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Liberalisation

Liberalisation and competition policy go hand-in-hand. But, whereas the rules on competition are generally enforced on a case-by-case basis, the principles of liberalisation are generally enshrined in legislation; in this context, by means of European Community Regulations and Directives. An example of this is the energy sector, for which it is proposed that further measures should be taken for the full liberalisation of both gas and electricity markets: a so-called acceleration directive and a regulation on cross-border trade of electricity. In February this year a common position was adopted by the Council on these proposals and the texts are currently subject to a second reading in the Parliament. The new legislation will eliminate the distortions of competition resulting from the different speeds at which the Member States have been opening up their markets and improve competition conditions for effective liberalisation. Meanwhile, as reported in our last issue, the Commission's antitrust investigation involving the dominant Danish gas supplier DONG and a consortium formed by the country's main gas producers Shell, A.P. Møller and Chevron Texacon was closed after the members of the consortium undertook to market their production individually. This case is the latest of a series of cases in the energy sector, which have focused on removing restrictions that limit supply competition or access to networks and, therefore, have reinforced the progressive liberalisation of the sector.

Liberalisation of the telecommunications industry is a further case in point. Today, we see already part of the results: over the past five years (1998-2002) prices of long-distance and international phone calls have fallen by over 45%. However, local phone call prices fell only marginally over the same period. This difference in price trends reflects the fact that today the local loop is still controlled by the incumbent operators, which also run nearly 70% of all broadband connection. Tackling these types of problem, remaining five years after the liberalisation of the telecommunication sector, is one of the main aims of the new regulatory framework for electronic communications adopted last year. Under the new framework, regulation remains still for such areas where competition can most likely not be safeguarded by the mere application of competition rules: for example, to guarantee effective and speedy access to facilities which are crucial for the development of competition.

Constitutional Reform in the European Union

One of the (many) criticisms of the proposed constitution for the European Union is the suggestion that the Union should be treated as a legal entity. Until the Union does become an entity, the European Community remains the authority responsible for the rules on competition; and the rules themselves are laid down in the Treaty establishing the European Community. References in official press releases to the "European Union rules" or even, in some cases, to the competition articles of the Treaty on European Union, are legally incorrect. ■

ABUSE OF DOMINANT POSITION (TELECOMS): THE DT CASE

Subject: Abuse of dominant position
Pricing policy
Discrimination

Industry: Telecommunications

Parties: Deutsche Telekom AG

Source: Commission Statement IP/03/717, dated 21 May 2003

(Note. This is another instance of competition rules being called in aid to give new market entrants an opportunity to have access to an already established infrastructure. Yet competition rules alone are not enough to guarantee access: in the present case, the position is governed by legislation at both the European and the national levels. What the competition rules can do is to accelerate the process by which access is granted, since they can be used to challenge pricing policies based on a denial of access: see the second paragraph of the section below entitled "Background: Access to the local loop".)

The Commission has adopted a decision against Deutsche Telekom AG (DT) for abusing its dominant position through unfair prices for the provision of local access to its fixed telecommunications network (local loops). The Commission has found that DT charges new entrants higher fees for wholesale access to the local loop than the fees paid by DT's subscribers for fixed line subscriptions. This discourages new companies from entering the market and reduces the choice of suppliers of telecommunications services as well as price competition for consumers. The Commission's action stems from complaints by numerous new entrants in the German telecommunications market. In line with the gravity and duration of the abuse, the Commission levies a fine of €12.6 million.

According to the Commission, DT has been legally obliged since 1998 to provide competitors access to its local loops. In spite of this clear obligation, there still is very little effective unbundling of the local loops; and DT, with a market share of 95%, remains the dominant provider of broadband and narrowband retail access. Many new entrants have tried to compete with the incumbent operator. None of them has been able to reach significant market share, not least because DT charges competitors higher fees for local loop access than it charges its end users. As the Commission points out, this is clearly harmful to consumers, because competition between operators is the best means to bring the overall prices down. That is the reason for the Commission's action against unfair pricing by Deutsche Telekom and for its determination to be vigilant on any infringements of this kind.

The Commission had found that Deutsche Telekom was abusing its dominant position through unfair pricing. DT holds a dominant position on both the markets for both wholesale and retail access to the local loop. Regarding wholesale access, DT is the only German network operator having a network with nation-wide coverage. To provide a variety of services to end users, new entrants need access to this infrastructure on a wholesale basis. Regarding retail access, even after five years of competition, DT still has around 95% market share and the remaining 5% is divided among large numbers of DT's competitors.

Because of the insufficient spread between DT's local loop access prices and the downstream tariffs for retail subscriptions, new entrants have no scope for competing with DT for end consumers. The Commission's decision compares upstream access to the local loops with a bundle of different types of retail offerings, namely analogue, ISDN and ADSL connections. To achieve a coherent comparison, the Commission used a weighted approach taking into account the numbers of DT's retail customers for the different access types on retail level.

The Commission's assessment reveals, for the period 1998 through 2001, that DT charged competitors more for unbundled access at wholesale level than it charged its subscribers for access at the retail level. This constitutes a clear case of margin squeeze, because it leaves new entrants no margin to compete for downstream retail subscribers. As of 2002, prices for wholesale access were lower than retail subscription prices but the difference was still not sufficient to cover DT's own downstream product-specific costs for the supply of the end-user services. Even after the latest reduction of the wholesale prices by the German regulatory authority (RegTP), which became effective on 1 May 2003, this margin squeeze remains in place.

Fine

According to the Commission's Guidelines on the method of setting fines (Official Journal of the European Communities, C.9, 1998), the criteria for determining the amount of a fine are gravity and duration of the infringement, as well as aggravating or attenuating circumstances. The margin squeeze implemented by DT as an undertaking dominant both at the wholesale and retail levels constitutes a serious infringement. The result of this pricing strategy is that new competitors who need access to the local loops in Germany are seriously impeded. The relevant markets are markets of considerable economic importance. On the other hand, DT has steadily reduced the margin squeeze through tariff adjustments. Therefore the basic amount for gravity was set at €10 million.

The abuse was found to have lasted from 1.1.1998 until today: the infringement is therefore of long duration. The infringement was, however, less important in the period since 1.1.2002, due to the reduced scope for price adjustments under the

regulatory provisions in Germany. Therefore only the first four years until the end of 2001 account for an increase of the basic amount to €14 million. Finally, the Commission has reduced the fine to €12.6 million by assuming mitigating circumstances due to the fact that, under the sector specific regulation in Germany, there was some degree of legal uncertainty about the tariffs under scrutiny.

Background: Access to the local loop

The local loop is the physical circuit between the customer's premises and the telecommunications operator's local switch. Traditionally it takes the form of pairs of copper wires. New entrants on the telecommunications markets need access on fair and non-discriminatory terms to the local loops ("local loop unbundling") to be able to offer retail services to end-customers, as it would be impossible to replicate such a network built over a century.

Effective local loop unbundling is key for the spread of electronic communications services. It was imposed on the incumbent operators by way of legislation at EU level and, in some Member States, such as Germany, also at national level. However, local loop unbundling is not developing fast enough. The regulatory framework is not the only tool available. The conditions of local loop unbundling, such as pricing, are also subject to scrutiny under the EU competition rules.

In Germany, DT offers local loop access at two different levels. Besides the retail subscriptions to end customers, DT also offers unbundled access to the local loop to competitors, which allows them direct access to end-users. DT is thus active on the upstream market for wholesale local loop access to competitors and on the downstream market for retail access services to end-customers. Both markets are closely linked to each other.

DT's local access network is not the only technical infrastructure allowing for the provision of wholesale access services to competitors and of retail access services to end-users. But the other options, which include fibre-optic networks, wireless local loops, satellites, power lines, and upgraded cable TV networks, are not yet sufficiently developed and cannot be considered as equivalent to DT's local loop network.

According to the Commission's 8th Implementation Report of December 2002 (COM(2002) 695), two years after the EC Regulation on local loop unbundling came in force, only 1 million subscriber lines have been unbundled across Europe. The large majority of them (855,000) are in Germany, where unbundling had been mandated by national law in 1998; but even in Germany unbundled lines account for fewer than 5% of the total. ■

STATE AIDS (POSTAL SERVICES): THE BRITISH POST OFFICE CASE

Subject: State aids

Industry: Postal services; related services

Parties: Post Office Ltd
Royal Mail Group plc

Source: Commission Statement IP/03/757, dated 27 May 2003

(Note. The decision described below marks the latest in a series of arrangements designed to ensure that the payments made – indirectly – to the British Post Office by way of compensation for carrying out certain social service functions are compatible with the rules on competition. As the Commission points out, since the Government loan and payments only compensate the Post Office for the net additional cost of the public tasks it is entrusted with, no real advantage is in the end conferred on it.)

The Commission has decided not to raise objections to a further series of financing measures in favour of Post Office Limited (POL), the retail subsidiary of Royal Mail Group plc. These measures complement earlier measures the Commission approved in 2002. On 12 March 2002 the Commission approved the funding of a basic postal account to credit social benefits and from which cash can be withdrawn at post office counters for those benefits holders who do not want to open an account with a bank. On 18 September 2002 the Commission approved minimum funding necessary for POL to close 3,000 urban counters no longer required under the 2000 UK Postal Services Act (2000).

POL is making losses on account of its statutory obligation to cover the entire territory of the UK. This entails the obligation to maintain counters that are structurally loss-making. In order to maintain POL as a going concern, Royal Mail Group plc, granted POL a loan.

The UK Government now wishes to compensate POL for the net public service cost of rural counter coverage. As the Government requires POL to keep open 8,600 rural post offices, it will compensate POL annually for the related net public service costs within a £150m ceiling. In addition, the Government will give POL the means to back its debt to Royal Mail Group plc, which had financed POL's balance-sheet deficits up to 31 March 2002, dispensing a total £726m in this respect. As of the financial year 2006/7, the Government will provide payment up to £574m to ensure that POL is able to meet its debts in full. Finally, the Government will provide POL with a rolling working capital loan for over-the-counter cash payments. This capital loan up to a ceiling of £1,150m in 2004/5 is meant to fund the basic postal account.

The three new measures constitute a transfer of State resources, grant an advantage to POL in the form of a loan and payments and potentially distort competition and intra-community trade. However, as long as the Government loan and payments only compensate POL for the net additional cost of the public tasks it is entrusted with, no real advantage is in the end conferred on POL.

The rural network support compensation is designed not to exceed the net additional public service cost of maintaining structurally loss-making counters. For the debt funding measure, the Government payments are the minimum necessary to keep POL going so that it can continue providing its public services. This minimum funding itself is reduced by the positive revenue contribution derived from competitive activities. A self-regulating mechanism has been designed to ensure that the rolling working capital loan is the minimum necessary to enable the provision of a basic postal account.

The Commission has verified that there are sufficient *a priori* and *a posteriori* mechanisms in place to prevent any overcompensation of the net additional cost of the public service. A system of "ring-fencing" prevents any double Government compensation. The British Government has committed itself to recovering any potential overcompensation as shown by separate accounts. As the mechanisms are in place to prevent any *a priori* over-compensation and, should such overcompensation occur, to recover it *a posteriori*, no real advantage has therefore been conferred to POL.

In the final analysis, this means that, according to the most recent Court jurisprudence, the measures do not constitute State aid. Even if they were deemed to be State aids, they would be compatible with the common market as no overcompensation is involved. The Commission has accordingly decided not to raise any objections to the measures.

Post Office Limited (POL) is the largest European retail network when measured in the number of outlets. It is an arms' length retail subsidiary of the Royal Mail Group plc. The Royal Mail Group is entirely owned by the British Government. POL provides countrywide over-the-counter access to Government and payment services. According to the British Government, POL's services are used disproportionately by those in the lower socio-economic groups, especially the aged and those living on social security. Around 90% of POL's turnover is attributable to services it provides in the public interest. ■

The Court cases reported in this Newsletter are taken from the website of the Court of Justice of the European Communities. The contents of this website are freely available. Reports on the website are subject to editing and revision.

Readers are asked to note that the newsletter is now edited in England and that mail should be sent to the address shown on the front cover of this issue.

ACQUISITIONS (POSTAL SERVICES): THE CSC / ROYAL MAIL CASE

Subject: Acquisitions

Industry: Postal services

Parties: Computer Sciences Corporation
Royal Mail Business Systems Ltd
Royal Mail Group plc

Source: Commission Statement IP/03/766, dated 27 May 2003

(Note. The interest of this case lies mainly in its insight into the workings of the Royal Mail Group, particularly when taken in conjunction with the British Post Office case on page 130 of this issue. Given the degree of competition in the field of information technology services, the case did not give rise to difficulties under the competition rules.)

The Commission has approved the acquisition of sole control over RM Business Systems Ltd, the Information Technology division of British postal operator Royal Mail Group plc, by the US-based IT services provider Computer Sciences Corporation (CSC). The Commission has concluded that no competition concerns arise from the transaction

Royal Mail has decided to outsource its IT services to CSS. Previously, its former RM Business Systems Division (RM-BSD) provided these services to Royal Mail. The approved transaction is part of the agreement entered into by CSC and Royal Mail Group, according to which the latter will outsource to CSC its IT services. The present operation concerns the outsourcing of IT management services, which can be defined as the day-to-day operation of IT assets and processes. IT management services comprise operational services, applications IT management services and helpdesk IT management.

Royal Mail and CSC are not engaged in overlapping activities. Nor are they active in each other's upstream or downstream markets. CSC is active on the market for IT services, while Royal Mail provides postal services in the United Kingdom. RM-BSD provides in-house IT services. Furthermore, the envisaged transfer of assets and resources will not result in any significant increase of CSC's market position with respect to IT services. Both the overall IT services market and the IT management services market are very fragmented markets, CSC having a very limited position in each of them.

The Commission has stated in previous cases (IBM/PWC Consulting; Cap Gemini/Ernst & Young; Getronics/Wang; HP/Compaq; Philips/Origin; General Electric/Compunet; Cap Gemini/Vodafone; and IBM Italia/Business Solutions/JV) that the relevant product market for such services may be either the overall market for IT services or the IT management segment itself. It has also

indicated that the markets for IT services continue to be national in scope, although increasing internationalisation has been identified. In any event, market definitions have frequently been left open since the operations at stake did not give raise to significant competition concerns. This is also true for the present case.

CSC is a multinational company providing information technology (IT) services to commercial and government customers: it is active in IT outsourcing/management services, IT management consulting and systems integration. RM-BSD is a former division within the Royal Mail Group, a public company wholly owned by the British government providing postal services in the United Kingdom. RM-BSD has been incorporated as a new company, RM Business Systems Limited, for the purposes of the present operation. It provides in-house IT services to Royal Mail Group. ■

The SEB/Moulinex Case

The Commission has decided to launch an in-depth investigation into the competitive impact of the merger between the two French manufacturers of electrical household appliances, SEB and Moulinex, in Italy, Spain, Finland, Ireland and the United Kingdom. The investigation follows the ruling by the Court of First Instance last month annulling the Commission's decision in respect of these five countries while upholding its analysis for nine other countries, as well as its referral of the French aspects of the case to France. The Commission re-opened the case on 4 April and at this stage has doubts about its impact in the five countries. The launching of an in-depth investigation, which lasts four months, does not prejudge the final decision. In 2002, the Commission authorised SEB to take over Moulinex on certain conditions but referred the scrutiny of the French aspects of the case to the appropriate French authorities, in accordance with their request, since the effects of the merger would be felt primarily in France. The Court's ruling in April partly upheld the Commission's decisions, but found that it had not sufficiently established that the merger created no competition concerns in Italy, Spain, Finland, the United Kingdom and Ireland. The Commission has therefore launched a new investigation in respect of these five countries, within the limits set by the Court's ruling.

SEB and Moulinex between them market a large number of small electrical household appliances such as deep-fat-fryers, tabletop ovens, toasters, waffle irons, steam cookers, fondue sets, meat grills, coffee makers, food processors and irons. The goods are sold under the brand names Krups, Tefal, Calor and Rowenta, besides the Moulinex and SEB brands themselves.

Source: Commission Statement IP/03/744, dated 23 May 2003

ACQUISITIONS (VITAMINS): THE DSM / ROCHE CASE

Subject: Acquisitions
Undertakings

Industry: Vitamins; animal feed additives; pharmaceuticals

Parties: DSM
Roche (Vitamins and Fine Chemicals Division)

Source: Commission Statement IP/03/712, dated 20 May 2003

(Note. Past experience of the world market for vitamins has led both the Commission of the European Communities and the United States Federal Trade Commission to be wary of the activities of the principal operators in this market, so that their suspicions of any substantial regrouping of those operators are at least understandable. The acquisition in this case is complicated by the existence of vertical alliances, to which each of the parties to the acquisition already belongs. In the ordinary way, the undertakings offered by DSM - namely, to dissolve its alliance with BASF, - might have been expected to suffice and may still do so; but the Commission and the FTC are clearly going to need further reassurance.)

The Commission has launched a detailed investigation into the planned acquisition of the Vitamins and Fine Chemicals division of Swiss company Roche by Dutch-based company DSM. At this stage of the investigation, the Commission has competition concerns in the market for feed enzymes, which are animal feed additives and only a small part of the overall transaction. During the first-phase review, the parties have submitted a package of undertakings, which will be considered further during the detailed evaluation. The decision to start an in-depth review does not prejudge the final outcome in a merger.

On 31 March 2003, DSM notified the Commission of an agreement under which it would acquire sole control of Roche Vitamins and Fine Chemicals (RV&FC). DSM and RV&FC are active in a broad range of product areas, however, the only overlaps regard feed enzymes added to animal feed, in particular non-starch polysaccharide degrading enzymes (NSP degrading enzymes) and phytase. NSP-degrading enzymes help animals release nutrients in their feed. Phytase is an enzyme used to increase the amount of digestible phosphorus in animal feed.

In this respect, it is pertinent that DSM and RV&FC belong to two different vertical alliances. DSM has an alliance with BASF, and RV&FC with Novozymes, a Danish producer of industrial enzymes. In their respective alliances DSM and Novozymes are mainly responsible for research and development and production while BASF and RV&FC are mainly responsible for sales and distribution. Both alliances provide for a high level of economic integration and mutual interdependence.

The acquisition of RV&FC by DSM will create a structural link between the two alliances and lead to near monopolies on the market for phytase at both the production and distribution levels. In the course of the first-phase review of the case, DSM offered undertakings to terminate the DSM/BASF alliance and to establish BASF as an effective competitor, but the Commission could not determine in a clear-cut manner, as it must do in order to be able to grant first-phase clearance, whether that solution would fully restore effective competition. However, the Commission does not rule out the possibility that the proposed undertakings could form the basis of a solution, in which case it may not need to use the full four-months available in second-phase merger proceedings.

DSM is incorporated in The Netherlands as a public limited liability company with its corporate seat in Heerlen. It is active worldwide in the development and production of a broad range of chemical and life science products including feed enzymes, performance materials and polymers and industrial chemicals. It has subsidiaries in Europe and in the United States. RV&FC is principally active in the production and sale of vitamins and carotenoids. In addition, RV&FC distributes feed enzymes, certain vitamins and amino acids.

The operation is also being reviewed by the United States Federal Trade Commission, with which the Commission is closely co-operating. ■

Copper Concentrate: Inspections

Following press inquires, the Commission's spokesman for Competition has confirmed that, on 13 May 2003, Commission inspectors, assisted by officials from the national competition authorities of the Member States concerned, launched simultaneous unannounced inspections at the premises of some of the major European producers of copper concentrate, located in the United Kingdom and Portugal. The purpose of these inspections is to ascertain whether there is evidence of a cartel agreement and related illegal practices concerning the fixing of sales prices and sales conditions, customer allocation and market sharing for this product. (Copper concentrate is an intermediate product, transformed into the finished product, generally referred to as copper cathode - 99% pure copper, - by a smelting and refining process. These inspections have been coordinated with the US Department of Justice and the Canadian Competition Bureau, who have enforced investigation measures simultaneously. International cooperation is a high priority area of the Commission in the field of anti-cartel policy. Surprise inspections are a preliminary step in investigations into suspected cartels. The fact that the Commission carries out such inspections does not mean that the companies are guilty of anti-competitive behaviour nor does it prejudge the outcome of the investigation itself. The Commission respects the rights of defence, in particular the right of companies to be heard in antitrust proceedings.

Source: Commission Memorandum MEMO/03/107, dated14 May 2003

ECONOMIC ACTIVITY (SICKNESS FUNDS): THE AOK CASE

Subject: "Economic activity"
Price fixing
Associations of undertakings
Proportionality
"General economic interest"

Industry: Sickness funds

Parties: AOK Budesverband et al
Ichthyol-Gesellschaft Cordes et al

Source: Opinion of Advocate General Francis Jacobs in Joined Cases C-264/01, C-306/01, C-354/01 and C-355/01 (*AOK Bundesverband and Others v Ichthyol-Gesellschaft Cordes and Others*), summarized in Court Statement CJE/03/44, dated 22 May 2003

(Note. This litigation turns on whether German sickness funds are pursuing an economic activity, in which case they meet the primary test for being subject to the rules on competition, and then on whether the price fixing carried on by the sickness funds are compatible with those rules. The Advocate General considers that the fixing of amounts paid for certain medicines by German sickness funds is, in principle, contrary to competition law, but is capable of justification. In his view, it is for the national courts to determine whether the sickness funds have exercised any margin of discretion left open to them by national law in an anti-competitive manner and whether the setting of fixed amounts is a manifestly disproportionate method for ensuring the provision of a service of general economic interest. The view of the Advocate General is not binding on the Court of Justice. The task of an Advocate General is to propose to the Court, in complete independence, a legal solution to a case. The Court now has to give its ruling.)

Under German law, the great majority of employees are required to belong to a statutory health insurance system unless their income exceeds a certain level. The system is funded by compulsory contributions from the insured persons and their employers. Ordinarily, the insurance funds are required to purchase medical services and supplies and supply them to their insured persons. However, for certain products a maximum fixed price is set and where the cost of the product exceeds that fixed price, the insured person must bear the remainder of the cost. Only about 7% of medicinal products to which a fixed amount applies are priced at a level above that amount.

The fixed amounts are decided in a two stage process. First, a committee, composed of representatives of the leading sickness fund associations and associations of doctors, decide which types of products are to be subject to a fixed amount. These selections are approved by the Ministry of Health. Secondly, the

associations of sickness funds together determine the fixed amounts following certain criteria laid down by law. Once set, the fixed amounts are subject to annual review and must be adapted to reflect changes in the market. They are also required to be published and are open to challenge before the Courts.

A number of pharmaceutical companies (the respondents) challenged decisions of the leading associations of sickness funds in Germany (the appellants) to alter the fixed amount payable for their products. The respondents argued that the decision to fix prices was anti-competitive behaviour, prohibited by Community competition law. The German courts hearing the appeals referred questions to the Court of Justice of the EC as to whether Community competition law was applicable to these associations of sickness funds, whether the decisions to set fixed amounts was contrary to Community law and whether those decisions could be justified as being necessary for the provision of a service of general economic interest.

Advocate General Jacobs delivered his Opinion in this case on 22 May. He believes that Community competition law is applicable in this case. In this respect the Advocate General recalls that an activity must be economic in nature, the decision taken must relate to that activity, and the decision must be taken by an association of undertakings for Community competition law to be applicable. Whilst the Court has previously held that certain social security schemes are not economic in nature, the Advocate General considers that, in this case, the existence of a certain degree of competition between the sickness funds, and between the sickness funds and private insurers demonstrates that the activity is economic in nature as it could be carried out for profit by a private undertaking. In addition, the Advocate General considers that the fixing of certain prices falls within the sphere of that economic activity as a sickness fund's decision regarding the parameters of the services to be offered cannot be dissociated from their core activity of the provision of health insurance. Finally, the Advocate General is of the opinion that, at least at the second stage of the procedure for setting fixed amounts, the leading associations of sickness funds can be said to act as associations of undertakings, given that, at that stage, there is no requirement to obtain the prior approval of the Ministry, the decision-making body is made up exclusively of the appellants' representatives, and the applicable criteria are insufficiently distinct from the appellants' own interest in setting fixed amounts at a low level.

Advocate General Jacobs considers that, in principle, the collective decisions to fix amounts are prohibited by Community competition law. He states that such a practice effectively fixes the price for certain medicinal products, which has the object and effect of restricting competition and is expressly identified in the EC Treaty as being an anti-competitive practice.

However, the Advocate General notes that Community competition law is applicable to anti-competitive conduct engaged in by undertakings only on their own initiative. If such conduct is required by national law, competition law cannot apply. It is for the national courts to determine whether the German law eliminates any scope for autonomous conduct on the part of the appellants when

setting the fixed amounts. In this respect the Advocate General suggests that the appellants were unable to avoid fixing an amount and that the appellants were not entirely free to choose the fixed amount because of the requirement to determine the amount on the basis of the lowest price of the comparator group. Advocate General Jacobs therefore suggests that the national courts should examine whether the appellants had used any remaining discretion that they had to create an appreciably greater restriction on competition than would have resulted from another permissible decision.

If the appellants have acted autonomously, there remains the possibility of justifying their conduct as being a necessary and proportionate means of ensuring the provision of a service of general economic interest. Advocate General Jacobs considers that the sickness funds are charged with such a service. He believes that in principle the appellants could defend their position. However, it is for the national courts to determine whether the setting of fixed amounts is necessary in order to allow the appellants to carry out their general interest task, that is whether the setting of fixed amounts is indeed necessary to assure the financial stability of the sickness funds. In doing so it would have to be shown that the system was manifestly disproportionate for ensuring the ability of the sickness funds to perform their tasks of general economic interest in conditions of financial stability for such a defence to fail. ■

State Aid: The BMW Case

The Commission has closed the formal proceedings into planned aid amounting to €37.2m for BMW's engine plant in Steyr. The Commission found that a total amount of €29.9m for regional aid, training aid, environmental aid and R&D aid was compatible with the respective Community rules. A further €7.3m could not be reconciled with these rules and should not be granted. The Research and Development aid concerns investments into the development of new diesel engine technology. However, as BMW would, even in the absence of aid, have to undertake the research for the remaining R&D projects in order to stay competitive, the necessary incentive effect for these projects has not been proven. Consequently, the planned aid for these projects is not compatible with the common market. Investment aid for innovation in the motor vehicle sector can be authorised only in duly justified cases, as an incentive to industrial or technological risk-taking. The project concerns investments into state of the art testing and measuring equipment. The Commission took the view that the project could not be regarded as genuinely innovative in the sense that the technology had not yet been used or marketed by other parties operating in the industry. In addition, the aid was not considered as an incentive for industrial or technological risk-taking, as BMW would have to carry out the investment even in the absence of state aid. Consequently, the planned innovation aid was not allowed.

Source: Commission Statement IP/03/755, dated 27 May 2003

STATE AIDS (LOGISTIC CENTRES): THE FRENCH TAX CASE

Subject: State aids
Tax relief
Legitimate expectations

Industry: Headquarters and logistic centers

Parties: Republic of France

Source: Commission Statement IP/03/698, dated 16 May 2003

(Note. The French scheme described here is a variant on an earlier Belgian scheme and represents a way of granting aid, by way of tax relief, to businesses making use of the headquarters and logistic centers in question. The Commission will have none of it, but concedes that earlier decisions on similar cases created legitimate expectations.)

Following an in-depth investigation, the Commission has concluded that the special tax regime available to so-called "Headquarters and Logistic Centres" located in France breaches the European Communities' State aid rules. The Commission started formal proceedings against the scheme in July 2001. These proceedings were part of a large-scale Commission investigation into fiscal aid schemes in twelve Member States. Because at the time of the implementation of the scheme the French authorities as well as the beneficiaries had legitimate reasons to believe that the scheme was not a state aid, the Commission has decided not to seek the reimbursement of the fiscal advantages that might have been received.

In its decision, the Commission takes the view that certain aspects of the French scheme constitute State aid. While the Commission does not challenge the use of a flat-rate method to determine taxable profits, it challenges the actual implementation of the method. In particular, the French scheme offers fiscal benefits to the Headquarters and Logistic Centres or to the multinational groups to which they belong, by reducing their normal tax burden. Taxable income is calculated by removing significant items of expenditure (subcontracting costs) from the tax base or by partially excluding the Headquarters and Logistic Centres from the application of the alternative-tax (IFA) a derogation from the French tax code.

The French Tax Code takes into consideration all gainful activities and makes all profitable companies subject to IFA. Under the Headquarters and Logistic Centres scheme, however, a French Headquarters or Logistic Centre operating under an approved agreement may exclude a significant amount of its activities from taxation by subcontracting them to third parties. Similarly, a Headquarters or Logistic Centre is substantively exempt from the advance payment of tax normally imposed under the IFA rules. The Commission has therefore concluded

that the French scheme reduces the taxable earnings of the French Headquarters and Logistic Centres and also confers a treasury advantage by exonerating them from the advance-payment of IFA. The above regime results in selective lower effective taxation, which is not allowed by State aid rules.

The French Headquarters and Logistic Centres regime is designed to promote the installation of subsidiaries or branches of multinational groups in France by providing a special agreement concerning the tax treatment of certain intra-group activities of such groups. French subsidiaries and branches of multinational groups may apply to the tax authorities to have their taxable income calculated as a fixed percentage of their expenditures, using the "cost-plus" method. However, under the French scheme, certain subcontracting costs are not taken into account for the cost-plus computation, if they represent less than 50% of the total business costs. Furthermore, the Headquarters and Logistic Centres are partially excluded from the application of the alternative-minimum-turnover-tax Impôt Forfaitaire Annuelle (IFA) provisions of the French tax code.

The scheme applies only to French subsidiaries or permanent establishments of foreign companies operating within a multinational group of companies. These subsidiaries have to agree with the tax authorities that they intend to operate under a special Headquarters and Logistic Centres regime agreement and that are prevalently engaged in providing certain cross-border services. "Prevalently engaged" is defined as having more than 50% of their global business costs connected to cross-border intra-group activities.

The French regime was originally introduced to attract the location of certain activities of multinational groups by increasing their international competitiveness. However, the Commission's investigation has revealed that the tax advantages granted under the regime constitute a selective advantage benefiting only French subsidiaries and branches operating under the above-described agreements. Especially in case of intra-group international activities such as research and development, which are subject to fierce competition and are potentially covered by the scheme, the distortion created by the tax advantage is very substantial. Thus, the negative effect on competition and trade in the single market could be considerable.

The Commission has found that the features of the French Headquarters and Logistic Centres scheme are similar to the Belgian co-ordination centres. With respect to the latter, the Commission had already initiated formal investigation proceedings, following Belgium's refusal to bring the scheme into line with the rules on competition, as recommended in July 2001. In February 2003, the Commission decided that certain special tax breaks provided for by Belgian scheme constituted State aid; but, as the Belgian scheme had, in 1984, not been considered to involve State aid, the Commission has concluded that the French authorities and the beneficiaries of the French Headquarters and Logistic Centres scheme could rely on legitimate expectations. Therefore, under the current decision, the Commission has not ordered recovery of the aid. ■

STATE AIDS (ELECTRONICS): THE SELECO CASE

Subject: State aids
Recovery
Statement of reasons

Industry: Electronics

Parties: Italian Republic
SIM 2 Multimedia SpA
Commission of the European Communities
Seleco SpA
Ristrutturazione Elettronica SpA

Source: Judgment of the Court of Justice of the European Communities, dated 8 May 2003 in Joined Cases C-328/99 and C-399/00 (*Italian Republic and SIM 2 Multimedia SpA v Commission of the European Communities*)

(Note. This action, which was partly successful, challenged a Commission decision requiring the recovery of illegally paid state aid. The Commission's case failed partly on account of its inadequate statement of reasons for its decision and partly for providing no evidence on the valuation of the financial benefits to the firm in question. The judgment offers an invaluable guide to the law on the recovery of illegally paid state aid.)

Judgment

1. By application lodged at the Court Registry on 1 September 1999 and registered under the number C-328/99, the Italian Republic brought an action under the first subparagraph of Article 230 of the EC Treaty for:
- annulment of Commission Decision 2000/536/EC of 2 June 1999 concerning State aid granted by Italy to Seleco SpA (hereinafter, the contested decision), and
- in the alternative, annulment of that decision in so far as it requires the Italian Republic to take the necessary measures to recover from Seleco SpA the incompatible aid granted by Ristrutturazione Elettronica SpA (hereinafter, REL) in 1996 and in so far as it requires the Italian Republic to adopt the necessary measures to recover from Seleco Multimedia Srl (hereinafter, Multimedia) and from any other undertaking which benefited from asset transfers the incompatible aid granted to Seleco, for the part not recoverable from the latter.

2. By application lodged at the Registry of the Court of First Instance on 6 September 1999 and registered under number T-195/99, SIM 2 Multimedia SpA (hereinafter, SIM Multimedia), legal successor to Multimedia, brought an action to annul Article 2(1) of the contested decision in so far as it requires the Italian Republic to take all the necessary measures to recover from Multimedia the

incompatible aid granted to Seleco, with regard to the part not recoverable from the latter.

[Paragraphs 3 and 4 concern the transfer of the second case to the Court of Justice and the joining of the two cases for the purposes of oral procedure and judgment.]

Legal background

5. Under Article 87(1) of the EC Treaty:
Save as otherwise provided in this 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, in so far as it affects trade between Member States, be incompatible with the common market.

6. The first subparagraph of Article 88(2) of the EC Treaty provides:
If, after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the common market having regard to Article 87, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission.

7. In accordance with Article 88(3) of the EC Treaty:
The Commission shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. If it considers that any such plan is not compatible with the common market having regard to Article 87, it shall without delay initiate the procedure provided for in paragraph 2. The Member State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision.

Facts in the proceedings

The parties concerned

8. Seleco was active in the consumer electronics market and, more specifically, in the sector of colour television sets, decoders for encrypted programmes and video projectors and monitors.

9. Multimedia was established in 1995. In March 1996 Seleco hived off its most profitable activities (video projectors and monitors) to Multimedia, providing ITL 29 billion in capital and becoming its sole owner. In June 1996, Multimedia was converted into a company limited by shares. In July 1996, Seleco sold 33.33% of the shares which it held in Multimedia to Italtel and 33.33% to Friulia SpA. Each package of shares was sold for ITL 10 billion. The remaining shares were transferred to a shell company belonging to Seleco and then sold to a private company at a public sale by court order which took place on 20 December 1997 in the context of the liquidation of Seleco.

[Paragraphs 10 to 16 amplify the foregoing facts.]

17. After it learned that the aid granted to Seleco, which had been notified to it by the Autonomous Region of Friulia-Venezia Giulia, had already been

implemented and that REL had partly written off its claims on Seleco under an agreement concluded in 1994 for the purpose of covering the losses for the financial year 1993, the Commission decided on 27 September 1994 to initiate the procedure laid down in Article 93(2) of the EC Treaty (now Article 88(2). After subsequently learning from press reports that other public aid had been granted to Seleco, the Commission extended that procedure to those other measures by decision of 3 February 1998.

18. That procedure ended in the adoption of the contested decision, the operative part of which is worded as follows:

Article 1
The following aid granted by Italy to Seleco SpA is hereby declared incompatible with the common market:
(a) the partial write-off in 1994 by Ristrutturazione Elettronica SpA of ITL 16.8 billion on a loan of ITL 82 billion;
(b) the repurchase in 1996 by Seleco SpA of its outstanding debt to Ristrutturazione Elettronica SpA of ITL 65.2 billion for ITL 20 billion;
(c) the conversion into shares by Friulia SpA of an ITL 6 billion loan granted by it in 1992;
(d) a capital injection of ITL 7 billion by Friulia SpA in 1994;
(e) a convertible loan of ITL 12 billion at 7% granted by Friulia in 1996 and guaranteed by a lien on four industrial brands owned by Seleco.

Article 2
1. Italy shall take all the necessary measures to recover the aid referred to in Article 1, which has already been granted unlawfully, from Seleco SpA and, additionally, with regard to the part not recoverable from Seleco, from Seleco Multimedia srl and any other firm which benefited from asset transfers designed to frustrate the effects of this decision.
2. Recovery shall be effected in accordance with the procedures of national law. The aid to be recovered shall include interest from the date on which it was made available to the recipient until the date of its recovery. Interest shall be calculated on the basis of the reference rate used for calculating the net grant equivalent of regional aid applicable at the time the aid was granted.

Article 3
Italy 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 Italian Republic.

19. In those circumstances, the Italian Republic and SIM Multimedia brought the present actions against the contested decision.

Substance

20. The action brought by the Italian Government calls in question the categorisation of the operations by REL and Friulia as State aid, the requirement to recover from Seleco the alleged aid which REL granted to it in 1996 and the requirement to cover the so-called State aid from SIM Multimedia.

Classification of the operations by REL and Friulia as State aid

[Paragraphs 21 et seq set out the arguments of the parties.]

Findings of the Court

31. It is appropriate, first, to consider whether the operations carried out by Friulia referred to in Article 1(c), (d) and (e) of the contested decision, mentioned *inter alia* in paragraph 18 of the present judgment, must be regarded as having been carried out by means of State resources within the meaning of Article 87(1) of the EC Treaty.

32. In that regard, although the Italian Government claims that Friulia's private partners have wide powers of decision-making and of disinvestment, it does not deny the Commission's claim that the company was under the control of the Region of Friulia-Venezia Giulia.

33. The financial resources of a private-law company such as Friulia, 87% of which is held by a public authority such as the Region of Friulia-Venezia Giulia and which acts under the control of that authority, may be regarded as State resources within the meaning of Article 87(1) of the EC Treaty (see, to that effect, Case 323/82, *Intermills* v *Commission*, paragraph 32, and Joined Cases 67/85, 68/85 and 70/85, *Van der Kooy* v *Commission*, paragraphs 36 and 38). The fact that Friulia participated using its own funds is irrelevant in that regard. For those funds to be categorised as State resources, it is sufficient that, as in the present case, they constantly remain under public control and therefore available to the competent national authorities (see, to that effect, Case C-482/99, *France* v *Commission*, paragraph 37).

34. It follows that the Commission was right in holding in the contested decision that Friulia's operations were carried out by means of State resources, within the meaning of Article 87(1) of the EC Treaty.

35. Next, it must be borne in mind that the aim of Article 87 of the EC Treaty is to prevent trade between Member States from being affected by advantages granted by public authorities which, in various forms, distort or threaten to distort competition by favouring certain undertakings or certain products. The notion of aid can thus encompass not only positive benefits such as subsidies, loans or direct investment in the capital of enterprises, but also interventions which in various forms mitigate the charges which are normally included in the budget of an undertaking and which therefore, without being subsidies in the strict sense of the word, are of the same character and have the same effect (see Case 234/84, *Belgium* v *Commission*, paragraph 13, and Case C-39/94, *SFEI and Others*, paragraph 58).

36. It is settled case-law that investment by the public authorities in the capital of an undertaking, in whatever form, may constitute State aid where all the conditions set out in Article 87(1) of the EC Treaty are fulfilled (see, in particular, Case C-142/87, *Belgium* v *Commission* (*Tubemeuse*), paragraph 25; Joined

Cases C-278/92 to C-280/92, *Spain* v *Commission*, paragraph 20, and *France* v *Commission*, cited above, paragraph 68).

37. It should also be noted that, pursuant to the principle that the public and private sectors are to be treated equally, capital placed directly or indirectly at the disposal of an undertaking by the State in circumstances which correspond to normal market conditions cannot be regarded as State aid (Case C-303/88, *Italy* v *Commission*, paragraph 20).

38. Therefore, in accordance with equally settled case-law, it is necessary to determine whether, in similar circumstances, a private investor of a dimension comparable to that of the bodies managing the public sector could have been prevailed upon to make capital contributions of the same size (Case C-261/89, *Italy* v *Commission*, paragraph 8; *Spain* v *Commission*, cited above, paragraph 21; and Case C-42/93, *Spain* v *Commission*, paragraph 13), having regard in particular to the information available and foreseeable developments at the date of those contributions (*France* v *Commission*, paragraph 70).

39. Since that involves a complex economic appraisal, in reviewing an act of the Commission which has necessitated such an appraisal, the Court must confine itself to verifying whether the Commission complied with the relevant rules governing procedure and the statement of reasons, whether the facts on which the contested finding was based have been accurately stated and whether there has been any manifest error of assessment or a misuse of powers (see *inter alia* Case C-56/93, *Belgium* v *Commission*, paragraph 11).

40. In this case, therefore, it is necessary to assess whether, in similar circumstances, a private investor of a dimension comparable to that of REL or Friulia could have been prevailed upon to make capital contributions of the same size, having regard in particular to the information available and foreseeable developments at the date of those contributions.

41. First, the parties agree that, at the time of the first recapitalisation of Seleco, that company's financial situation was poor...

42. Secondly, Seleco's restructuring plan for 1993 to 1996, which was the second since the beginning of the decade, forecast a return to profitability in 1995, while the first plan, which covered the period 1990 to 1993, had forecast a return to significant profits in 1993 (point 68 of the grounds of the contested decision). However, at the request of Friulia, the restructuring plan for 1993 to 1996 was studied by KPMG Peat Marwick Corporate Finance, an independent outside expert, which came to the conclusion that it was too ambitious, on the basis of both the firm's position and the plan's underlying assumptions...

43. Thirdly, it is clear from the minutes of Seleco's general meeting of 1 February 1994, a copy of which is attached to the Italian Government's application, that REL, whose representatives took part in several meetings with representatives of the Ministry of Industry and the Presidency of the Council, had stated that it was ready, in view of the interests linked to employment, to cover the amount of the

losses which exceeded the company's net assets in proportion to its shares, by partially waiving the debt owed it by Seleco.

44. It follows from the foregoing that, as regards the recapitalisation of Seleco in 1994, neither Friulia nor REL acted like a private investor operating under normal market conditions. A private investor would not, under those conditions, have made the capital contributions made by Friulia or REL to an undertaking in difficulty such as Seleco without having a credible and realistic restructuring plan or taking social concerns into account (see, as regards the latter point, Case C-303/88, *Italy* v *Commission*, cited above, paragraphs 18 and 24), and thus not seeking to ensure the likelihood of profitability for such contributions.

45. The Commission was therefore right to consider that REL and Friulia could not expect that the capital contributions made in the context of the 1994 recapitalisation of Seleco would generate an acceptable profit for a private investor operating under normal market conditions.

46. Accordingly, it must be held that the interventions by REL and Friulia in the first recapitalisation of Seleco constitute State aid within the meaning of Article 87(1) of the EC Treaty.

47. As regards the second recapitalisation of Seleco, it must be pointed out that Seleco showed a loss of ITL 64.2 billion for the financial year 1995, almost twice the amount of its equity capital, although the company's restructuring plan for 1993 to 1996 counted on a return to profitability in 1995.

48. Since Seleco's restructuring plan had proved to be unachievable, and in the absence of any information concerning any other restructuring plan which would make it possible in the present case to consider that second intervention acceptable, the Commission was entitled to take the view that no informed private investor operating under normal market conditions would have made the capital contributions that REL and Friulia made to Seleco at the time of its recapitalisation in 1996, since its financial situation remained poor, and indeed critical.

49. Therefore, the interventions by REL and Friulia in the second recapitalisation of Seleco also constituted State aid within the meaning of Article 87(1) of the EC Treaty.

50. The first plea put forward by the Italian Government must therefore be rejected.

The obligation to recover the aid REL granted Seleco in 1996

[Paragraphs 51 and 52 set out the arguments of the parties.]

53. In that respect, it must be borne in mind that it is settled case-law that recovery of unlawful aid is the logical consequence of a finding that it is unlawful

(see, in particular, *Tubemeuse*, cited above, paragraph 66, and Case C-261/99, *Commission* v *France*, paragraph 22).

54. Accordingly, since the repurchase in 1996 by Seleco of its outstanding debt to REL of ITL 65.2 billion for ITL 20 billion constitutes unlawful State aid, the Commission is entitled to order the Italian Republic to take the necessary measures to recover it (see, to that effect, Case 310/85. *Deufil* v *Commission*, paragraph 24).

55. The fact that REL must return ITL 20 billion to the bankrupt company and apply for its earlier unsecured claim of ITL 65.2 billion to be registered among the liabilities of Seleco, even assuming it to be established, cannot in this instance call in question the principle that unlawful aid must be recovered.

56. Accordingly, the second plea of the Italian Government must be rejected.

The obligation to recover State aid from Multimedia

57. The contested decision, in so far as it requires the Italian Republic to recover the aid at issue from Multimedia, is the subject of several pleas in law put forward as grounds for annulment. The Italian Government and SIM Multimedia both put forward a plea alleging infringement of the right to a fair hearing. SIM Multimedia also puts forward pleas alleging the non-existence of State aid to Multimedia, inadequacy of and contradictions in the statement of reasons for the contested decision, and disproportion between the recovery order to the detriment of Multimedia and the size of the branch of the undertaking at issue.

58. It is appropriate first to consider the plea alleging non-existence of aid to Multimedia.

[Paragraphs 59 et seq set out the arguments of the parties.]

65. As a preliminary observation, it should be pointed out that, in accordance with Community law, when the Commission finds that aid is incompatible with the common market, it may order the Member State to recover that aid from the recipient (Case 70/72, *Commission* v *Germany*, paragraph 20).

66. The recovery of unlawful aid is the logical consequence of a finding that it is unlawful (see *Tubemeuse*, paragraph 66) and seeks to re-establish the previously existing situation (Case C-382/99, *Netherlands* v *Commission*, paragraph 89).

67. Article 2(1) of the contested decision provides that the Italian Republic is to take all the necessary measures to recover the incompatible aid identified by the Commission, and which has already been granted unlawfully, from Seleco SpA and, additionally, with regard to the part not recoverable from Seleco, from Multimedia and any other firm which benefited from asset transfers designed to frustrate the effects of the contested decision.

68. The Commission, in giving the reasons for that element of the operative part of the contested decision, was right to observe in point 113 that in order to ensure that the decision is implemented correctly the Member State is required to act like a private creditor.

69. The Commission was also right to state in points 113 to 115 of the grounds of the contested decision, that:
- ... To ensure that the Commission decision is implemented correctly, the Member State is required ... to recover the aid without delay, using all the legal means at its disposal, including seizure of the firm's assets and, where necessary, its liquidation if it is unable to repay the amounts in question. The proceeds of the sale of the assets allow the creditors, including the Member State, to be repaid even if they are not sufficient to cover all the debts of the firm and even if, consequently, the aid is not recovered in full. In such circumstances, the liquidation of the firm is still important from a competition standpoint as it frees the market segment previously held by the firm and makes it available to creditors, while giving them the opportunity to acquire the assets and reallocate them more effectively.
- There are, however, circumstances which can hamper that process, jeopardise the effectiveness of the recovery decision and frustrate the rules on State aid. Such is the case when, following a Commission investigation or decision, the assets and liabilities of the firm as an ongoing concern are transferred to another firm controlled by the same persons at below-market prices or by way of procedures that lack transparency. The purpose of such a transaction can be to place the assets out of reach of the Commission decision and to continue the economic activity in question indefinitely.
- As in any other recovery procedure, the Member State must, like any other diligent creditor, exhaust all the legal instruments available under its own legal system, such as those used to combat fraud against creditors in the form of acts carried out by the firm in liquidation during the suspect period prior to the bankruptcy, which would allow such acts to be declared invalid.

[Paragraphs 70 et seq describe the arrangements made for hiving off Seleco's activities, assets and debts. The facts were not disputed.]

72. In the present case, it is also common ground that the value of the multimedia branch transferred by Seleco to Multimedia in exchange for all of the latter's shares had been estimated by a sworn expert appointed by the national court for that purpose. It is also common ground that the price Friulia and Italtel paid for the purchase of two thirds of the shares which Seleco held in Multimedia, which took place several months after that transfer, in effect corresponded to two thirds of the value of the multimedia branch, as estimated by the above-mentioned sworn expert. The Commission has not put forward any concrete evidence that that expert estimated the value of the multimedia branch transferred by Seleco to Multimedia taking into account the risk that the latter company might be required, should the case arise, to repay all or part of the aid granted to Seleco.

73. It is further not in dispute that the administrator appointed by the court in Seleco's bankruptcy did not act to revoke the transfer by Seleco of the two thirds of the shares which it held in Multimedia.

74. Finally, it is clear from the documents before the Court that the expert's report produced at the end of 1997 at the request of the bankruptcy court set the value of Multimedia's trading capital considerably lower than what had been estimated in the previous expert's report.

75. In those circumstances, the question arises whether Multimedia should also be considered as having been a beneficiary of the aid.

76. In that regard, it is appropriate to point out that the possibility of a company in economic difficulties taking measures to rehabilitate the business cannot be ruled out *a priori* because of requirements relating to recovery of the aid which is incompatible with the common market.

77. However, as the Commission is essentially maintaining before the Court, if it were permissible, without any condition, for an undertaking experiencing difficulties and on the point of being declared bankrupt to create, during the formal inquiry into the aid granted it, a subsidiary to which it then transfers its most profitable assets before the conclusion of the inquiry, that would amount to accepting that any company may remove such assets from the parent undertaking when aid is recovered, which would risk depriving the recovery of that aid of its effect in whole or in part.

78. Thus the Commission pointed out at points 116 and 117 of the grounds of the contested decision that:
- in order to prevent the effectiveness of the decision to recover the aid 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 firm but is extended to the firm which continues the activity of the original firm, using the transferred means of production, in cases where certain elements of the transfer point to economic continuity between the two firms;
- the elements examined by the Commission include the purpose of the transfer (assets and liabilities, continuity of the workforce, bundled assets, etc.), the transfer price, the identity of the shareholders or owners of the acquiring firm and of the original firm, the moment at which the transfer was carried out(after the start of the investigation, the initiation of the procedure or the final decision) and, lastly, the economic logic of the transaction.

79. In this case, it is, admittedly, relevant to point out, as the Commission does in points 118 and 119 of the grounds of the contested decision, that:
- Seleco hived off in March 1996 its most profitable assets to Multimedia, injecting ITL 29 billion into the capital of that company;
- that transaction, which helped to deprive Seleco of its substance in two respects (activities and capital), occurred at a time when the Commission had initiated the procedure laid down in Article 93(2) of the Treaty;

- it is likely that the transaction was not limited to a transfer of assets and that the transfer of Seleco's main activities was accompanied by the transfer to Multimedia of the corresponding workforce (or part of it) and hence of its social security debts at the very least;
- after Seleco sold two thirds of its shares in Multimedia, the latter remained under the control of Seleco and/or Friulia (which was itself Seleco's third shareholder and which had granted Seleco a convertible loan of ITL 12 billion).

80. However, it must be observed that, in that statement of reasons, the Commission makes no mention of the price of the transfer, although it referred to that element in the contested decision as one of the two which had to be taken into account.

[Paragraphs 81 to 83 refer to the Commission's assumptions.]

84. In addition, the Commission did not take into account in the contested decision the consequences of the obligation on the part of the Italian Republic to recover the unlawful aid from Multimedia with regard to the private company which, at a court-ordered public sale as part of the liquidation of Seleco, bought the final third of the shares in Multimedia.

85. In the light of the foregoing, it is apparent that the statement of the reasons on which the contested decision is based is inadequate for the purposes of Article 253 of the EC Treaty, in particular as regards the alleged irrelevance of the fact that the shares in Multimedia were bought at a price which seemed to be the market price, although that point was required also to be taken into account in the present case.

86. In those circumstances, Article 2(1) of the contested decision must be annulled in so far as it provides that the Italian Republic is to take all the necessary measures to recover the aid referred to in Article 1 from Multimedia, with regard to the part not recoverable from Seleco.

87. The remainder of the application is dismissed.

[Paragraphs 88 and 89 deal with costs, referred to in the ruling below.]

Court's Ruling

The Court hereby: 1. Annuls Article 2(1) of Commission Decision 2000/536/EC of 2 June 1999 concerning State aid granted by Italy to Seleco SpA in so far as it provides that the Italian Republic is to take all the necessary measures to recover the aid referred to in Article 1 from Seleco Multimedia Srl with regard to the part not recoverable from Seleco SpA;
2. Dismisses the remainder of the application;
3. Orders, in Case C-328/99, the Italian Republic and the Commission of the European Communities to bear their own costs;
4. Orders, in Case C-399/00, the Commission of the European Communities to pay the costs. ■