aid.
- (100) *Measure 13*: the Commission would point out once again that this grant was awarded under an aid scheme against which the Commission initiated the formal investigation procedure on the grounds of misuse⁽¹⁶⁾. The Commission would also point out that the scheme was only meant for SMEs that were not in difficulty⁽¹⁷⁾. According to the data submitted, GvH1 never qualified as an SME and was a company in difficulty at the time of the award of this grant. The Commission thus maintains that the aid was manifestly not covered by the scheme under which it was allegedly granted and falls to be assessed as ad hoc aid.
- (101) *Measures 15, 16 and 19*: Germany claims that the scheme under which these guarantees were awarded was known to the Commission and that the guarantees should be regarded as existing aid⁽¹⁸⁾. The Commission notes, however, that a registration as non-notified aid does not imply that the scheme is approved, and consequently these guarantees are regarded as ad hoc aid.

⁽¹³⁾ OJ L 83, 27.3.1999, p. 1.

⁽¹⁴⁾ N 591/90, SG(90) D/91620, 20 December 1990.

⁽¹⁵⁾ N 318/90, SG(90) D/27178, 14 November 1990.

⁽¹⁶⁾ C 69/98, ex N 408/93.

⁽¹⁷⁾ According to the scheme, an SME will not have more than 250 employees and either a turnover of DEM 40 million or assets of DEM 20 million.

⁽¹⁸⁾ NN 25/95.

- (102) *Measure 25*: investment tax refunds allegedly granted under approved regional aid schemes⁽¹⁹⁾. After an assessment of the information provided by Germany, the Commission concludes that these measures complied with the ceilings provided for in the schemes under which they were granted. These grants thus constitute existing aid.
- (103) *Measure 26*: the Commission has verified that, according to the information available, these grants for R&D respected the conditions laid out in the scheme under which they were granted⁽²⁰⁾, particularly those concerning maximum aid allowable per year and intensity. They thus constitute existing aid.
- (104) *Measure 27*: as stated in the extension of the formal investigation procedure, these grants for the promotion of employment manifestly do not comply with the terms of the scheme under which they were granted⁽²¹⁾. The Commission would point out that the scheme provides that such measures do not rank as aid because they did not grant any advantage to a particular company. Privatised enterprises were not therefore eligible to benefit from such measures since after privatisation the projects developed would take place in their own interest and not in the general interest. The information available indicates that effectively the project consisted in cleaning up part of the installations of GvH1 by removing old machinery and installations. The project therefore took place in its interest. Consequently, the Commission cannot conclude that the project did not represent an economic advantage for GvH1. Moreover, the Commission notes that privatised companies were not eligible to participate in such projects and that part of these grants were awarded by the *Land* of Thuringia, whereas only the Federal Labour Office was regarded as authorised to award such grants. Consequently, the Commission maintains its view that these grants constitute aid which falls to be assessed as ad hoc.
- (105) *Measure 36*: direct investment grants allegedly awarded on the basis of a regional aid scheme⁽²²⁾ up to the ceilings allowed for SMEs under Commission Recommendation 96/280/EC of 3 April 1996 concerning the definition of small and medium-sized enterprises⁽²³⁾. As the Commission already stated in its extension of the formal investigation procedure, GvH2 did not qualify as an SME at the time of the award of these grants. Consequently, despite Germany's claims that the relevant time should be the time of application for this aid, the Commission maintains that the aid manifestly does not comply with the scheme and falls to be assessed as ad hoc aid⁽²⁴⁾.
- (106) *Measure 39*: the Commission partially reviews its assessment in respect of the grants awarded after 1997. The grants awarded during 1996 amounting to some DEM 0,686 million were allegedly based on the same scheme as measure 27 and do not comply with its terms for the same reasons. On the other hand, the grants awarded as from 1997 totalling some DEM 1,358 million were based on a different approved aid scheme⁽²⁵⁾. According to the information available, the terms of this scheme have been complied with. Consequently, this latter amount constitutes existing aid.

⁽¹⁹⁾ Investment Allowance Acts 1991 (C 59/91, SG(92) D/8068, 18 June 1993) and 1993 (N 561/92, SG(92) D/16623, 24 November 1992). These schemes provide for different aid intensities for large and small enterprises. Rules on cumulation with other regional aids must also be complied with.

⁽²⁰⁾ N 477/91, SG(91) D/22704, 25 November 1991.

⁽²¹⁾ NN 117/92, SG(95) D/341, 13 January 1995.

⁽²²⁾ 24th outline plan of the joint Federal Government/*Länder* scheme for improving regional economic structures N 531/95, (OJ C 291, 4.10.1996, p. 4.)

⁽²³⁾ OJ L 107, 30.4.1996, p. 4.

⁽²⁴⁾ See Commission Regulation (EC) No 69/2001: 'aid should be considered to be granted at the moment the legal right to receive the aid is conferred to the beneficiary' (OJ L 10, 13.1.2001, p. 30). See also Annex II of Commission Regulation (EC) No 70/2001 where reference is always made to the granting of aid (OJ L 10, 13.1.2001, p. 33). See also Council Regulation (EC) No 659/1999 which always refers to the granting of aid (footnote 13).

⁽²⁵⁾ NN 107/97, in force since 1 April 1997, approved by letter SG(98) 1049, 6 February 1993.

- (107) *Measure 40*: after an assessment of the information provided by Germany, the Commission concludes that, according to the information available, these investment tax refunds complied with the ceilings laid down in the schemes under which they were granted⁽²⁶⁾. These grants thus constitute existing aid.
- (108) *Measure 43*: grants for R&D awarded from 1997 to 2000, which in the extension of the investigation procedure were considered to manifestly not comply with the aid scheme for SMEs⁽²⁷⁾ under which they were granted. According to the accounting reports, GvH2 fell below the SME thresholds in 2000. However, these reports do not seem to take the employees of Glashütte Schmiedefeld into account. Moreover, since SME status is only acquired when this phenomenon is repeated over two consecutive years, all these grants still fall to be considered as new aid.
- (109) In view of the foregoing, measures 2, 3, 4, 8, 25, 26 and part of measures 39 and 40 constitute, according to the information available, existing aid. Their amount has to be taken into account in assessing proportionality.

C. *De minimis* aid

- (110) Germany claims that measures 15, 16, 21 and 42 fall under the *de minimis* rule. Under this rule, the ceiling for aid to be considered *de minimis* is EUR 100 000 over a three-year period beginning when the first *de minimis* aid was granted. This ceiling applies to the total of public assistance considered to be *de minimis* aid and does not affect the possibility of the recipient obtaining aid under schemes approved by the Commission.
- (111) In respect of the guarantees under measures 15, 16 and 21, the Commission considers that the fact that their amount is not taken into account to avoid double counting does not mean that they do not constitute aid. According to the Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees, 'where, at the time the loan is granted, there is a strong probability that the borrower will default, e.g. because he is in financial difficulty, the value of the guarantee may be as high as the amount effectively covered by that guarantee'⁽²⁸⁾. This means that the aid element in these guarantees is 90 % of the credits to which they relate, which is well beyond the *de minimis* rules.
- (112) As regards measure 42, the *de minimis* ceilings have been complied with both for the period 1996 to 1999 and for the period 1999 to 2000. Germany has stated that the conditions for application of this rule have been complied with. The Commission therefore considers these amounts covered by the *de minimis* rule.

D. Derogation under Article 87(3)(c) of the EC Treaty

- (113) In view of the previous sections, aid of some DEM 139,399 million falls to be assessed as ad hoc aid by the Commission. Article 87(2) and (3) of the EC Treaty provides for derogations from the general ban on aid laid down in Article 87(1).

⁽²⁶⁾ The Investment Allowance Act 1996 provides for different aid intensities for small and large undertakings (N 494/95, SG(95) D/17154, 27 December 1995).

⁽²⁷⁾ N 331/96, SG(97) D/482, 23 January 1997.

⁽²⁸⁾ OJ C 71, 11.3.2000, p. 14, point 3.2.

- (114) The exemptions in Article 87(2) of the EC Treaty do not apply in the present case because the aid measures do not have a social character and are not granted to individual consumers, do not make good the damage caused by natural disasters or exceptional occurrences, and are not granted to the economy of certain areas of the Federal Republic of Germany affected by its division.
- (115) Further exemptions are provided for in Article 87(3)(a) and (c) of the EC Treaty. As the primary objective of the aid is not regional, but concerns the restoration of long-term viability of an undertaking in difficulty, only the exemptions provided for in Article 87(3)(c) of the EC Treaty apply. Article 87(3)(c) provides for the authorisation of State aid granted to promote the development of certain economic sectors, where such aid does not adversely affect trading conditions to an extent contrary to the common interest. For its assessment of rescue and restructuring aid, the Commission has issued special guidelines. In the light of the examination it has carried out, the Commission considers that none of the other Community guidelines, such as those for research and development, the environment, small and medium-sized enterprises or for employment and training, could apply here.
- (116) Since, according to the information available, the aid was granted before 30 April 2000, the Community guidelines of 23 December 1994 on State aid for rescuing and restructuring firms in difficulty⁽²⁹⁾ (guidelines) apply⁽³⁰⁾. The Commission would point out that the guidelines codify its practice for the assessment of the compatibility of rescue and restructuring aid with the common market. The guidelines are therefore also applicable to aid granted before 1994, since they reflect a long-standing Commission practice.
- (a) *Restoration of viability*
- (117) Award of restructuring aid requires a feasible, coherent and far-reaching restructuring plan capable of restoring the long-term viability of the firm within a reasonable timescale and on the basis of realistic assumptions. Restructuring aid should normally only need to be granted once.
- (118) In the present case GvH1, GvHiA and GvH2/3 have benefited from continuous awards of aid, presumably granted for the purpose of restructuring on the basis of a series of plans submitted to the Commission. All but the last plan failed and it is difficult to determine which steps were actually implemented. The Commission identifies two main restructuring periods: 1990 to 1995 and from 1995 onwards. The bankruptcy of GvH1 and change of investor meant a substantial break in the process. Nonetheless important changes in the plans took place within each period.

The first restructuring period

- (119) The first plan acknowledged market saturation and foresaw the closure of 50 % to 70 % of capacities in Thuringia and Saxony. However, GvH1 expected to double its sales within two years relying on the positive effects of the common market. In the Commission's view, these figures were over-optimistic, and this first plan, fully financed by State resources and accounting measures, was not based on internal measures, but on external factors outside the company's control.

⁽²⁹⁾ OJ C 368, 23.12.1994, p. 12.

⁽³⁰⁾ Point 7.5 of the 1999 guidelines states that 'the Commission will examine the compatibility with the common market of any rescuing and restructuring aid granted without its authorisation (...) on the basis of the guidelines in force at the time the aid is granted (...)' (OJ C 288, 9.10.1999, p. 2).

- (120) The plan revised for the period 1993 to 1996 included new awards of aid. In the Commission's view, the loss of orders from Russia and Iran is not attributable to external reasons which the company could not foresee, but to wrong market forecasts. The replacement of a defective oven was not external, and since the investor claimed warrant liability from the THA, this implies that it should not have been unforeseeable at the time of the privatisation. Moreover, an exception to the principle that restructuring aid should be granted only once can be accepted only if a restructuring plan ensures restoration to long-term viability. In view of the results obtained by GvH1 up to that date, its level of over-indebtedness, the market saturation and the collapse of GvH1's traditional markets, the Commission doubted that the revised plan was realistic. The sales forecasts seem again over-optimistic⁽³¹⁾, are not supported by a market analysis and although the urgent need to renegotiate debts was pointed out, no specific steps were described. These doubts were confirmed by the fact that GvH1 filed for bankruptcy in 1995.
- (121) Regarding GvHiA, the estate in bankruptcy did not have any restructuring or liquidation plan at the time the aid was granted. As stated in the extension of the formal investigation procedure, measures 28 and 29 do not comply with the criteria set out for rescue aid. The generally accepted period of six months is well exceeded here without any justification. Germany submitted no evidence that the credits were granted on market terms. The waiver of debt under measure 30 does not consist of liquidity. There is no evidence that their amount was the strict needed to keep the firm in business. Finally, it is unlikely that these measures had no undue adverse effects on the industrial situation in other Member States, given the overall over-capacity of the porcelain industry. In the absence of a restructuring plan for GvHiA, these measures do not comply with the compatibility criteria as restructuring aid either.

The second restructuring period

- (122) In view of the development of GvH1 it is doubtful that bankruptcy could be considered unforeseeable. The setting-up of GvH2 was linked to subsequent awards of restructuring aid, which were not justified. Moreover the restoration of long-term viability on the basis of the reports submitted seems doubtful. The report dated 15 December 1995 analysing the situation in the light of the TIB participation lacked an appropriate market analysis and an account of restructuring costs (apart from investments) and provides no explanation as to how the restructuring should be financed. The planned return to viability was established on the basis of three possible scenarios depending on sales' volumes, none of which seemed based on realistic assumptions. Taking into account that the porcelain industry has been suffering from over-capacity since 1992, even the turnover figures forecast for the worst-case scenario were not likely to be achieved. Such high turnover figures had never been achieved before, and it was unlikely that a company coming out of bankruptcy proceedings could achieve them. In addition, since GvH1 underwent no successful restructuring, it should have been clear that the on-going concern would have to undergo substantial restructuring in order to operate efficiently. It is doubtful that such a process would only take two years.
- (123) These doubts were confirmed by an external evaluation for the year 1997 which stated, in a report dated 3 July 1998, that it was impossible to determine whether GvH2 could be successfully restructured. The main critical points leading to such an assessment lie in the over-optimistic estimation of turnover growth, given the limited orders entered in the books.

⁽³¹⁾ Without any justification, the turnover was supposed to increase from DEM 14 million to over DEM 40 million within one year.

- (124) The plan was revised in 1998 upon takeover by Mr Frowein, who counted on obtaining a positive operating result of DEM 0,195 million in 1999 and of DEM 0,655 million in 2000. These results had been forecast in the light of cumulated losses of DEM 0,8 million in June 1998. However, two months later losses had quadrupled. The plan was again revised. The expected results were calculated on the basis of a waiver of debt, which seems to have been promised to Mr Frowein upon takeover⁽³²⁾, but which does not seem to have taken place yet. In addition, the company expected to obtain fresh credits from banks, but this has not taken place either. Banks seem to have withdrawn their support, apart from the TAB, which still agreed in 1999 to waive its position in the list of creditors in order to avoid insolvency. This is regarded as a further restructuring aid measure which is hardly justifiable after the previous series of restructuring aid awards. No justification for the 'one time last time' principle has been provided.
- (125) The second revision of this plan was evaluated by a consultancy in 1999. Their report concluded that as at 31 December 1998 the company had losses of DEM 8,166 million not covered by capital and that a waiver of debt and new capital injections as well as the implementation of investments were vital for the continuation of the company. The report expressly did not analyse the company's solvency. The Commission notes that in the year 2000 the company has achieved a balance-sheet trading profit of DEM 24 000. However, the management report for this year indicates over-indebtedness of DEM 9,298 million. This confirms the doubts expressed by the Commission in both its initiation and its extension of the formal investigation procedure that the restoration of GvH2/3's viability is very doubtful.
- (126) In view of the above, the Commission cannot conclude that the repeated aid awards were justified by external and unforeseeable reasons. The Commission cannot conclude either that aid was granted on the basis of any restructuring plan based on realistic assumptions leading to the restoration of the company's long-term viability.
- (b) *No undue distortions of competition*
- (127) The restructuring plan must contain measures taken to offset as far as possible adverse effects on competitors, otherwise the aid involved could be contrary to the common interest and not eligible for exemption pursuant to Article 87(3)(c) of the EC Treaty. This means that if the undertaking is situated in a relevant market in the EU where an assessment of demand and supply shows that there is a structural excess of production capacity, the plan must make a contribution, proportionate to the aid received, to the restructuring of the industry serving the relevant market by irreversibly reducing or closing capacity.
- (128) The porcelain industry is saturated and suffers from over-capacity, thus any aid granted to an undertaking active in this sector is bound to seriously distort competition and adversely affect trade among Member States. In view of the large amounts of aid involved in this case, the contribution by the beneficiary in terms of capacity reduction should be particularly substantial.
- (129) The different restructuring plans submitted provide for capacity reductions both in terms of personnel and in terms of production. According to the first restructuring plan, as at December 1991 GvH1 had a workforce of 626, while in December 1999 its workforce was 269. As regards production, Germany states that within the first restructuring period production was reduced from 8 000 to 6 500 tonnes per annum to 4 000 tonnes per annum. Germany further states that the replacement of several ovens by a single oven further implied a reduction to some 2 300 tons per annum. Germany states that the ovens were destroyed and the production surface reduced.

⁽³²⁾ As stated in a letter from Mr Frowein dated 3 January 1998 which is in the Commission's possession.

- (130) In view of the latest information supplied by Germany, the Commission acknowledges that a permanent reduction in capacity did in fact take place.

(c) *Proportionality to restructuring costs and benefits*

- (131) The amount and intensity of the aid must be limited to the strict minimum needed to enable restructuring to be undertaken and must be related to the benefits anticipated from the Community's viewpoint. Therefore, the investors must make a contribution to the restructuring plan from their own resources. Moreover, the way in which the aid is granted must be such as to avoid providing the company with surplus cash which would be used for aggressive, market-distorting activities not linked to the restructuring process.
- (132) As stated in the extension of the formal investigation procedure, although several plans have been provided, there is still no accurate calculation of restructuring costs. The plans have constantly been changed and the cost of restructuring steps actually implemented cannot be determined. In the absence of an overall account of restructuring costs, it cannot be determined whether the aid was the strict minimum, and it is unclear what the aid was used for.
- (133) As stated in both the initiation and the extension of the formal investigation procedure, the Commission notes the lack of a private contribution to the restructuring. As regards GvH1, the investor never paid the purchase price of GvH1 nor did he bring in this amount into GvH1's capital as agreed with the THA under the revision of the privatisation contract. None of the guarantees provided within a security pool, subsidiary to other securities, could be enforced. As regards GvH2/3, only DEM 0,2 million were brought in as the purchase price by Mr Frowein. Germany now claims that, as soon as the formal investigation procedure is closed, DEM 6 million will be brought in as a private contribution. The Commission would point out, however, that it is the award of aid and not the contribution from the investor which must be made dependent upon a Commission decision. The conditionality does not demonstrate commitment from the investor to the company. In addition, there is no evidence that this amount will be effectively contributed. In view of the recent bankruptcy of GvH2/3, it is highly doubtful that any amounts will be paid in.
- (134) Consequently, the Commission cannot conclude that the aid granted is proportional to the costs and benefits of the restructuring. Moreover, the fact that a substantial amount of the aid received has a liquidity effect suggests the possibility that the aid may have provided the company with surplus cash which could be used for aggressive, market-distorting activities, such as predatory pricing or buying controlling stakes in rival companies. The Commission particularly notes that the complainants have specifically invoked these two possibilities.
- (135) The information available does not allow the Commission to take a view on whether predatory pricing has taken place. However, regarding the acquisition of the shares in Glashütte Schmiedefeld GmbH, the Commission cannot exclude the possibility that aid to GvH2/3 was used for this purpose.

(d) *Full implementation of the restructuring plan*

- (136) In view of the series of plans, most of which have failed, and their constant amendments, the Commission cannot conclude that this requirement of the guidelines has been fulfilled.

VII. CONCLUSIONS

- (137) The Commission finds that Germany has unlawfully implemented the aid in question in breach of Article 83(3) of the Treaty. Moreover, the aid is incompatible with the common market and has been recovered from the recipient. In accordance with the Commission's standard practice and the case-law of the Court of Justice of the European Communities, aid must be recovered from the undertaking which actually benefited from the aid. In view of the changes which have taken place as regards the aid recipient, the Commission deems it appropriate to define the extent of the obligation to recover the aid.
- (138) In its decision to initiate and extend the formal investigation procedure, the Commission found that GvH2 was continuing the business activity of GvH1. Both companies owned the same assets, were active on the same product markets and under the same corporate name, and produced the same products with the same plant and employees (even if the workforce was reduced). There was, moreover, no indication that third parties were looking after the new set-up.
- (139) The Commission recognises that GvH1 and GvH2 are distinct legal persons. However, the business activity of GvH1 was continued during the bankruptcy proceedings and assets were sold to GvH2 within the framework of the ongoing business activity. The Commission also notes that the sale of the assets of GvHiA to GvH2 did not take place in an open and unconditional bidding procedure. The alleged search for an investor lasted only four months. According to information presented prior to the initiation of the formal investigation procedure, the *Land* of Thuringia even sought via LEG, before the bankruptcy proceedings were initiated, a solution for GvHiA involving a State holding; this is what subsequently actually occurred. The Commission does not therefore recognise that the new investors in GvH2 (GvHiA and TIB) were selected as the highest bidders in an open and unconditional call to tender. Although Germany stated that negotiations were initiated with several potential investors, the Commission received a reply from a competitor stating that it was prevented from submitting a bid.
- (140) The Commission found that there was congruity between GvH1 and GvH2 particularly in terms of control: 51 % of the bankrupt GvH1's assets were formally in the possession of GvHiA. Furthermore, the start-up capital of GvH2 was financed with money from the bankrupt GvH1's assets. The remaining DEM 0,49 million and the price of DEM 8,5 million paid for the assets were contributed by the State, GvH1's principal creditor. After the sale or assignment of the assets, the cash, assets and control of the new legal entity remained in the same hands as before.
- (141) In accordance with the Commission's established practice, when a company receiving aid is sold at its market value, the benefit of the aid remains with the seller. Since no unconditional call for tender was made in the present case, the Commission cannot conclude that the purchase price paid for the assets of GvH1 corresponded to the normal market price. The buyer, GvH2, therefore likewise benefited from the aid granted to GvH1.
- (142) Furthermore, as the principal creditor of the company being wound up, the State should have behaved as a private creditor would have done, in order to rule out the possibility that State aid was involved in its action. A private creditor would presumably have wound up the company so as to fulfil its claims, unless a new company was to be formed and assets subsequently transferred for the purpose of selling the assets to the highest bidder at the highest price, thereby fulfilling its claims. The Commission cannot conclude that this was the case, since the State itself had obviously taken over 49 % of the company, financed the purchase of the assets and, only two years later, sold the shares at a much lower price than it itself had paid.

- (143) Finally, in its decision on the extension of the formal investigation procedure, the Commission pointed out with regard to GvH3 that changes in shareholding ownership relationships did not result in the creation of a new legal entity exempt from claims. Buyers are able to protect themselves by exercising normal due diligence in transactions. This applies in particular to Mr Frowein, who was aware of the company's situation from the outset of the bankruptcy proceedings. Consequently, GvH3 is to be regarded as one and the same company as GvH2 ⁽³³⁾. It should also be noted that Mr Frowein was not selected in an open, unconditional and transparent tendering procedure.
- (144) The Commission concludes that, in order to implement this Decision correctly, Germany must behave in the same way as a private creditor acting with due diligence. National law may not be applied in a disadvantageous way so as to impede collection or make it extremely difficult. In principle, this means that Germany must seek to collect the debts immediately, using all means at its disposal. No principle of national law may stand in the way of the complete application of European law ⁽³⁴⁾.
- (145) In order to prevent the effectiveness of this Decision from being frustrated and the market from continuing to be distorted, the Commission may be compelled to require that the recovery is not restricted to the original undertaking, but is extended to the undertaking which continues the activities of the original undertaking using the transferred means of production, in cases where certain elements of the transfer point to economic continuity between the two undertakings ⁽³⁵⁾.
- (146) The Commission considers that, in addition to the aid directly granted to it, GvH2/3 also benefits from the aid to its predecessors. Consequently, in order to duly comply with this Decision, Germany must take action not only against the direct aid recipient, but also against its successors. Accordingly, GvH2/3 is not only obliged to repay the aid unlawfully received in its own name, but also jointly obliged to repay the unlawful aid granted to GvH1, including the aid granted during the bankruptcy proceedings. Germany must also take action against any other firm which could benefit from a transfer of the assets in question, thereby helping to frustrate the effectiveness of this Decision ⁽³⁶⁾.

HAS ADOPTED THIS DECISION:

Article 1

1. The State aid which Germany has granted to Graf von Henneberg Porzellan GmbH is incompatible with the common market.
2. The incompatible aid referred to in paragraph 1 includes the following measures in support of Graf von Henneberg Porzellan GmbH, established in 1990, which later became Graf von Henneberg in Abwicklung:
 - (a) loans from Hessische Landesbank (HeLaBa) under measures 5, 20 and 21, originally totalling DEM 28,530 million;
 - (b) loans from Bayerische Landesbank under measures 7, 12, 17 and 18, originally totalling DEM 43,023 million;

⁽³³⁾ In the event of a share purchase, the obligation to repay the aid remains with the company. See, for example, Case C-303/88 Italy v Commission [1991] ECR I-1433.

⁽³⁴⁾ See footnote 33, recital 60.

⁽³⁵⁾ Commission Decision 2000/536/EC, Seleco SpA (OJ L 227, 7.9.2000, p. 24).

⁽³⁶⁾ Commission Decisions 2000/567/EC, SMI (OJ L 238, 22.9.2000, p. 50) and 2000/796/EC, CDA (OJ L 318, 16.12.2000, p. 62).

- (c) a guarantee from the Treuhandanstalt (THA) of DEM 8,629 million under measure 10;
- (d) grants of DEM 13,871 million from the THA under measure 11;
- (e) a grant of DEM 5 million under measure 13;
- (f) a loan from the Sparkasse Ilmenau under measure 22, originally amounting to DEM 3,2 million;
- (g) a loan from the Sparkasse Erfurt under measure 23, originally amounting to DEM 1,5 million;
- (h) an advance payment of DEM 2 million from the Thüringer Aufbaubank (TAB) under measure 24;
- (i) grants of DEM 2,077 million for the promotion of employment under measure 27.

The incompatible aid also includes the following measures in support of Graf von Henneberg Porzellan GmbH, established in 1995 and still active on the market:

- (a) a loan of DEM 2 million from the HeLaBa under measure 28;
- (b) a waiver of debt of DEM 0,940 million from the Federal Office for Special Tasks related to Unification (BvS) under measure 30;
- (c) a participation of DEM 0,490 million from the Thüringer Industriebeteiligungs GmbH & Co. KG (TIB) in GvH2's initial capital under measure 31;
- (d) a shareholder loan of DEM 0,490 million from the TIB under measure 32;
- (e) loans from the TAB under measures 33, 34, 35, 37 and 38, originally totalling DEM 20,521 million;
- (f) direct investment grants of DEM 5,981 million under measure 36;
- (g) the amount of DEM 0,686 million paid up to 1996 out of the grants for the promotion of employment under measure 39;
- (h) grants of DEM 0,451 million for research and development under measure 43.

Article 2

1. Germany shall take all necessary measures to recover from the beneficiary the aid referred to in Article 1 and unlawfully made available to the beneficiary, with the exception of those aid measures which have already been paid back with interest since the date on which they were granted.

2. Recovery shall be effected without delay and in accordance with the procedures of national law, provided they allow the immediate and effective execution of the Decision. The aid to be recovered shall include interest from the date on which it was at the disposal of the beneficiary until the date of its recovery. Interest shall be calculated on the basis of the reference rate used for calculating the grant-equivalent of regional aid.

3. For the purpose of paragraph 2, the term 'beneficiary' includes Graf von Henneberg Porzellan GmbH, established in 1990 and currently in bankruptcy, Graf von Henneberg Porzellan GmbH, established in 1995, which is also liable for the aid granted to its predecessor, and any other undertaking to which the assets of the abovementioned legal persons have been transferred or will be transferred in such a way as to frustrate the effectiveness of this Decision.

Article 3

Germany shall inform the Commission, within two months of notification of this Decision, of the measures taken to comply with it.

Article 4

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 30 October 2001.

For the Commission

Mario MONTI

Member of the Commission

COMMISSION DECISION**of 27 February 2002****on the State aid implemented by Germany for Hoch- und Ingenieurbau GmbH (HIG)***(notified under document number C(2002) 589)***(Only the German text is authentic)****(Text with EEA relevance)**

(2002/866/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 88(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above ⁽¹⁾,

Whereas:

I. PROCEDURE

- (1) By fax of 29 December 1999, registered by the Commission on 10 January 2000 as aid case NN 3/2000, Germany informed the Commission of financial measures to assist Hoch- und Ingenieurbau GmbH, Gera (hereinafter referred to as HIG). In response to requests for information sent by the Commission on 4 February 2000, 7 March 2001 and 9 July 2001, Germany replied by letters of 17 March 2000, 10 May 2001 and 20 August 2001.
- (2) By letter of 29 September 2001, the Commission informed Germany that it had decided to initiate the procedure laid down in Article 88(2) of the EC Treaty in respect of the aid.
- (3) The Commission decision to initiate the procedure was published in the *Official Journal of the European Communities* ⁽²⁾. The Commission called on interested parties to submit their comments. The case was then registered under number C 67/2001. No comments were received from third parties. Comments from Germany were received on 7 November 2001.

⁽¹⁾ OJ C, 335, 29.11.2001, p. 2.

⁽²⁾ See footnote 1.

II. DESCRIPTION OF THE AID

- (4) The case concerns financial measures for the restructuring of HIG, an SME active in the construction sector in Gera (Thuringia). Some important economic data relating to the firm are given below:

	(in DEM '000.) (*)					
	1996	1997	1998	1999	2000	2001 (**)
Turnover	7 000	13 000	12 053	11 943	9 400	10 000
Net profit	22	52	12	9	25	50
Workers	80	80	80	80	72	52

(*) Where applicable

(**) Planned.

1. The restructuring

- (5) The restructuring took place in the period from 1996 to 2000. The restructuring plan envisaged a shift of activities to more profitable areas. Other internal measures comprised the introduction of flexible working hours, new accounting and control systems and better utilisation of plant and machinery. The restructuring costs were given as follows:

	(in DEM)	
1.	Investments	2 700 000
	Premises	830 000
	Buildings/plant/tools	570 000
	Machinery	1 300 000
2.	Interim financing	750 000
3.	Personnel costs	951 000
4.	Operating resources	1 150 000
5.	Guarantees (granted to suppliers and other contractual partners)	400 000
	Total	5 951 000

2. Financial contribution by the public authorities to the restructuring

- (6) On 11 April 1996 the Bundesanstalt für vereinigungsbedingte Sonderaufgaben (BvS, a successor to the Treuhond privatisation agency) granted DEM 1,42 million consisting of two grants towards the restructuring of HIG ⁽³⁾. The first instalment of DEM 918 000 was disbursed on 18 January 1998 ⁽⁴⁾.

⁽³⁾ Germany states that these measures were earmarked for the financing of the fixed assets.

⁽⁴⁾ Subsequent instalments of DEM 385 000 and DEM 117 000 were disbursed in September 1998 and December 1999 respectively.

- (7) On 7 July 1997 the *Land* of Thuringia participated in the support for HIG by means of an 80 % deficiency guarantee via the Thüringer Aufbaubank (TAB) granted under the latter's approved guarantee scheme⁽⁵⁾. This corresponds to a contribution of DEM 1,545 million covering loans and credits in the form of bank guarantees (Avale) from the Deutsche Kreditbank e.G., Gera (DKB) amounting to DEM 1,932 million.
- (8) Three of the loans mentioned in recital 7 were refinanced by public resources. Germany states that two of them were refinanced under an approved aid scheme⁽⁶⁾: one of DEM 382 000 granted on 1 July 1998 at 4,75 % p.a. and the other of DEM 368 000 also granted on 1 July 1998 at 6.25 % p.a.. A third loan of DEM 400 000 was refinanced via the TAB at 5,5 % p.a. and disbursed on 31 July 1998. Germany states that this measure was granted in accordance with the Commission notice on the *de minimis* rule for State aid⁽⁷⁾.
- (9) In 1996 HIG obtained a one-off investment allowance of DEM 2 500 under an approved investment allowance scheme⁽⁸⁾.
- (10) Furthermore, a direct investment grant of DEM 325 000 for investments amounting to DEM 1,801 million was granted which, according to Germany, is covered by the SME investment safeguard scheme of the *Land* of Thuringia, a scheme approved by the Commission⁽⁹⁾.

3. Financial contributions from other sources

- (11) In the course of the preliminary assessment, Germany indicated the following contributions from the recipient or external commercial sources:
- an interim financing loan from the Sparkasse Gera amounting to DEM 750 000 and covering the period prior to the implementation of the BvS and SME measures: this loan was jointly secured by the two investors Knauthe and Müller to the amount of DEM 300 000,
 - personal liability on the part of the two investors, amounting to DEM 966 000 each, in respect of the loans and credits in the form of a bank guarantee (Avalrahmen) provided by the DKB with prior ranking over the 80 % deficiency guarantee,
 - a credit line (Kontokorrent) from the DKB amounting to DEM 382 000 at an annual interest rate of 7,5 % and a credit in the form of a bank guarantee (Avalrahmen) of DEM 400 000 at an annual interest rate of 1 %: both measures were covered by the 80 % deficiency guarantee,
 - decision by the workforce to forgo the Christmas allowance in the period 1997 to 1999, representing DEM 951 000,
 - cash flow of DEM 186 000.

4. Reasons for initiating the procedure

- (12) In its decision to initiate the formal investigation procedure, the Commission classified the DEM 325 000 direct investment grant mentioned in recital 10, which was allegedly provided under an approved SME investment scheme⁽¹⁰⁾, as ad hoc aid because, by letter of 26 August 1993, Germany explicitly ruled out the application of that scheme to companies in difficulty.

⁽⁵⁾ Bürgschaftsrichtlinie der Thüringer Aufbaubank, SG(96) D/11696 of 27 December 1996 (N 117/96).

⁽⁶⁾ ERP-Existenzgründungsprogramm, SG(97) D/1413 of 25 February 1997 (E 4/94).

⁽⁷⁾ OJ C 68, 6.3.1996, p. 9.

⁽⁸⁾ Investitionszulage für die neuen Bundesländer, SG(95) D/17154 of 27 December 1995, as amended by SG(96) D/3794 of 12 April 1996 (N 494/A/95).

⁽⁹⁾ KMU-Investitionssicherungsprogramm des Landes Thüringen, SG(93) D/19245 of 26 November 1993, as amended by SG(98) D/4313 of 2 June 1998 (N 408/93).

⁽¹⁰⁾ See footnote 9.

- (13) Furthermore, the Commission expressed doubts as to the compatibility of the aid with the common market namely:
- whether the interim financing loan of DEM 750 000 from the Sparkasse Gera can be regarded as external commercial financing since the information provided by Germany in the preliminary assessment was ambiguous as to the extent to which this contribution was secured,
 - whether the cash flow of DEM 189 000 can be regarded as a contribution by the firm to the restructuring exercise since it is realised mainly on the basis of aid measures to be granted and since the estimated amount cannot be guaranteed,
 - whether the decision by the workforce to forgo the Christmas allowance can be regarded as a contribution by the company to the restructuring since the employees are not themselves investors in the company,
 - whether the investors' personal liability can be regarded as external commercial financing with prior ranking over the 80 % public deficiency guarantee since, in the Commission's view, the 'substantial' liability for granting the loans falls within the scope of the deficiency guarantee and not within the investors' personal liability,
 - whether the 20 % of the contributions not covered by the public deficiency guarantee can be regarded as external commercial financing since these contributions were also made or refinanced out of public resources on preferential terms, with the result that two aid elements are present in the same contribution,
 - whether the credit line of DEM 382 000 can be regarded as external commercial financing since it appears to have been counted twice.
- (14) The Commission has doubts therefore as to the proportionality of the aid within the meaning of the Community guidelines on rescue and restructuring aid ⁽¹¹⁾ (the guidelines) since it is unclear whether the recipient made a contribution to the restructuring from its own resources or from external commercial financing.

III. COMMENTS PRESENTED BY GERMANY

- (15) Germany stated in its reply that the direct investment grant allegedly made under the SME investment scheme of the *Land* of Thuringia ⁽¹²⁾ was not made until 15 July 1998, i.e. after the Commission had authorised an extension of the scheme.
- (16) It also argued that the recipient's contributions from its own resources or external commercial financing should be considered sufficient within the meaning of the guidelines because the personal liability of the investors should be taken into account. In this connection, it informed the Commission that capital amounting to DEM 51 000 and also financed by the two investors should also be taken into account although it had not been indicated as investor contribution.
- (17) As regards the DEM 750 000 interim financing loan from the Sparkasse Gera, it is argued that it was granted on market terms. With regard to the collateral provided, it was made clear that the two investors were personally liable for this loan up to the amount of DEM 300 000 each. Moreover, it was stated that the loan had been granted in the first half of 1996, when the reference rate was 6,69 %.

⁽¹¹⁾ OJ C 368, 23.12.1994.

⁽¹²⁾ KMU-Investitionssicherungsprogramm des Landes Thüringen, SG(93) D/19245 of 26 November 1993, as amended by SG(98) D/4313 of 2 June 1998 (N 408/93).

- (18) With respect to the collateral provided by the investors for the TAB loan of DEM 1 932 000, it was stressed, contrary to previous communications, that this consisted not only of personal liabilities but also of the assignment of claims and assets as well as a mortgage on company premises.
- (19) With regard to the investors' personal liabilities with prior ranking over the 80 % public deficiency guarantee, Germany disputes that the guarantee represents the 'substantial' liability for this part of the loan because all the collateral provided should be seen as part of an overall plan. Therefore, the personal liabilities should also be regarded as investor contributions.
- (20) The 20 % of the loans not covered by the public deficiency guarantee do not involve subsidised interest rates. It is claimed that the interest rates corresponded to market rates since the loans were granted not to a firm in difficulty but to the investors, who have to be regarded as solvent borrowers. Moreover, the reference rate applied to these measures was 6,69 %.
- (21) With regard to the DEM 382 000 credit line, which was allegedly counted twice, Germany claims that this amount had been indicated as a credit line by mistake and had, in fact, been financed through the company's cash flow.
- (22) As regards the cash flow used to finance the restructuring, Germany claims that the public measures were used mainly for working assets. Therefore, the cash flow derived primarily from ongoing business activity.
- (23) As regards the workforce's decision to forgo the Christmas allowance, Germany argues that the company as a whole should be regarded as the recipient. Since the decision by the workforce also reduced the company's need for aid, it considers that this should also be taken into account as a contribution by the recipient to the restructuring.

IV. ASSESSMENT OF THE AID

- (24) Article 87(1) of the EC Treaty states that any aid granted through state resources to certain undertakings is incompatible with the common market where such aid distorts or threatens to distort competition, in so far as it affects trade between Member States.

1. State aid

- (25) According to the available information, the interest subsidies contained in the TAB-refinanced loan of DEM 400 000 fall within the scope of the Commission notice on the *de minimis* rule for State aid and does not, therefore, require further assessment in this decision.
- (26) All the other financial measures taken by Germany to assist the recipient company are caught by the prohibition of Article 87(1) of the EC Treaty. They confer on a specific undertaking economic benefits which it would not have received on market terms. The measures therefore constitute aid which, by its nature, is likely to distort competition. Given the nature of the assistance and the existence of inter-State trade within the common market in the sector in which the recipient is active, the financial measures in question fall within the scope of Article 87(1).
- (27) The Commission notes that, according to the available information, the 80 % deficiency guarantee from the TAB (recital 7), the two loans refinanced under the ERP-Existenzgründungsprogramm (recital 8) and the investment allowance (recital 9) are covered by approved schemes and need not to be further assessed in this decision.

- (28) Germany considers that the direct investment grant of DEM 325 000 was made in accordance with an approved SME investment scheme of the *Land* of Thuringia ⁽¹³⁾ after its extension. However, the Commission notes that the extension of the scheme was approved on the basis of the fact that the granting of aid to firms in difficulty was ruled out. According to the information available to it, the Commission nevertheless must assume that the measures in question were granted to a firm in difficulty and are therefore quite clearly not covered by the conditions of the decision approving that scheme. The measure is, therefore, to be regarded as ad hoc aid in this decision.
- (29) The DEM 382 000 credit line and the DEM 400 000 credit in the form of a bank guarantee (Avalrahmen) from the DKB were granted out of public resources on preferential terms. The difference between the actual costs and the market costs is to be regarded as ad hoc aid in this decision.
- (30) The actual annual interest rate on the DKB credit line was 7,5 %. Since a comparison of those terms with actual market terms is currently not possible, the Commission's reference rate, which was increased by four percentage points has been applied ⁽¹⁴⁾. In the first half of 1998, when this measure was granted, the reference rate was 5,94 %. Hence, the actual interest rate of 7,5 % is 2,44 percentage points below the increased reference rate of 9,94 %. This interest premium of 2,44 percentage points p.a. should therefore be regarded as an ad hoc aid component of this measure.
- (31) As regards the DKB credit in the form of a bank guarantee (Avalrahmen), this is a contingent liability and therefore has to be compared to a guarantee rather than a loan. On the basis of the information at the Commission's disposal, it can be concluded that an SME in a situation comparable to that of HIG between 1998 and 1999 would have had to pay an annual interest rate of at least 3 % for a comparable bank guarantee (Avalrahmen) on the market. The actual rate of 1 % p.a. falls two percentage points short of the normal market rate. The Commission considers therefore that the amount represented by the annual interest-rate subsidy of two percentage points inherent in this measure is ad hoc aid.
- (32) The DEM 1,02 million grant and the interest-free loan of DEM 400 000 from the BvS also constitute measures that HIG could not have obtained free of charge from commercial sources and should therefore be assessed as ad hoc aid in this decision.
- (33) The Commission further notes that the Germany failed to comply with its obligation under Article 88(3) of the EC Treaty. The aid is therefore unlawful from a formal point of view. This does not necessarily mean, however, that it is incompatible with the common market. The individual measures must therefore be examined under Article 87(3) of the EC Treaty.

2. Derogations under Article 87(3) of the EC Treaty

- (34) Measures that are caught by the prohibition laid down by Article 87(1) of the EC Treaty and do not constitute existing aid are incompatible with the common market unless they qualify for one the derogations under Article 87(2) or (3) of the EC Treaty. In the present case, Article 87(3) is relevant.

⁽¹³⁾ See footnote 9.

⁽¹⁴⁾ In accordance with the Commission notice on the method for setting the reference and discount rates (OJ C 273, 9.9.1997).

- (35) In its guidelines ⁽¹⁵⁾, the Commission laid down the conditions for a favourable exercise of its discretion under Article 87(3)(c) of the EC Treaty. According to paragraph 101 of its 1999 guidelines ⁽¹⁶⁾, this amended version applies only in cases where some or all of the aid is granted after their publication. Since the present aid was granted to the recipient before the publication of the revised guidelines in 1999, the 1994 guidelines are applicable.
- (36) The guidelines lay down three criteria for the authorisation of restructuring aid: (i) restoration of viability; (ii) avoidance of undue distortions of competition and (iii) proportionality of the aid to the restructuring costs and benefits. All of these criteria were assessed in detail in the decision to initiate the procedure. The Commission came to the conclusion that the first two criteria were met, but it had doubts as to whether the third criterion had been met.
- (37) The guidelines state that aid beneficiaries will normally be expected to make a significant contribution to the restructuring plan from their own resources or from external commercial financing. The notion 'external commercial financing' has been interpreted in the Commission's practice as being equivalent to financing under market conditions.
- (38) According to the latest information submitted by Germany, the restructuring costs of DEM 5,951 million were financed as follows:

	(in DEM) (*)
1. BvS grant	1 020 000
2. Interest-free loan (BvS)	400 000
3. Direct investment grant from the <i>Land</i> of Thuringia	325 000
4. Public investment allowance	2 500
5. Capital stock	51 000
6. Interim financing loan from the Sparkasse Gera (at 10,5 % p.a.)	750 000
7. Cash flow	521 000
8. Decision by workforce to forgo Christmas allowance	951 000
9. Loans from the Deutsche Kreditbank Gera (totalling DEM 1 932 000):	
a) ERP loan (at 4,75 % p.a. until 30.9.2012)	382 000
b) ERP loan (at 6,25 % p.a. until 31.3.2003)	368 000
c) TAB loan (at 5,5 % p.a. until 30.6.2000)	400 000
d) Credit line (at 7,5 % p.a. until 31.1.1999)	382 000
e) Credit in the form of a bank guarantee (Avalrahmen) (at 1 % p.a. until 31.1.1999)	400 000
Total	5 952 500

(*) The table contains rounded figures and is not arithmetically correct.

⁽¹⁵⁾ See footnote 11.

⁽¹⁶⁾ OJ C 288, 9.10.1999, p. 2.

- (39) Germany takes the view that the recipient's contributions from its own resources or external commercial financing amount to 44,7 %, comprising the measures referred to in points 5 to 8 and an own contribution of 20 % in respect of the measures in point 9.
- (40) The Commission notes that the capital of DEM 51 000 provided by the investors (point 5) may be regarded as a contribution from the recipient.
- (41) With regard to the interim financing loan of DEM 750 000 (point 6), Germany made it clear in its reply to the decision to initiate the procedure, that the investors were personally liable for 80 % of the loan. The loan was granted at 10,5 % p.a. in the first half of 1996, when the reference rate was 6,69 %. Moreover, it was granted for a limited bridging period of 18 months. In the light of the specific circumstances of this case, the Commission regards this loan as an external commercial contribution to the restructuring.
- (42) In relation to Germany's comments regarding cash flow (point 7), the Commission holds to the position it expressed in its decision to initiate proceedings. Cash flow cannot normally be regarded as a contribution by the recipient since it is directly or indirectly generated through granted aid measures and its exact amount still cannot be guaranteed at the time the restructuring plan is being drawn up. The Commission takes the view therefore that this measure cannot be regarded as a contribution by the recipient.
- (43) The Commission does not share Germany's view that the workforce forms part of the recipient within the meaning of paragraph 3.2.2(iii) of the guidelines. Its contribution cannot therefore be considered as a contribution by the recipient.
- (44) With respect to the loans and credit in the form of a bank guarantee (Avalrahmen) granted by the DKB and totalling DEM 1 932 000 (point 9), the Commission notes that no part of these measures can be regarded as a contribution by the recipient.
- (45) Firstly, it has to be noted that 80 % of these loans were secured by a public deficiency guarantee under an approved aid scheme. In its reply to the decision to initiate proceedings, Germany points out that the total amount of the loans was also secured by private collateral, which should be regarded as a contribution by the recipient. However, the Commission takes the view that the public guarantees meant that the bank did not need to assess the risk of default on this part of the loan because this risk was covered by the State, i.e. an unquestionably solvent debtor. The total amount covered by the 80 % public deficiency guarantee is therefore considered as aid.
- (46) It should also be noted that all the loans and credits in the form of a bank guarantee were also granted by the public authorities at below market terms and therefore contain aid in the form of interest subsidies. The difference between the reduced interest rate and the market interest rate also has to be regarded as aid. Germany argues that at least the amount remaining after deduction of the guarantee and interest subsidy should be regarded as a contribution by the recipient. However, the Commission takes the view that no part of these measures can be considered as having been granted on market terms given the cumulation of the two aid elements and that, to this extent, there was no contribution by the recipient.
- (47) The contribution by the recipient from its own or external commercial sources therefore amounts to DEM 801 000, i.e. 13,45 %. HIG is an SME in an assisted area currently employing some 50 people. The Commission's practice to date has been to approve aid to SMEs with similar investor contributions⁽¹⁷⁾. In these cases, the aid granted had a limited liquidity effect which prevented the firm from being provided with surplus cash that could be used for aggressive, market-distorting behaviour vis-à-vis competitors. In addition, the investors had themselves contributed to the restructuring with their private assets.

⁽¹⁷⁾ Cases: KHK Verbindetechnik GmbH Brotterode (11,5 %), OJ L 31 of 1.2.2002 p. 80; GMB Magnete Bitterfeld (12 %), OJ C 50 of 17.2.1998, p. 6; Stahl- und Maschinenbau Rostock (12 %), OJ C 365 of 18.12.1999, p. 9; Draiswerke (11 %), OJ L 108 of 27.4.1999, p. 44.

- (48) In the present case most of the aid is provided under approved schemes (some DEM 1,75 million). The ad hoc aid of around DEM 1,8 million was used for the acquisition of the assets. It thus had a limited liquidity effect. In addition, of all the bank loans and credits granted to the company (DEM 2 682 000), DEM 2 532 000 was secured by personal guarantees by the investors with prior ranking over the public guarantees. The investors have therefore committed themselves to the restructuring with their personal assets.
- (49) For these reasons, the Commission considers that the investor contribution can be considered significant within the meaning of the guidelines. The aid thus meets the condition of paragraph 3.2.2(iii) of the guidelines that aid must be in proportion to the restructuring costs and benefits.

V. CONCLUSION

- (50) The Commission finds that Germany has unlawfully implemented the aid in question in breach of Article 88(3) of the EC Treaty. However, it notes that, since the aid complies with the 1994 Community guidelines on State aid for rescuing and restructuring firms in difficulty, it is compatible with Article 87(3)(c) of the EC Treaty,

HAS ADOPTED THIS DECISION:

Article 1

The State aid which Germany has implemented for Hoch- und Ingenieurbau GmbH (HIG), amounting to EUR 892 204 (DEM 1 745 000), plus the interest subsidies represented by the annual premiums of 2,44 percentage points inherent in the credit line of EUR 195 313 (DEM 382 000) and of two percentage points inherent in the credit in the form of a bank guarantee (Avalrahmen) of EUR 204 516 (DEM 400 000) from the Deutsche Kreditbank Gera, is compatible with the common market within the meaning of Article 87(3)(c) of the EC Treaty.

Article 2

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 27 February 2002.

For the Commission

Mario MONTI

Member of the Commission

COMMISSION DECISION**of 9 April 2002****on State aid measure C 86/2001 (ex N 334/2001) by which Germany plans to assist Infineon Technologies SC 300 GmbH & Co. KG***(notified under document number C(2002) 1346)***(Only the German text is authentic)****(Text with EEA relevance)**

(2002/867/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 88(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments in accordance with those provisions⁽¹⁾,

Whereas:

the case was discussed with representatives of the German authorities. By letter of 30 August the Commission asked Germany to expand the provisions on *ex post* monitoring in the notification. By letter of 19 September 2001 the Commission reminded Germany that it still had to supply further information. By letter of 24 September 2001, received on 25 September 2001, Germany supplied information which was incomplete. By letter of 1 October 2001 the Commission confirmed that it had received that letter and advised Germany that it still regarded the notification as incomplete. By letter of 22 October 2001, received on 23 October 2001, Germany supplied additional information. By letter of 26 October 2001 the Commission informed Germany that it considered the notification complete, and said it would adopt a final position within two months of the date of receipt of the letter completing the information.

I. PROCEDURE

(1) By letter of 22 May 2001, received on 28 May 2001, Germany informed the Commission that it planned to grant Infineon Technologies SC 300 GmbH & Co. KG investment aid within the scope of the multisectoral framework for regional aid to large investment projects ('the multisectoral framework')⁽²⁾. The Commission registered the planned measure as aid measure N 334/01.

(2) By letter of 13 June 2001 the Commission confirmed that it had received the letter, but informed Germany that it considered the notification incomplete, and asked a number of supplementary questions. By letter of 18 June 2001 the Commission sought further information. Germany supplied further information in letters dated 3 July 2001, received on 5 July 2001, and 16 July 2001, received on 17 July 2001. On 17 August 2001

(3) On 21 November 2001 Germany sent a last letter, received on 22 November 2001, arguing that the aid ought to be declared compatible with the common market under Article 87(3)(b) of the EC Treaty.

(4) On 30 November 2001 the Commission informed Germany that it had decided to initiate the procedure laid down in Article 88(2) of the EC Treaty in respect of the aid.

(5) The Commission's decision to initiate the procedure was published in the *Official Journal of the European Communities* ⁽³⁾. The Commission there asked interested parties to submit comments.

⁽¹⁾ OJ C 368, 22.12.2001, p. 2.

⁽²⁾ OJ C 107, 7.4.1998, p. 7.

⁽³⁾ See footnote 1.

- (6) By letters of 10 January 2002, received on 14 January 2002, and 28 January 2002, received on 29 January 2002, Germany responded to the initiation of the procedure. By letter of 15 February 2002 the Commission sought additional information. Germany replied by letter of 27 February 2002, received on 28 February 2002. The Commission put further questions by letter of 21 March 2002, which Germany answered by letter of 24 March 2002, received on 25 March 2002.
- (7) Three interested parties sent observations to the Commission, which the Commission forwarded to Germany for comment; Germany replied by letter of 18 February 2002, received on 19 February 2002.
- (8) The undertaking concerned supplied additional information by letter of 7 March 2002, received on the same day.

- (10) Germany has supplied the following figures for Infineon's turnover and staffing in the years 1999 to 2001:

	Worldwide		(EUR million)		Workforce	
	EEA Germany	Turnover	Workforce Turnover	(EUR million)	Turnover (EUR million)	Workforce
1998/1999	4 237	24 541	2 444	15 543	1 241	12 352
1999/2000	7 283	27 210	3 259	16 603	1 612	13 522
2000/2001	5 671	33 813	3 005	21 821	1 745	16 814

- (11) In the financial year 1997/1998 Infineon made a loss of EUR 775 million; in 1998/1999 it showed a profit of EUR 61 million; and in 1999/2000 it made a profit of EUR 1 126 million.

2.2. The project

- (12) The investment project is located in Dresden, in Saxony, which is an assisted area within the scope of Article 87(3)(a) of the EC Treaty.
- (13) A fabrication plant is to be built for dynamic random access memories (DRAMs) with a line width of 0,14 µm and below, using 300 mm silicon disks, also known as 'wafers'. This will be the first production line in the world for memory chips on 300 mm wafers. In addition to the production line, SC 300 will also operate a pilot and development line with the facilities already existing in the plant.

II. DESCRIPTION

2.1. The recipient

- (9) The recipient, Infineon Technologies SC 300 GmbH & Co. KG (SC 300), was founded in February 1998, and is an 87 %-owned subsidiary of Infineon Technologies AG, of Munich (Infineon). Infineon itself became a publicly quoted company in March 2000; it had been hived off from Siemens AG, taking Siemens's semiconductor business with it. The remaining shares in SC 300 are held 4 % by the private limited company M + W Zander Facility Engineering GmbH, through SC 300 Beteiligungs GmbH, of Stuttgart, and 9 % by the private limited company Leipziger Messe GmbH, which is controlled by the Land of Saxony and the City of Leipzig. Infineon's core business is semiconductors. Germany emphasises that Infineon is the only European undertaking competing on this market.

- (14) The project started in April 2000, and is to be completed by the end of 2003. Total output is ultimately to reach 5 000 wafer starts per week. The plant is to be built in two phases. Mass production began at the end of 2001, but is still substantially below final capacity. In the second phase, lasting until approximately the beginning of 2003, production capacity is to be raised to maximum. According to the information supplied this two-phase expansion is economically the most viable approach, especially because mass production of the new technology is still in the process of development.

- (15) The DRAMs to be manufactured will have a storage capacity of 512 megabits and beyond. These DRAMs will gradually replace DRAMs with a capacity of 256 megabits or less. Infineon currently produces the lower-capacity DRAMs in Dresden, the United States of America and Taiwan.

(16) The move from the production of chips on 200 mm wafers to production on 300 mm wafers means that the number of chips per wafer (or productivity) will increase about 2,5 times. This is expected to reduce manufacturing costs per chip by 30 % to 40 %. The lower line width reduces production costs further. It also permits a smaller minimum feature size, enabling computer parts to be smaller and cheaper.

(17) The costs of the project can be broken down as follows:

(in EUR million)		
Item	Total	Eligible
Land	[...] (*)	[...]
Buildings	[...]	[...]
Plant and machinery	[...]	[...]
Tools	[...]	[...]
Other	[...]	[...]
Total	1 106	1 106

(*) Business secret.

(18) The new project will increase Infineon's worldwide share of the market for DRAMs from 8 % in 1999 to 10 % in 2003, and its share of the market in semiconductors from 3,5 % in 1999 to 3,7 % in 2003.

(19) The notification stated that the investment would create 1 300 permanent jobs and safeguard 400 permanent jobs. Indirectly the project was expected to lead to the creation of 1 030 jobs in its own assisted region and an adjacent assisted region.

2.3. Aid measures

(20) The proposed assistance consists of investment aid in the form of a non-repayable grant amounting to EUR 88 073 million, to be granted in accordance with the 29th Outline programme under the Joint Federal Government/Länder Scheme for the improvement of regional economic structures (*Gemeinschaftsaufgabe Verbesserung der regionalen Wirtschaftsstruktur*), a scheme which has been authorised by the Commission. An investment allowance of EUR 128,846 million is to be granted under the Investment Allowance Act 1999, a scheme likewise authorised by the Commission⁽⁴⁾. A

guarantee is also to be given on a loan of EUR 450 million, covering 80 %, or EUR 360 million, once again under an authorised scheme⁽⁵⁾. On the basis of the information supplied by Germany the Commission calculates that the aid component in this guarantee is EUR 1,8 million. The total aid to the recipient amounts to EUR 218,718 million, which corresponds to 19,8 % of the eligible investment costs. The non-repayable grant is given only towards the first phase of construction.

2.4. Grounds for initiation of formal enquiry

(21) On 30 November 2001 the Commission informed Germany that it had decided to initiate the formal investigation procedure laid down in Article 88(2) of the EC Treaty with respect to the proposed aid to the project. The Commission doubted whether the planned aid intensity of 19,8 % was compatible with the maximum allowable aid intensity which has to be calculated in accordance with the multisectoral framework. In particular, the Commission had no reliable information that would enable it finally to determine the characteristics of the market, and it could not exclude the possibility that the market was in absolute decline. It doubted whether account could properly be taken of all of the research and development jobs claimed, because some might not be directly associated with the project. It questioned whether the number of jobs indirectly created which had been estimated by Germany could be used to assess the regional impact of the project.

(22) The Commission also doubted whether the project would qualify as a 'project of common European interest', which might allow it to be authorised under Article 87(3)(b) of the EC Treaty.

III. COMMENTS FROM INTERESTED PARTIES

(23) The Commission received comments from two associations of downstream industries in which DRAMs are used, and from an independent association of European businesses and research institutes in the European circuit board industry. The comments were forwarded to Germany by letters of 22 and 24 January 2001. Germany replied by letter of 18 February 2002.

⁽⁴⁾ Investitionszulagengesetz, aid measure C 72/98 (ex N 702/97), SG (98) D/12438, 30.12.1998, and SG (2001) D/28651, 2.3.2001.

⁽⁵⁾ Federal Government and Länder direct guarantee scheme in the new Länder and East Berlin (*Programm für unmittelbare Bürgschaften des Bundes und der Länder in den neuen Bundesländern und Berlin Ost*), aid measure N 297/91, SG (91) D/1344, 15.7.1991, and aid measure E 24/95, SG (96) D/5500, 18.6.1996, and SG (98) D/54570, 11.11.1998.

(24) All three interested parties were in favour of the proposed aid. They stressed the importance of the European semiconductor industry and the significant role of the project in strengthening the competitiveness of the semiconductor and related industries.

(25) In a letter of 7 March 2002, SC 300 pointed out that prices for DRAMs were recovering, and that a further increase was expected. According to a business news service the market in DRAMs would increase by 55 % in 2002.

IV. COMMENTS FROM GERMANY

(26) In its comments on the initiation of the procedure Germany stressed the importance of the project. Infineon was the only producer of DRAMs in Europe, and the new 300 mm technology would give it a cost advantage over its competitors. Infineon expected the demand for memory chips (measured in bits) to grow by 50 % between 2001 and 2002.

(27) According to Germany, the market in DRAMs was characterised by pronounced cyclical fluctuations and strong discrepancies between the value and volume of the market. The competition factor should be set at 1, as there was no overcapacity and the market was not declining.

(28) Germany argued that there was no overcapacity at the aggregated NACE 32.10 level, and submitted relevant data. If the Commission were to consider that the capacity situation at this aggregated level did not adequately reflect the situation of the DRAM industry, Germany argued in the alternative that a subsector at a lower level could be considered. Data on capacity utilisation did not necessarily have to be based on the lowest NACE level in order to assess the competition factor. Germany provided figures to show that there was no overcapacity no matter how tightly the relevant subsector was defined. According to Germany, capacities for DRAMs were almost fully utilised (95 % to 100 %) in the years 1994 to 1999.

(29) In the event that the Commission did not agree to base its assessment of the competition factor on capacity utilisation data, Germany submitted that the market in DRAMs was not in decline. The multisectoral framework provided for a period of five years for the calculation of the average annual growth rate to assess the development of the market. For the project at issue here, therefore, the relevant period was 1996 to 2000, and

the average annual growth over that period had been positive. In 1995, market volume in value terms had been exceptionally high. That year was not representative, and no account should be taken of it in the assessment of market developments.

(30) Germany submitted that when the Commission had decided to initiate the formal investigation procedure it had based its assessment of the market purely on the movement of apparent consumption in value terms. But apparent consumption in volume terms, measured in bits, had grown strongly over the period 1996 to 2000, at an average of 83,3 % per annum. Volume figures gave a better picture of the market position, because especially on markets such as the market in DRAMs, where prices fluctuated widely, value figures did not properly reflect market capacity. In value terms consumption was volatile, but expressed in bits it had been growing constantly. In earlier decisions taken under the multisectoral framework the Commission had considered consumption in volume terms too. Germany also argued that consumption figures in value terms were not meaningful, because they were distorted by subsidies given by the Korean Government.

(31) Germany submitted the latest forecasts for the DRAM market, which predicted an average annual growth rate of 17,7 % for the years 2001 to 2004.

(32) On the question of jobs created directly, Germany argued that all jobs related to research and development should be taken into account. The semiconductor industry was research-intensive, and the project at stake would implement a new production technology. A highly innovative project such as the 300 mm technology consequently required particularly heavy expenditure in research and development, not only before implementation, but also during the production period, in order to optimise the application of the new technology.

(33) On the question of the jobs created indirectly, Germany submitted that the total number of jobs created for every job created by the recipient itself was in the medium range. It was difficult to give precise figures for the jobs that would be created by suppliers and customers. Germany submitted statements of intent from SC 300 suppliers and customers according to which 729 jobs had already been created indirectly as a result of the project, and another 666 would be forthcoming.

- (34) Germany therefore took the view that an assessment of the aid under the multisectoral framework should not lead to a reduction in the proposed aid intensity. If the Commission did not accept this view, Germany asked that the aid be authorised under Article 87(3)(b) of the EC Treaty. Germany considered that the four tests of applicability of that provision were satisfied.
- (35) Without the proposed aid measures SC 300 would not be able to carry out the investment project. The semiconductor industry was highly capital-intensive, and was characterised by high technological risks. In view of the financial and technological dimensions of the project it could not be expected that SC 300 would carry out the project without public assistance.
- (39) The DRAM industry was a strategic sector. The Commission had authorised State aid for research and development in the past. It would be contradictory to limit State aid now that this new technology was to be implemented.
- (40) Germany therefore took the view that the proposed aid could be authorised under Article 87(3)(b).
- (41) In its reply to the comments submitted by interested parties, Germany pointed out that they confirmed that European industry had an interest in the SC 300 project because of the expected synergies, which could lead to increased growth in European industry. The comments of the interested parties also showed that industry supported the proposed State aid.

V. ASSESSMENT

5.1. Assessment under Article 87(3)(a) of the EC Treaty

- (36) The project was important both quantitatively and qualitatively. Infineon was the only European producer of DRAMs, a market dominated by non-European producers. It could maintain its position on the market only if it succeeded in applying the 300 mm technology, in which it was a step ahead of the competition, and which gave it a significant cost advantage over its competitors. The fact that for the first time a European producer was leading in innovation would give the semiconductor industry and its suppliers an opportunity to catch up with the leading economies.
- (37) As regards the criterion of common European interest, Germany submitted that the implementation of the new 300 mm technology would improve fundamental production processes for semiconductors. The project would thus enhance the competitiveness and effectiveness of European industry. For equipment manufacturers it was of great importance that there should be a European DRAM producer. Owing to the close connection with related industries, the existence of a European DRAM producer favoured the development of those industries and of the semiconductor industry as a whole.
- (38) For a project to qualify as being of common European interest, it was not necessary that more than one Member State be involved. A strengthening of the economic structure in one Member State could be in the Community interest if it enhanced the international competitiveness of European industry. The participation of several Member States was not indispensable.
- (42) The aid has been granted for a new investment in an assisted area within the scope of Article 87(3)(a) of the EC Treaty, and must be assessed as regional aid.
- (43) The proposed aid amounts to EUR 218,718 million. This is above the notification threshold of EUR 50 million, so that the project is subject to the notification requirement laid down in the multisectoral framework, and has to be assessed accordingly.
- (44) Before the proposed aid can be assessed, the multilateral framework requires that the relevant market be determined.
- 5.1.1. *The relevant market*
- (45) The relevant product market to be referred to, in order to determine market share, comprises the product to which the investment project relates and any products regarded by customers or producers as substitutes.
- (46) The investment involved here relates to the production of DRAMs. DRAMs belong to class 32.10 in the NACE nomenclature, which comprises the manufacture of electronic components. DRAMs are electronic components: they are semiconductors that store binary data. They are the most common type of semiconductor memory. Their main applications are in PCs and low-cost manufacturing.

- (47) DRAMs can be differentiated according to their memory size, i.e. the quantity of data that can be stored on the chips. The size depends on the generation of the chips. The product is subject to rapid technological change, with a new generation arriving on the market every three or four years. DRAMs can also be differentiated according to the intended application (FPM DRAMs, EDO DRAMs, SDRAMs or RDRAMs), or the type of product in which they are to be installed.
- (48) There are other types of chip, such as SRAMs (static random access memories), EPROMs (electrically programmable read-only memories), and flash memories. In general these perform functions different from DRAMs, and cannot be regarded as substitutes.
- (49) DRAMs are commodity products whose specifications are standardised. Seen from the demand side, the same type of DRAM is available to customers from various suppliers around the world. New generations of DRAMs are targeted to compete with older ones. The preference of a customer for a specific type depends on the cost-performance relationship and the function of the DRAM in the finished product.
- (50) Seen from the supply side, manufacturers can produce DRAMs with different capacities, because the technologies employed are similar. However, switching between different generations of DRAMs is in general not easy within a particular facility.
- (51) The Commission accordingly considers that the relevant product market is the market in DRAMs⁽⁶⁾. No separate NACE classification exists for this market.
- (52) Turning to the relevant geographic market, it can be accepted that DRAMs are traded worldwide on the basis of the same classifications and marketing concepts. Transport costs are low, and there are no structural barriers to market entry. The Commission therefore considers that the relevant geographic market is the world.
- 5.1.2. *Multisectoral framework on regional aid*
- (53) Under the multisectoral framework on regional aid, the Commission, in order to determine the maximum allowable aid intensity for a proposed aid project, must begin by identifying the maximum aid intensity (regional aid ceiling) which a company could obtain in the assisted area concerned within the context of the authorised regional aid scheme valid at the moment of the notification.
- (54) In the area in which SC 300 is located the maximum aid intensity for large undertakings splits into two rates, 28 % and 35 % gross. The 35 % intensity is available only on certain conditions: higher rates of aid may be granted in justified special cases, on application by a *Land*, and with the approval of the subcommittee of the Planning Committee, towards measures with a high structural impact in areas exposed to international competition in respect of business location⁽⁷⁾.
- (55) Germany has not indicated whether these conditions are met here. As SC 300 is a large undertaking, the Commission presumes that the authorised maximum aid intensity (R) in this case is 28 %. The planned gross aid intensity of 19,8 % is therefore within the admissible ceiling for a large undertaking in the region.
- (56) The Commission has then to adjust the 28 % percentage figure in accordance with three specific assessment factors in order to calculate a maximum allowable aid intensity for the project in question: these are the competition factor (T), the capital-labour factor (I), and the regional impact factor (M).
- The competition factor (T)
- (57) The authorisation of aid to companies operating in sectors which are in structural overcapacity poses particular risks for the distortion of competition. Any capacity expansion which is not compensated by capacity reductions elsewhere will exacerbate the problem of structural overcapacity. The sector or subsector to be considered will be established at the lowest available segmentation of the NACE classification.
- (58) The lowest available NACE code including the manufacture of DRAMs is class 32.10, which covers the manufacture of electronic components of all kinds. Germany has provided figures for capacity utilisation in this NACE class, and has argued that there is no overcapacity. But DRAMs account for only a small part of NACE class 32.10, and capacity utilisation at this aggregated level does not provide an adequate picture of the situation on the market in DRAMs.

⁽⁶⁾ The relevant product market was defined in the same way in the Commission Decision in Hitachi/NEC Case IV/M 0044, Decision of 3.5.2000 (OJ C 153, 1.6.2000, p. 8).

⁽⁷⁾ OJ C 340, 27.11.1999, p. 8.

- (59) As mentioned in recital 28, Germany argues that the subsector need not necessarily correspond to a level in the NACE nomenclature. But footnote 13 to point 7.7 of the multisectoral framework states that 'the sector or subsector will be established at the lowest available segmentation of the NACE classification'. The lowest available segmentation of the NACE classification is NACE code 32.10. As explained in recital 58, capacity data for this aggregated level are not sufficient to allow a determination of the capacity position on the market in DRAMs, which is considered to be the relevant product market. The Commission therefore takes the view that the assessment of the competition factor should not take account of an analysis of the capacity position.
- (60) Point 3.4 of the multisectoral framework states that 'In the absence of sufficient data on capacity utilisation, the Commission will consider whether the investment takes place in a declining market.' A market is considered to be 'declining' if, over the last five years, the average annual growth rate of apparent consumption of the product in question is more than 10 % below the annual average of EEA manufacturing industry as a whole, unless there is a strong upward trend in the relative growth rate of demand for the product. A market is 'absolutely declining' if the average annual growth rate of apparent consumption over the last five years is negative.
- (61) As explained in recitals 45 to 51, the relevant product market is considered to be the market in DRAMs, as there is only limited substitutability between different types of memory chip. DRAMs are traded on a world-wide basis, so that the relevant geographic market is global.
- (62) The market share of SC 300 and Infineon does not exceed 40 % of the relevant market, nor will it exceed this percentage as a result of the new investment. In 1999 Infineon's share of the DRAMs market was 8 %. In 2003, when the project has been completed, Infineon and SC 300 are expected to have a share of 10 %.

- (63) Germany has submitted the following figures for apparent consumption of DRAMs in the world from 1995 to 2000, based on data provided by an independent research institute, VLSI Research Inc.:

	1995	1996	1997	1998	1999	2000	Average annual growth rate
Value (EUR billion)	31,952	20,101	17,594	12,514	19,431	31,285	- 0,42 %

- (64) According to these figures, the average annual growth in apparent consumption on the DRAMs market in the years 1995 to 2000 was -0,42 %. In the preceding period, i.e. from 1994 to 1999, the rate was likewise negative, at -1,3 %. This would lead to the conclusion that the market in DRAMs is in absolute decline.
- (65) Germany argues that in order to assess the movement of apparent consumption the Commission should consider a period of five years, i.e. 1996 to 2000, rather than a six-year period. But the multisectoral framework refers to the average annual growth rate of the last five years. It has therefore been the Commission's practice to look at apparent consumption over six years, so as to be able to calculate five growth rates ⁽⁸⁾.
- (66) Germany has submitted the most recent forecast of the future development of the DRAMs market provided by an independent research institute ⁽⁹⁾:

	2001	2002	2003	2004	Average annual growth rate
Value (EUR billion)	12,502	12,919	16,748	20,559	18,1 %

⁽⁸⁾ See Wacker Chemie, State aid measure N 783/2000, Commission Decision of 8.5.2001, Kronoply, State aid measure N 813/2000, Commission Decision of 3.7.2001, and Hamburger AG, State aid measure C 72/2001, Commission Decision of 2.10.2000, OJ C 342, 5.12.2001, p. 9.

⁽⁹⁾ WSTS, fourth quarter forecast update (February 2002).

- (67) Despite the serious difficulties being experienced at present, the outlook for the DRAMs market is positive. Latest forecasts expect apparent consumption of DRAMs to grow in value by an average of 18,1 % in the years 2001 to 2004. According to this forecast, however, apparent consumption in 2004 would still be below the level of the year 2000. Another study considered by the Commission predicts an even stronger upward tendency in future, with apparent consumption exceeding the level of 2000 in 2003 and 2004.
- (68) The market in DRAMs is highly cyclical and characterised by strong fluctuations. Average annual growth rates in value terms differ significantly depending on the period considered. In the period 1993 to 2000 the average annual growth rate of apparent consumption, expressed in terms of value, was positive, at 14,66 % per year. Despite a drastic fall in apparent consumption between 2000 and 2001, the average annual growth measured from 1993 to 2001 was still just positive, at 0,51 %.
- (69) The wide fluctuations on the market in DRAMs are due mainly to the fact that prices are extremely volatile. The DRAM production process is characterised by relatively high sunk costs and low marginal costs. As a consequence, prices can move in a very wide range, as companies can produce DRAMs profitably as long as their marginal costs are covered. To look at the development of apparent consumption only in value terms, therefore, may give an inadequate picture of the market in DRAMs.
- (70) Apparent consumption expressed in terms of volume, that is to say measured in units sold, has in recent years seen steady and substantial growth. From 1995 to 2000 the average annual growth rate was 10 %, and from 1994 to 1999 it was 11 %.
- (71) Over the long term DRAM prices have shown a downward trend. But this does not seem to be a consequence of overcapacity in the industry, although it is true that stocks have sometimes built up to a high level, and prices have collapsed as a result. Production costs have fallen considerably in recent years. The falls in prices have thus been caused by constant improvements in the efficiency of production resulting from the reduction in the line width and routine changes in wafer diameter, from one inch in the 1970s to 300 mm today. The yield has also improved constantly, as manufacturers have sought to reduce the number of non-functioning circuits and to increase the number of working circuits on the wafer.
- (72) When it initiated the procedure the Commission said that it had not got sufficient reliable information to be able finally to determine the exact characteristics of the market for the purpose of setting the correct competition factor.
- (73) The Commission accordingly concludes that the market should be considered to be in relative decline, rather than in absolute decline. This is confirmed by the fact that capacities have been used nearly to the full in recent years, with capacity utilisation rates significantly above the average for manufacturing as a whole. The Commission therefore sets the competition factor at 0,75.

The capital-labour factor (I)

- (74) For highly capital-intensive projects the multisectoral framework provides for a 'capital-labour factor' which is intended to adjust the maximum allowable intensity so as to give an advantage to projects that make a genuine and better contribution to reducing unemployment by creating or safeguarding a relatively higher number of jobs. This factor also takes account of any distorting effects of the aid on the price of the final product.

- (75) The multisectoral framework expressly provides that jobs safeguarded are to be considered only where it is shown that they are directly associated with the investment project, would require a significant amount of retraining, and would otherwise no longer exist when the project goes into production.
- (76) In the case at issue the number of jobs created would be 1 300, and the number safeguarded would be 400. They break down as follows:

	Jobs safeguarded	New jobs	Total
Management	9	1	10
Business administration	11	28	39
Production control	9	12	21
Production operators	177	584	761
Production maintenance	64	204	268
Production engineers	62	87	149
Process development	35	64	99
Automation/IT/CIM	18	32	50
Facilities		59	59
Technology, quality, product engineering	15	90	105
Technology development		102	102
Environmental protection		6	6
Logistics		31	31
TOTAL	400	1 300	1 700

- (77) The jobs to be safeguarded are related to SC 300's existing pilot and development line. According to Germany, if the new project were not carried out, SC 300 would not continue its activities, the equipment would be sold, and the jobs would be lost. The jobs safeguarded are therefore directly associated with the project. The Commission understands that a large part of these jobs are in research and development work for ordinary product development.
- (78) The capital-labour ratio is significantly lower than in two other projects in the semiconductor industry. According to Germany this is partly the result of the integration of engineering activities and jobs linked to research and development activities. When it initiated the procedure the Commission said it doubted whether all jobs in research and development could be taken into account, as they might not be directly associated with the project.

- (79) In the comments it put forward following the initiation of the procedure, Germany explained the high number of jobs in research and development. Germany also confirmed that SC 300 was not receiving any State aid towards R&D. The Commission therefore concludes that all of the 1 700 direct jobs claimed by Germany can be taken into account in the calculation of the capital-labour factor. The capital-labour factor for an investment of EUR 1 106 million which would directly create or safeguard 1 700 jobs corresponds to EUR 650 588 per job, and can therefore be set at 0,8.

The regional impact factor (M)

- (80) The regional impact factor reflects the economic benefit to the assisted area. The Commission considers that job creation can be taken as an indicator of the contribution of an investment project to regional development. Capital-intensive investments may indirectly create jobs in the assisted area or in an adjacent assisted area; 'job creation' here refers to jobs created directly by the project and jobs created by first-tier suppliers and customers.
- (81) The notification stated that the jobs created indirectly as a result of the investment were estimated at 1 030, mainly among suppliers. They broke down as follows:

	Indirectly created jobs
Supply of 300 mm silicon wafers	600
Reclaiming of 300 mm test wafers	100
Extension of infrastructure (safety, cleaning, catering)	12
Supply of materials	40
Maintenance of equipment	90
Transport	30
Building infrastructure	50
TOTAL	1 030

This figure of 1 030 was revised in the most recent information supplied by Germany.

lines for 150 mm and 200 mm wafers. Germany states that Freiberg city council has recently agreed to the development plan for the extension of the plant. Germany has also submitted a letter of intent from [...]. Germany argues that there is no reason to doubt that the project will be carried out.

- (82) A new plant was originally to be constructed by [...] to deliver 300 mm disks to SC 300, and this was expected to create 600 indirect jobs. When it initiated the procedure the Commission said it doubted whether this project would be carried out, and argued that no account could be taken of the 600 jobs which were allegedly to be created there.

- (83) [...] currently has two production sites in Germany, in Burghausen and Freiberg. In Freiberg it runs production

- (84) In the letter of intent [...] it states that the SC 300 project will lead to the creation of 120 jobs. According to Germany, this figure is based on the assumption that 20 % of [...]’s output will be delivered to SC 300. SC 300 has given [...] express confirmation of this figure, but it should be regarded as a minimum. It is fair to assume

that [...] will deliver at least 50 % of its output to SC 300, which would mean that the number of jobs indirectly created would be 300. For legal reasons SC 300 was unable to give [...] an express undertaking to take this quantity, so that the figures in the letter of intent are too low. The Commission takes the view that for the assessment of the regional impact account can be taken of 120 jobs created by [...].

- (85) Germany has also submitted a letter of intent from [...], a company which already supplies SC 300, and plans to set up a new plant for reclaiming test wafers. Reclaiming is a process for recycling wafers that are used at various points for monitoring the DRAM production process, and which can be reused. Recycling silicon wafers is worthwhile because they are very expensive. Most recycled wafers are used once again as test wafers. In the notification Germany said that 100 jobs would be created in the reclaiming of test wafers. According to the most recent information supplied, [...] would create 130 indirect jobs. Germany states that 95 of these are attributable to the SC 300 project. The Commission takes the view that for the assessment of the regional impact account can be taken of 95 indirect jobs created by [...].
- (86) Germany originally indicated that 330 jobs would be created indirectly by the extension of the infrastructure, the supply of materials, transport and building maintenance. In letters of 29 January 2002, 27 February 2002 and 25 March 2002, Germany expressed the opinion that the number of jobs indirectly created in these areas would be 1 145, and submitted statements of intent from 53 firms which were customers of or suppliers to SC 300. Germany stated that 729 of these jobs had already been created, and another 416 were expected.
- (87) The number of jobs to be created in infrastructure is 224. This comprises jobs related to safety, catering and cleaning. As mass production has already begun, and the majority of the employees are already at work, 150 of these jobs have already been created.
- (88) The number of jobs expected to be created in the supply of materials is 174. This comprises the supply of gas, water, electricity and the chemicals needed for the production process, the associated preparatory processing and logistics. Of these 122 jobs have already been created.
- (89) A further 438 jobs are expected to be created in equipment maintenance. Of these, 282 have already been created. Germany has stated that these jobs involve activities relating to the maintenance of the equipment installed in the factory. Servicing of this kind is necessary because the operation of semiconductor factories is characterised by a constant turnover in production plant and components.
- (90) In the transport of raw materials and inputs, 21 jobs have already been indirectly created. Another 13 indirect jobs are to be created here.
- (91) For the maintenance of the building infrastructure, Germany expects a total of 275 jobs indirectly created. These jobs arise out of regular work that has to be done to preserve the quality of the building infrastructure, including such things as IT services, operation and maintenance of electrical systems, ventilation and clean-room installations, and work related to the management of the building. Of these jobs 121 have already been created.
- (92) The multisectoral framework provides that for the assessment of the regional impact of a project jobs created indirectly by first-tier suppliers and customers in response to the aided investment can be taken into account. In this context a 'job' means a permanent full-time job or its part-time equivalent.
- (93) Germany has confirmed that the indirect jobs satisfy these tests. In explanation of the fact that a large proportion of the indirect jobs has already been created, even though the plant will be working at full capacity only at the beginning of 2003, Germany says that the building work was completed in April 2001. After that the initial phase or 'ramp up' began. At that stage the plant and machinery was installed in order to begin test and pilot production; this was done in early summer 2001. Mass production started in December 2001.
- (94) On the basis of the information provided by Germany, the Commission takes the view that the calculation of jobs indirectly created is a fair one. The Commission concludes that the number of jobs indirectly created in response to the aided programme will be 1 360. As compared with the 1 700 jobs created or safeguarded directly, the degree of indirect job creation is therefore medium (between 50 % and 100 %), and the Commission accordingly sets the regional impact factor at 1,25.

Maximum allowable aid intensity

- (95) For these reasons, the maximum allowable aid intensity is to be calculated as follows: $28 \% \times 0,75 \times 0,8 \times 1,25 = 21 \%$ gross. The aid of EUR 218 718 million which Germany plans to grant to SC 300 towards its investments in Dresden, Saxony, equivalent to an aid intensity of 19,8 % gross, is therefore within the maximum allowable aid intensity calculated in accordance with the multisectoral framework on regional aid.

5.1.3. Ex post monitoring

- (96) In view of the sensitive nature of the large mobile investments involved, it is essential that a mechanism exists which helps to ensure that the level of aid actually disbursed conforms with the Commission Decision.
- (97) For each aided project approved by the Commission under the multisectoral framework, therefore, the Commission requires either that any aid contract between the relevant authority of the Member State and the aid recipient contains a reimbursement provision in the event of non-compliance with the contract, or that the final significant payment of the aid (e.g. 25 %) will be made only when the Commission, on the basis of information from the recipient provided by the Member State, is satisfied that execution of the project is in compliance with the Commission decision and within 60 working days has indicated its agreement or raised no objections to the final payment of the aid.
- (98) The Commission notes that the proposed decision to grant aid to SC 300 contains a provision providing for reimbursement in the event that the recipient infringes the decision granting the aid.
- (99) The Commission notes that the final significant payment of the aid (25 %) will be made only when SC 300 has shown the German authorities that the project has been carried out in conformity with the Commission Decision.

- (100) The Commission also notes that the undertaking given by Germany concerning *ex post* monitoring complies with the obligations laid down in point 6 of the multisectoral framework. In particular, Germany has undertaken to supply a copy of the decision to grant the aid, an annual report on the project, and the other information and documents referred to in point 6.4 of the multisectoral framework.

5.2. Article 87(3)(b) of the EC Treaty

- (101) In the event that the Commission does not authorise the proposed aid intensity of 19,8 %, Germany relies alternatively on Article 87(3)(b) of the EC Treaty, and argues that the establishment of the chip factory is a project of common European interest. However, as aid of the planned intensity of 19,8 % is within the maximum allowable aid intensity calculated in accordance with the multisectoral framework on regional aid, there is no need to consider the question of the common European interest any further here.

VI. CONCLUSIONS

- (102) On these grounds the Commission concludes that the aid satisfies the tests of compatibility with the common market,

HAS ADOPTED THIS DECISION:

Article 1

The state aid amounting to EUR 218 717 884 which Germany plans to grant to Infineon Technologies SC 300 GmbH & Co. KG is compatible with the common market.

Article 2

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 9 April 2002.

For the Commission

Mario MONTI

Member of the Commission

COMMISSION DECISION**of 17 July 2002****on the aid scheme implemented by Italy in order to reduce the number of single-hull tankers older than 20 years in the Italian tanker fleet***(notified under document number C(2002) 2437)***(Only the Italian text is authentic)****(Text with EEA relevance)**

(2002/868/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 88(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provision(s) cited above and having regard to their comments⁽¹⁾,

Whereas:

1. PROCEDURE

(1) By letter No 542 of 15 January 2001, registered on 18 January 2001 as SG(2001)A/787, Italy notified, in accordance with Article 88(3) of the EC Treaty, a draft aid scheme to speed up the elimination of single-hull tankers 20 years of age or older. By letter of 23 February 2001, registered on the same day, Italy sent details of the current status of the draft law. By letter of 6 March 2001, the Commission asked the Italian Government to supply further information, which was received by letter No 5786 of 4 May 2001, registered on 7 May 2001 as SG(2001)A/5870. Thereafter, Italy provided additional information by letter No 8665 of 5 July 2001, registered on 10 July 2001, by letter of 19 July 2001, registered on 23 July 2001, by letter of 3 September 2001, registered on 4 September 2001, by letter of 25 September 2001, registered on 9 October 2001 (as SG(2001)A/11100), by letter of 24 October 2001, registered on 24 October 2001 (as SG(2001)A/11814), and by letter of 22 November 2001, registered on 27 November 2001 as No 14632.

(2) By Decision of 20 December 2001, notified to the Italian Government by letter dated 28 December 2001 (SG(2001) D/293162), the Commission initiated the procedure laid down in Article 88(2) of the Treaty in respect of the present aid. The procedure has been registered under C 97/2001.

(3) The Commission Decision to initiate the formal investigation procedure has been published in the *Official Journal of the European Communities* ⁽²⁾. The Commission invited interested parties to submit their comments on the aid.

(4) Italy forwarded comments to the Commission by letter of 25 January 2002, registered on 31 January 2002. A further letter with additional information and commitments was sent on 3 May 2002.

(5) Within the time frame indicated in the publication, the Commission received comments from the following interested parties: the Comité Central des Armateurs de France by letter of 21 March 2002, the Swedish shipowners' association by letter of 21 March 2002, the Chamber of Shipping by letter of 21 March 2002, Norges Rederiforbund by letter of 21 March 2002, the Norwegian Royal Ministry of Trade and Industry by letter of 22 March 2002, Danmarks Rederiforening by letter of 21 March, and finally Mediterranea di Navigazione by letter of 4 March 2002. The Commission also received comments from Ermewa Maritime by letter of 4 April and Confitarma by letter of 25 March, sent after the expiry of the formal deadline for reaction of 22 March 2002.

⁽¹⁾ OJ C 50, 23.2.2002, p. 7.

⁽²⁾ See footnote 1.

2. DETAILED DESCRIPTION OF THE AID

2.1. The aid scheme

- (6) The aid scheme is intended to promote and expedite the ban on single-hull ships in Italy and is targeted at owners of oil and chemical tankers. It is based on Articles 3, 4 and 5 of Law 51/2001 (*Disposizioni per la prevenzione dell'inquinamento derivante dal trasporto marittimo di idrocarburi*) designed to prevent accidents at sea involving tankers, which was published on 7 March 2001 and entered into force on the same day. The Italian authorities have, however, undertaken not to pay any aid before obtaining authorisation from the Commission.

2.2. Background

- (7) The sinking on 12 December 1999 of the oil tanker Erika, a 25 year-old single hull, aroused great public concern about the safety of maritime transport. The disaster highlighted the potential environmental and safety risks inherent in old, poorly maintained vessels and the consequent need to strengthen and harmonise maritime safety standards and rules on the inspection of vessels in ports. In the circumstances, the Italian authorities, like the Commission, took the view that they should, if necessary, go beyond the international rules existing or planned at that time.
- (8) Italy regarded the ships used for cabotage services between Italian ports as representing the greatest source of risk to the environment and to safety. The situation in Italy at that time gave grounds for particular concern as 54 % of oil or oil products were not shipped either in double-hull tankers or in single-hull tankers complying with the highest standards⁽³⁾. Moreover, Italy was particularly involved in the Erika case as the company operating the wrecked tanker was Italian, even though it was sailing under the flag of a third country, and, having taken its cargo on board in Dunkirk, France, the vessel was heading for the Italian port of Milazzo.
- (9) Following the sinking of the Erika, the Italian Minister for the Environment announced his intention to ban single-hull ships from the majority of Italian ports, taking up the measures applied in the port of Venice since December 1999. Debates on improving safety and on the present aid scheme, which was formally brought

before the Italian Parliament in March 2000, enabled the Italian Government to come up with a solution more flexible than the total ban, to which there were objections at international level. The International Maritime Organisation (IMO) and Community later both passed legislation which went further, in some respects, than the Italian measures.

2.3. The environmental and safety context

Safety legislation

- (10) In March 2000, the Commission presented a Communication on the safety of the seaborne oil trade⁽⁴⁾. The Commission presented a second Communication with an additional set of proposals in December 2000⁽⁵⁾. In the Communication of March 2000, the Commission proposed three measures to be adopted in the short term:
- more stringent in-port inspections of ships calling at Community ports,
 - closer supervision of classification societies, and
 - accelerating the timetable, which had previously been agreed at the IMO, for banning single-hull oil tankers from EU waters.
- (11) The third measure was motivated by the statistical evidence of increased accident rates for older ships and by the need to align with the American Oil Pollution Act of 1990 in order to prevent the single hull tankers banned from American waters after 2005 starting to operate in European waters.
- (12) It is in the Community's interest to adopt measures to ensure that oil tankers entering ports and offshore terminals under Member State jurisdiction and, oil tankers flying the flags of Member States comply with Community legislation. Such measures are aimed at reducing the risk of accidental oil pollution in European waters.

⁽³⁾ SBT/PL: double-hull tanker, segregated ballast tanks in protective locations.

⁽⁴⁾ Erika I: Communication from the Commission to the European Parliament and the Council on the safety of the seaborne oil trade, COM(2000) 142 final, 21 March 2000.

⁽⁵⁾ Erika II: Communication from the Commission to the European Parliament and the Council on a second set of Community measures on maritime safety following the sinking of the oil tanker Erika, COM(2000) 802 final, 6 December 2000.

(13) The final accelerated schedule (hereinafter referred to as 'the IMO compromise') ⁽⁶⁾ was agreed at the International Maritime Organisation (IMO) in April 2001.

(14) Although, on an exceptional basis, the IMO compromise allows newer single-hull ships complying with certain technical specifications to continue operating until the 25th anniversary of their delivery, EU Member States formally announced that after 2015 they would not allow single-hull tankers to enter their ports.

(15) As a result, the Community adopted Regulation (EC) No 417/2002 of the European Parliament and of the Council of 18 February 2002 on the accelerated phasing-in of double-hull or equivalent design requirements for single-hull oil tankers and repealing Council Regulation (EC) No 2978/94 ⁽⁷⁾. The regulation applies as of 1 September 2002 and transposes Community objectives to prevent major biological and environmental damage caused by shipping accidents involving old ships and in particular in relation to those carrying dangerous and potentially polluting goods.

(16) Regulation (EC) No 417/2002 prevents single-hull oil tankers from entering EU ports and operating under EU flags ⁽⁸⁾. It covers three categories of tankers:

- Category 1 oil tankers, commonly known as pre-MARPOL tankers ⁽⁹⁾, are to be gradually phased out between 2003 and 2007 (vessels without CAS will be banned from 2005),
- Category 2 oil tankers, commonly known as MARPOL tankers ⁽¹⁰⁾, will be gradually phased out between 2003 and 2015 (vessels without CAS will be banned from 2010),

- Category 3 oil tankers, with deadweights of 5 000 tons and above but less than the tonnage specified for Category 1 and 2 tankers, will be gradually phased out between 2003 and 2015.

Environmental considerations

(17) Article 6 of the EC Treaty stipulates that environmental protection requirements must be integrated into the definition and implementation of Community policy, including Community transport policies and activities.

(18) The Communication from the Commission to the Council and the European Parliament 'Enhancing Euro-Mediterranean cooperation on transport and energy' ⁽¹¹⁾ highlights the need to improve the safety of shipping. It particularly mentions the transportation of oil and chemicals, and notes that this is 'all the more acute in the Mediterranean, an enclosed sea with a fragile ecological balance'.

2.4. Objective of the aid

(19) The objective of the aid scheme is to ensure that maritime transport in Italy complies with the most stringent safety and environmental protection standards. The aid scheme promotes the scrapping of Italian-flagged single-hull tankers more than 20 years old well in advance of the IMO timetable confirmed by Regulation (EC) No 417/2002. It will cover all tankers older than 20 years on 31 December 1999 and thus considerably brings forward the legislative timeframe of the Community legislation. In addition, of the total 67 tankers eligible under the aid scheme, it will eliminate 26 which are not covered by either Community or international legislation on the phasing-out of tankers.

(20) The aid measure forms an integral part of a law aimed at preventing incidents at sea involving tankers and limiting the consequences of accidents, which can cause enormous harm to the marine environment. The law moreover steps up inspections of oil tanker shipping, bearing in mind the delicate ecological balance of the Mediterranean Sea. The incentive scheme is clearly targeted at reducing the numbers of older single-hull tankers, the category which poses the greatest potential risk of environmental damage in Italian waters and elsewhere. The scheme is aimed at, and to a large extent succeeds in, reducing the number of these generally low-cost tankers, in particular those with deadweight tonnage of less than 30 000 tons used for traffic between Italian ports.

⁽⁶⁾ Regulation 13G of Annex I of MARPOL 73/78, as amended in 2001 by Resolution MEPC.95(46).

⁽⁷⁾ OJ C 64, 7.3.2002, p. 1.

⁽⁸⁾ Category 1 and 2 oil tankers may only continue to operate after 2005 and 2010 respectively subject to compliance with a condition assessment scheme (CAS) introducing a more stringent inspection procedure. The Italian authorities have announced that they will not use the CAS procedure for oil tankers flying the Italian flag. Nonetheless, the three categories will be subject to the 2005, 2010 and 2015 deadlines.

⁽⁹⁾ Oil tankers of 20 000 tons deadweight and above, equipped to carry crude oil, fuel oil, heavy diesel oil or lubricating oil as cargo, and of 30 000 tons deadweight and above, equipped to carry oil other than the above, which DO NOT COMPLY with the requirements for tankers with regard to protectively located segregated ballast tanks.

⁽¹⁰⁾ Oil tankers of 20 000 tons deadweight and above, equipped to carry crude oil, fuel oil, heavy diesel oil or lubricating oil as cargo, and of 30 000 tons deadweight and above, equipped to carry oil other than the above, which COMPLY with the requirements for tankers with regard to protectively located segregated ballast tanks.

⁽¹¹⁾ COM(2001) 126 final, 7 March 2001, with particular reference to point 2.3.3.

- (21) There is no doubt but that single-hull tankers pose the greatest risks of pollution if involved in accidents at sea and that they are more worn out than other vessels because of their relative age. Italy considers that speeding up the phasing out of single-hull tankers helps to achieve the objective of rendering Community waters safer.
- (22) Italian Law 51/2001 on the aid scheme is one of several measures designed to improve safety and protection of the marine environment. In addition to the scrapping of obsolete tankers, it introduces other safety measures, including measures relating to the increased use of maritime traffic systems (VTS) and delegating powers to the Minister for Transport and Shipping in order to, if necessary, prevent merchant vessels shown to pose a risk to the safety of shipping and the marine environment from transiting via or remaining in Italian territorial waters. In addition, an agreement was signed on 1 June 2001 between the Italian Government and industrial and environmental associations on voluntary restrictions upon the use of single-hull tankers.

2.5. Budget

- (23) Italy is setting aside a maximum EUR 5,16 million (ITL 10 000 million) per year for a period of 15 years, amounting to a total budget of EUR 77,4 million including interest.
- (24) Ship owners will receive EUR 129,11 (ITL 0,25 million)⁽¹²⁾ per deadweight ton⁽¹³⁾ up to a maximum deadweight tonnage of 30 000 tons. The maximum possible aid for a single ship would therefore be EUR 3 873 427 (ITL 7 500 million). The maximum aid that a single ship owner may receive depends on the number of ships owned which fulfil the qualifying criteria.
- (25) The Ministry of Infrastructure and Transport administers the aid. The aid will be granted in form of loans from Italian or European credit institutions in the amount of the aid direct to the beneficiaries. Once the aid is granted, recipients have no further obligations to the banks, as the loans will be redeemed by the State using resources from the general State budget⁽¹⁴⁾.

2.6. Duration

- (26) The scrapping of the ship needs to start between 1 January 2000 and 31 December 2002, and has to be completed within six months thereafter.
- (27) The aid will be payable as of 2001. Shipowners benefit immediately once the demolition has been completed and the administrative procedure authorising the raising of loans has been finalised. Thereafter, as described above, the individual loan contracts are binding upon the State. The Italian Government confirms that, due to its commitment to the Commission to suspend any payment, it has not as yet taken on any such loans.

2.7. Beneficiaries

- (28) The aid scheme is limited to shipping companies which own single-hull tankers with deadweight tonnage of more than 1 000 tons, equipped to transport crude oil or oil or chemical products. Such vessels must have become the property of the company prior to 30 September 2000, and must have been entered in the Italian shipping registers before that date⁽¹⁵⁾. The aid scheme also applies to vessels which have been in service for more than 20 years on 31 December 1999, and which are sold for scrap or whose scrapping is arranged in accordance with the time constraints.
- (29) At the end of 1999 and the beginning of 2000, immediately after the Erika disaster, the Italian authorities working with industry initially identified 72 ships, belonging to 35 companies, which may be eligible for aid, provided that they are scrapped in line with the stipulated conditions. The ships can be classified by age and size as follows:

⁽¹²⁾ Fixed exchange rate: EUR 1 = ITL 1 936,27.

⁽¹³⁾ Deadweight tonnage: the authorised carrying capacity of a ship when fully loaded. The maximum weight of cargo, stores, fuel and water that may be loaded on a vessel to bring it to its summer marks.

⁽¹⁴⁾ The relevant payments are to be made at six-monthly intervals on 30 June and 31 December of each year. The loan contracts must provide for a payment plan of at most 15 years, at a rate of interest fixed by decree of the Treasury Minister and published in the Official Gazette of the Italian Republic, pursuant to Law 431 of 31 December 1991 as amended by Law 413 of 30 November 1998. This arrangement is designed to spread the financial burden of the aid scheme over a period longer than a few financial years.

⁽¹⁵⁾ Article 143 of the Italian Shipping Code (*Requisiti di nazionalità dei proprietari di navi italiane*) stipulates that, in order to be entered in the Italian shipping registers, vessels must either:

- be more than 50 % owned by natural or legal persons or entities from Italy or other EU Member States; or
- if owned by non-Community natural or legal persons or entities who are directly responsible for operating a vessel via a permanent organisation located on Italian territory, management must be delegated to a natural or legal person of Italian or other EU nationality, domiciled at the ship's place of registration, who directly controls and assumes full responsibility for the operation of the vessel with regard to the administration and to third parties.

Deadweight tonnage	Age of the vessel (in years)		
	25 to 30	25 to 30	More than 30
1 000 < DWT < 5 000	8	11	12
5 000 < DWT < 30 000	9	11	3
30 000 < DWT	14	5	0
Total	31	27	15

(30) Of the 72 tankers originally identified as eligible for aid, 59 were registered in the Italian national shipping register and were engaged in cabotage (they represent 51 % of the total 115 tankers entered in the Italian shipping register). Twenty of the oil tankers identified as eligible for the aid are registered in the Italian International Register and are mainly engaged in international traffic from and to Italian ports, although some are also engaged in cabotage services. These internationally operating ships represent less than 7 % of the total Italian tanker fleet of 205 ships and around 1 % of the total Community tanker fleet of 1 211 ships.

(31) The latest information provided by the Italian authorities on the situation in 2002 was that 28 of these tankers had already been scrapped by 30 March 2002⁽¹⁶⁾, thus eliminating nearly half of the high-risk ships from the market. Another two tankers are currently in the process of being scrapped. In the meantime, five tankers have been sold and are therefore no longer eligible for the aid. There have been delays in the scrapping of the remaining 37 ships in view of uncertainties regarding the legal status of the scheme and pending the outcome of the Commission's assessment.

(32) There is no requirement for a ship to be scrapped in any specific shipyard.

2.8. Expected effect of the aid

(33) Single-hull tankers more than 20 years old will be and have been removed from the Italian cabotage market in advance of obligations to do so under IMO and Community legislation. At least 28 tankers have already been scrapped, effectively reducing environmental risks and increasing the safety of shipping and, there are plans to scrap more in the near future. IMO and Community legislation require only 14 of the 67 tankers to be taken out of operation by 1 January 2003. Twenty-one tankers had already been scrapped before the Commission decision to open the formal investigation procedure (in December 2001), which brought operations to a virtual standstill.

⁽¹⁶⁾ 12 vessels in 2000, 11 in 2001 and 5 in 2002.

(34) The vast majority of the remaining 37 tankers eligible for the aid have a deadweight tonnage of less than 10 000 tons. There is no requirement for more than half of the vessels in this category to be removed from the market before 2015. This is due to the fact that the aid measure also promotes the removal of smaller tankers, of less than 5 000 deadweight tonnage, whose continued operation is not regulated by either Community legislation or any of the aforementioned international rules.

2.9. Conditions, eligible costs, aid intensity, etc.

(35) The aid amounts are intended as compensation for the revenue lost by a shipping company due to the early withdrawal of a tanker from service. Since the objective of the law is to reduce the risks inherent in the carriage of polluting and dangerous goods in single-hull tankers, the aid amount is directly proportional to deadweight tonnage, which represents the loading capacity of a ship. The Italian authorities maintain that a link is thus established between the amount of the aid and the amount of high-risk products carried in single-hull tankers (and thus any potential damage deriving from that) thereby avoided. The Italian authorities also maintain that the amount of aid has to be enough to discourage shipowners from seeking possible alternative revenue by selling the vessels to other markets in or outside the European Community. The Italian aid scheme in question consistently insists that the ship be withdrawn definitively from service, without fail.

Calculation of the aid

(36) The amount of the aid is calculated on the basis of the revenue that might be derived from an eligible single-hull tanker over a period of one year⁽¹⁷⁾. For example, a single-hull tanker with a deadweight tonnage of 30 000 tons aged between 25 and 28 years could currently be expected to earn approximately EUR 17 765 (USD 15 500)⁽¹⁸⁾ per day based on its operating approximately 330 days a year. The cost, principally the costs of crew, maintenance and repairs, fuel and other minor expenses such as insurance (since the full cost of a ship more than 20 years old would already have been written off), are currently estimated at approximately EUR 5 157 (USD 4 500) a day, 365 days a year. Therefore:

⁽¹⁷⁾ Further information from the Italian authorities indicates that the intention was to make the amount of aid proportional to the cost of the potential damage that had been avoided.

⁽¹⁸⁾ Rate of exchange as at the second quarter of 2001: EUR 1 = USD 0,872518.

- revenue: EUR 17 765 × 330 days = EUR 5 862 450,
- costs: EUR 5 157 × 365 days = EUR 1 882 305.

Annual return is therefore approximately EUR 3 980 145, or ITL 7 706 million⁽¹⁹⁾. Around 20 tankers are currently eligible for the maximum aid theoretically possible for a single vessel, EUR 3 873 427 (ITL 7 500 million).

- (37) The Italian authorities have preferred to base the calculation on deadweight tonnage rather than on a sliding scale according to the age of the vessel, since age is not the sole criterion determining a ship's safety and environmental credentials. The Italian authorities regard as equally important to consider criteria such as the type and technical specification of the vessel, and its state of repair.
- (38) The aid amount thus calculated is not subject to any preferential fiscal treatment.

Conditions governing the scrapping of vessels

- (39) In order to be eligible for aid, the shipowners whose ship(s) were originally identified as potential beneficiaries must apply to the Ministry of Infrastructure and Transport within three months of the date on which the demolition works begin. The application must identify the ship concerned, provide documentary proof of ownership and of the scrapping of the vessel (for instance, the contract of sale for demolition or simply for demolition, and certification from the competent maritime or consular authority authorising the demolition).
- (40) In order to obtain definitive payment of the aid, shipowners must, within six months of the date on which the demolition began, submit to the Ministry of Infrastructure and Transport a certificate from the maritime or consular authority confirming the dates when the demolition began and was completed. The six-month period runs from the date when the law enters into force in the case of initiatives launched prior to that date.

Accompanying obligations

- (41) Under Article 4 of Law 51/2001, as of the date on which the aid is awarded, shipping companies benefiting from the aid scheme are barred from using single-hull tankers more than 20 years old for national cabotage, except for

the Italian-flagged ships already owned or operated by these companies. If this provision is not respected, the aid must be paid back plus interest and penalties.

- (42) Law No 51/2001 also requires that, as of the date when Articles 3, 4 and 5 are applied, no single-hull tankers equipped to transport crude oil, oil or chemical products may be entered in the Italian national shipping registers if they are more than 20 years old.
- (43) The aid is also subject to compliance with conditions on future investment. The aid measure stipulates that the recipient company must reinvest an amount equivalent to the scrapping premium in its maritime business activities. This investment must be made within 18 months of the demolition being completed or of the date when the relevant articles of Law 51/2001 entered into force, whichever comes first. However, the scrapping premium is not related to this new investment, being merely compensation for the loss of revenue suffered by the beneficiary for the period during which the scrapped tanker could have continued to operate.
- (44) The above conditions contained in the aid measure as originally notified already placed restrictions upon the recipients' future use of single-hull tankers more than 20 years old, quite apart from the tankers actually scrapped. However, in the aid measure as originally notified, the purchase of single-hull tankers of less than 20 years of age as replacement capacity was still an option. In the course of these proceedings, however, Italy has proposed that it undertakes to impose a further condition, ruling out single-hull tankers of any age as replacement capacity. Thus, Italy intends to require that any replacement capacity purchased by the beneficiaries of the aid measure may consist of double hull tankers only. Italy has further confirmed that the investment benefiting the maritime business of the beneficiary which is foreseen in the law may also be for specific training or any other projects or assets meeting that objective. If the aforementioned conditions are not fulfilled, the aid must be paid back plus interest and penalties.
- (45) These conditions attached to the granting of the aid incorporate the terms agreed between the Italian authorities and the shipping industry immediately after the sinking of the Erika.
- (46) Beneficiaries of the aid have to inform the Italian administration of the details of the investment. The Italian administration further reserves the right to carry out the necessary administrative checks, by means of inspections, to ensure that the recipient company complies with these conditions.

⁽¹⁹⁾ Rate of exchange as at the second quarter of 2001: USD 1 = ITL 2 219.

2.10. Market analysis

(47) The Italian tanker fleet of 205 ships with a total deadweight tonnage of 3 715 073 tons represents, in terms of dwt, 9,2 % of the tankers entered in EU Member State registers (as defined in the Annex to the Community guidelines on State aid to maritime transport⁽²⁰⁾, hereinafter referred to as the 'relevant Community guidelines') and, specifically, 5 % of the Community's crude oil tankers, approximately 30 % of its tankers carrying oil products and 20 % of its chemical tankers⁽²¹⁾. The Community tanker fleet represents some 13 % of the world tanker fleet.

(48) The official statistics for 1999 (the latest available) show that 30,1 of the 31 million tons of petrochemicals transported in the Italian cabotage market were carried by Italian-flagged vessels, a market share of 97 % in a market that has been opened to competition since 1 January 1997 pursuant to Council Regulation (EEC) No 3577/92 of 7 December 1992 applying the principle of freedom to provide services to maritime transport within Member States (maritime cabotage)⁽²²⁾. The scheme also applies to a limited number of Italian-registered tankers operating on international markets but which entered or could enter Italian ports, an activity that has clearly been open to European as well as global competition for a long time.

3. THE FORMAL INVESTIGATION PROCEDURE

3.1. Grounds for initiating the procedure

(49) The Commission decision to initiate the procedure laid down in Article 88(2) of the EC Treaty and to request clarification from the Italian authorities was the outcome of an initial examination of the notified aid scheme embodied in Law 51/2001. The law itself does not specify the type of projects, training, or assets in which the beneficiary of the aid must invest under the requirement to invest in the maritime business.

(50) Furthermore, concern was expressed at the fact that 97 % of the ships operating in the relevant, recently opened market were Italian flagged tankers.

(51) The Commission expressed doubts regarding the following issues in particular:

- the limitation of the aid scheme to single-hull tankers at least 20 years of age,

- the option of purchasing single-hull tankers, even if they must be less than 20 years old, as replacements, and

- the lack of clarity as to the type of investment required of the beneficiaries.

(52) The Italian authorities were therefore asked to provide the necessary information to enable the Commission to assess whether the aid scheme was compatible with the EC Treaty. Nevertheless, the Commission did accept (see recitals 65 to 67 of that Decision) that the objectives of the aid scheme as such are in line with Community maritime policy and implement important policy guidelines intended to raise safety standards in maritime shipping.

3.2. Comments from interested parties

(53) According to *Mediterranea di Navigazione*, *Danmarks Rederiforening*, the Norwegian Royal Ministry of Trade and Industry, *Norges Rederiforbund*, the Chamber of Shipping, the Swedish shipowners' association, *Comité Central des Armateurs de France*, and *Ermewa Maritime*:

the measure does not seem to meet the requirements for any of the exceptions provided for in the EC Treaty or in the guidelines on State aid for environmental protection. In terms of State aid policy, it constitutes a net direct subsidy to companies owning ships under the national flags of a single Member State. Such net direct subsidies are not deemed admissible under either the EC Treaty or the guidelines on State aid, except in very limited circumstances, which may include the one-off restructuring of a company or its involvement in an important project of common European interest. On the oil tanker market, however, there is overcapacity, and the aid will encourage shipbuilding, which may inflate the market;

(54) moreover, the aid scheme distorts competition in the European and international shipping market, as beneficiaries will be able to buy new ships at a price 12 % to 15 % lower than that of their competitors. Some Member States have given advance notice of the renewal of their tanker fleets so as to comply with new international and European safety standards without the use of public funding. Because of the method used to calculate the aid, it could even benefit ships not usually used for cabotage services (30 000 dwt and more) and penalise those which are (3 000 to 15 000 tons deadweight);

⁽²⁰⁾ OJ C 205, 7.7.1997, p. 5.

⁽²¹⁾ Source: World Fleet Statistics 2000, Lloyd's Register.

⁽²²⁾ OJ L 364, 12.12.1992, p. 7.

- (55) the measure may also lead to a race for scrapping subsidies, which would seriously distort competition. Furthermore, it may stand in the way of international solutions designed to boost safety or prevent pollution in the future;
- (56) the comments also stress the danger that the aid might bring costs down substantially, potentially placing rival shipowning companies at a commercial disadvantage. The scheme may lead to artificially low freight rates in the Italian tanker cabotage market, creating an entry barrier for non-Italian EEA ships to the Italian cabotage market. In addition, the subsidised replacement ships (tankers or other types of vessels) may operate in other EU markets, causing distortions of competition there;
- (57) the aid is not proportionate. In particular, the owners of a 30 000 ton tanker more than 20 years old will receive ten times as much as the owners of a 3 000 ton tanker, even though the ratio of their relative construction cost is approximately 3:1. Reinvestment in ships between 15 and 19 years old may lead to extremely high aid intensity, with the value of the ships actually less than the amount of the aid;
- (58) alternative, more efficient and less distortive solutions to promote safe seas should have been envisaged, for example a long-term commitment to investment in crew training or technical improvement going beyond existing legislation or international agreements. One alternative would have been to increase the resources available for Italian flag and port State control activities, benefiting all tankers operating in Italian waters.
- According to Confitarma:
- (59) the aid measure is non-selective and is unlikely to affect trade between Member States or to distort competition between EU shipping companies. Instead, the aid scheme will considerably reduce the risk stemming from the use of older ships;
- (60) in its proposal for a regulation on the accelerated phasing-in of double hull standards, the Commission stated that the replacement of single-hull ships would probably lead to 'insufficient double-hull tonnage' causing 'increased demand arising from this proposal' which would circumvent the objection to reduce supply regarding the reduction of capacity offered;
- (61) the aid measure pursues the same objectives as Community legislation (Regulation (EC) No 417/2002) and therefore clearly has to be deemed compatible with the, less stringent, Community standards, which were adopted after the aid measure entered into force;
- (62) Confitarma also pointed out that, with regard to public service, Member States should be entitled to establish new safety regulations when they perceive a shortcoming in European or international rules.
- ### 3.3. Comments from Italy
- (63) The Italian authorities stress that there is no contradiction between the proposed aid scheme and the IMO timetable, since the latter gives the latest possible deadline by which the ships in question should be removed. There is no reason why ships cannot be scrapped ahead of schedule. This does not constitute failure to comply with IMO commitments. The objective of environmental protection is achieved all the more effectively if ships presenting increased risk are scrapped ahead of schedule.
- (64) The purpose of the aid measure is to eliminate potential risk and not to provide incentives to invest in ships. The Commission, misguided by the condition that beneficiaries must invest an amount equivalent to the aid received in their maritime business, was wrong to conclude that the aid would cause unacceptable distortions of competition.
- (65) Law No 51/2001 already promotes the use of double-hull tankers since Article 4(3) stipulates that recipients of aid may not thereafter enter single-hull tankers in the national shipping registers if they are more than 20 years old.
- (66) Concerning the aid intensity, the system may be regarded as sufficiently fair and in line with the environmental and safety objectives stated in the law. It is inaccurate to describe the aid as a form of operating aid because the motives of safeguarding the safety of shipping and the marine environment preclude the possibility that the aid is intended as operating aid.
- (67) The aid should be considered a 'one-off' measure not likely to alter the commercial policy of a maritime shipping company. The economic effects of the aid are very short-term and will not make a company able to offer anything other than the standard commercial rates without compromising the profitability of its activities.

- (68) Italy has stated its intention of promoting the opening up of the cabotage market in accordance with Council Regulation (EEC) 3577/92 of 7 December 1992. There are, in any case, no barriers to the use of EU-owned ships on the Italian cabotage market. Any advantage for the beneficiaries deriving from the aid is very limited and cannot affect the common market to an extent contrary to the common interest.

4. ASSESSMENT OF THE AID

4.1. Existence of aid within the meaning of Article 87(1) of the EC Treaty

- (69) According to Article 87(1) of the EC Treaty, 'any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between the Member States, be incompatible with the common market.'
- (70) *Transfer of State resources*: the concept of State aid applies to any advantage granted directly or indirectly, financed out of State resources, granted by the State itself or by an intermediary body acting by virtue of powers conferred on it. Under this aid scheme, the amounts paid immediately and directly to the shipowners are raised by means of loans which the Italian administration undertakes to pay back over a 15-year period. The loan arrangement is thus simply an instrument by means of which the State may grant a lump sum payment to the aid beneficiary while meeting specific budgetary constraints.
- (71) *Advantage*: the aid measure in question confers an advantage upon Italian owners of single hull oil tankers 20 years of age or older operating in the Italian cabotage market as well as internationally. Shipping companies operating more recent ships in the same markets do not benefit.
- (72) *Selectivity*: the aid measure favours the shipping sector, in particular the maritime carriage of oil and chemicals, and is therefore selective in nature.
- (73) *Effects on trade and distortion of competition*: it strengthens the position of a limited number of shipping companies in the Italian market. The possibility of scrapping essential assets while continuing to receive compensation for the revenue lost as a result of the elimination of the scrapped tonnage could place the beneficiaries at

an advantage in relation to companies established in other Member States. Since the entry into force of all the provisions of Regulation (EEC) No 3577/92 allowing free market access to almost all national markets within the EU, shipping companies compete in a liberalised market in Europe. The measure may have an effect on competition in a liberalised market.

- (74) The measure in question confers an advantage upon certain undertakings, is State-financed, selective in character, affects trade between Member States and affects competition. As such, it constitutes State aid within the meaning of Article 87(1) of the EC Treaty and is incompatible with the common market, unless it can meet the requirements of the exemptions provided for in the Treaty.

4.2. Legal basis for the assessment

- (75) Article 87(2) of the EC Treaty, which provides for aid having a social character, aid making good the damage caused by natural disasters or exceptional occurrences and aid granted to the economy of certain areas of the Federal Republic of Germany is not applicable in the present case.
- (76) Nor is Article 87(3)(a) of the EC Treaty applicable, which provides for aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment, because the measure under consideration affects the maritime industry and is not focussed on a particular region or regions.
- (77) Article 87(3)(b) of the EC Treaty, which provides for aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State, and Article 87(3)(d) of the EC Treaty, which provides for aid to promote cultural and heritage conservation, are not applicable to aid to the maritime transport sector.
- (78) Under Article 87(3)(c) of the Treaty, aid to facilitate the development of certain economic activities or of certain economic areas may be considered compatible with the common market, where such aid does not adversely affect trading conditions to an extent contrary to the common interest. In the case in point, the Commission considers Article 87(3)(c) of the Treaty as the legal instrument which may provide an exemption.

4.3. Appraisal of the compatibility of the aid

4.3.1. *Compatibility in the light of the Community guidelines on State aid to maritime transport*

- (79) The relevant Community guidelines set out the arrangements and criteria according to which State aid may be authorised in this sector. In general terms, aid schemes should not be at the expense of other Member States' economies and must be shown not to risk distortion of competition between Member States to an extent contrary to the common interest. State aid must always be restricted to the minimum necessary to achieve its purpose and must be granted in a transparent manner. In addition, the cumulative effect of all aid granted by State authorities (including national, regional and local authorities) must always be taken into account.
- (80) The relevant Community guidelines define the State aid schemes which may be introduced to support the maritime interests of the Community. Such aid should have the following objectives:
- safeguarding employment within the Community (for on-board and on-shore staff),
 - preserving maritime know-how in the Community and developing maritime skills,
 - improving safety.
- (81) With respect to safety, the fourth paragraph of section 1.1 of the relevant Community guidelines points out that, 'There is also at present cyclical and structural overcapacity which means that the industry is demanded and that shippers can drive down freight rates; this, combined with high fixed costs for shipowners, means that the incentive to cut costs and possibly corners increases and the pursuit of high quality in operations may not be commercially attractive. This may then undermine the long-term interests of the Community in safe, efficient, environmentally friendly transport.'
- (82) The second paragraph of Chapter 5 of the guidelines states the Commission's reluctance to approve subsidies for fleet renewal, except where such aid is part of a structural reform leading to reductions in overall fleet capacity. However, the Italian scheme does not explicitly require reduction of capacity.
- (83) However, according to the fourth paragraph of Chapter 5 of the guidelines, 'aid may however be permitted, in the line with the Community safe-seas policy ⁽²³⁾, in certain restricted circumstances (...) to promote the use of safe and clean ships.' Incentives may be permitted 'to upgrade

Community-registered ships to standards, which exceed the mandatory safety and environmental standards laid down in international conventions and anticipating agreed higher standards.'

- (84) The Italian aid scheme is not specifically targeted at renewing the tanker fleet but rather at launching a process that will improve levels of safety and environmental protection by removing a great number of high-risk tankers from the market. The objective of the aid scheme, expediting the phasing-out of single-hull tankers, particularly older ones, is in line with Community objectives following the Erika disaster. The Italian aid scheme promotes, and anticipates, the achievement of Community objectives by increasing and anticipating protection against the risks stemming from the use of older ships which meet lower technical standards.
- (85) In addition, by bringing forward the timescales and encouraging the scrapping of single-hull tankers more than 20 years old in preference to selling them to other Member States or to third countries, the scheme helps to make seas outside Community waters safer too. It thus definitively removes 67 of the most high-risk tankers from operation anywhere in the world.
- (86) The Commission notes, furthermore, that the scrapping of tankers under the Italian aid scheme goes further than the IMO compromise and the Community standards set out in the Commission Communication on the safety of the seaborne oil trade and in Regulation (EC) No 417/2002, with respect to single hull tankers.

The Italian scheme promotes the scrapping of single-hull tankers with deadweight tonnages of less than 5 000 tons (some 31 single-hull tankers) and gives incentives for scrapping other (larger) single-hull tankers that were at least 20 years old on 31 December 1999. This anticipates the IMO and Community timetable by a considerable period of time, as the first tankers were scrapped as early as January 2000.

- (87) The aid scheme was devised, discussed with potential beneficiaries, presented to and adopted by the Italian Parliament before Regulation (EC) No 417/2002 came into force, even if, as has been reported above, no aid has been awarded pending the Commission's approval. It can thus be regarded as a one-off interim arrangement to regulate a situation of legal uncertainty, in a period during which, however, the potential risk and the effects of a catastrophe similar to the Erika disaster were already well known. The aid was, and is, necessary in order to achieve the objective of phasing out single-hull tankers ahead of schedule since, without compensation for the loss of revenue, shipping companies would have no incentive for removing dangerous and polluting tankers from operation. The additional conditions agreed to by the Italian authorities and ordered by the Commission in this decision will further restrict the use of single-hull tankers.

(23) A common policy on Safe Seas, COM(93) 66 final.

- (88) The aid in question is a scrapping premium necessary to remove from operation tonnage representing the greatest risks to safety and to the maritime environment. Thanks to the conditions attached to the scheme, the aid reduces risky and polluting capacity and ultimately encourages the use of safer tankers. Negotiations at Community and international level had precisely that objective. It can therefore be confirmed that the objectives pursued by the Italian aid scheme are in line with the common transport policy.
- (89) It is in the Community's interest to adopt measures to reduce risky and polluting capacity. Although the present aid scheme concerns only a limited number of the oldest of such tankers in a single Member State, and although the beneficiaries which own several single-hull tankers more than 20 years old may continue to use those for which they do not receive the aid (at least, until their use is banned by IMO and/or Community regulations), it is clear that every single demolition of unsafe vessels ahead of the schedule laid out in Community legislation counts towards achieving the final objective of safer seas.
- (90) Beneficiaries are free to use the aid on expenditure related to their maritime business. By imposing conditions limiting the use of single-hull tankers, the Italian authorities are influencing the financial decisions of the shipping company with regard to future investment and, potentially, replacement capacity, thereby improving environmental and safety conditions in Italian and, indeed, in international waters. Other forms of expenditure (crew training, for example) are regarded as meeting the criterion of a maritime business investment.
- (91) In view of the above and since the granting of aid will be made subject to the application of a number of strict conditions imposed by the Commission through the present decision, which will in particular prevent any overcompensation, the Commission considers that the aid measure favours the development of a specific sector (safer maritime transport) without being contrary to the common interest and therefore complies with Article 87(3)c and also with the Community guidelines on State aid.
- (92) The aid is aimed exclusively at offsetting the loss of revenue (and any additional costs incurred) by the shipowner as a result of ceasing to use the single-hull vessel which has been scrapped. It should also be noted that the Commission imposes certain conditions in this decision in order to prevent overcompensation. Moreover, Italy has stated that it will consider any spillover of the scrapping aid (limited to compensation for lost revenue) to the shipbuilding market as automatically ineligible under the present aid scheme.
- (93) In the light of the conditions imposed in this decision it cannot be concluded that the aid qualifies as indirect aid to shipbuilding within the meaning of Council Regulation (EC) No 1540/98/EC.
- (94) In its decision to open the formal investigation procedure, the Commission expressed doubts about the compatibility of the aid because there were no clear conditions regarding the potential use of the aid. The amounts of aid awarded under such schemes must be strictly monitored to ensure that they are spent in compliance with Community policies and rules on State aid. The amounts of aid must be limited to the strict minimum necessary to achieve the desired effect.
- (95) The aid is calculated on the basis of deadweight tonnage, since this correlates best to the potential pollution risk. The Commission may agree to this method of calculation provided that it is applied in a proportional way. At the time of the decision to open the formal investigation procedure, the Commission expressed concerns on this point, which were confirmed by the comments from the interested parties.
- (96) The Commission acknowledges that a scrapping premium should provide sufficient incentive to accomplish the scrapping as early as possible, and that the aid in question is necessary in order to achieve the scrapping of tonnage considered to be high-risk before the shipowner has replaced it with less risky, environmentally safer capacity. However, the Commission insists that the basis for calculating the aid must be limited to compensation for loss of revenue during the actual time period during which such loss is suffered. Without such a link, the aid amount may not be considered proportional to the actual compensation of the losses suffered because it could spill over to other economic interests of the shipping company perhaps not in line with the objective of Community policy.

4.4. Description of the measures to be taken by Italy and the conditions imposed in this decision to make the aid compatible

4.4.1. Proportionality of the aid amount

4.3.2. Compatibility with legislation on shipbuilding

- (92) The third paragraph of Chapter 5 of the relevant Community guidelines requires that aid approved under it must comply with the provisions of Council Regulation (EC) No 1540/98 of 29 June 1998 on aid to shipbuilding⁽²⁴⁾. In that respect, the following observations can be made, taking account also of the information provided by the Italian authorities during the procedure under Article 88(2).

⁽²⁴⁾ OJ L 202, 18.7.1998, p. 1.

(98) Accordingly, the present aid scheme should be implemented in a way which eliminates the risk of an aid recipient benefiting from aid despite the fact that compensation for loss of revenue is no longer necessary, either because the shipping company had already arranged for replacement capacity within a period of less than a year, or because the scrapped tanker would have anyhow had to cease operating before the end of one full year in accordance with Regulation (EC) No 417/2002 of 8 February 2002. A report must be presented to the Commission setting out in detail, for each beneficiary and vessel, the method used to calculate the amount of aid. The Commission reserves the right to submit the information regarding individual aid amounts to third parties, in particular, experts, for their opinion. This report, and further reports which the Commission may request from Italy on the implementation of the aid, must also include information on the total tonnage owned by the beneficiary before the granting of the aid and throughout the year following the granting of the aid.

4.4.2. *Non-discriminatory and transparent application*

(99) Further conditions should be added in order to guarantee greater transparency and non-discrimination, and to provide for the possibility of appealing against the decision on the amount of the aid. The Commission is aware that the aid scheme appears to allow the Italian authorities a certain margin of discretion with regard to taking into consideration the technical standards of the tanker to be scrapped. Accordingly, further conditions must be complied with when applying the aid scheme in order to ensure the necessary transparency, non-discrimination and legal certainty.

4.4.3. *Compliance with objectives of maritime policy*

(100) With regard to the conditions on the subsequent investment of the aid in the maritime business of the shipping companies concerned, the latter are free to choose the form of investment they think necessary, so long as it is considered in line with the Community's maritime policy. This may be deemed acceptable, but it is however indispensable that aid recipients are restricted in their choice concerning the purchase of replacement capacity, whether by new or second-hand tankers. In view of the Community's maritime policy and legislation on the phasing-out of single-hull tankers, the Commission considers it important to insist that the condition governing investment does not permit any purchase of single-hull tankers by beneficiaries.

(101) In the course of these proceedings, the Italian authorities already committed themselves to specifying further conditions regarding the purchase of single-hull tankers as indicated above, offering to make it a condition that, in relation to the obligation of aid recipients to further invest in their maritime business, the purchase of single-hull ships would not be considered an admissible investment under the aid scheme. It offered to impose that in relation to the obligation of aid recipients to further invest in the maritime business that the purchase of single-hull ships would not be considered an admissible investment under the aid scheme.

4.4.4. *Cumulation requirements*

(102) Italy is also reminded of the cumulation rule contained in paragraph 2 of Chapter 10 of the guidelines on State aid to maritime transport, which states: 'A reduction to zero of taxation and social charges for seafarers and of corporate taxation of shipping activities is the maximum level of aid which may be permitted. To avoid distortion of competition, other systems of aid may not provide greater benefit than this. Consequently, although each aid scheme notified by a Member State will be examined on its own merits, it is considered that the total amount of aid in the form of direct payments in the framework of Chapters 3, 4, 5 and 6 should not exceed the total amount of taxes and social contributions collected from shipping activities and seafarers; to do so would, it is considered, affect trading conditions to an extent contrary to the Treaty provisions, as the aid would be disproportionate to the objective.'

4.4.5. *Cabotage market*

(103) Although Italy confirms that its cabotage market is open in compliance with Council Regulation (EEC) No 3577/92, the exceptionally high number of Italian ships in this market gives cause for concern. A certain imbalance also derives from restricting access to ships in the registers of other Member States, whereas ships registered in the second Italian register may not only operate in this market but may also benefit from the aid. The Commission therefore considers it necessary to monitor this issue closely with the help of detailed information provided to it by the Italian authorities during the coming five years.

4.5. **Legal application of the aid scheme**

(104) Prior to introducing a formal proposal for what later became Law 51/2001 to the Italian Parliament on 16 March 2000, the Italian Government and industry had already agreed on the conditions for the granting of the aid and had already identified eligible tankers. The aid measure based on a political agreement in substance was therefore already being applied. It is however true that no loan obligations seem to have been transferred to the Italian government, which would constitute the actual granting of the aid. On account of the large expectations raised and the actual reaction of the market to it, the Commission considers that the aid measure was however being applied prior to its authorisation, already in January 2000 and prior to its adoption in March 2001. However, the Commission accepts that this course of action by the Italian authorities was probably inevitable in the wake of the Erika disaster and in order to induce the beneficiaries to scrap the vessels as early as possible.

5. CONCLUSION

(105) The Commission finds that Italy has unlawfully implemented the aid for the scrapping and renewal of the Italian oil tanker fleet in breach of Article 88(3) of the Treaty. However, assessment of the measure has shown that the aid may be declared compatible with Article 87(3)(c) of the EC Treaty provided that it is adapted in line with the conditions established by the Commission,

HAS ADOPTED THIS DECISION:

Article 1

The aid, provided for under Law 51/2001, which Italy has implemented for the benefit of the Italian oil tanker fleet, amounting to EUR 77,4 million as a total budget including interest, is compatible with the common market, subject to the conditions set out in Articles 2 and 3 of this Decision.

Article 2

1. In addition to the procedures proposed by Italy, individual aid amounts must be calculated in a transparent way based on objective criteria, as specified in particular in paragraphs 2 to 6.

2. The calculation of the aid amount must be limited to the minimum necessary.

Account is to be taken, in line with the conditions of this aid scheme of the actual period during which an aid recipient has suffered loss of revenue due to the scrapping of a tanker.

3. The Italian authorities must provide the Commission in particular with detailed reports for each beneficiary and vessel, regarding the method of calculation and the amount of tonnage in the beneficiary's possession during a period of at least one year after the granting of the aid.

The first report is to be forwarded within two months of the notification of this Decision.

4. Before the scheme may be implemented fully, any margin of discretion concerning the choice of eligible vessels and the extent to which they may benefit from this scheme has to be eliminated.

5. The calculation of the individual aid amounts has to be made public to all aid recipients.

6. Individual aid recipients and companies which have applied for aid need to be granted the possibility to appeal.

Article 3

1. The obligation regarding investment in maritime business has to comply with maritime policy objectives. In particular, therefore, beneficiaries are not permitted to purchase single-hull tankers.

2. The overall aid received by a company benefiting from the present aid may not exceed the limit imposed by paragraph 2 of Chapter 10 of the guidelines on State aid to maritime transport.

3. During a period of five years as of 2003, Italy has to inform the Commission on a yearly basis of detailed developments in the Italian tanker cabotage market for the transport of oil, oil products and chemicals.

Article 4

Aid already granted but which does not comply with the conditions referred to in Articles 2 and 3 has to be recovered.

Article 5

The Italian authorities shall inform the Commission, within two months of notification of this Decision, of the measures taken to comply with it.

Article 6

This Decision is addressed to the Italian Republic.

Done at Brussels, 17 July 2002.

For the Commission

Loyola DE PALACIO

Vice-President