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EUROPEAN COMMISSION

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Commission's enforcement record in 2006

By Philip LOWE, Director-General for Competition

2006 was another landmark year for competition policy and enforcement. In this and earlier editions of the Competition Policy Newsletter, you can find articles that describe the policy and impact of the Commission's enforcement actions. Here, I would like to sum up some of the practical achievements of 2006, in addition to those mentioned elsewhere in this edition of the Newsletter, most notably those related to the sector inquiries.

In antitrust, the Commission took seven cartel decisions ([1]) fining 41 undertakings ([2]) a total of €1,846 million. By the end of 2006 the Commission had received 104 applications for immunity and 99 for a reduction of fines under the 2002 Leniency Notice. Four of the cartel decisions adopted in 2006 were based on this Notice and one on the earlier 1996 Notice. In these cases the Commission granted substantial reductions of fines for 10 companies in return for the evidence which they provided.

The Commission adopted a revised version of the Notice ([3]), providing more guidance and transparency, reflecting more than four years of experience in applying the 2002 Leniency Notice ([4]) and bringing it fully into line with the ECN's Model Leniency Programme, also adopted in 2006. Improvements include clarification of the thresholds for immunity and reduction of fines and the conditions that must be fulfilled by applicants, and amendments to the procedure, such as introducing a discretionary marker system.

In order to increase the deterrent effect of its fines in Article 81 and 82 cases, the Commission adopted new Guidelines ([5]), basing the basic amount of the fine on up to 30% of the undertaking's yearly sales of the product, in the geographic area concerned. This amount will then be multiplied by the number of years of the undertaking's participation. For repeat offenders, the Commission may increase the fine by up to 100 % for each prior infringement, including those found by National Competition Authorities applying Article 81 or Article 82.

([1]) COMP 38.620, 38.645, 38.456, 38.121, 38.907, 38.638, and 39.234.
([2]) Excluding companies that received immunity from fines.
([3]) OJ C 298, 8.12.2006.
([4]) OJ C 45, 19.2.2002.
([5]) OJ C 210, 1.9.2006.

2006 was the first year when the Commission had to use its powers to fix a periodic penalty payment, in order to compel an undertaking to comply with a decision ordering it to bring an infringement of Article 81 or 82 EC to an end. It imposed on Microsoft a definitive penalty payment of €280.5 million for non-compliance with certain of its obligations under the 2004 Article 82 decision. The Commission also adopted one final abuse of dominance decision, fining Tomra €24 million for violating Article 82 by operating a system of exclusivity agreements, individualised quantity commitments and individualised retroactive rebate schemes, which restricted or at least delayed the market entry of its competitors ([6]).

Fines and, more generally, public enforcement, is not enough for a fully effective competition policy: the Green Paper on damages ([7]) was broadly welcomed and discussed widely in Europe and elsewhere. The Commission received almost 150 submissions from governments, competition authorities, industry, consumer organisations, lawyers and academics, the vast majority supportive. As a follow-up, the Commission intends to issue a White Paper by the end of 2007 ([8]).

In mergers, the number of notifications reached a record high of 356, surpassing the previous record reached in 2000. The Commission adopted 352 final decisions: in phase I, 336 transactions were cleared, 13 of them subject to conditions. Thirteen phase II proceedings were opened, culminating in ten Article 8 decisions, with two notifications being withdrawn by the parties during Phase II. There were no prohibitions.

There were two noteworthy cases of "non-coordinated" effects: *Linde/BOC* ([9]) and *T-Mobile Austria/tele.ring* ([10]): in both cases, the Commission found that the merger would significantly impede competition although the merged entity would not become the market leader in the relevant market. Both cases were cleared subject to remedies. Claims of efficiencies were substantiated in two cases, *Korsnas/AD Cartonboard* ([11]) and *Inco/Fal-*

([6]) COMP/38.113.
([7]) See http://ec.europa.eu/comm/competition/antitrust/actionsdamages/documents.html
([8]) See http://ec.europa.eu/atwork/programmes/index_en.htm
([9]) COMP/M.4141.
([10]) COMP/M.3916.
([11]) COMP/M.4057.

conbridge (12). The Commission assessed the extent to which these efficiencies would impact on an overall appraisal of the competitive effects of the transactions in question, in line with the approach set out in the Horizontal Merger Guidelines (13).

Although the loss of the Sony/BMG case was a disappointment, the Commission welcomed the greater clarity that the case provided for the assessment of such cases, as well as the further confirmation that the test under the merger regulation is symmetric — the burden is just as high on the Commission to clear a merger as it is to prohibit it.

The Commission consulted on a new draft Commission Consolidated Jurisdictional Notice (14), to replace the existing four Jurisdictional Notices from 1998. This covers all issues of jurisdiction relevant for establishing the Commission's competence under the Merger Regulation (save for referrals), and is expected to be adopted later this year.

State aid also saw a significant increase in workload. 921 new State aid cases were registered (a 36 % increase on 2005) and the Commission took 710 final decisions (15) (a 12 % increase). In the vast majority of cases, the Commission approved the measures, concluding that the examined aid was compatible with the State aid rules (91 %) or did not constitute State aid (4 %). Where the Commission had doubts as to compliance it carried out a formal investigation, leading to positive, conditional or no aid decisions in 3 % of cases and a finding that the aid did not comply with State aid rules in 2 % of cases.

The main regional aid cases concerned large investment projects covered by the 2002 Multisectoral framework (16). The Commission approved aid in 9 Polish cases concerning investment by *LG Philips LCD Poland Sp. z o.o.* (17), two German investment projects — *First Solar GmbH* (18) and *HighSi GmbH* (19) — and one investment from a Korean firm in Hungary (20).

A major €2 billion R&D&I scheme concerning the French Innovation Agency (21) was approved. In line with the new framework, the impact of the aid on competition was carefully analysed in some aeronautical cases — concerning aid to *Rolls-Royce* (22) and to *Eurocopter* (23) — and in the first large project notified by the French Agency, *BioHub* (24).

Continuing efforts were made to implement recovery decisions more effectively and immediately: of the €8.7 billion of aid to be recovered under decisions adopted since 2000, some €7.2 billion (i.e. 83 % of the total amount) had been effectively recovered by the end of 2006.

Finally, significant progress was made in implementing the State Aid Action Plan and modernising the State aid rules: the Commission simplified the approval of regional aid by adopting a block exemption Regulation for regional investment aid (25) and approving 18 regional aid maps. The Commission also adopted the new State aid framework for Research, Development and Innovation (26), to help Member States channel a larger share of their total State aid budgets towards boosting R,D&I, new Risk capital Guidelines (27), allowing Member States to improve access to finance for SMEs, and a new de minimis Regulation (28) exempting small subsidies of up to €200,000 over three years from the obligation to be cleared by the Commission in advance.

As you can see from the above, the roughly 700 staff of DG Competition achieved a considerable amount in 2006. Every indication is that achievements in 2007 will be similarly great.

(12) COMP/M.4000.
(13) See paragraphs 76-88, OJ C 31, 5.2.2004, p. 5.
(14) OJ L 24, 29.1.2004, p. 1.
(15) Excluding decisions to open the formal investigation procedure, corrigenda, injunctions, proposals for appropriate measures.
(16) OJ C 70, 19.3.2002, p. 8.
(17) N 245/2006, N 246/2006, N 247/2006, N 248/2006, N 249/2006, N 250/2006, N 251/2006, N 256/2006, N 257/2006.
(18) N 17/2006.
(19) N 409/2006.
(20) N 34/2006.
(21) N 121/2006.
(22) N 193/2006.
(23) N 186/2006.
(24) N 708/2006.
(25) OJ L 302, 1.11.2006, p. 29.
(26) OJ C 323, 30.12.2006, p. 1.
(27) OJ C 194, 18.8.2006, p. 2.
(28) OJ L 379, 28.12.2006.

The new community framework for state aid for research and development and innovation (1)

Thibaut KLEINER and Renate REPPLINGER-HACH, Directorate-General for Competition, unit I-1

On 22/11/2006, the Commission has adopted a new Community framework for state aid for research and development and innovation. The new framework has been published in the Official Journal on 30/12/2006 (2) and has entered into force on 01/01/2007. This document modernises the 1996 R&D framework, introduces new possibilities for granting State aid to innovation and implements the refined economic approach outlined in the State Aid Action Plan. It requires better economic justification for State aid measures in order to be approved and introduces a detailed assessment to deal with large aid amounts. The new framework is a significant contribution from the Commission to the re-launched Lisbon Strategy and it offers an opportunity for Member States to better use their State budget to deliver growth and jobs in the Union.

A process of analysis and consultation

The Commission adopted a Community framework on State aid for research and development (R&D) already in 1996. With the State Aid Action Plan (SAAP) of June 2005, the Commission set out an ambitious roadmap for State aid reform, where it inter alia announced its intention to review the current State aid framework for Research and Development (R&D) and considered extending the scope of the framework to certain innovative activities, thereby creating a Framework for R&D and Innovation (R&D&I). Given the high expectations associated with the new R&D&I framework, its adoption, following a substantial process of analysis and consultation, represents a noticeable achievement for the SAAP.

Several activities preceded the adoption of the new framework: DG Competition conducted an analysis of its case practice on State aid for innovation, resulting in a staff paper, the *Vademecum on Community rules on State aid for Innovation* (3) of November 2004. In 2004, the Commission had also launched a study on the R&D State aid rules (4). In 2005, it conducted a study on innovation market failures and state aid (5) and developed some ideas on a series of innovation activities that could benefit from State aid. This resulted in September 2005 in the Commission adopting a Communication on State aid for Innovation (6). Stakeholder consultation on State aid for innovation, following the communication and following a conference organised by DG Competition, made it possible to integrate new measure in a draft new R&D&I framework. This draft itself was subject to extended consultation: two draft versions were submitted to public scrutiny in May and September 2006 and discussed with Member States twice. Besides, on a more political level, the European Parliament issued an opinion on the Communication on State aid for innovation, and the European Council referred several times in its conclusions to the new R&D&I framework. As a result, the text of the new framework has been improved throughout 2006 and has benefited from the insight of experts not only from national and regional governments, but also from industry.

The new framework illustrates how the Commission is implementing the refined economic approach introduced in the SAAP and already used for the new State Aid Risk Capital Guidelines (7) adopted in July 2006. Both texts form part of the Commission's State aid package for the re-launched Lisbon Strategy. They also show that competition policy, one of the few areas where the Commission has exclusive competence, can be mobilised pro-actively towards the objectives of growth and jobs.

The new framework plays a prominent role in this Commission's work programme. It corresponds to Action 6 in the ten priority actions to achieve a broad-based innovation strategy for the European

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.
(2) OJ C 323 of 30.12.2006, p. 1.
(3) http://ec.europa.eu/comm/competition/state_aid/reform/innovation_vademecum.pdf
(4) "The Impact of R&D State aid and its appraisal on the level of EU research expenditures in the context of the Barcelona European Council Objectives", available upon request from the European Commission, DG RTD C 2.
(5) http://ec.europa.eu/enterprise/library/lib-competition/doc/innovation_market_failures_and_state_aid.pdf
(6) http://ec.europa.eu/comm/competition/state_aid/reform/rdi_frame_en.pdf
(7) OJ C 194 of 18.8.2006, p. 2.

Union ([8]) and to Action 10a in the Community Lisbon programme ([9]). By adopting this new framework, the Commission demonstrates its commitment to supporting innovation, growth and jobs in the European Union.

A better use of State aid

European companies must invest more in R&D and Innovation if they are to strive in front of global competition. The most important way to stimulate innovation is by fostering effective competition. As recognized both in the Commission's Communication to the Lahti informal European Council ([10]) and in the Aho report ([11]), effective competition and a fully-functioning single market are pre-requisites for more innovation. Innovation is a way for firms to differentiate their products, increase their appeal to customers and thereby survive competitive pressures. Preserving free and fair competition is therefore the single most important contribution to innovation policy.

By contrast, State aid can be abused to protect national players, keep inefficient firms afloat, distort competition and artificially maintain costly, fragmented markets. This creates disincentives for State aid beneficiaries and non-aided companies alike. What is more, State aid is not some sort of 'magic wand' to solve Europe's innovation problems. It is only one complementary element in the much larger tool-box needed to spur R&D and innovation. State aid can not replace the structural reforms Europe badly needs — and it should certainly not delay them. This is why State aid control is necessary.

At the same time, there are situations where the market on its own fails to deliver an optimal outcome. Sometimes, private firms consider that their investments in R&D and Innovation will not bring them any profit, either because they cannot avoid that the results of their research will be appropriated by competitors, because of uncertainties about the success of their efforts or because of difficulties to coordinate with business partners. As a result, private firms will refrain from investing in R&D&I projects, which would however bring benefits to society. In such cases, State aid can help change the incentives of private firms and make them invest in R&D&I. State aid can contribute to generate more R&D&I if it addresses those well identified market failures which prevent markets from reaching optimal R&D&I levels, and if it is well designed to limit distortions to competition to the minimum.

The primary objective of this new framework is therefore essentially twofold:

- Help Member States invest more in R&D and Innovation and increase the share of aid for R&D&I as a percentage of total State aid budgets; and
- Use better economics to help Member States target State aid on the right projects, so that distortions of competition and trade are minimised and public spending efficiency maximised.

A refined economic approach

The new R&D&I framework is a concrete implementation of the refined economic approach laid down in the SAAP. More economic analysis should help Member States better design their State aid measures, taking due account of the risks for competition and trade, so that only valuable projects are aided.

The framework recalls the overall methodology, based on the 'balancing test' which outlines how the positive and negative effects of State aid are analysed. The balancing test specifies that State aid for R&D&I is only acceptable in so far as i) it addresses a well-defined market failure, ii) it is well targeted and iii) it does not distort competition too much so that it can be on balance compatible with the common market. The market failures hampering R&D&I are clearly identified, as are possible distortions of competition and trade that may be triggered by State aid.

The following market failures were considered relevant, on the basis of the existing economic literature, consultations and dedicated studies on state aid and innovation:

- Positive externalities: R&D&I activities generate new knowledge, which is beneficial to society because it can be used by many companies to invent or improve products and services. However, from the perspective of a single company, only the private benefits from investing in R&D&I are accounted for. As a result, R&D&I activities are sometimes not undertaken by private companies, because they consider the

([8]) 'Putting knowledge into practice: A broad-based innovation strategy for the EU' COM(2006) 502 final.

([9]) Communication from the Commission to the Council and the European Parliament; Common Actions for Growth and Employment: The Community Lisbon Programme, COM(2005) 330 final.

([10]) Communication from the Commission to the European Council (Informal meeting in Lahti — Finland, 20 October 2006), COM(2006) 589 final.

([11]) 'Creating an Innovative Europe'; Report of the Independent Expert Group on R&D and Innovation appointed following the Hampton Court Summit and chaired by Mr. Esko Aho; http://ec.europa.eu/invest-in-research/pdf/download_en/aho_report.pdf resulting private benefits too limited, whereas the benefits for society, due to the knowledge spill-overs of R&D&I, could be important.

- Public goods: R&D&I activities generate new knowledge, which cannot always be protected (e.g. through patents). Private companies may thus refrain from investing in R&D&I because they are afraid that the results of their investments may be used by competitors and they consequently cannot generate any profit from their investments.
- Imperfect and asymmetric information: R&D&I activities are particularly risky and uncertain. This means that they are affected by imperfect and asymmetric information. As a result, too few human and financial resources may be invested in R&D&I projects, which would however be highly valuable for society.
- Coordination and network failures: R&D&I activities are often unsure and complex and it is not easy for private companies to work together, identify suitable partners and coordinate R&D&I projects. As a result of these coordination and network failures, R&D&I projects that could have been conducted in common between a group of firms are sometimes not undertaken at all, whereas society as a whole would have benefited.

As a result, permissible aid measures, eligible costs, aid intensities and other conditions are designed to address the identified market failures and ensure that such aid is compatible with the common market.

A flexible package offering more possibilities for Member States to support R&D&I

The new rules on Research, Development and Innovation contain a flexible package of measures which can be used by Member States to tailor their support to R&D&I according to their national preferences, needs and specificities. On the basis of economic analysis a series of measures are offered to Member States to grant aid, to help them direct more aid to R&D&I than currently the case and to better target their funds to measures that are on balance beneficial to the common interest.

The framework pays great attention to the needs of small and medium-sized enterprises, which are most affected by market failures. But it also offers many possibilities for large enterprises to receive support, when duly needed and justified. Consequently, the new framework in principle maintains high aid intensities for large enterprises, and even increases aid intensities for SMEs by comparison with the previous framework. A new category of experimental development is introduced, which substantially broadens the previous category of "precompetitive development" to include innovation activities. The bonus system is simplified, with increased incentives for collaboration. Due account is also taken of regional considerations when assessing the justification of State aid.

New measures on support for innovation are introduced. They include:

- aid for young innovative start-ups;
- aid to SMEs for innovation advisory and support services,
- aid for the loan of highly qualified personnel;
- aid for process and organisational innovation in services; and
- aid for innovation clusters.

Last but not least, the new framework provides more guidance as regards the question whether State aid is involved in an R&D&I-project. Under the old framework, need for clarification existed in particular for public-private partnerships, universities and innovation intermediaries. Special efforts are now made to be more transparent and secure legal certainty for research organisations, to ensure they can perform non-economic and economic activities, subject to meeting clear and simple rules. All this should enhance the role of public research entities, and facilitate public-private collaboration.

An improved architecture of the rules

The framework relies on an improved architecture to help the Commission focus its scrutiny on the potentially most distortive cases. Whereas measures including high aid amounts are subject to a detailed assessment (and -as previously- the incentive effect of aid to large enterprises must be demonstrated), lower aid amounts, and aid for SMEs, are subject to a lighter assessment and may in the future benefit from the forthcoming General Block Exemption.

Thresholds are established to fix a ceiling above which large R&D-projects must be notified individually to the Commission, even if they come under an aid programme already approved by the Commission. Aid above the ceiling has a greater risk of distorting competition and trade, and will therefore be subject to a detailed assessment. The new framework has introduced differentiated thresholds of €20 million for projects that are predominantly for fundamental research, €10 million for projects that are predominantly for industrial research and €7.5 million for projects that are predominantly for experimental development. The Commission considers that such differentiated ceilings best reflect the underlying risks of distortions of competition. These risks depend primarily on the amount of aid a Member State wants to grant, but also on the question how far the research project is away from the market, since aid to a close-to-the-market experimental development project has a much greater potential for distortion than aid for fundamental research.

The new framework presents a series of criteria and explanation about how the Commission will undertake its detailed assessment. The focus of the analysis is on the concrete effects that the aid may have on the beneficiary's behaviour, and on markets. Even though the central part of the analysis is on the ability of the aid to change the incentive of the company to conduct more R&D&I, the Commission will also assess more specifically whether the market actually fails to deliver on its own the expected outcome, whether the aid is properly designed and whether its impact on competition is not exaggerated. Risks are in particular that the aid leads competitors to the beneficiary to reduce their R&D&I efforts, or that the beneficiary increases of maintains market power.

Finally, to avoid circumvention of the State aid rules, ex-post monitoring is enhanced to allow effective Commission control. This means, in particular, that Member States will need to be transparent about the aid above € 3 million they grant under approved schemes to individual companies, even though this aid does not have to be notified to the Commission. Annual reports will also have to provide basic information to allow the Commission, if needs be, to verify the correct application of the framework.

Conclusion

The new Community framework for State aid to R&D&I is a document, which not only promotes a better use of State aid but also establishes with a comprehensive methodology to assess State aid measures. It represents an important contribution to the State Aid Action Plan and offers an opportunity for Member States to use State aid wisely, in order to support growth and jobs.

Commission adopts revised Leniency Notice to reward companies that report hard-core cartels (1)

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Directorate-General for Competition, units F-3 and F-4

On 6 December 2006 the Commission adopted a revised Notice on Immunity from Fines and Reduction of Fines in Cartel Cases (the "2006 Leniency Notice"). The 2006 Leniency Notice builds on the achievements of the 2002 Leniency Notice, which has undoubtedly made a key contribution to uncover and put an end to numerous hard-core cartels. Therefore the improvements in the Leniency Notice have focused on providing more guidance to applicants and increasing the transparency of the procedure. This further guidance is expected to result into leniency applications of better quality for the purpose of the investigation. The revised Leniency Notice entered into force on 8th December 2006, upon its publication in the Official Journal of the European Union (2). From that date it has been applicable to companies which file for leniency in a cartel case as long as no other company is already co-operating with the Commission under the 2002 Leniency Notice in the same cartel. The procedure to protect corporate statements applies, however, from the moment of publication of the Notice to all pending and new applications for leniency.

Background

The Commission has given a high priority for detection and deterrence of cartels for several years. Effective action against cartels requires a combination of appropriate sanctions and incentives for participants to report cartels, thereby contributing to deter the creation of cartels as well as to terminate and punish them. Rewarding participants uncovering secret hardcore cartels introduces a destabilising factor in the otherwise comfortable environment of a cartel and increases the chances of their detection. The Commission leniency policy applies only to secret hardcore cartels in the understanding that their secrecy (sometimes protected with sophisticated means and technology), and the fact that such arrangements are concluded between, competitors justifies this approach. Other infringements of the EC competition rules are easier to detect and prove with the other enforcement tools or with the help of complainants.

Therefore, since adoption of the first Leniency Notice in 1996 (3), leniency policy has been one of the central elements in the Commission action against cartels. The 1996 Leniency Notice was replaced on 19 February 2002 by a new Notice (4), of which the Commission has now launched a revised version.

The 2002 Leniency Notice has been a formidable and successful tool to destabilise and disrupt cartels and to encourage companies to report wrongdoings to competition authorities. However, it had become apparent that there is a need to increase its effectiveness. Until the end of 2005 the Commission had received 87 requests for immunity, but granted a conditional immunity only on 51 applications. These figures reflect the fact that numerous immunity applications have not provided the necessary insider information and evidence on the alleged cartel to meet the immunity threshold. In addition, there have been cases where immunity has been granted after an applicant has supplemented its application, but the process has taken a lot of time. The reason behind this is that the 2002 Leniency Notice does not provide specific guidance to the applicants as to what to submit in order to qualify for the immunity threshold. This has often resulted in a lot of time being spent on supplementing the applications.

Hence, following more than four years of practice in the implementation of the 2002 Notice, it was time to have the experience gained reflected in the Notice, in particular by clarifying the immunity threshold as well as the conditions for immunity, which now extend to the reduction of fines. Some clarification has also been added to the threshold for reduction of fines. Finally, the procedure now incorporates certain flexibility with the introduction of a discretionary marker system, whereby an applicant's place in the queue for leniency can be protected for a limited period of time. Moreover, the new Notice finally includes the procedure already in force to protect corporate statements

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors. The authors wish to thank Flavio Laina for his comments.

(2) OJ C 298, 8.12.2006, p. 17-22.

(3) OJ C 207, 18.7.1996, p. 4.

(4) OJ C 45, 19.2.2002, p. 3-5.

made by companies within the Leniency programme from the risk of discovery in civil damage proceedings, in particular in third country jurisdictions. Each of these areas is discussed further below.

The amendments to the Leniency Notice are also fully in line with the European Competition Network's Model Leniency Programme, which was adopted on 29 September by the heads of the EU competition authorities. The revision also takes account of public consultations held on revision of the Notice in February (on the oral statements procedure) and October 2006 (on a draft revised Notice).

The immunity threshold

Only the first undertaking making a decisive contribution to the Commission case will be eligible for immunity from fines, provided that one of the two thresholds set in the Notice are met. Several clarifications have been made to the immunity thresholds. At the same time there remains for companies at least the same incentives as before to come forward with their applications.

a) Immunity for enabling the Commission to carry out a targeted inspection

In particular, experience shows that there was a need for further guidance for potential applicants on the point 8(a) threshold of the Notice that applies in situations where the Commission does not yet have enough information to carry out an inspection. To avoid uncertainties as to what type of information and evidence is necessary to meet this threshold for immunity, the Notice provides a list which helps applicants to anticipate what is required (see point 9 of the Notice). This list includes both a corporate statement describing the functioning and participants to the cartel, and giving all relevant explanations on the pieces of evidence submitted, as well as documentary evidence available to the applicant at the time of its submission.

The Notice also specifies that the applicants should provide sufficient evidence to enable the Commission to carry out the inspection in a "targeted" manner. An immunity applicant by definition has been a party to an alleged cartel that is subject to the application. It should therefore be in a position to provide to the Commission such "insider" knowledge of the cartel that would allow it to better target its inspection with more precise information as to, for instance, what to look for in terms of evidence and where it might be found. The information and evidence listed in point 9 of the Notice will accordingly allow for the inspections to be better focused. Some respondents to the public consultation on the draft Notice queried what the word "targeted" meant and whether it had something to do with the expected result of the inspection. To make this point clear, the Notice specifies that the assessment of the "targeted inspection" threshold will have to be carried out *ex ante,* i.e. without taking into account whether a given inspection has been successful or even whether an inspection has been carried out. The assessment will be made exclusively on the basis of the type and quality of the information submitted by the applicant ([5]).

However, since immunity applicants are expected to enable the Commission to carry out surprise inspections, they are expected to be diligent in safeguarding the element of surprise, as far as they are concerned. Under the 2002 Leniency Notice, it was not clear how to balance this concern with the interest of an applicant to provide upfront as much information and evidence as is available to it in order to qualify for conditional immunity. The 2006 Leniency Notice spells it out that applicants are not required to produce in their initial application for immunity information and evidence, the collection of which would jeopardise a Commission inspection. If an applicant learns that its internal inquiries, carried out for the purposes of completing or supplementing an application, raise a real concern of alerting other cartel members prior to an inspection, it should communicate its concerns to the Commission. The Commission may agree that applicants provide such further information under the continuous cooperation obligation of point 12 of the Notice.

According to point 12 of the Notice, the applicant should provide the Commission promptly with all relevant information and evidence relating to the alleged cartel that comes into its possession or is available to it throughout the whole administrative proceedings. Therefore, if after its initial submission the applicant comes across — or can obtain — any piece of information or evidence related to the cartel (and not only the information and evidence listed in point 9), it should provide those to the Commission. This also means that if the applicant has not completed its internal inquiries due to risk of leaks prior to a conditional immunity decision and/or a Commission inspection, the applicant should complete such inquiries directly thereafter, unless the Commission otherwise requires.

([5]) See also paragraph 19 of the Explanatory Notes to the ECN Model Leniency Programme, which contains the same concept.

It should also be added that the Commission services have a practice of discussing with an applicant the collection and submission of information and evidence. In such discussions the applicants have been able to raise any queries they have for instance on the immunity thresholds or measures they intend to take to collect evidence. Any supplementary submissions by an applicant can be taken into account as part of its application, until such time as the Commission receives another application for immunity in the same case or, if the applicant has been granted a marker (a new concept in the revised Notice, see point on Marker system below for details), until the marker period expires.

The Leniency Notice now also states explicitly that the applicants need to disclose their participation in the cartel. This has not been in all cases clear for the applicants and in some cases the applicants have not described clearly enough their own participation in the alleged cartel.

b) *Immunity for enabling the Commission to establish an infringement of Article 81 EC*

If the Commission has carried out an inspection concerning an alleged cartel or has already sufficient evidence in its possession to carry out an inspection, immunity under point 8(a) of the Notice is no longer available. However, in such a situation an applicant can still qualify for immunity under point 8(b) of the Notice, provided that no other applicant has already been granted immunity (under either point 8(a) or 8(b)). To meet the point 8(b) threshold for immunity an applicant needs to submit information and evidence which will enable the Commission *"to find an infringement of Article 81 of the EC Treaty"* in connection with the alleged cartel. This threshold, which has remained unchanged in the revision of the Notice, corresponds to the one required under Article 7 of Regulation 1/2003 for the Commission to be able to adopt an infringement decision, which is also the ultimate goal of the Leniency Notice. It appears both from the public consultation on the revised Notice and from individual cases that the companies and their legal advisors have not always understood the difference with the 8(a) threshold. It is only natural that this 8(b) threshold for immunity is higher than in a situation where the Commission does not yet have any knowledge of the alleged cartel. If the Commission has already information on the cartel and has used or is about to use its strongest investigatory measure — the surprise inspections — any immunity applicant coming forward in such a scenario should provide convincing evidence on the alleged cartel. Information and evidence to trigger an inspection would simply not be enough as the surprise element of the inspection works only once in each individual case.

In particular, it appears that it has not been clear for the applicants what kind of evidence they need to provide in a post inspection scenario. The Notice now clarifies that applicants should provide both "contemporaneous, incriminating evidence" and a corporate statement describing the functioning and participants to the cartel as well as giving all relevant explanations on the pieces of evidence provided. In order to find an infringement against the suspected cartel participants, and not only the applicant that self-reports on the cartel, the applicant needs to submit incriminating evidence that originates from the time of the infringement. Experience also shows that corporate statements are needed in addition to the evidence to explain the pieces of evidence and to give insight to the alleged cartel that only an ex-cartel member can provide. For example, in the *Raw Tobacco Italy* case (6), the Commission granted conditional immunity under point 8(b), to reward the applicant for providing the Commission with decisive incriminating evidence for the establishment of objections which the Commission included in the Statement of Objections and in the final Decision.

The possibility for an immunity applicant to get a delay to complete its application: a marker system

An important novelty in the 2006 Notice is the introduction of a discretionary marker system. The revised Commission Leniency Notice stipulates that, where justified, an immunity application can be accepted on the basis of only limited information, as specified in the Notice. The applicant is then granted time to perfect the information and evidence to qualify for immunity.

The Leniency Notice makes a marker available for immunity applicants at the discretion of the Commission. There have been calls from the legal community for having an automatic marker system and extending it also to the reduction of fines applicants. The reason why the Commission opted

(6) Commission decision of 20 October 2005 in case COMP/38.281 — Raw Tobacco Italy. See the Commission press release IP/05/1315. Non-confidential version published at the Commission competition web-site: http://ec.europa.eu/comm/competition/cartels/cases/cases.html.

for a discretionary market system is that, above all, it is in the public interest to maintain the race between companies to provide the information and evidence required to meet the conditions for immunity and thereby to facilitate the detection and termination of infringements. The interest is not in the race to simply get a place in the queue. One should keep in mind that the overall purpose of the Leniency Notice is to enhance actual cartel reporting and destabilising.

As to the call to have a marker system also for reduction of fines applicants, it is difficult to see how such a system would bring such advantages that would outweigh the apparent disadvantages. First, practical experience shows that following or even during the Commission inspections, there may be several reductions of fines applications in a short interval. Thus it seems that when the companies compete on the reduction of fines, this creates incentives for the companies both to come forward quickly and to provide the best possible evidence. Second, the critical factor for the detection of cartels under the Leniency Notice is the submission of an immunity application. Therefore, it may be justified to grant an immunity applicant, which reports on a previously unknown cartel, a delay to complete its application. However, this does not apply when the Commission has already engaged in an investigation of the cartel. Third, since applications for reductions of fines are assessed on the basis of their relative significant added value at the point of time when such an application is made, it would also not be feasible for the Commission to effectively process and assess several simultaneous markers.

While the practical modalities of the marker system will develop when experience is gained on marker applications, it is strongly encouraged for the potential applicants to contact the Commission beforehand to discuss steps to be taken in a potential application and requirements in each step.

It should first be made clear that in practice a marker would be granted for an immunity applicant when it appears that that applicant would be in a position to perfect it so that inspections under Article 20 of Council Regulation No 1/2003 (and Article 21 as the case may be) can be carried out within a short time period. This is essential in order to ensure that evidence remains intact at any premises to be inspected. The applicant should thus be prepared to explain what kind of internal investigatory measures it would intend to take during the marker period and to provide detailed information and reasoning for time needed for each such measure. This is necessary to make an informed decision on the time granted to perfect a marker. In this decision and in the decision on the conditional immunity, it should also be taken into account if some information is more difficult to access or is simply not at all accessible to the applicant. Due to the need to carry out inspections in a timely manner, the marker period is also necessarily limited.

As mentioned above, surprise inspections are the Commission's strongest investigatory instrument within the EU competition law enforcement system. Therefore, the Commission leniency programme is naturally built to work in a harmonious way with this investigative tool. The link between immunity applications and inspections thus sets natural limits to the marker system too. A question has also been raised whether the Commission services could tell a potential applicant if a marker is available. In practice it would not, however, be possible to give out such information as that would de facto give a warning for the undertaking on an imminent inspection. Like in the case of any formal immunity applications, an applicant can be informed on availability of immunity and/or marker only if it is prepared immediately to lodge an application. This is necessary to protect any upcoming inspections following an immunity application.

Moreover, when making the application, a marker applicant could be asked to submit immediately the information and evidence it has on the alleged cartel. It may also be asked to provide supplementary information and evidence as soon as it becomes available instead of waiting until the end of the marker period.

A question has also been raised as to what happens if a company does not perfect a marker within the time-limit set and an extension is not granted. In such a situation that company can still present a formal application for immunity at any time, but its place in the queue is no longer protected. If it happens to meet the threshold before anybody else, it gets immunity and for that purpose, all the information provided by that company is taken into account (under the marker and under the full application). It should be recalled that the lowest threshold is having been the first to enable the Commission to make a targeted inspection. The date at which the company qualifies for immunity is the date when it meets the threshold; while, if it had perfected the marker within the delay granted for that purpose, the date of the marker would have been deemed as the date of qualifying for immunity.

Some respondents to the public consultation on the draft revised Leniency Notice compared the information required in the envisaged Commission system with the information required for instance by the American competition authorities and argued that it should be sufficient for a marker to tell the Commission only what sector the alleged cartel concerns. It should first be stressed, however, that in the Commission system the applicant is only asked to provide a very limited amount of information: the applicant's name and address, the parties to the alleged cartel, the affected products and territories, the estimated duration of the cartel and the nature of the cartel conduct. This information is necessary to ensure both that this is a serious application and that there are no prior applications relating to the same alleged infringement. Second, this information would also allow the Commission to see whether the case concerns one or more Member States. Taking into account the parallel application of Article 81 by the Commission and the Member States' competition authorities, it is only natural that the Commission should be able to assess at the very beginning of a case whether a national competition authority in the EU would be well placed to deal with the case instead of the Commission. This would allow the applicant to submit its application to the relevant authority ([7]). This is also in line with the ECN Model Leniency Programme which aims at reducing the burden on applicants created by multiple leniency systems in the EU.

The Applicants are expected to genuinely cooperate in the application process and they should also have faith on the Commission services. Some legal advisers seem to be concerned that on the basis of the information submitted in a marker application, the Commission would launch own initiative investigations in case an applicant failed to perfect the marker. The applicants can be sure that any information asked by the Commission services in the application process is necessary for the purposes of processing their application. The idea is not that the Commission would launch own initiative inspections on the basis of the information received from an applicant either in the marker application or in a formal application. The purpose of the system is to encourage the applicants to provide the information and evidence required to meet the immunity threshold.

The threshold for reduction of fines

When immunity is not (or no longer) available in a given case, decisive contributions to the investigation may still be rewarded with a reduction of the fine, provided that they meet the relevant threshold. The threshold for reduction of fines has remained the same in revision of the Notice: in order to qualify, an applicant for a reduction of fines needs to provide evidence of the cartel which represents significant added value as compared to the evidence already in the Commission's file at the time of the submission.

The choice of the concept of "significant added value" as a threshold for reduction of fines encourages the race between the undertakings interested in leniency, since the chances for the next applicant to add significant value to the investigation considerably diminishes with every new submission. Moreover, the 2006 Leniency Notice retains the same bands to reward successful applicants for reductions of fines, depending on the order in which they approached the Commission. The specification that, within each band, the level of reduction will depend on the time of the submission and the extent of the added value provided also remains the same.

The Notice contains some guidance on the Commission's criteria in order to assess how helpful has been to its investigation the evidence provided by each individual applicant, that is, whether it added to its ability to prove the cartel ([8]) and whether it did so in a significant way. In this regard, the Commission will consider the level of relevant detail and accuracy provided in the submission ([9]). In addition, the Commission will logically focus on the nature of the evidence submitted. In view of the fact that the Commission bears the burden of proving the infringement with evidence meeting a certain standard, the Leniency Notice rewards undertakings which make a decisive contribution to this task of public interest. The 2006 Notice is more explicit than the 2002 Notice. It does not only specify that evidence contemporaneous to the facts or directly relevant ([10]) to them is more valuable than, respectively, evidence subsequently established or indirect evidence; it also stresses the value of "incriminating evidence" and "compelling evidence". This addition does not

([7]) See for reference paragraph 38 of the Commission Notice on cooperation within the Network of Competition Authorities, OJ C 101, 27.4.2004, p. 43.

([8]) According to point 25: "*The concept of 'added value' refers to the extent to which the evidence provided strengthens, by is very nature and/or its level of detail, the Commission's ability to prove the alleged cartel (…)*".

([9]) On the probative value of precise, consistent evidence, see for instance the judgment of the Court of Justice of 25 January 2007 in Joined Cases C-403/04 P and C-405/04 P, *Sumimoto Metal Industries Ltd., Nippon Steel Corp. v Commission,* (at paras. 42-46, 56 and 60), upholding the judgment of the Court of First Instance of 8 July 2004 in Joined Cases T-67/00, T-68/00, T-71/00 and T-78/00, *JFE Engineering Corp. v Commission*.

([10]) See for instance the judgement of the Court of Justice of 7 January 2004 in Cases C-204/00 P, C-205/00 P, C-211/00 P, C-217/00 P and C-219/00, *Aalborg Portland A/S a.o. v. Commission,* at paras. 236 to 244.

change or raise the existing threshold. It simply adds further guidance to clarify some of the factors relevant to the Commission assessment ([11]). In the light of the applicable case-law, conclusive, stand-alone evidence that requires little or no corroboration to prove the case provides higher contribution to discharge the Commission's burden of proof than evidence, which largely requires corroboration if it is contested. Such conclusive, stand-alone evidence of which the probative value cannot be challenged by simple contestation, is called "compelling evidence" in the Notice. Certainly, even uncorroborated corporate statements may constitute evidence against other parties ([12]), provided that they are not generally contested by then or contradicted by similar statements or other pieces of evidence, and they may withstand contestation in the context of a wider, consistent body of evidence, but they objectively offer a lower intrinsic probative value than, for instance, a piece of incriminating contemporaneous documentary evidence ([13]). This does not mean that corporate statements can never provide significant added value, but it signals that they are more likely to provide it when they corroborate other corporate or witness statements ([14]) or other pieces of evidence.

For the sake of legal certainty, the 2006 Leniency Notice maintains the so-called "partial immunity" provision. When an undertaking provides "significant added value" because it happens to provide compelling evidence enabling the Commission to establish new or additional facts liable to extend the gravity or the duration of the infringement, these facts will not be taken into account when setting the fine for the undertaking providing the evidence. This "partial immunity" constitutes a supplementary benefit to be added to the corresponding reduction of fines. This provision should not only reassure applicants that their liability will not suffer from their own decisive submission, but it should also encourage them to provide all conclusive evidence as early as possible in the procedure in order to benefit from any extra reduction before others do. Possibility for getting such a "partial immunity" was already included in the 2002 Leniency Notice and the Commission has already implemented this provision in the cases concerning *bleaching chemicals* ([15]) and *acrylic glass* ([16]).

Conditions for immunity and reduction of fines

When considering applying for leniency, a company should not only look at the relevant threshold, but also pay particular attention to the conditions in point 12 and 13 of the Notice, as appropriate. This is due to the fact that some of those conditions apply from the very moment of the application and others even during its preparation. Pursuant to point 12 (and point 24) of the Notice, leniency applicants must meet the following conditions in order to qualify for immunity or for reduction of fines:

(a) The undertaking cooperates genuinely, fully, on a continuous basis and expeditiously from the time it submits its application throughout the Commission's administrative procedure. This includes:

- providing the Commission promptly with all relevant information and evidence relating to the alleged cartel that comes into its possession or is available to it;
- remaining at the Commission's disposal to answer promptly to any request that may contribute to the establishment of the facts;
- making current (and, if possible, former) employees and directors available for interviews with the Commission;

([11]) In any event, point 25 of the Notice is meant to provide guidance to the applicants, but it is not meant to provide an exhaustive list of criteria.

([12]) See, for instance, the judgment of the Court of First Instance of 25 October 2005 in Case T-38/02, *Groupe Danone v. Commission,* at paras. 285 to 293.

([13]) See, for instance, the judgment of the Court of First Instance of 15 March 2000 in Joined Cases T-25/95, T-26/95, T-30/95, T-31/95, T-32/95, T-34/95, T-35/95, T-36/95, T-37/95, T-38/95, T-39/95, T-42/95, T-43/95, T-44/95, T-45/95, T-46/95, T-48/95, T-50/95, T-51/95, T-52/95, T-53/95, T-54/95, T-55/95, T-56/95, T-57/95, T-58/95, T-59/95, T-60/95, T-61/95, T-62/95, T-63/95, T-64/95, T-65/95, T-68/95, T-69/95, T-70/95, T-71/95, T-87/95, T-88/95, T-103/95 and T-104/95, *Cimenteries CBR SA Groupe Danone a.o. v Commission,* at par. 1838.

([14]) As regards corroboration and contestation of corporate and witness statements, see for instance the above mentioned judgment of the Court of Justice of 25 January 2007 in Joined Cases C-403/04 P and C-405/04 P, *Sumimoto Metal Industries Ltd., Nippon Steel Corp. v Commission,* (at paras 60 to76 and 101 to 109), upholding the judgment of the Court of First Instance of 8 July 2004 in Joined Cases T-67/00, T-68/00, T-71/00 and T-78/00, *JFE Engineering Corp. v Commission.* See also the judgement of the Court of First Instance of 5 December 2006 in Case T-303/02, *Westfalen Gassen Nederland BV v Commission,* at paras. 79-104.

([15]) Commission Decision of 3 May 2006 in Case COMP/F/38.620 — Hydrogen Peroxide and Perborate. See Commission press release IP/06/560. No public version yet available.

([16]) Commission Decision of 31 May 2006 in Case COMP/F/38.645 — Methacrylates. See the summary of the decision in OJ L 322, 22.11.2006, p. 20–23 and Commission press release IP/06/698.

- not destroying, falsifying or concealing relevant information or evidence relating to the alleged cartel; and
- not disclosing the fact or any of the content of its application before the Commission has issued a statement of objections in the case, unless otherwise agreed;

(b) The undertaking ended its involvement in the alleged cartel immediately following its application, except for what would, in the Commission's view, be reasonably necessary to preserve the integrity of the inspections;

(c) When contemplating making its application to the Commission, the undertaking must not have destroyed, falsified or concealed evidence of the alleged cartel nor disclosed the fact or any of the content of its contemplated application, except to other competition authorities.

Moreover, pursuant to point 13 of the Notice, an undertaking which took steps to coerce other undertakings to join the cartel or to remain in it is not eligible for immunity from fines. It may still qualify for a reduction of fines if it fulfils the relevant requirements and meets all the conditions as set out above.

Cooperation is an essential feature of the leniency programme that rewards those who assist the Commission in its investigation. The case-law recalls that an undertaking may receive favourable treatment under the Leniency Notice *"if it reveals a spirit of cooperation and if that cooperation allowed the Commission to establish an infringement with less difficulty and, where appropriate, to put an end to it"* and requires all leniency applicants to show *"genuine cooperation"* ([17]), that is, to cooperate sincerely with the Commission, in good faith, by providing accurate and complete information that is not misleading. In line with that case-law, the 2006 Leniency Notice specifies that every applicant are expected to *"cooperate genuinely, fully, on a continuous basis and expeditiously from the time it submits its application"* and no longer distinguishes between applicants for immunity and those for reduction of fines with respect to the continuous cooperation obligation.

It is also important to avoid any uncertainty concerning the scope of the conditions that the applicants must meet under the duty of continuous cooperation. In practice the Commission Directorate General for Competition has specified in its acknowledgement of receipt of an application various facets of the cooperation obligation. In particular, the acknowledgement of receipt has spelled out that the duty of continuous cooperation encompasses not destroying, falsifying or concealing information that is of relevance for the investigation as well as not revealing the facts or the contents of the application during a period when doing so can jeopardise the investigation. By way of exception from the rule that cooperation obligation starts at the time of the application, it is necessary that this condition covers also the period when a company prepares to come forward with a leniency application. It cannot be tolerated that an applicant destroys, falsifies or conceals information and can still be entitled to get immunity or reduction of fines. Such actions can seriously undermine the investigation of the case and are flagrantly against the spirit of cooperation under the Leniency Notice. Therefore the Leniency Notice makes it clear that this obligation applies from the moment when the applicant is *"contemplating making its application"*, i.e. when the applicant is deciding on and preparing its application. This reference to the timing, as well as the reference to *"the undertaking"* and not to any employee, also makes it clear that the Commission wants to catch deliberate actions of destruction, falsification and concealment of evidence.

Respondents to public consultation on the draft revised Leniency Notice had concerns that the obligation not to disclose the fact or content of the application could go counter to other legal obligations of the applicant which may oblige it to make such a disclosure. This was already taken into account when the revision was prepared. It is indeed true that leniency applicants may have legal obligations to acknowledge in public their cooperation under the Leniency Notice (e.g. listed companies). This is why the revised Leniency Notice provides that the restriction on disclosure to third parties applies *"unless otherwise agreed"* with the Commission. This point of the Notice also covers the practice of the Commission to discuss with the applicants the question of how to address discovery requests in third country jurisdictions, while protecting the EU leniency programme. Naturally, the applicants are free to approach other competition authorities, in which case the Commission may ask for a waiver to discuss the application and exchange information with such authorities.

The requirement in the 2002 Leniency Notice to terminate participation in the alleged cartel at the latest at the time of the application had in practice

([17]) See for instance the judgement of the Court of Justice of 29 June 2006 in Case C-301/04 P, *Commission v. SGL Carbon AG, a.o.*, at paras. 66 to 80; and the judgement of the Court of Justice of 28 June 2005 in Cases C-189/02 P, C-202/02 P, C-205/02 P, C-208/02 P and C-213/02 P, *Dansk Rørindustri A/S a.o. v Commission*, at paras 395 and 399.

raised concerns that in some cases the termination may alert other cartel participants and endanger the effectiveness of a planned Commission inspection. While as a general rule undertakings that apply for leniency should terminate all cartel activities as soon as possible, it is in the public interest that such termination should not always entail an abrupt interruption of their involvement in those activities where their participation is expected by other cartel members, such as planned meetings or exchanges. The complete termination of all involvement might have to be delayed until the point in time necessary to safeguard the Commission inspection. This is now clearly spelled out in point 12(b) of the Leniency Notice. When, in the Commission's view, that limited involvement is indispensable to preserve the Commission's inspections, it does not qualify as a continuation of the undertakings' infringement, unless the participation still continues thereafter.

Some respondents to the public consultation were afraid that an applicant might not be able to meet the requirement of continuous cooperation if its personnel refused to answer questions from Commission's investigators by fear of criminal sanctions by EU Member States. It should be taken into account, however, that it is already the established practice of the Commission under the 2002 Leniency Notice to interview directors and employees of the applicants. Natural persons interviewed can be subject to different types of sanctions in different EU Member States. There are therefore safeguards in place regarding transfer of information to Member States that apply criminal sanctions. Regulation 1/2003 EC ensures that information exchanged in the network of EU Member States' competition authorities can only be used by the receiving authority if it has been collected in a way which respects the same level of protection of the rights of defence of natural persons as in the receiving authority. Moreover, exchanged information can only be used by the receiving authority to impose custodial sanctions if the law of the transmitting authority foresees such sanctions for antitrust infringements, which is not the case for the Commission. Moreover, making directors and employees available for interviews does not imply that they have to provide self-incriminating information.

Finally, a question was raised in the public consultation as to what happens if an immunity or reduction of fines applicant does not meet some of the conditions. Can they still get some reduction of fines? The Leniency Notice makes it clear that failure to comply with the conditions will disqualify the applicant from the leniency programme. This question has already been addressed in the Commission decision in the Raw Tobacco Italy case (see above), which demonstrates that, in exceptional circumstances, particularly when the company has contributed substantially to the Commission's investigation, the Commission may take the cooperation into account by granting a reduction of fines under the Fines Guidelines ([18]) as cooperation outside leniency.

The specific procedure to protect corporate statements

In February 2006, the Commission published for comments a proposed procedure to protect corporate statements, which are made pursuant to the Commission Leniency Notice, from discovery in civil damage proceedings, in particular in third country jurisdictions. In such corporate statements which are made especially to help the Commission's investigation, leniency applicants describe in detail their own involvement as well as that of other undertakings. While the Commission strongly supports effective civil proceedings for damages against cartel participants, the production in such proceedings of corporate statements made under the Leniency Notice would create a considerable disincentive for companies to come forward and hence would seriously undermine the effectiveness of the Commission leniency policy and ultimately jeopardise the effectiveness of the Commission's fight against cartels. In general the respondents to the February 2006 publication strongly supported the proposed procedure to protect corporate statements from discovery. Essential elements of this procedure are now included in the Leniency Notice, taking into account the comments received in the public consultation.

The procedure to protect corporate statements applies to voluntary corporate statements supplied in the framework of the Leniency Notice, with a view to applying for immunity or for a reduction of fines. Those corporate statements (and the protection provided to them) will be covered by the relevant provisions in the Notice irrespective of whether the applicant finally obtains immunity from or reduction of fines. However, to avoid any misuses of this new system, if the applicant itself discloses the content of its statement to third parties in other jurisdictions, while at the same time asking the Commission to protect its statement, no protection of the statement would be justified.

The process works in such a way that oral corporate statements will be recorded and verbatim

([18]) See the recently revised fines guidelines: Official Journal C 210, 1.09.2006, p. 2-5. See also IP/06/857 and MEMO/06/256 written transcripts will be made of each statement. The recording and transcribing of the statements will take place at the Commission's premises. Applicants making oral statements will not retain or receive from the Commission any copies of these statements, but as soon as the oral statement has been submitted, it will become a Commission document. This ensures that the applicant keeps no document on its statement that it would be required to produce at a third country court.

Oral corporate statements are considered as evidence on alleged cartels and both the tape and the transcript form part of the Commission file. In order to guarantee the value as evidence provided by a transcript, the applicant making the statement will need to check, at the Commission premises, the accuracy of the written transcript as compared to the recording.

Concluding remarks

The Leniency Notice has to be seen in the overall context of the enforcement tools that the Commission is using in its action against cartels, in particular the investigation powers, and the rigour used in application of the sanctions policy. These instruments together should provide appropriate incentives for companies to race to apply for leniency. In 2006 the Commission has updated two key instruments used in this area: the Leniency Notice and the Guidelines on fines ([19]). The revised Leniency Notice entered into force on 8 December 2006 and it is already being applied in first cases.

([19]) Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003; OJ C 210, 1.9.2006, p. 2-5.

Commission launches public consultation on draft Non-Horizontal Merger Guidelines (1)

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I. Introduction

On 13 February, the Commission launched a public consultation on draft Guidelines on the assessment of non-horizontal mergers under the Merger Regulation. Non-horizontal mergers include vertical mergers, such as the acquisition of a supplier by a customer (for example, a car manufacturer acquiring a gearbox supplier), and conglomerate mergers, which concern companies whose activities are complementary or otherwise related (for instance, a company producing razors buying a company producing shaving foam).

Interested parties are invited to submit their comments on the draft Guidelines by 12 May. It is anticipated that, following the consultations, the definitive version of the Guidelines will be adopted by the Commission before the end of the year. The non-horizontal Merger Guidelines will then serve to provide guidance to companies envisaging such types of merger. They will complement the existing Guidelines on the assessment of horizontal mergers, which deal with mergers of companies who are actual or potential competitors on the same relevant market(s) (2).

In the following sections, we provide an overview of the draft Guidelines and the public consultation process.

II. Overview of the draft Non-Horizontal Merger Guidelines

Article 2 of the EC Merger Regulation (3) provides that the European Commission has to appraise mergers with a view to establishing whether or not they "would significantly impede effective competition, in particular as a result of the creation or strengthening of a dominant position", in the EU market or a substantial part of it.

With the draft Guidelines on Non-Horizontal Mergers, the Commission intends to set out the analytical approach it takes in assessing the likely competitive impact of vertical and conglomerate mergers.

The draft Guidelines are structured in four main parts: (i) a general overview, (ii) the definition of "safe harbours" in terms of market shares and concentration levels, (iii) the assessment of vertical mergers, (iv) the assessment of conglomerate mergers.

(i) General overview of the Commission's analysis of non-horizontal mergers

One important message included in the introductory sections of the draft Guidelines is that non-horizontal mergers are generally less likely to create competition concerns than horizontal mergers.

First, unlike horizontal mergers, vertical or conglomerate mergers do not entail the loss of direct competition between the merging firms in the same relevant market. As a result, the main source of anti-competitive effect in horizontal mergers is absent from vertical and conglomerate mergers.

Second, vertical and conglomerate mergers provide substantial scope for efficiencies. A characteristic of vertical mergers and certain conglomerate mergers is that the activities and/or the products of the companies involved are complementary to each other (4). The integration of complementary activities or products within a single firm may produce significant efficiencies and be pro-competitive. For instance, in vertical merg-

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors

(2) Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, Official Journal C 31, 05.02.2004, p. 5-18.

(3) Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings, Official Journal L 24, 29.01.2004, p. 1.

(4) Products or services are called "complementary" (or "economic complements") when they are worth more to a customer when used or consumed together than when used or consumed separately. Also a merger between upstream and downstream activities can be seen as a combination of complements which go into the final product. For instance, both production and distribution fulfil an indispensable role in getting a product to the market.

ers, efforts to increase sales at one level (e.g. by lowering price, or by stepping up innovation) will benefit sales at the other level. Depending on the market conditions, integration may increase the incentive to carry out such efforts. In particular, after the vertical integration, lowering the mark-up upstream may lead to increased sales not only upstream but also downstream and vice versa. This is often referred to as the "internalisation of double mark-ups".

The draft Guidelines also acknowledge that vertical and conglomerate mergers may reduce transaction costs and allow for a better co-ordination in terms of product design, the organisation of the production process, investments in production factors along the value chain and the way in which the products are sold. Similarly, mergers which involve products belonging to a range of products that are generally sold to the same set of customers (be they complementary products or not) may give rise to customer benefits such as one-stop-shopping.

Nonetheless, there are circumstances in which non-horizontal mergers may significantly impede effective competition. This is essentially because a non-horizontal merger may change the ability and incentive to compete on the part of the merging companies and their competitors in ways that cause harm to consumers (including intermediate customers).

The draft Guidelines make clear in this respect that when intermediate customers are actual or potential competitors of the parties to the merger, the Commission will focus on the effects of the merger on the customers to which the merged entity and those competitors are selling. Consequently, the fact that a merger affects competitors is not in and of itself viewed as a problem. It is the impact on effective competition on which the Commission will focus, not the mere impact on competitors at some level of the supply chain.

As to the possible anticompetitive effects of non-horizontal mergers, the draft Guidelines distinguish between two main ways in which non-horizontal mergers may significantly impede effective competition: non-coordinated effects and coordinated effects.

Non-coordinated effects may principally arise when non-horizontal mergers give rise to foreclosure. In the draft Guidelines, the term "foreclosure" is used to describe any instance where actual or potential rivals' access to supplies or markets is hampered or eliminated as a result of the merger, thereby reducing these companies' ability and/or incentive to compete. As a result of such foreclosure, the merging companies — and, possibly, some of its competitors as well — may be able to profitably increase the price charged to consumers or cause harm to consumers in other ways. These instances are referred to as "anticompetitive foreclosure".

In assessing the likelihood of an anticompetitive foreclosure scenario, the Commission will examine, first, whether the merged entity would have, post-merger, the ability to substantially foreclose a market, second, whether it would have the incentive to do so, and third, whether a foreclosure strategy would have a significant detrimental effect on competition, thus causing harm to consumers.

In practice, these three factors are often examined together since they are closely intertwined. Nonetheless, the Commission finds it useful to make clear that even though the merged entity may have the ability to foreclose, it may not have the incentive to do so. Second, even where the merged entity may have the ability and incentive to foreclose, this may not have a significant detrimental effect on consumers. The latter may hold true, in particular, when the merger gives rise to substantial efficiencies.

Coordinated effects arise where the merger changes the nature of competition in such a way that firms that previously were not coordinating their behaviour, are now significantly more likely to coordinate and raise prices or otherwise harm effective competition. A merger may also make coordination easier, more stable or more effective for firms, which were coordinating prior to the merger.

In assessing the effects of a merger, the Commission will consider both the possible anti-competitive effects arising from the merger and the pro-competitive effects stemming from efficiencies identified and substantiated by the parties.

(ii) Definition of "safe harbours"

One important objective of the draft Guidelines is to provide firms with guidance not only about possible theories of harm but also to enable them to identify mergers that are unlikely to be challenged on competition grounds. The draft states in this context that non-horizontal mergers pose no threat to effective competition unless the merged entity has market power in at least one of the markets concerned.

For this purpose, the draft specifies "safe harbours" as a screen to identify cases that are clearly unlikely to raise competition issues. The draft stipulates that the Commission is unlikely to find concern in non-horizontal mergers where the market share post-merger of the new entity in each of the markets concerned is below [30%] ([5]) and where the post-merger Herfindahl-Hirschman-Index (HHI) is below [2000]. In practice, it will not extensively investigate such mergers, except where some special circumstances are present, which render market shares less useful as a proxy for the competitive conditions in the market.

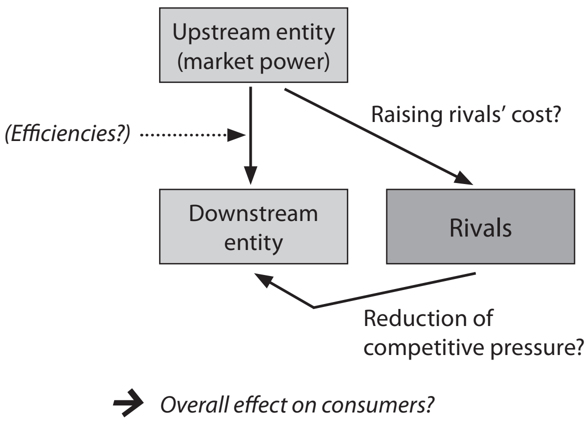
(iii) Assessment of vertical mergers

Non-coordinated effects: foreclosure

With regard to vertical mergers, the draft Guidelines identify two principal foreclosure scenarios, input foreclosure and customer foreclosure. The first is where the merger is likely to raise the costs of downstream rivals by restricting their access to an important input (input foreclosure). The second is where the merger is likely to foreclose upstream rivals by restricting their access to a sufficient customer base (customer foreclosure).

Input foreclosure

A merger may significantly impede effective competition through input foreclosure where, post-merger, the new entity would be likely to restrict access to the products or services that it would have otherwise supplied absent the merger, thereby raising its downstream rivals' costs by making it harder for them to obtain supplies of the input under similar prices and conditions as absent the merger. This may give the merged entity the ability and the incentive to profitably increase the price charged to consumers. Any efficiencies resulting from the merger, however, may lead the merged entity to reduce price, so that the overall likely impact on consumers may be neutral or positive. The figure below gives a graphical presentation of this mechanism:



([5]) In analogy to the indications given in Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, Official Journal L 336, 29.12.1999, pages 21-25.

The draft Guidelines outline a variety of factors that may in practice affect a merged firm's ability and incentive to foreclose, and the size of any impact on consumers. For example, a foreclosure strategy can be effective only if the merged firm has market power in the input market and the input represents a significant cost factor or an otherwise critical component for rival firms. Incentives to foreclose are affected, among other factors, by the trade-off the merged firm has to make between the profit lost in the upstream market due to a reduction of input sales to (actual or potential) rivals and the profit gain from expanding sales downstream or, as the case may be, being able to raise price in that market ([6]).

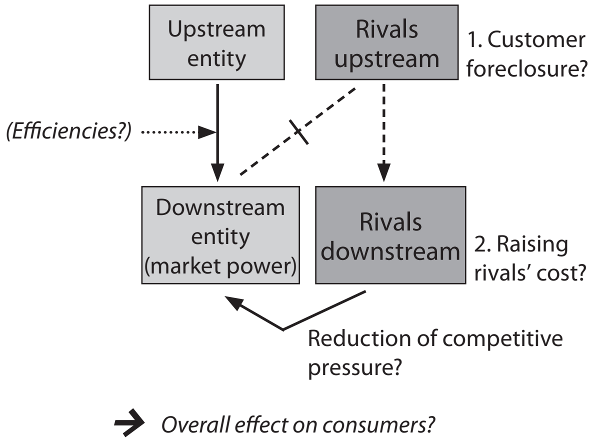
Further, the effect of the merger on competition needs to be assessed in light of efficiencies identified and substantiated by the merging parties. For the Commission to take account of efficiency claims in its assessment of the merger, the efficiencies have to benefit consumers, be merger-specific and be verifiable.

Customer foreclosure

Customer foreclosure may occur when a supplier integrates with an important customer in the downstream market. Because of this downstream presence, the merged entity may foreclose access to a sufficient customer base to its actual or potential rivals in the upstream market (the input market) and reduce their ability or incentive to compete. In turn, this may raise downstream rivals' costs by making it harder for them to obtain supplies of the input under similar prices and conditions as absent the merger. This may allow the merged entity profitably to establish higher prices on the downstream market. Again, any efficiencies resulting from the merger may lead the merged

([6]) When the adoption of a specific course of conduct by the merged entity is an essential step in foreclosure, the Commission examines both the incentives to adopt such conduct and the factors liable to reduce, or even eliminate, those incentives, including the possibility that the conduct is unlawful. This appraisal, however, does not require an exhaustive and detailed examination of the rules of the various legal orders which might be applicable and of the enforcement policy practised within them (see Case C-12/03 P, Commission v. Tetra Laval BV, ECR I-000, paragraphs 74-76. Case T-210/01, General Electric v. Commission [2005], ECR II-000, at paragraph 73). Moreover, the illegality of a conduct may be likely to provide significant disincentives for the merged entity to engage in such conduct only in certain circumstances. In particular, the Commission will consider, on the basis of a summary analysis: (i) the likelihood that this conduct would be clearly, or highly probably, unlawful under Community law, (ii) the likelihood that this illegal conduct could be detected, and (iii) the penalties which could be imposed.

entity to reduce price, so that there is overall not a negative impact on consumers. Like for input foreclosure, the Commission's assessment will include an analysis of the merged firm's ability and incentive to engage in a foreclosure strategy, as well as an evaluation of the potential size of the detrimental impact on consumers. A graphical representation of this mechanism is provided by the figure below:



Coordinated effects

The draft Guidelines provide an overview of factors that foster firms' ability to effectively co-ordinate their competitive behaviour. The section is based on the requirements set out by the CFI in its Airtours judgement [7]. Three conditions are, thus, necessary for coordination to be sustainable. First, the coordinating firms must be able to monitor to a sufficient degree whether the terms of coordination are being adhered to. Second, discipline requires that there is some form of credible deterrent mechanism that can be activated if deviation is detected. Third, the reactions of outsiders, such as current and future competitors not participating in the coordination, as well as customers, should not be able to jeopardise the results expected from the coordination.

(iv) Assessment of conglomerate mergers

The final sections of the draft Guidelines are dedicated to conglomerate mergers. These are mergers between firms that are in a relationship which is neither purely horizontal (as competitors in the same relevant market) nor vertical (as supplier and customer). In practice, the focus is on mergers between companies that are active in closely related markets (e.g. mergers involving suppliers of complementary products or of products which belong to a range of products that is generally purchased by the same set of customers for the same end use).

While the draft Guidelines acknowledge that conglomerate mergers in the majority of circumstances will not lead to any competition problems, it sets out those specific cases where there may be harm to competition. The section on conglomerate mergers follows essentially the same structure as the guidance on vertical mergers. The draft distinguishes between non-coordinated effects (foreclosure) and co-ordinated effects as principal theories of harm. Foreclosure through tying and bundling are among the principal potential theories of harm discussed in the section. The section outlines the factors that may give a merged firm the ability and the incentive to foreclose and presents the parameters affecting the overall likely impact of a conglomerate merger on prices and consumer choice, and discusses potential sources of efficiency gains in this context.

III. Conclusion and next steps

Through the adoption of Guidelines on the assessment of non-horizontal mergers, the Commission aims to give further guidance on its policy in this area. By providing a coherent analytical framework, the Guidelines will contribute to the level of predictability of the Commission's assessment of non-horizontal mergers. The Guidelines, thus, form an important element of the Commission's aim to provide clear and predictable competition rules grounded in an effects-based approach.

Following an initial consultation among the EU Member States, the draft Guidelines were adopted by the Commission for public consultation. The three-month consultation period, lasting until 12 May 2007, now gives an opportunity to the general public to participate in the debate and to provide their input to the Guidelines. The text of the draft Guidelines is available on DG Competition's website under: http://ec.europa.eu/comm/competition/consultations/open.html

(7) Case T-342/99, Airtours v Commission, [2002] ECR II-2585.

Milestones in maritime transport: EU ends exemptions [1]

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On 25 September 2006, the Competitiveness Council unanimously adopted the Commission's proposal to repeal the block exemption for liner conferences on routes to and from the EU [2]. This is a historic date since the EU is the first jurisdiction world-wide to lift this type of anti-trust immunity for conferences.

The block exemption, established by Council Regulation 4056/86 [3], allowed carriers to fix prices and regulate capacity jointly in liner conferences. The abolition of conferences in trades to and from the EU will enter into effect in October 2008, after a two-year transitional period. In order to smooth the transition to a more competitive regime, the Commission will issue Guidelines on the application of the competition rules to maritime transport services before the end of the transitional period.

The Council has also extended the scope of the procedural rules needed to implement Articles 81 and 82 of the EC Treaty [4] to include cabotage [5] and tramp shipping. The necessary amendment of Regulation 1/2003 entered into force on 18 October 2006. The procedural rules now apply to all sectors of the economy without exception.

Liner conferences

The Council's decision to put an end to the possibility for shipping lines to organise themselves in cartel-like liner conferences marks a milestone in the application of competition law to the maritime transport sector. It represents a fundamental change in the application of competition law to this transport sector. As such, it is welcome that the change was brought about by broad consensus among the European institutions. The Council decided only 9 months after the Commission presented its proposal, and by unanimity, whereas qualified majority sufficed. The European Parliament adopted a favourable report in July 2006 with an overwhelming majority and also the European Economic and Social Committee issued a favourable opinion.

Liner shipping involves the provision of regular, scheduled transport of cargo, usually by container. Given the regularity of the service, in order to serve a particular route (e.g. from Europe to China) it is necessary to deploy several ships of a similar size. Regular scheduling of services however does not ensure that vessels are sailing at full capacity while on the other hand it entails high investments costs which triggered since the 1870s the organisation of shipping lines in the form of cartels called liner conferences.

The importance of liner conferences generally declined over the last decades. However liner carriers continue to join conferences and these retain very large market shares [6]. The longevity of conferences is also impressive. Conferences like the Indian Pakistan Bangladesh Conference successor of the Calcutta conference founded in 1875 survived despite considerable technical progress in maritime transport (e.g. steamships or containerisation) and major changes in management as well as industrial organisation, e.g. hub and spoke systems or the emergence of consortia and alliances.

To date there is no other jurisdiction that has taken the step to outlaw price fixing and capacity regulation by liner shipping carriers. This however does not imply that there is an international

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) Council Regulation (EC) No 1419/2006 repealing Council Regulation (EC) No 4056/1986 on the application of Articles 85 and 86 (now 81 and 82) EC to maritime transport and amending Council Regulation No 1/2003, Official Journal L 269, 28.9.2006, p.1. See "Commission proposes to repeal liner conference block exemption", Competition Policy Newsletter, No. 1, spring 2006, p.43-47.

(3) Council Regulation (EEC) No 4056/86 laying down detailed rules for the application of Articles 85 and 86 [now 81 and 82] of the Treaty to maritime transport (Liner shipping conferences), Official Journal L 378, 1.12.1986, p. 4.

(4) Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, Official Journal L 1, 4.1.2003, p. 1-25.

(5) Cabotage are maritime transport services that exclusively take place between ports within one and the same Member State.

(6) See Dynaliner 4/2007, p.1: "In mid-September, to the surprise of some, MSC joined the Far Eastern Freight Conference (FEFC). Seeing this carrier's substantial capacity growth, it signalled a significant increase of the conference share by (nominal) shipboard TEU space in this trade. As of mid-January, the North Europe capacity share of conference members stood at 72% and even 78% in the Mediterranean, translating into a total of 73% for both trade areas."

conflict of law. This would only be the case if one jurisdiction were to require carriers to participate in conferences, whereas another was to prohibit it. This is not the case, on the contrary a number of the EU's major international trading partners (e.g. USA, China, Japan or Australia) also embarked on a review of the liner conference system in their respective jurisdictions. The Commission has established close and frequent contacts with these partners to promote further competitive reform of the liner shipping sector.

Liner conferences like many other cartel organisations are also sources of market information. In this context the liner industry organisation has identified a need for a successor regime. The European Liner Affairs Association ("ELAA") on behalf of 21 global carriers submitted that, if Regulation No 4056/86 was repealed, continued stability of supply of liner services required the setting up of an exchange of information system to replace the conference system.

The Commission accepted this need in principle since it is common practice in many industries that statistics and general market information are gathered, exchanged and published. If on the one hand these exchanges are a good means of increasing market transparency and knowledge, hence of enabling firms to fine tune supply to demand, reduce costs and avoid risky strategy choices. On the other hand in some industries safeguards are needed to make sure they are not used for collusion purposes. The Commission therefore stated that any new system for exchange of information system in liner shipping, must respect competition rules ([7]) namely the Court's case law and the Commission practice on exchanges of information between competitors. The forthcoming guidelines will provide further guidance to the industry in this respect.

In September 2006, as an interim step in the preparation of the Guidelines, the Commission published a staff "issues paper" ([8]). It sets out a preliminary assessment of the issues relating to information exchanges raised by the industry's proposal for information exchange in the liner market.

The Guidelines are prepared in consultation with stakeholders. The Commission has been discussing with the liner industry how best to issue appropriate guidance on how competition law should apply to the sector, once the abolition of Regulation 4056/86 enters into force. This dialogue has resulted in a number of submissions from the shipping industry, which are all available on the Commission website ([9]).

Tramp shipping

Tramp shipping services concern the non-regular, non-advertised maritime transport of bulk cargo that is not containerised, and include a range of economically important services such as the transport of oil, ores and agricultural products. The Council extended the scope of Regulation 1/2003 which does not involve a change to the applicable law as EU competition rules already apply to cabotage and tramp shipping. It rather improves the possibilities for the Commission to enforce the competition rules in these sectors, in addition to national competition authorities and courts.

The impact on international tramp shipping should not be substantial because EC Treaty competition rules (Articles 81 and 82) always applied to cabotage and tramp shipping. It is rather a question of including these sectors within the generally applicable procedural framework laid down by Council Regulation 1/2003 and so better enable the Commission, in addition to national authorities and courts, to apply these rules to cabotage and tramp shipping.

Given that the Commission is yet to enforce competition rules in tramp shipping there is also a need for the forthcoming Guidelines on the application of competition rules to cover issues specific to tramp shipping services, such as market definition or pool agreements, a common form of co-operation between competitors in the sector. Preparatory work is already underway and the Commission engaged in discussions with tramp operators. It also has contracted an external study on the sector which has been published ([10]).

The way forward

The Commission's Green Paper on maritime policy stresses the vital importance of a competitive shipping industry for Europe ([11]). The abolition of

([7]) MEMO/05/480:http://europa.eu.int/rapid/pressReleasesAction.do?reference=MEMO/05/480&format=HTML&aged=0&language=EN&guiLanguage=fr

([8]) See: http://ec.europa.eu/comm/competition/antitrust/legislation/maritime/issues_paper_shipping.pdf

([9]) http://ec.europa.eu/comm/competition/antitrust/legislation/maritime/

([10]) ibid.

([11]) *"Given Europe's export-based economy, the increase in trade volumes and its geographical circumstances, the EU has a vital interest in the competitiveness of shipping […]. To assure this competitiveness it is necessary to provide an international level playing field for those industries. This is even more important as maritime activities mostly compete in a global market."* Green Paper: Towards a future Maritime Policy for the Union: A European vision for the oceans and seas"; p. 8; available at: http://ec.europa.eu/maritimeaffairs/pdf/com_2006_0275_en_part2.pdf liner shipping conferences will certainly render liner markets more competitive. On the other hand shipping operators may maintain co-operation within liner consortia or tramp shipping pools. To this end the forthcoming guidelines will provide maritime operators with the necessary tools to self-assess these agreements and ultimately foster competitiveness in this sector.

Effective unbundling of energy transmission networks: lessons from the Energy Sector Inquiry (1)

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Introduction

During the late 1990s, the European Union decided to fundamentally change the basis for the provision of electricity and gas from a monopolistic to a competitive market framework. This objective was introduced via the first electricity and gas Directives (2), which removed the legal monopolies and partially opened the market to competition by allowing large users to choose their suppliers. Already at that early stage, the Community legislator identified the risk that vertically integrated incumbents could use their monopolies over the transmission networks in order to stifle the emergence of competition in the supply business. Rules were established to mitigate that risk, including the introduction of a Third Party Access regime and some unbundling provisions to ensure that vertically integrated operators would not discriminate against new entrants or create other entry barriers.

This commitment to competition was confirmed and strengthened with the adoption of the second package of Directives in 2003 (3). With this legislation Member States agreed a timetable to open electricity and gas markets fully to competition. The unbundling provisions were reinforced, a *regulated* Third Party Access regime was introduced and the creation of national regulators became mandatory. In addition, Regulations (4) were introduced which allowed for the adoption of legally binding guidelines with the aim of facilitating cross border competition.

However, after several years of experience with this new paradigm for energy markets, the Commission has become increasingly aware of the presence of significant remaining obstacles to competition. Because of these obstacles, consumers are not reaping the full benefits of the liberalisation process. Accordingly, in mid-2005, the Commission launched the Sector Inquiry into the European gas and electricity sectors pursuant to Article 17 of Regulation 1/2003 (5).

In January 2007 the Commission adopted and published the Final Report on the Sector Inquiry (6). One of the main shortcomings identified in the Final Report relates to continued vertical foreclosure, i.e. the obstacles to competition stemming from the vertical integration of companies active in the supply and network business. The Final Report concluded that there is an ongoing conflict of interest in these vertically integrated companies with a continued risk that they use their control over the network to make market entry and expansion of their competitors in the supply markets difficult. Whilst the Directives have already sought to address these issues by introducing a minimum level of unbundling, the Sector Inquiry has demonstrated that the current unbundling regime is inadequate.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity. (OJ L 27, 30.1.1997, p. 20–29).
Directive 98/30/EC of the European Parliament and of the Council of 22 June 1998 concerning common rules for the internal market in natural gas. (OJ L 204, 21.7.1998, p. 1–12).

(3) Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC. (OJ L 176, 15.7.2003, p. 37–56).
Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC. (OJ L 176, 15.7.2003, p. 57–78) (Hereafter — the Electricity and Gas Directives).

(4) Regulation (EC) No 1228/2003 of the European Parliament and of the Council of 26 June 2003 on conditions for access to the network for cross-border exchanges in electricity. (OJ L 176, 15.7.2003, p. 1–10).
Regulation (EC) No 1775/2005 of the European Parliament and of the Council of 28 September 2005 on conditions for access to the natural gas transmission network. (OJ L 289, 3.11.2005, p. 1–13).

(5) Commission decision (EC) No C(2005) 1682 of 13 June 2005 initiating an inquiry into the gas and electricity sectors pursuant to Article 17 of Council Regulation (EC) No 1/2003.

(6) Communication from the Commission (COM(2006) 851 final): "Inquiry pursuant to Article 17 of Regulation (EC) No 1/2003 into the European gas and electricity sectors (Final Report)" and its Technical Annex SEC(2006) 1724. (Hereinafter — the Final report).

More than anything, at a time when very large investments are needed to promote market integration and ensure security of supply, the way the current unbundling is set up, leads to worrying distortions of investment incentives. In many Member States it is currently left to the vertically integrated incumbents to invest in the additional transmission capacity that could bring more competition to their own supply business: such a setting is unlikely to yield socially optimal investment decisions. There is little doubt that a co-ordinated European response is required.

The endeavour to establish a genuine European internal market for electricity and gas is ongoing. The Energy Council of 15 February 2007 emphasised that there should be effective separation of supply and production activities ensuring equal and open access to transport infrastructures and independence of decisions on investment in infrastructure. The European Council of 8-9 March 2007 approved to a large extent the conclusions of the Energy Council as regards the internal energy market, thus maintaining the mandate that the Commission had been given by the Energy Council of 15 February to proceed with an additional unbundling agenda. The European Council based its conclusions *inter alia* on the Commission's Final Report following the Sector Inquiry thus following the Commission's position. In particular, the Council agreed on the need for a number of new developments of the internal market rules including effective separation of supply and production activities from network operations (unbundling), guaranteeing equal and open access and independence of decisions on investment in infrastructure with relevant investment signals contributing to the efficient and more secure operation of the transmission grid. Furthermore, the European Council invited the Commission to elaborate measures to this effect and to come forward with relevant proposals including through the development of existing legislation where possible.

DG Transport and Energy has already initiated an impact assessment procedure to identify the most suitable methods for implementing unbundling that effectively addresses the inherent conflicts of interest resulting from the integration of network and supply interests. A further Communication including detailed formal proposals to the Council and the European Parliament will be produced, based on guidance from Council and Parliament.

The present article discusses the findings of the Sector Inquiry that are most relevant to the issue of unbundling, how they demonstrate that the current unbundling regime is ineffective, and point to the need for a structural solution. It is structured as follows: first, a short description of the current unbundling regime is provided. Then the deficiencies of the regime are identified and illustrated (7). It is also explained why ownership unbundling stands out, in the light of these findings, as the most effective solution. It then turns to legal considerations related to the introduction of ownership unbundling; and concludes that Europe should reflect carefully whether it can afford to introduce a sub-optimal unbundling regime.

Current unbundling regime

It has been clear since the beginning of the liberalisation process that a significant degree of unbundling is needed in order to ensure non-discriminatory access to the networks and to avoid conflicts of interest within vertically integrated energy companies.

The current Electricity and Gas Directives impose minimum obligations on energy network operators with regard to *legal and functional unbundling* between transmission/distribution networks on the one hand and upstream (generation or production)/downstream (supply) functions on the other (8). The companies concerned are obliged to create separate legal entities for network activities. There must also be separation of executive management and decision-making with respect to operation, maintenance and development of the network. The day-to-day management of the network operator and all related decisions must be made independently and without interference by the parent company. Legal unbundling also presupposes the creation of separate accounts.

Furthermore, Transmission Systems Operators ('TSOs') are obliged to treat all system users alike, including as regards access to information (principle of transparency and non-discrimination). In order to ensure that this obligation is respected, the Directives require "information unbundling" through the creation of information barriers between supply and network activities ("Chinese Walls"). Network operators must act independently and must not be influenced by the vertically integrated group.

The unbundled network operators also have to actively implement a compliance programme serving as a formal framework for preventing discriminatory behaviour and protecting confidentiality of business information. In order to facili-

(7) The article focuses in particular on transmission and distribution activities. However, the problems caused by the insufficient unbundling also exist on e.g. gas storage markets which are not covered by this article.

(8) Unbundling requirements for gas and electricity companies are essentially the same.

tate their supervision, network operators have to submit annual reports on the implementation of the compliance programmes to the regulatory authority.

Legal and functional unbundling for transmission networks is required from July 2004, as is functional unbundling for distribution networks ([9]).

Deficiencies of current unbundling regime

The Sector Inquiry as well as the analysis carried out by DG Transport and Energy in preparation of the Strategic Energy Review confirmed that significant differences persist in the level of the implementation of the unbundling provisions. In a number of Member States, the unbundling provisions are still missing due to the lack of timely, complete or correct transposition of the Directives into national law ([10]). In practice this means that different degrees of market opening exist between Member States undermining the creation of a level playing field.

However, even where Member States have adopted the unbundling provisions required under the Electricity and Gas Directives, this does not mean that network operators necessarily comply with them. Furthermore, even where the unbundling provisions are fully implemented, the Sector Inquiry has demonstrated that incentives for preferential treatment within vertically integrated operators remain.

It also appears that national regulators cannot verify to a satisfactory degree whether unbundling provisions are respected in practice. Various reasons can be named for this, such as lack of resources and appropriate powers.

Fundamentally, the current unbundling regime does not suppress the inherent conflict of interest that stems from vertical integration of network and generation and/or supply interest. The incumbent suppliers view their networks as strategic assets that serve their commercial interests.

Even when there is a more sincere attempt to abide by the letter and spirit of the current unbundling rules, the network company is often unclear of its objective and role. It cannot combine diverging targets, i.e. non-discriminatory third party access and compliance with unbundling regime versus optimisation of the return to the vertically integrated company. This leads to a high risk that the companies concerned will engage in anti-competitive strategies or, more generally, to sub-optimal behaviour as a network operator.

Indeed, the current unbundling rules do not remove the incentives and possibilities for ***discrimination with respect to third party access.*** Often, changes to network access conditions have, like investment projects, to be approved by the TSO's parent company where supply affiliates are represented. Network operators that have supply interests usually have both the ability and incentives to offer preferential treatment to that supply business and this leads to discrimination of their competitors. There are various means through which such discrimination may take place, some of which are difficult to detect and/or expeditiously remedy and sanction, even for a specialized regulatory body: delaying or complicating the connection of new entrants' power plants to networks, maintaining artificially small balancing zones, charging high balancing fees, which will be primarily paid by new entrants, not making available unused capacities or not using the most efficient allocation methods: e.g. implicit auctions.

- One of the German gas incumbents was recently able to offer a gas delivery contract for a new power plant requiring a substantial import capacity, to be shipped through the network of its "associated" network company. At the same time new entrants were not granted firm capacity on an almost identical pipelines path, although the capacities they requested were substantially lower than the ones granted to the power plant. Under the current provisions, such discrimination is difficult to detect ([11]).

([9]) Member States are permitted to postpone legal unbundling of all distribution networks until 1 July 2007. They are also authorised to relieve integrated gas and electricity distributors supplying less that 100,000 customers, or small isolated networks, from the legal unbundling requirements.
There is a possibility of exemptions from the requirement of legal and functional unbundling for Distribution System Operators until July 2007 foreseen in the Electricity and Gas Directives.

([10]) As a consequence, the Commission has initiated infringements proceedings in April 2006 by sending letters of formal notice to Austria, the Czech Republic, France, Ireland, Italy, Poland, Slovakia and Spain. In these Member States, legal and/or functional unbundling is not yet complete. In addition, five Member States benefit from derogations under the provisions of the Second Gas Directive or do not have a functioning gas market. Reasoned opinions, the second step in the infringement procedure, were sent in December 2006, cf. press release IP/06/1768.

([11]) Cf. Final Report, Technical Annex SEC(2006) 1724, para 168.

- The Commission gathered indications during its Sector Inquiry that one transmission system operator grants its affiliated supply company substantive rebates for the transportation fees as compared to non-affiliated network users. In doing so, the network operator directly supports the competitive position of the related supply company. This appears to be an overall business strategy carried out by some integrated gas companies and leads to excessive access tariffs, which raise competitors' costs ([12]).
- The nomination procedure of gas transport capacities appears to be different vis-à-vis different shippers. While the supply company of vertically integrated operators can nominate their capacities directly to the network's dispatching centre, third parties with short term interruptible contracts still have to nominate their capacities in advance to the network operator who aggregates them before sending to the dispatching centre for execution ([13]).
- Various shippers allege that the access to transit capacities is in some cases made conditional upon the prior existence of gas purchase or supply contracts, so that planning ahead becomes difficult for smaller independent shippers. In addition, gas incumbents do not offer new entrants wheeling services, enabling them to redirect gas flows of purchased capacities once put into the pipeline system ([14]).

More generally, ***information leakage*** between the supply and network affiliates of legally unbundled, but still vertically integrated, network operators tends to be a common practice ([15]). Despite information barriers, i. e. "Chinese walls" being in place under the legal unbundling regime, information that facilitates discrimination is, in some cases, systematically shared between the network operator and company's competitive activities. This undermines the trust of alternative producers and suppliers in the functioning of the market.

- In the Sector Inquiry, the TSOs were asked to provide information about their practical implementation of the unbundling requirements. Where this has not yet been fully completed, the process is allegedly under way. The TSO's replies however point to a certain number of admitted shortcomings as regards the current level of unbundling. For example, top management of the supply branch, which are represented at the parent level, often have access to strategic business information of the transport company, either directly or as a result of their representation in the Supervisory or Administrative Board of the latter. The same holds true for both transmission and distribution system operators where insights into the activities of competitors are made available to affiliate supply businesses ([16]).
- The network operator is informed about the envisaged change of supplier, as this supplier has to access the network in order to supply the customer. Information provided in the Sector Inquiry shows that network operators may find a way to inform the management of the vertically integrated supply branch when a customer is considering switching supplier. As a result, customers are prevented from switching suppliers; market entry for competitors becomes difficult.
- Network companies provide more detailed information on, for example, load, outages, generation from wind turbines, to their affiliate supply company so that they can better optimise their trading and production portfolio.

([12]) Cf. Final Report, Technical Annex SEC(2006) 1724, para 155.
The fact that tariffs have historically been too high has also been confirmed by the decision of regulators to reduce the tariffs submitted for approval by transmission system operators.
([13]) Cf. Final Report, Technical Annex SEC(2006) 1724, para 165.
([14]) Cf. Final Report, Technical Annex SEC(2006) 1724, para 170.
([15]) Newbery, David (2005). Refining Market Design. Paper presented at the Conference "Implementing the Internal Market of Electricity: Proposals and Time-Tables". Brussels. Page 20: "Vertically integrated transmission and generation companies can exploit informational advantages, discriminate in the provision of access, balancing and other ancillary services, and cross-subsidise competitive activities by inflating monopoly costs." http://www.sessa.eu.com/documents/final/SESSA_report_wp3.pdf
([16]) Cf. Final Report, Technical Annex SEC(2006) 1724, para 153.

Most importantly, with the current state of unbundling ***investment incentives remain distorted.*** The degree of autonomy over investment decisions to be taken by the legally and functionally unbundled network operators tends to be too low vis-à-vis their parent companies, so that investment decisions in new infrastructure projects are in practice taken by the group as a whole ([17]). As such, investment decisions of vertically integrated undertakings are very often biased towards the needs of supply affiliates ([18]). Since the vertically integrated incumbents normally have very strong market positions as a supplier in the area where they control the network, it is often in their interest *not* to invest in infrastructure that would bring additional competition to this area: the interest in protecting the market power and the profitability of their supply business trumps their interest in increasing their (regulated) network business. The few examples in the box below are illustrative of this phenomenon.

- ENI, the Italian gas incumbent, has delayed investments, which would increase the capacity in a pipeline owned by one of ENI's subsidiaries, the Trans Tunisian Pipeline Company. The increased capacity would have improved the ability for competitors to import Algerian gas to Italy and to compete with ENI on the Italian gas wholesale market. The discontinuation of the pipeline expansion was driven by ENI's supply interest in Italy (alleged fear of a "gas bubble"). ENI solved the conflict of interest between its network business and supply activities to the detriment of its own network business and of its competitors on the gas supply market. The Italian competition authority imposed a fine on ENI and ordered ENI to desist from its anti-competitive conduct ([19]).
- Indications of discriminatory behaviour have been found with regard to investment decisions taken by the integrated gas companies. Certain investment decisions on network extensions of the transport company have to be approved by an investment committee of the parent company of the TSO. In a number of cases, companies have only invested in capacity expansions if their related supply arms had previously confirmed their interest for the bulk of the extra capacity. By contrast, the investment did not take place if the interest in extra capacity merely stemmed from competitors ([20]).
- While the auctioning of scarce electricity interconnector capacity has generated large congestion rents ([21]), there has been limited investment in such new capacity. For instance, in the period 2001 to 2005 three German transmission system operators, which are all part of vertically integrated companies, generated congestion revenues of Euro 400-500 million. Of these revenues only Euro 20-30 million were used to reinforce/build new interconnectors. No regulatory approval took place on how these companies used the congestion rents as no regulator was in place.

In addition, the fact that the incumbent suppliers own the transmission network has a chilling effect on the investment of other companies (third parties). New entrants will hesitate to invest if they are not convinced that the network operator will treat them fairly. For instance, it is not attractive for new entrants to invest in a power plant or new gas import infrastructure if there is a risk that requests for connection to the network are met with unreasonable requirements for unreasonable payments to remove the alleged congestion supposedly caused by the newly connected plant.

The three above-described limits of the current unbundling regime (discrimination, information leakage and distorted investment incentives) are reinforced by the current governance of network operators vertically integrated with a

([17]) Under the existing Electricity and Gas Directives, certain coordination mechanisms are still allowed to ensure supervision rights of the parent companies regarding the return on assets. For instance, the parent companies are able to approve the financial plan and to set global limits to the indebtedness of its subsidiary.

([18]) See the national sections on network operator and unbundling in the Commission Staff Working Document, Implementation report on electricity and gas EU regulatory framework: country reviews — SEC(2006) 1709; and the Final Report, Technical Annex SEC(2006) 1724, especially from para 157 (gas) and 487 (electricity).

([19]) See ENI-Trans Tunisian Pipeline Decision of 15/02/2006 of the Autorità Garante della Concorrenza e del Mercato, published in the Bollettino of the AGCM no. 5/2006 (reference: A358). See also Decision of 29/11/2006 of the Tribunale Amministrativo Regionale (TAR) del Lazio, on appeal no. 3582/2006 by ENI Spa against the decision of 15/02/2006 in the ENI-Trans Tunisian Pipeline case. To date only the operative part of the judgement has been published. It appears that the decision of the competition authority was upheld, but the fine was lowered.

([20]) Cf. Final Report, Technical Annex SEC(2006) 1724, para 157.

([21]) Article 6 (6) of the Regulation 1228/2003 states that revenues resulting from the allocations of congested interconnector capacity shall be used for inter alia network investments maintaining or increasing interconnector capacities. Cf. Final Report, Technical Annex SEC (2006) 1724, para 541.

supply activity, which exacerbates the conflict of interest between supply and network business. A governance issue that mere regulatory oversight is insufficient to address in a satisfactory manner (for lack of monitoring, lack of powers, lack of resources, and a lack of cooperation between regional operators).

- A number of supply and transport companies within vertically integrated company share physical assets such as office buildings and IT systems. Employees working for the supply and for the transport company still work in the same premises and meet each other on regular basis. All these seemingly small factors contribute to continuous regular contacts between employees of both companies. The persisting links facilitate a coordinated approach between the supply branch and transport branch ([22]).
- The need to take into account the interests of the vertically integrated supply branch is reinforced by the fact that managers in the TSO might have career perspectives in the holding or the supply branch. Also the head of the network company often participates in strategic discussions, business review meetings and training sessions organised within the parent company.
- Complete regulatory oversight/control is very difficult to achieve. Particularly in Member States with a high number of transmission and distribution companies it is virtually impossible for the regulator to verify in all companies that the unbundling provisions are fully respected. Generally the regulator will simply not have the resources to ensure that unbundling requirements are complied with.
- Moreover, national regulatory authorities are unable to monitor cross-border related unbundling due to their competences being restricted to national activities ([23]). There is a regulatory cross-border gap, which cannot be remedied by application of competition rules alone.

The experience and evidence collected by the Commission, as indicated above, confirms that the mere implementation of existing unbundling legislation is not sufficient and does not address the malfunctioning of the energy markets. More needs to be done.

In its Final Report for the Energy Sector Inquiry the Commission reached the conclusion that ownership unbundling would be the most effective cure to the above-described problems.

Ownership unbundling as an optimal solution

What is ownership unbundling?

Ownership unbundling can be defined as a separation of the previously common ownership structure between network and supply activities of a company (supply within this meaning includes retail supply as well as production/generation). In other words, it is separation of all network functions from the other activities — also with respect to the ownership of the assets.

Ownership unbundling implies the creation of a separate company, which owns and operates network assets and the removal of any significant shareholding by one type of company in the other. In practice it means that no supply company could have a significant stake in the network operator and certainly not a stake that would give a company any type of control — individually or jointly with others — over the other ([24]). Whilst there is considerable scope to reflect about options how to best implement ownership unbundling, it should be clear from the outset that companies which are actual or potential suppliers in a given Member State could not acquire/maintain networks in this Member State. This also applies to companies located outside the EU.

The ownership unbundled network operator would manage system operation (i.e. the interface with the system users), network maintenance and network investment in a coordinated manner. The main advantage of such a system would be that the conflicts of interest inherent in the current unbundling regime would no longer exist. Whilst regulatory oversight would still be required the network operator could focus on efficient provision of network service and optimised investments.

It is important to underline that ownership unbundling would not oblige Member States to privatise the supply and/or network business. Where both

([22]) The Sector Inquiry has revealed that the "special relationship" leads to a (systematic) copying of emails to the other formally unbundled, but affiliated branch (lack of "information unbundling"), whilst obviously third parties do not get access to such information at the same time.

([23]) Where the related supply company is incumbent in the neighbouring market there is a conflict of interests when improvement of the third party access regime on a pipeline system necessary to supply the incumbent's home market is required.

([24]) Energy companies active in upstream and downstream markets would be prevented from owning shares in the network company above a certain threshold.

network and supply activities are currently in public hands, it would be possible to retain the public ownership, provided that sufficient structural separation is achieved (e.g. the separated businesses are run by two different ministries, or one business is run by municipalities and the other by the State).

Even though ownership unbundling is not required by the current unbundling regime, a significant number of companies have already successfully undergone the ownership unbundling process. This is the case for electricity transmission system operators in Member States like the United Kingdom (in England and Wales), the Netherlands, Portugal, Slovenia and Spain, but also in the Czech Republic, Denmark (for the main TSO), Finland, Lithuania, Romania, Slovakia and Sweden ([25]). In the gas sector, ownership unbundling at the transmission system operators' level has taken place in Denmark, Great Britain, Portugal, Romania, Spain and the Netherlands ([26]).

What are the advantages?

The benefits of ownership unbundling of transmission from production seem to be widely acknowledged ([27]). There is increasing evidence that the implementation of ownership unbundling would be welfare enhancing ([28]). Ownership unbundling would clearly generate benefits for *competitors* on the one hand, and for the *network companies* on the other hand. It is ultimately to the advantage of the energy sector as a whole and possibly even to the *shareholders* of the vertically integrated incumbents. Whilst it is not the miracle solution removing all obstacles to a successful completion of the liberalisation process in one go, it would certainly address the main shortcomings of the current regime by removing a key barrier to entry.

As regards the **competitors,** network operators will have no incentive any more to discriminate between market participants. "Passive" discrimination (inertia) of the incumbent vis-à-vis third parties will also be excluded. As a result, new entrants and existing suppliers will get better access to unused transmission capacity from the network operator seeking to optimise its profits. The competitors' concern that the vertically integrated network operator provides its supply arm with confidential information will be eliminated.

The strategic benefits of full ownership unbundling for **network operators** include the fact that the network operator will be able to focus on optimising its main business — the use of the network. As the network business is regulated, a network operator can only generate more revenues if it

([25]) In the Czech Republic, Denmark (for the main TSO), Finland, Hungary, Ireland, Lithuania, Slovakia and Sweden, the TSO is under state control.

([26]) The choice of these Member States to adopt full ownership unbundling was triggered by various considerations, mainly stemming from the expected strategic benefits. In some cases, separation has been the result of national legislation. In other cases, the undertakings heavily influenced by the regulatory environment and the fact that a bundled organisation structure was failing to meet the expectations of customers or shareholders, have opted for a voluntarily ownership separation (e.g. British Gas).
European Commission (2006). Unbundling of electricity and gas transmission and distribution system operators. Final Report. Gómez-Acebo & Pombo Abogados, S.L. and Charles Russell LLP. http://ec.europa.eu/energy/electricity/publications/doc/2006_03_08_final_common_report.pdf

([27]) For instance, regulators favour full ownership unbundling. The European Group of Regulators for Electricity and Gas (ERGEG) has confirmed that this is its preferred option.
See ERGEG's response to the European Commission's Communication "An Energy Policy for Europe", 6 February 2007. http://www.ergeg.org/portal/page/portal/ERGEG_HOME/ERGEG_DOCS/ERGEG_DOCUMENTS_NEW/Energy%20documents.
Cf Deutsche Bank Research. EU-Monitor 44. Beiträge zur europäischen Integration. Aurer, Josef (2007). EU-Energiepolitik: Höchste Zeit zu handeln! Page 7 ff. http://www.dbresearch.de/PROD/DBR_INTERNET_DE-PROD/PROD0000000000207530.PDF
Cf. Economic survey of Germany 2006: Sustained Competition is absent in Energy Markets. Excerpt of the OECD Economic Survey of Germany, 2006, Chapter 5. Page 7: "(O)wnership separation of transmission from generation is, in principle, preferable. Introducing an independent systems operator while leaving transmission and generation in the ownership of the Verbundunternehmen would entail separation of transmission asset ownership from transmission asset management, which may result in inefficiencies." http://www.oecd.org/dataoecd/24/63/36789821.pdf
Cf. Jamasb, T.J. and Pollitt, M.G (2005). Electricity market reform in the European Union: review of progress towards liberalisation and integration. University of Cambridge. Page 7: "Unbundling can take the form of functional, accounting, legal, or ownership separation, with the last being the most effective."
http://www.electricitypolicy.org.uk/pubs/wp/ep66.pdf

([28]) Cf. Economides, Nicholas. The Economics of networks. International Journal of Industrial Organization. 14 (1996) 673-699. page 694: " For example, if competition between an entrant and the incumbent reduces the market power of the incumbent, entry may increase social welfare even when the entrant produces at higher cost than the incumbent." http://www.stern.nyu.edu/networks/Economides_Economics_of_Networks.pdf
Cf. Van Koten, Silvester, Ortmann Andreas (2006). The unbundling regime for electricity utilities in the EU: A case of legislative and regulatory capture? "There seems wide agreement that the quick implementation of ownership unbundling would be welfare enhancing". (Pittman, Russell (2003). Vertical restructuring (or not) of the infrastructure sectors of transition economies, Journal of Industry, Competition and Trade. 3:1/2, 5-26.).

expands its network. Incentives (e.g. higher return on investments) can be given for new infrastructure so that ownership unbundling will allow investments in the network infrastructure when it is beneficial for the network business and the market in general. In addition, the network operator would avoid a burdensome part of the regulatory oversight and heavy unbundling compliance programmes would become superfluous. The complex, intrusive and resource intensive regulatory approach for network operators (and regulators) will be avoided.

The experience to date is positive, especially regarding the important question of whether ownership unbundling will ensure adequate network investment. As an example, the experience in particularly from the United Kingdom and the Netherlands can be mentioned.

The *United Kingdom* (England and Wales) markets underwent a gradual unbundling process of the gas transmission networks since 1990, which lead to full ownership unbundling ([29]). An analysis of this example confirms that the levels of investment increased significantly after ownership unbundling (see table below). During the same time the UK model has delivered a more than 50% reduction (in real terms) in transmission costs since privatisation due to the internalisation of the system operator/transmission owner interface, innovation, aligned incentives and a reduction of balancing costs. The effective incentivisation led to significant technical innovation in investment and maintenance. The gas transmission system operator has supported the development of significant new LNG and pipeline capacity, which has led to the rapid reverse of the high 2005 price levels ([30]).

*Change of **investment levels** in the ownership unbundled British Gas Group* ([31])*:*

- *Transco when owned by British Gas Group (upstream integration)* ([32]).

3/1997-3/1998	*£ 147m*
1998-1999	*£ 191m*
1999-2000	*£ 140m*

- *Fully unbundled period* ([33])*:*

2000-2001	*£ 228m*
2001-2002	*£ 239m*
2002-2003	*£ 182m*
2003-2004	*£ 159m*
2004-2005	*£ 128m*
2005-2006	*£ 360m*

([29]) Before the British gas incumbent was ownership unbundled there had been persistent discrimination in third party access. The United Kingdom regulatory and competition authorities took repeated actions to solve these problems, which successively increased separation of network and supply activities. The costs of complying with onerous and intrusive regulation were one of the factors which led to the choice made by British Gas to separate ownership. The ownership unbundling appeared to the company to be the best way to move supply and trading business outside of the scope of regulatory control and provide the market participants with strategic benefits. The company eventually separated the network company into new independent companies which are able to focus on their core activities leading to optimisation of network activities. It has facilitated cross border activities and network integration.

([30]) Cf. Joskow, P. (2005). Patterns of Transmission Investment, Centre for Energy and Environmental Policy Research, page 31: "The organizational and regulatory arrangements that characterize the system in England and Wales are generally viewed to have been quite successful in supporting competitive wholesale and retail power markets with a transmission system that has attractive operating and investment results. During the period, demand grew, about 25,000 MW of new generating capacity entered the system, and almost an equal amount was retired. Power flows changed significantly on the network. While network investment is cyclical, following cycles of generation additions and retirements, intracontrol area investment post-restructuring has increased significantly compared to intracontrol area investment pre-restructuring (Figure 6), while congestion costs have declined significantly since 1994. Network losses have also declined."
http://econ-www.mit.edu/faculty/download_pdf.php?id=1133
Cf. Newbery, David (2005). Refining Market Design. Paper presented at the Conference "Implementing the Internal Market of Electricity: Proposals and Time-Tables" 2005. Brussels. Page 8: "*The first lesson one can draw from the British experience is that unbundling ownership of transmission from generation has been critical in enabling competition to deliver cost reductions in England and Wales*". http://www.sessa.eu.com/documents/final/SESSA_report_wp3.pdf

([31]) DG Competition calculations made on the basis of Transco, Lattice, NGC annual accounts and price review documents from the Competition Commission, Ofgem incentives review document.

([32]) Cf. Ofgem: Review of Transco's Price Control from 2002. Final Proposals, September 2001, Table 4.8 page 59.

([33]) Source: Lattice and National Grid Annual accounts.

In *the Netherlands,* the gas transmission system operator has been ownership unbundled since 2005 (Gasunie). The unbundled operator, driven by the optimisation of network activities, has started the Gate LNG terminal in Rotterdam; the construction of gas storage project in the Zuidwendig is underway. Gasunie now has a natural business drive to attract additional gas flows, and to accommodate a broad customer base for gas-related infrastructure services through timely investment. One can observe that the average annual 2001-2004 investments were 63 million Euro whereas the average ex post 2005 average annual investments are estimated 127 million Euro ([34]).

For Spain, the boom of LNG terminals (also needing investments in connecting infrastructure) was significantly facilitated by (progressive) unbundling. One can also make the observation that the only countries that have incumbent-supplier independent LNG terminals are the United Kingdom, Spain and the Netherlands (ongoing project), all of which have ownership unbundled companies.

Furthermore, cross border activities will be facilitated. Network operators will cooperate more freely with neighbouring transmission system operators. By contrast, cross-border cooperation between vertically integrated network operators creates a real risk of collusion and is thus problematic from a competition point of view.

This will encourage cross border mergers of network companies ([35]). Cross border investments and EU energy infrastructure capacity will also increase (see the Dutch example).

These various positive developments will in the end benefit shareholders in the vertically integrated energy companies. From a more short-term perspective, the combined value of the two companies will increase given the traditional discount that conglomerates trade at. The management of both the network and the supply arm will be encouraged to concentrate fully on their own business and so to improve their operational efficiency and so their return on capital. This will be reflected in companies share price. Unbundling could also facilitate the development of wider geographical markets, which would allow and encourage mergers in the supply business.

More generally, effective unbundling will allow for a better allocation of capital by allowing for low risk — low return profile of a regulated network business to be clearly separated from the more variable returns associated with the production and supply businesses.

Options other than ownership unbundling, such as reinforced legal unbundling ([36]) have a major shortcoming: they do not address at the root the

([34]) Clearly the arguments for investments can not easily be disentangled from each other: such as facilitate markets, security of supply, etc. See: http://www.nvnederlandse gasunie.nl/media/pdfs/Gasunie-jv2005.NL.pdf and see: http://www.dte.nl/images/102259%20Informele%20 zienswijze%20uitbreiding%20H-gas%20transportsys teem_ tcm7-93518.pdf.

([35]) Cf. Mulder Machiel, Shestalova Victoria and Lijesen Mark. Vertical separation of the energy-distribution industry. An assessment of several options for unbundling. CPB Netherlands Bureau for Economic Policy Analysis. Page 28: "The entirely independent status following from full ownership unbundling will further improve the management of networks, as network firms will now no longer be compromising between the interests of the network and other activities. Furthermore, depending on the scenario with respect to regional transmission, full unbundling may facilitate horizontal mergers at the transmission level, which may give rise to economies of scale." http://www.cpb.nl/nl/pub/cpbreeksen/document/84/doc84.pdf
Cf. also Newbery, David (2005). Refining Market Design. Paper presented at the Conference "Implementing the Internal Market of Electricity: Proposals and Time-Tables" 2005. Brussels. Page 20: "Simulations suggest that the cross-border ownership (Electrabel in Belgium and the Netherlands, E.On and RWE spanning the Dutch-German border, in both cases owning transmission and interconnection) makes market integration more problematic. This again highlights the importance of acquisition and mergers that are viewed too narrowly in national terms." http://www.sessa.eu.com/documents/final/SESSA_report_wp3.pdf

([36]) The same applies also for the Independent System Operator model. Due to the different focus of this article, deficiencies of the Independent System Operator model are not addressed here.

fundamental conflict of interest that stems from vertical integration between the supply business and the network business. It is from this conflict of interest that the distortion of investment incentives or the incentives for third party access discrimination derive.

Alleged disadvantages

Concerns have been expressed that ownership unbundling would lead to considerable disadvantages and that there is uncertainty regarding its impact on the welfare of European consumers. Ownership unbundling would thus, it is said, reduce economies of scale, bring possibly large one-off transaction costs, increase the cost of capital of the supply business, or weaken the position of European suppliers in negotiations with external suppliers. This, it is argued, would then lead to less investment, higher prices and endanger security of supply.

As a matter of fact, where full ownership unbundling has been established, there have been, as yet, no such unexpected negative consequences flowing from that change. To the contrary, in such cases, both the network business and the supply businesses have gone on to perform well on an independent basis and under different regulatory regimes and associated risk profiles. The concerns expressed above are thus somewhat theoretical. They are very unlikely to apply in practice.

More specifically, as to the alleged loss of economies of scale or one-off transaction costs, these would not likely be significant when we move from the *current* system to ownership unbundling. Legal and management unbundling (which are already required under the current EU legislation) should have already brought about these supposed negative consequences — and the empirical evidence available suggests that these have been fairly limited. Concerning more specifically the transaction costs of ownership unbundling, the experience of the UK shows that they are small, even for a move from full vertical integration to ownership unbundling of the transmission network: the one-off cost of the British Gas de-merger in 2000 was around 3.2% of the company's yearly turnover.

Similarly, as has been already mentioned, ownership unbundling is actually likely to spur investment in transmission networks. It certainly will also facilitate entry, and thus positively influence investments by other actors than the vertically integrated incumbents. Some suggest however, that vertically integrated incumbents benefit from retaining ownership over the transmission network, in that the stable regulated returns of that activity diminishes their overall cost of capital. This is said to facilitate their investment in the supply business. As a result, it is argued that ownership unbundling would diminish investments by the (previously vertically integrated) incumbents in supply activities. Similarly, there is a concern that ownership unbundling will leave an independent supply business that has much weaker bargaining position vis-à-vis external supplier of energy sources.

In practice, it is very doubtful that this theoretical mechanism would lead to an overall net negative impact on investment, not least because energy suppliers have many other corporate strategies to diminish their overall cost of capital, or increase their bargaining power. The completion of the internal energy market will also open up opportunities for growth of the supply business by merger and acquisition, in particular outside the home countries of the companies in question — spreading the risk over a bigger scale of activity. Moreover, the added value of the vertically integrated companies is not so much their ownership of the network. It is rather their customer base and their knowledge of how to supply these customers efficiently. The advantage is thus rooted in the retail supply expertise. Unbundling the transmission assets will therefore not necessarily weaken the negotiation position of the EU suppliers vis-à-vis the producers.

Another strategy, which has actually been used by the very same companies in the past, is to develop into "multi-utilities", by investing for example in the water sector (which is close in risk profile to the transmission network business). These various types of growth by acquisition, or simply an increase of the gearing level, should allow the companies to hedge their risks.

Legal questions under EC Law

Structural unbundling remedies of various forms have been accepted by the Commission in several key energy merger cases ([37]). The Commission

([37]) The Commission dealt with merger cases like EDP/GDP, E.ON/MOL, and, recently, with GDF/Suez which were approved only after the parties concerned had accepted structural remedies. Each merger case was unique and review by the Commission focused on addressing competition concerns arising from the transaction via appropriate remedies on the affected markets.
Case No. COMP/M.3696 E.ON/MOL. IP/05/1658, 21 December 2005.
Case No. COMP/M.4180 GdF/Suez. Published on 14.12.2006.
http://ec.europa.eu/comm/competition/mergers/cases/decisions/m4180_20061114_20600_fr.pdf
Case No. COMP M. 3868 DONG / ELSAM / ENERGI E2, published on 27.03.2006.
http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:C2005/233/04:EN:NOT

is also vested with the powers to impose structural remedies in antitrust cases, where there is no equally effective behavioural remedy or where such a behavioural remedy would be more burdensome for the undertaking concerned ([38]). However, in both merger cases and antitrust cases the remedies must accurately address the competition concerns raised on the affected markets. Consequently, competition policy — in its case-based approach — is not an effective method for delivering ownership unbundling across the board. In order to achieve a level playing field throughout the EU, it is therefore necessary to address structural unbundling through legislative and regulatory measures.

Various legal objections have been voiced against introducing ownership unbundling through EU legislation. Such objections include that it would constitute a form of expropriation (falling foul of Article 295 EC or of general principles of EC law) or a limitation of free movement of capital under the EC Treaty.

Firstly, it must be however clarified that in certain Member States, limits in ownership links could, for example, be introduced through licensing rules (i.e. it would not be possible for the same group to hold both a licence for network operation and a licence for supply/production activities). Vertically integrated energy groups would also be able to freely dispose of one or the other activity, at market price, and over a certain period of time.

Secondly, the limitations resulting from ownership unbundling can be lawfully imposed. Article 295 EC ([39]) is generally interpreted to guarantee neutrality as regards the public or private ownership of companies. Consequently, as already explained above, where both network and supply/production activities are currently in public hands, it would be possible to retain the public ownership, provided that sufficient structural separation is achieved (e.g. the separated businesses are independently run by two different ministries, or one business is run by municipalities and the other by the State).

In as far as it could be argued that Article 295 also protects the core rights of ownership, it does not have the effect of exempting the Member States' systems of property ownership from the fundamental rules of the Treaty ([40]). In addition, the right to property is not an absolute right but must be viewed in relation to its social function. Consequently, its exercise may be restricted, provided that those restrictions in fact correspond to objectives of general interest pursued by the Community and do not constitute a disproportionate and intolerable interference, impairing the very substance of the rights guaranteed ([41]). As has been shown above, ownership unbundling is necessary in order to ensure that competition in the internal market is not distorted, and less far-reaching measures are insufficient to achieve this.

A similar necessity and proportionality test would also be applied when assessing the compatibility of ownership unbundling with the general principles of EC law (in particular, the rules on protection of property derived from the European Convention on Human Rights and Fundamental Freedoms). In the same way, any restrictions to the free movement of capital under Article 56 of the EC Treaty can be justified. Furthermore, as regards the subsidiarity test in Article 5 of the EC Treaty, the arguments brought forward for ownership unbundling, and the need to ensure a level playing field across an integrated EU energy market, clearly justify action at EU level.

Conclusions

The need for unbundling of transmission networks in EU energy markets is not a theoretical construct: as evidenced by the information collected in the Sector Inquiry, there are many indications that unbundling is necessary for fully functioning markets. This information is unequivocal: vertical integration of network and supply business creates a situation of conflict of interest resulting, among others, in distorted investment incentives and discriminatory third party access for competitors.

It is also clear from the Sector Inquiry findings that the current unbundling provisions as required by the Second Electricity and Gas Directives are not fully adequate. Even where they are transposed into national law, these directives fail to address this conflict of interest, which is at the root of the competition problems observed. The ineffectiveness of current unbundling requirements is a major reason for the slow pace of market inte-

([38]) See Article 7 and recital 12 of Regulation (EC) No 1/2003.

([39]) "This Treaty shall in no way prejudice the rules in Member States governing the system of property ownership."

([40]) Cf. Case C-302/97 Konle [1999] ECR I-3099, paragraph 38, and Case C-503/99 Commission v Belgium [2002] ECR I-4809, paragraph 44.

([41]) Cf. Case 44/79 Hauer [1979] ECR 3727, paragraph 23; Case 265/87 Schräder [1989] ECR 2237, paragraph 15, Case C-280/93 Germany v Commission [1994] ECR I-4973, paragraph 78; Case T-65/98 Van den Bergh Foods Ltd v Commission, paragraph 170.

gration and the low growth in cross border trade observed in EU electricity and gas markets. Since the Energy Council of 15 February and the European Council of 8-9 March 2007, the Commission has a clear mandate to proceed with a solution for an effective unbundling of the energy transmission networks.

A structural solution, whereby no undertaking would have a significant stake in the network business of a Member State in which it is an actual or potential supplier, would address this fundamental issue. Such ownership unbundling is, in the Commission's view, the best available option ([42]). It is legally feasible, and has been successfully implemented by many Member States. There are no legal obstacles that would prevent the Community from introducing it, and a growing body of evidence that it would bring significant benefits to the completion of the European energy market: more investment into the network, a lower cost for network users, and more competition on the supply side. By contrast, there is a growing recognition that working on improving legal and management unbundling without ownership separation will be a very complicated task — and one that will require a lot of fine-tuning and entail a heavy regulatory burden.

Should we take this time to experiment a "third way" or move forward now in the direction of full ownership unbundling? The case for ownership unbundling is strong from a technical standpoint, and solidly grounded on an extensive empirical basis — amongst others, thanks to the Commission's Energy Sector Inquiry. Ownership unbundling is a cleaner, one-off and less intrusive form of intervention in the market. A "third way" would therefore essentially mean postponing the decision and gathering more experience in the meantime. It would create significant uncertainty as to the future regulatory design of the energy sector — with the prospect of further iterations in adapting the unbundling provisions, against the background of a possible "full ownership unbundling", which in the short run will not disappear from the agenda. While increased experience is always helpful to make a choice, persisting uncertainty has a cost: it depresses investments across the sector. At a time where security of supply is becoming a key concern for our economy, this is a cost that the EU may not be able to afford.

([42]) See Communication from the Commission to the European Council and the European Parliament — An energy policy for Europe SEC(2007) 12.

ECN Model Leniency Programme — a first step towards a harmonised leniency policy in the EU (1)

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Introduction

The co-existence of several leniency programmes within the EU and the practical implications of the ECN work-sharing mechanisms for the handling of leniency cases has been debated since the entry into force of Regulation 1/2003. In the Spring 2006 issue of the EC Competition Policy Newsletter, the authors outlined the deficits and scope for improvement of the current multiple leniency filing system and presented some intermediate steps that had been undertaken within the ECN to streamline the leniency filing system and to avoid that applicants were confronted with contradictory demands when lodging applications with several authorities (2). Since then, reflections have been ongoing within the Commission and the ECN leniency working group to find an appropriate solution to the multiple filing issue. This article will present the outcome of this work, culminating in the publication of the ECN Model Leniency Programme on 29 September 2006.

Background

The fight against hard core cartels has been a top priority for the Commission and other ECN members during the last years. The importance of attractive and effective leniency programmes in that fight has not at least been confirmed by the literally explosion of the number of national leniency programmes introduced since 2002 (3). The co-existence of several programmes in the EU means that a leniency applicant that has been involved in a cartel covering more than one Member State can get protection throughout the Community, provided that it approaches those authorities that can realistically pursue a case against it and satisfies a variety of different rules and conditions. Discrepancies between the programmes may not only make the assessment and the decision to report illegal activities more complex, but might deter applicants from reporting certain conduct at all. Likewise, having to file and process applications in cases that an authority will not take action in is unnecessary burdensome for both applicants and authorities. In 2005, Commissioner Neelie Kroes therefore called for the need to reflect on "one stop shop" options for the handling of leniency issues within the ECN (4). She made it clear that such reflections should be guided by the need to fully exploit the dimension of the ECN.

Since then, a number of plausible "one stop leniency shop" options have been discussed (5). The option retained after these discussions has two main elements. The first is to harmonise those rules and procedures that could deter applicants from reporting cartels and thereby have an impact on the attractiveness and effectiveness of all EU leniency programmes. Secondly, introducing a uniform summary application filing system that will facilitate the task of applicants and authorities in those cases where the co-existence of different programmes may lead to inefficiencies. The tool through which this option should be realised is the ECN Model Leniency Programme (ECN Model Programme).

ECN Model Leniency Programme: purpose

The ECN Model Programme is the result of work carried out by a dedicated ECN working group during a 12 month period. The programme was unanimously endorsed by the heads of all com-

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) C. Gauer and M. Jaspers, The European Competition Network: Achievements and challenges — a case in point: leniency, CPN Spring 2006, p.8.

(3) An updated list of all ECN members that operate a leniency programme can be found on the ECN webpage (http://ec.europa.eu/comm/Competition/ecn/index_en.html). In 2002, only four Member States had a leniency policy in place. Five years later, that number has increased to currently 23, with ongoing reflections in a number of other Member States.

(4) See N. Kroes „The First Hundred Days 40th Anniversary of the Studienvereinigung Kartellrech 1965-2005" SPEECH/05/205, April 7, 2005.

(5) For an overview of the "one stop shop" options most commonly referred to and their assessment from an enforcer's perspective as well as more detailed information on the key provisions of the ECN Model Leniency Programme, see C.Gauer and M. Jaspers, Designing a European Solution for a „One-stop leniency shop", in ECLR issue 12, December 2006, p. 685.

petition authorities within the EU in a meeting on 29 September 2006 and made public the same day ([6]).

The purpose of the ECN Model Programme is to set out the basis for soft harmonisation of all European leniency programmes and to convince the few Member States that do not yet have a programme in place to adopt one. It is for each authority to implement and incorporate the provisions of the ECN Model Programme in its respective leniency programme. In order to achieve this objective, the ECN Model Programme has been drafted as a coherent programme, setting out all rules and conditions that the ECN members believe should be common in all EU leniency programmes. This clearly distinguishes the ECN Model Programme from efforts undertaken in other international fora to take stock of provisions that are common in successful leniency programmes and/or list a number of vaguely defined key elements that should ideally be included in a leniency programme. It is however not a programme under which an applicant can apply and does not create any rights or legitimate expectations in the relationship between an applicant and an authority.

The ECN Model Programme itself is accompanied by more detailed Explanatory Notes that provide useful guidance on the various provisions ([7]). The Commission (2002) Leniency Notice served as the basis for the discussions and drafting of the ECN Model Programme ([8]). The scope of the ECN Model Programme also mirrors that of the Commission; i.e. a corporate leniency policy limited to secret cartels ([9]).

([6]) Available at http://ec.europa.eu/competition/ecn/index_en.html together with a list of most frequently asked questions (MEMO/06/356). See also the press release issued by the Commission (IP/06/288) and press releases issued by the Office of Fair Trading and the French Conseil de la Concurrence the same day.

([7]) The Explanatory Notes are an integral part of the ECN Model Programme.

([8]) This did not prevent the working group from discussing issues that were either not included or regulated in a different way in the 2002 Leniency Notice, which is evident from the differences between the ECN Model Programme and the 2002 Leniency Notice. The discussions also included issues that exist under some programmes but which were disregarded for the ECN Model Programme, like Amnesty + provisions.

([9]) The ECN Model Programme does not cover sanctions against individuals, but does recommend that adequate protection from such sanctions needs to be provided by those authorities that can impose sanctions on individuals, in order not to undermine corporate leniency programmes. As concerns the scope of corporate leniency programmes, the ECN Model Programme explicitly states that vertical agreements and horizontal restrictions other than cartels are normally less difficult to detect and investigate and do therefore not require being dealt with under a leniency programme.

The ECN Model Programme does however not loose sight of what it intends to solve. It is not the intention to establish one common leniency programme. The intention is rather to ensure that applicants are not dissuaded from reporting cartels due to important discrepancies between the programmes or uncertainty concerning what information is needed and what is expected from them in terms of cooperation obligations etc.

That is the reason why some provisions are more detailed than others. It is clear that the focus of the project has been to improve the situation for immunity applicants, and in particular for those applicants that come forward before the authorities had sufficient information to start an investigation (in the Model Programme referred to as Type 1A).

Harmonised rules and standards

The ECN Model Programme contains detailed provisions on all issues where it was feared that discrepancies between the programmes might dissuade applicants from disclosing the existence of a cartel to any authority. This concerns the category of applicants that are to be excluded from immunity (due to the role they played in the cartel), the type of information an applicant should be prepared to provide in order to get immunity and the conditions it needs to satisfy in order to benefit from immunity. It also covers some procedural aspects where a stream-lined approach was regarded as useful, and in some aspects necessary, to achieve the objectives of the ECN Model Programme. This concerns notably the summary application system (see below) but also the existence of a marker system and of procedural steps aimed at increasing legal certainty, such as when and how the authorities take position on the application. The changes and clarifications made in the revised Commission Leniency Notice of December 2006 concerning immunity under point 8(a), termination and co-operation obligations for immunity and reduction of fines applicants as well as the introduction of a discretionary marker system reflect the orientations agreed under the ECN Model Programme ([10]).

([10]) This article will therefore not further address the policy choices made for these provisions. Reference is instead made to the article *"Commission adopts revised Leniency Notice to reward companies that report hard-core cartels"* published in this newsletter. To the extent that the Model Programme has taken over provisions and policy choices already existing in the COM 2002 Leniency Programme, reference is made to B. van Barlingen and M. Barennes, The European Commission's 2002 Leniency Notice in practice, CPN Autumn 2005, page 6.

The ECN Model Programme is less detailed on rules and procedures for “post-inspection” immunity applications (referred to as Type 1B) or reduction of fines applications (referred to as Type 2). The reason for this is two-fold. In the vast majority of cases, this type of applicants would only come forward after an investigation has started. The applicant will therefore know which authority is handling the case and will know what rules it has to comply with if it wants to benefit from that authority’s leniency programme. Secondly, if that authority has chosen a very strict policy for rewarding such “post-inspection” co-operation, this will (contrary to the “pre-inspection” scenario) not have a negative impact on other authorities’ programmes.

The ECN Model Programme does however contain two noteworthy provisions for these types of applications. The underlining principle behind both these provisions is to ensure that there should always be an incentive to approach the authority at a time when the cartel has not yet been uncovered. For immunity, the ECN Model Programme makes a distinction between the 1A and 1B threshold, thereby sending a clear signal that applicants have to be prepared that evidence that might have enabled them to obtain immunity in a Type 1A scenario would be far from sufficient to meet the Type 1B threshold ([11]). For reduction of fines applicants (Type 2), it states that the reward given for providing significant added value to the investigation should not exceed 50 percent. The purpose of this statement it to ensure that there is a significant gap between the reward to be given to immunity applicants and the reward to reduction of fines applicants ([12]).

The Model Programme only sets out the basis for minimal harmonisation. Each authority remains free to offer more favourable treatment to applicants if it considers it necessary in order to ensure efficient enforcement. It is not to be excluded that different incentives may be required to successfully break regional or national cartels compared to larger cartels. By creating a “common highest denominator standard”, the applicant will however know from the outset what it can expect in terms of evidentiary standard and cooperation obligations. The fact that it may in certain situations be rewarded on the basis of a less strict standard cannot be a detriment to either itself or to other competition authorities.

Summary applications

The summary application system is the mechanism through which the ECN members aim to reduce the administrative burden (for authorities and applicants) associated with multiple leniency filings. The underlying idea is to create a system that would fulfil this objective without jeopardizing the flexible and efficient work-sharing within the ECN. Rather than having to file complete leniency applications with all authorities that could take actions against the cartel, a summary application system allows the national competition authorities to temporarily protect the immunity applicant’s place in the queue on the basis of more limited information if a full application has been given to the Commission. The ECN Model Programme does not foresee a general summary application system for all types of cases. It only covers Type 1A applications (i.e. applications for immunity in situations where an investigation has not yet been started) for cases covering more than three Member States where a full application has been lodged with the Commission ([13]). This is the type of situation where the ECN members agree that the current system may lead to inefficiencies. The system chosen does not foresee that the Commission will accept summary applications. On the other hand, it does not exclude that certain competition authorities may accept summary applications in situations which are not explicitly mentioned.

The provisions concerning the filing and the processing of summary applications have been regulated in detail in the ECN Model Programme. This is in order to ensure that the system is implemented in a coherent and consistent manner. The Model Programme lists the information that should be given, which is equivalent to what would be required to secure a marker. The Model programme does not regulate in which form the application should be made, but does prescribe that such applications can always be made orally (irrespective of whether the national competition authority would accept oral applications in other scenarios). It also explains the type of reaction the applicant can expect from the national authorities. The idea is that the system should work as an indefinite marker. The national authority will not take position on the application, i.e. it will neither grant nor reject conditional immunity. It will simply confirm that the applicant is

([11]) See section III of the Model programme and point 18 of the Explanatory Notes.

([12]) See section IV of the Model Programme and point 24 of the Explanatory Notes.

([13]) Point 46 of the Explanatory Notes explains why Type 1B and Type 2 applications (i.e. immunity in a „post-inspection“ scenario and reduction of fines applications) were not included in the summary application system the first to file with that authority and that it will grant the applicant a period of time to complete its application should the national authority later decide to act on the case. As long as the applicant has not been informed that the authority intends to act, its duty to assist in the investigation only exists towards the Commission. The fact that the national authority has accepted the summary application does not create any legitimate expectations as to whether or not it would grant (conditional) immunity should it at a later stage deal with the case.

Status and implementation

By endorsing the ECN Model Programme, the heads of the EU authorities have entered into a political commitment vis-à-vis the other ECN members to ensure that the ECN Model Programme can achieve its intended result. The Commission was the first authority to take concrete actions to live up to this commitment, by announcing revisions to its 2002 Leniency Notice the very same day the ECN Model Programme was endorsed and published and by swiftly adopting the revisions needed to ensure that the Commission Leniency Notice fully reflects the ECN Model Programme ([14]). Other authorities are currently engaged in similar exercises. Those authorities that already have leniency programmes in place are undertaking what is required to ensure that their programmes are either revised or, as regards those programmes that are regulated in a less detailed way, applied in a manner that is in line with the ECN Model Programme. Those that are in the process of adopting new programmes have closely followed and benefited from the work behind the ECN Model Programme.

The ECN Model Programme foresees that the state of convergence is assessed in 2008. Taking into account that a large number of national competition authorities need the involvement of the national legislator in order to change (parts of) their leniency policy, this seems to be an adequate and realistic time-frame. The Commission and its colleagues in the ECN are however already closely monitoring one aspect of the ECN Model Programme, namely the introduction of a summary application system. In order to facilitate the work of potential immunity applicants, a list of all authorities that already today accept summary applications is listed on the ECN website ([15]). At the time of writing, 15 authorities now offer this possibility, including for example the United Kingdom, Germany, France and the Netherlands. As mentioned above, the summary application provisions have deliberately been drafted in a manner that would ensure that they can easily be incorporated in the national leniency programmes in a coherent way. It is interesting to see that the Office of Fair Trading, rather than copying the provisions into their programme, has chosen to make direct references to the ECN Model Programme ([16]).

Conclusions

A significant amount of convergence between the European leniency policies has already been achieved through the unique working methods resulting in the ECN Model Programme. Comments received in the context of the public consultation of the revised Commission Leniency Notice show that the ECN Model Programme has been received as a tool to interpret less specific provisions in individual programmes.

The next step is for the competition authorities to live up to their political commitment and align their respective programmes or introduce new programmes on the basis of the ECN Model Programme. This does not mean that one can expect a total uniform leniency policy within a foreseeable future. This is arguably also not necessary. It is for each authority to implement the programme in a manner that fits its own enforcement system. A harmonised leniency policy that ensures that immunity applicants know what they can expect from the different authorities in terms of the evidence to be provided and the cooperation and assistance they may have to give would be sufficient to remove the deficits of the current system. Should experience show that the ECN Model Programme will not achieve its intended result, it is not to be excluded that the Commission may choose to pursue more traditional harmonisation instruments.

(14) See the press release (IP/06/1705) and the Memo (MEMO/06/469) published by the Commission on 7 December 2006.

(15) Available at http://ec.europa.eu/comm/competition/ecn/index_en.html

(16) See "Leniency and no-action, OFT's draft final guidance note on the handling of applications", published for public comments in November 2006 and available at http://www.oft.gov.uk/NR/rdonlyres/85BD0E14-DDF2-4D42-805B-BD615D722BFB/0/oft803a.pdf.

Competition in Pharmaceuticals: the challenges ahead post AstraZeneca (1)

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1. Introduction

Traditionally, the Commission's anti-trust enforcement activity in the pharmaceutical sector has focused on removing private obstacles to parallel trade in pharmaceuticals within the Single Market. In the summer of 2005, however, the Commission adopted its first abuse of dominance decision in that sector (2). Since then, much has been happening in terms of anti-trust enforcement activity in pharmaceuticals at Community level. The time has come to take stock of the most recent developments post *AstraZeneca,* and to take a glimpse at some of the challenges ahead.

In the area of health care, the European Union ("EU") shares competence with its Member States who are responsible for the organisation and delivery of health services and medical care within their territories (3). In particular, this means that national pricing and re-imbursement rules for pharmaceuticals are not harmonised within the Single Market. Nevertheless, in carrying out their responsibilities, Member States and health care stakeholders such as national health services and pharmaceutical companies are bound to respect the EC Treaty rules on free competition and the free movement of goods and services within the internal market.

This is where the Community comes in notably the European Commission ("the Commission"). The Commission is responsible for ensuring compliance with these EC Treaty freedoms. The Commission's activities in this area are focused on two pillars: first enforcement action, and second advocacy. In this respect, the Community is no different from its other major trading partners such as the United States and Canada.

2. Enforcement action: A two pronged approach

Since *AstraZeneca,* the focus of competition policy enforcement action in pharmaceuticals in the EU has been twofold. First, there is the traditional focus on intra-brand competition, by going after barriers to parallel trade in pharmaceuticals within the Single Market. Second, the adoption of the *AstraZeneca* case has heralded a new era in the Commission's enforcement activities in pharmaceuticals aimed at promoting inter-brand competition by spurring on innovation between pharmaceutical producers and by increasing price competition stemming from generic entry after patent expiry.

(a) Intra-brand competition

On intra-brand competition, we are faced with two types of conduct by pharmaceutical companies to impede parallel trade within the Community. First, there are the so-called dual pricing schemes where companies seek to apply differential pricing depending on the destination of their supplies within the Community, thereby reducing the scope for arbitrage. Second, there are the so-called supply quota systems where companies restrict the quantities they supply wholesalers in each national market to meet local demand alone thereby reducing the quantities available for parallel exports.

Regarding dual pricing schemes, the Commission's decision in the *Glaxo Wellcome* case (4), condemned GSK's dual pricing scheme in Spain as contrary to Article 81(1) of EC Treaty and refused to grant an exemption under Article 81(3) of the

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(2) COMP/37.507 — Generics/Astra Zeneca, 15.06.2005. See also, "*AstraZeneca*: the first abuse case in the pharmaceutical sector." EC Competition Policy Newsletter, Number 3 — Autumn 2005, page 54.

(3) See Article 152(5) EC Treaty.

(4) Cases: IV/36.957/F3 *Glaxo Wellcome* (notification), IV/36.997/F3 *Aseprofar and Fedifar* (complaint), IV/37.121/F3 *Spain Pharma* (complaint), IV/37.138/F3 BAI (complaint), IV/37.380/F3 *EAEPC* (complaint), 8 May 2001, OJ [2001] L 302/1.

EC Treaty. The Commission's approach is predicated by two principles (5):

- The Single Market in pharmaceuticals requires the unhindered free movement of products — private companies cannot erect barriers to undermine this without distorting intra-brand competition.
- The efficiency claims advanced by the research based pharmaceutical industry is unsubstantiated — i.e. there is no evidence that partitioning the common market would spur on global investment in inter-brand innovation.

On 27 September 2006, the Court of First Instance ("CFI") delivered its long awaited judgment in the *GlaxoSmithKline* case (6), partially annulling the Commission's decision in the *Glaxo Wellcome* case. The GSK case is currently pending on appeal before the European Court of Justice ("ECJ"). It was appealed by all parties including the Commission in December 2006. Such multiple appeals may be expected to arose judicial interest and consequently receive its fair share of scrutiny by the ECJ (7).

Regarding supply quota systems, on 21 November 2006, the Athens Appeals Court (AAC) referred a number of questions in several civil cases pending before it, brought by Greek wholesalers against GSK, to the ECJ, the so-called *Syfait II* preliminary reference (8). The questions referred are more or less identical to those referred to the ECJ by the Greek competition authority in the *Syfait I* case (9).

In essence, the AAC is asking the ECJ to rule on whether the refusal of a dominant undertaking to meet fully the orders sent to it by pharmaceutical wholesalers, an association of pharmacies and an association of warehousing pharmaceutical products, due to its intention to limit their export activity and, thereby, the harm caused to it by parallel trade, constitutes *per se* an abuse within the meaning of Article 82 EC Treaty (10). The AAC asks *inter alia* if such refusal to supply may be an abuse even when parallel trade is particularly profitable for the wholesalers due to price difference, resulting from Member State intervention, that is to say where pure conditions of competition do not prevail in the pharmaceuticals market.

The Commission intervened before the ECJ in the *Syfait I* case and may be expected to do the same in the *Syfait II* preliminary reference. In his Opinion in the *Syfait I* case, Advocate General Jacobs summarised the Commission's position as follows: (11)

"… a restriction of supply is abusive unless the dominant undertaking can point to an appropriate and sufficiently substantial objective justification for its conduct. … [none] of the factors identified by the Greek Competition Commission could be relevant for the purpose of such a justification.

The European Commission supports its conclusion partly on the basis of the anti-competitive character of the conduct in question. A dominant undertaking is understood to abuse its position when it refuses to supply its goods and services with the aim of limiting or excluding actual or potential competitors from a given market and of reinforcing its position on that market. Given that any attempt by a producer to restrict supply in order to limit parallel trade is usually motivated by a concern to restrict intra-brand competition on the market of import, such a restriction is normally to be regarded as abusive. Partly, also, the Commission relies upon the market-partitioning object of the conduct at issue. The Court has consistently interpreted Articles 81 and 82 EC as prohibiting conduct aimed at dividing the common market."

Thus, in the last months of 2006, the ECJ was seized of two cases on parallel imports: one involving the applicability of Article 81 of the EC Treaty to dual pricing schemes and the other invoking the applicability of Article 82 of the EC Treaty to supply quota systems. Such timing means that the long standing debate on whether parallel trade in pharmaceuticals affects innovation or is pro-competitive and an important factor in market integration, is now firmly before the ECJ.

(5) On the pros and cons of parallel trade from an economic perspective, see in particular, "Parallel imports and price controls" by Gene M. Grossman and Edwin L.-C. Lai, CEPR Discussion Paper No. 5779, August 2006; "The economic impact of parallel imports of pharmaceuticals" by Ulrika Enemark, Kjeld Møller Pedersen, Jan Sørensen, June 2006, CAST and University of Southern Denmark; and "Pharmaceutical parallel trade in Europe: stakeholder and competition effects" by Panos Kanavos and Joan Costa-Font, Economic Policy October 2005 pp. 751–798.

(6) Case T-168/01 *GalxoSmithKline v Commission,* judgment of 27 September 2006. For commentary on the judgment see "Parallel Exports in the Pharmaceuticals Sector: Take Nothing For Granted", Richard Eccles, [2007] ECLR 134.

(7) See Case C-501/06 P before the ECJ.

(8) See Cases C-468-478 *Sot. Lelos kai Sia EE & Others v GlaxoSmithKline,* OJ [2007] C20/03-13.

(9) See Case C-53/03 Syfait & Others v Glaxosmithkline, opinion of Advocate General Jacobs 28 October 2004 and judgment of the ECJ of 31 May 2005.

(10) See further "An analysis of the application of Article 82 EC to supply-restrictions in the pharmaceutical sector", September 2005, EAEPC.

(11) See Case C-53/03 *Syfait & Others v Glaxosmithkline,* opinion of Advocate General Jacobs 28 October 2004, paragraphs 49 and 50.

(b) *Inter-brand competition*

As the much contested and long debated issues surrounding parallel trade in pharmaceuticals were making their way to the Community's highest judicial instance, the Commission's enforcement efforts have been focused on promoting inter-brand competition.

In 2005 the Commission adopted the *AstraZeneca* decision on inter-brand competition. AstraZeneca was fined for abusing its dominant position by misusing the Community rules for the grant of supplementary patent certificates and marketing authorisations to delay generic entry of its ulcer treatment drug Losec.

The *AstraZeneca* decision is currently under appeal to the CFI where the Commission is actively defending its decision and would naturally hope to prevail ([12]).

Since the adoption of the *AstraZeneca* decision, Commissioner Neelie Kroes explained to the European Parliament ("EP") in response to an oral question in the summer of 2006 ([13]), that the aim here is *"to promote competition in innovation for patented medicines between the pharmaceutical producers, which has declined in Europe in the last decade, and to encourage inter-brand competition from generic substitutes after patent expiry"*. Commissioner Kroes emphasised that this should *"in time, contribute to ensuring a wider choice of both patented and generic pharmaceutical products to European patients at affordable prices"*. Commissioner Kroes also stressed that the Commission will take due account *"of the need for the industry to recover its research and development costs, given the industry's heavy dependence on innovation for its further competitiveness."* Commissioner Kroes assured the EP that the Commission was *"not circumspect about rigorously applying the anti-monopoly provisions in the pharmaceutical sector, for generic competition is an area which has suffered from under-enforcement in the past."* Especially since, as Commissioner Kroes pointed out *"the importance of the generic segment for the provision of affordable medicines in the enlarged Union cannot be ignored."* Commissioner Kroes summed up that this was why *"the Commission will give greater priority to competition in the generic sector in the immediate future."*

In doing so, the Commission will likely continue to build on the experience gained from the adoption of the *AstraZeneca* decision, and tackle various types of life cycle management strategies by research based pharmaceutical companies aimed at raising rivals' entry barriers, thereby dampening inter-brand competition. It may also be expected that current enforcement activities would contribute to the Lisbon Agenda by stimulating innovation in the pharmaceutical sector whilst delivering on cost-containment through generic competition.

3. The importance from a competition policy standpoint of inter-brand competition in pharmaceuticals

Commissioner Kroes' announced focus on enforcement action aimed at inter-brand competition reflects the importance of that topic from a competition policy — and from a broader economic policy — standpoint.

(a) *The importance and specific features of the pharmaceutical sector*

The pharmaceutical sector is a knowledge-based manufacturing industry and an important part of the health care sector. In the past decade, the health care sector has created millions of new jobs. It employs 10% of the active EU population. As life expectancy of EU citizens is steadily rising, the health-care related economy has a strong growth potential with the greying of Europe, and the increasing demand for medicinal products.

The industry is characterised by players of a different nature: a limited number of R&D based multinationals and an increasing number of niche innovative small and medium sized enterprises ("SMEs"), as well as generic producers which compete with medicinal products for which patent protection has expired. The industry has been undergoing a concentration process concerning mainly R&D based multinationals. However, a recent trend might have started with the multinational Novartis taking over the generic producer Hexal ([14]).

The research based pharmaceutical producers attempt to out compete each other on innovation, as demand for innovative products is relatively inelastic allowing for high prices. As patent term expiry approaches, companies are increasingly confronted with the prospect of competition from generic equivalents with significantly lower price levels, the race to innovate and migrate the patient population to the next generation medicinal products intensifies.

([12]) See Case T-321/05 *AstraZeneca AB & AstraZeneca plc v Commission*, 2005/C 271/47.

([13]) Commissioner Neelie Kroes' reply to Oral Question put by the honourable Member of the European Parliament Mr von Boguslaw Sonik, (H-0459/06).

([14]) See Case M.3751 Novartis/Hexal.

Focussing enforcement activities on inter-brand competition means dealing with elements exercising direct pressure on competitors' prices. Such action has the potential to yield significant welfare enhancing effects. This is all the more so in the EU-27, in view of the importance of the affordability of medicines for the EU-12.

Obstacles to the entry of innovative medicinal products and generics may pose competition problems for example when, in order to maintain its market power, a dominant undertaking strategically uses patent procedures. Such strategic use raise additional barriers to entry, for which little economic justification but for the maintenance of market power is likely to exist, and are often coupled with the dominant undertaking's effective threat of vexatious litigation. As a result, such behaviour often deny patients the use of better, more and cheaper medicinal products, because the incumbent's strategy aims at prolonging the product-life cycle of its product rather than competing with innovative new medicinal products and generics.

The risks that such behaviour cause to patients and to the economy is all the more acute, since the current cycle of the pharmaceutical industry is characterised by dwindling R&D pipelines coupled with increasing numbers of medicinal products approaching patent expiry.

(b) Competitiveness in the pharmaceutical sector

The Commission's selection of competition law enforcement priorities is only one aspect of the Commission's initiatives, aimed at enhancing the competitiveness of the EU pharmaceutical sector and at creating welfare benefits in Europe. By way of illustration, the Recommendations of the High Level Group on Innovation and Provision of Medicines (the so-called "G10 Medicines Group") *inter alia* identified that full competition should take place (through generics and for non-reimbursed medicines). The G10 Medicines Group Recommendations have led to an overreaching review of the EU's pharmaceutical legislation (the so-called "Pharmaceutical Review") managed by the Commission's Directorate-General Enterprise. The Pharmaceutical Review (2000-2004) aims to improve market access for innovative medicines and to deliver a competitive generic market. MEMO/05/186.

Work is currently on-going on the potential for convergence of national pricing and reimbursement schemes. This is taking place within the Pharmaceutical Forum (2005-2008), which is a collaborative effort between Directorate-General Enterprise and Directorate-General Health and Consumer Protection. One of the aims of the Pharmaceutical Forum is to find alternative ways of controlling national health care expenditures including the option of letting manufacturers set the prices of new products, while negotiating appropriate safeguard mechanisms for Member States to contain expenditure in compliance with EU competition rules IP/06/1282. Competition law enforcement action that protects inter-brand competition between generics and patented drugs, such as the *AstraZeneca* decision, has the potential of contributing to important savings for national health care systems: for example, the introduction of generics can lead to the increased availability of more affordable alternatives to patented branded pharmaceutical products — usually in the region of 20-50%, but possibly up to 80%, cheaper.

Competition law enforcement has also a major contribution to make to promoting more innovation in pharmaceuticals. In the early 1990s, the European pharmaceutical industry was the leader in innovation on a world-wide scale. Today, the US pharmaceutical industry has become the leading inventor of new active ingredients. In particular, the EU-based R&D has been moving to the US at a time when the EU will be facing new challenges from India and China. A particular attention must thus be given to deterring behaviour that stifles innovation — such as abuses of dominance that fend off small, innovative SMEs. A stronger competitive constraint on "old" block-busters will also provide additional incentives to pharmaceutical companies to develop new products through efficient and timely R&D programmes rather than resting on their laurels, and focussing their energy on the preservation of the rents based on past R&D efforts.

4. The need for Community-wide collaboration and advocacy

Article 152(2) of the EC Treaty provides that:

"The Community shall encourage cooperation between the Member States in [public health] …. and, if necessary, lend support to their action. Member States shall, in liaison with the Commission, coordinate among themselves their policies and programmes in [public health]. The Commission may, in close contact with the Member States, take any useful initiative to promote such coordination."

In the area of competition policy, since the entry into force of Regulation 1/2003 and the package for the modernisation of the Community's framework for the enforcement of Articles 81 and 82 of the EC Treaty, on 1 May 2004, a network of proactive public enforcers made up of the national competition authorities ("NCAs") of the Member States, otherwise known as European Competition Network ("ECN") has been set up.

The ECN provides a framework for applying and developing the EC anti-trust rules. It does so through work-sharing and case-allocation between NCAs and the Commission; as well as through joint action and assistance in fact-findings and investigations. Just as importantly, it also promotes the exchange of information and sharing of experiences both in terms of cases and policy. By doing so it provides a forum to foster the development of a common competition culture within the ECN.

To enhance the effectiveness of the ECN, a number of Working Groups have been set up, some deal with horizontal issues such as leniency and abuse of dominance whilst others have a sectoral focus. In 2005 the ECN Pharmaceuticals Sub-group was established. It is made up of the NCAs of the Member States and the Commission.

The initiative was highly welcomed as it was anticipated that it would help all those concerned in learning from the experiences of the other members of the network. In time it is hoped that it will prove to be a valuable vehicle to support its members' enforcement and advocacy efforts in the pharmaceutical sector. At the very least, it may be expected to foster a culture of finding common solutions to shared problems in the enforcement of the EC anti-trust rules in the pharmaceuticals sector. The purpose of the ECN Pharmaceuticals Sub-group is to harness the collective expertise of the ECN to deliver not only better and consistent competition enforcement throughout the EU, but also to assist the Member States in their own advocacy efforts aimed at injecting more competition into their respective health care sector.

Typically, this involves the reforming of the national regulatory framework for the provision of medical care, by introducing greater inter-play of market forces, based on patient/practitioner choice, value for money, the rational distribution of medicines and services and the availability of greater information on the different products and services. The ECN Pharmaceuticals Sub-group aims to harness this process by providing a focal point for the sharing of the different experiences, processes, tools and analytical frameworks applied throughout its Member States.

Such a coordinated approach is all the more important in public health where responsibility for the achievement of the primary objective of delivering *"high level of human health protection"* ([15]) for Europe's citizens is split not only between the Community institutions and its Member States, but necessitates that orchestration of different Community and national policy areas of which competition policy forms one part.

In such circumstances, competition enforcement action alone constitutes a partial response to the competition policy challenges facing the Community in the pharmaceutical sector. To deal with these challenges in a credible and sustainable manner, attention must also be given to advocacy, policy screening and reflection initiatives aimed at delivering an analytical framework for promoting an environment for the rational and efficient allocation of resources in the pharmaceutical sector, based on informed consumer choice and transparency.

The ECN Pharmaceuticals Sub-group provides an important vehicle for the dissemination of such analytical tools thus empowering its members in turn to harness the efficiency gains and associated cost savings that may be derived from the injection of greater competition in the delivery of pharmaceuticals to European patients.

5. Conclusion

It would seem that interesting times lie ahead in terms of competition policy enforcement and advocacy in the pharmaceutical sector.

At the very least, the Commission's past focus on intra-brand competition may be expected to be complemented by a more nuanced multi-faceted approach aimed at inter-brand competition to deliver enhanced consumer welfare in medicines to patients throughout the EU.

The greater emphasis placed on advocating competition based market led solutions to the address challenges facing the EU in delivering innovative yet affordable pharmaceuticals to European patients may in time be expected to empower the EU to reap dividends in this area.

However, doing so will require steady and sustained efforts from all those concerned within the EU to work together and stay the course.

([15]) See Article 152(1) EC Treaty.

State aid for films — a policy in motion? ([1])

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In late 2006, the Commission approved the new UK and German film support schemes. This article explains the application of the State aid rules in these two cases, in particular in view of the recent trends such as the global competition to attract large budget films. It also considers the future perspectives of the Commission's State aid policy in this field.

US productions generally dominate European screens. It is commonly believed that, in the absence of public support to film production in most Member States, most European productions would already have disappeared. In the four years 2002-2005, they provided over € 6.5 billion of State aid for film production ([2]), which helped to produce over 3,600 films. France provides the highest overall amounts of State aid for films, followed by the UK, Germany, Italy and Spain, Public support in these five countries is accounting for 83% of the total. According to the European Audiovisual Observatory, there are over 600 film support schemes operating across the EU.

Legal basis for State aid control

Cinema and TV production support mechanisms are assessed on the basis of Article 87(3)(d) EC which was introduced by the Maastricht Treaty. This provision specifically deals with State resources being dedicated to culture. Following this provision "*aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest, may be considered to be compatible with the common market*". Since the introduction of this article into the Treaty, it is clear that, in principle, culture is not excluded from the application of the Community State aid discipline ([3]).

In 2001, based on its experience of assessing various national film support schemes and particularly the French system, the Commission published a Communication setting out the conditions for the application of Article 87 (3)(d) ([4]) to the production of "*cinematographic and other audiovisual works,* (the 'Cinema Communication'). This Communication requires the so-called general legality principle to be respected and sets out four additional specific compatibility criteria according to which aid for cinema and TV production can be approved as cultural aid under the exception in Article 87(3)(d) EC:

([1]) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

([2]) Copenhagen Think Tank / European Audiovisual Observatory:
http://www.dfi.dk/NR/rdonlyres/1BE19F2D-F61F-403F-934C-B0AB2447D9D8/0/CTT_Information_Notes_300606.pdf

([3]) The issue of whether or not the Treaty, and hence State aid rules, is applicable to culture at all has been settled a long time ago. Already in one of its early cases, the Court of Justice dismissed the argument that the Treaty was an economic Treaty and would not apply to cultural goods (case 7/68 Commission v Italy [1968] ECR 617). Moreover, despite the fact that prior to the introduction of Article 87(3)(d) EC, it was a frequent assumption that culture in general should be exempted from the application of State aid rules, the Commission actually examined and approved a range of aid mechanisms for culture under Article 87(3)(c) EC, including aid to the audiovisual sector. See also Rapport présenté par la Commission au Conseil sur la prise en compte des aspects culturels dans l'action de la Communauté européenne of 17. 4.1996, COM(1996) 160 final, page 22.

([4]) Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions on certain legal aspects relating to cinematographic and other audiovisual works (COM(2001)534 final of 26.09.2001,OJ C 43 of 16.2.2002); prolonged by Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions on the follow-up of the Commission communication on certain legal aspects relating to cinematographic and other audiovisual works of 26.09.2001 (COM(2004)171 final of 16.3.2004, OJ C 123 of 30 April 2004.

a) The general legality principle

The general legality principle is essentially enshrining into the Cinema Communication the established case law according to which State aid incorporating conditions which contravene other provisions of the Treaty cannot be approved by the Commission ([5]). For example the benefit of aid schemes cannot be restricted on the basis of nationality. Also, schemes of aid to cinema and TV production financed by parafiscal charges are incompatible with the Treaty when such schemes benefit solely national producers.

b) Aid must benefit a cultural product

The aid must be directed at a cultural product. Each Member State must ensure that the content of the aided production is cultural according to verifiable national criteria (in compliance with the application of the subsidiarity principle). Therefore, the Commission does not assess what is culture and what is not. The Commission only verifies that the national authorities have drawn up a verifiable selection system which ensures that only cultural products, as defined by the national authorities, will benefit from the aid. It is only where the Commission considers that there is a manifest error in the definition of the cultural products concerned that the Commission might question the substance of the cultural definition.

c) Territorialisation

This criterion foresees that the producer must be free to spend at least 20 per cent of the film budget in other Member States without suffering any reduction in the aid provided for under the scheme (so-called territorial conditions).

d) Aid intensity

The aid intensity must in principle be limited to 50 per cent of the production budget with a view to stimulating normal commercial initiatives inherent in a market economy and avoiding a bidding contest between Member States. Difficult and low budget films are excluded from this limit. Under the subsidiarity principle it is up to each Member State to establish a definition of difficult and low budget film according to national parameters. For example, a derogation might be granted for works in a language which is not widely spoken.

([5]) Case 73/79 Commission v Italy [1980] ECR 1533, paragraph 11; Case C-225/91 Matra v Commission [1993] ECR I-3203, paragraph 41; Case C-156/98 *Germany v Commission* [2000] ECR I-6857, paragraph 78.

e) Aid supplements

Finally, the last criterion stipulates that aid supplements for specific film-making activities (e.g. post-production) are not allowed in order to ensure that the aid has a neutral incentive effect and consequently that the protection/attraction of those specific activities in/to the Member State granting the aid is avoided.

It should be noted that the Cinema Communication only refers to the production of films. In its more recent Decisions the Commission applied the Communication by analogy also to the development of film projects, including the writing of screenplays ([6]), as well as to the promotion and distribution ([7]) of films. This approach is motivated by the idea that these activities are so closely linked to the production of films that the principles developed in the Communication are also applicable to them ([8]).

While the Commission's approach in assessing these criteria has not significantly changed over the 5 years since the Communication was first published, various new trends have emerged in the funding policies applied across the EU.

Films as cultural goods

In the past, State aid for the film industry was mainly given in order to promote a 'national cultural film industry' and it is against this background that the current rules were drafted. One recent trend however has been the global incentive 'war' to attract large budget films. Two analyses, one for the UK ([9]) and one for

([6]) For example State aid N 181/2004 — Germany, *Förderung von Film- und Fernsehproduktionen in Baden-Württemberg: Medien- und Filmgesellschaft Baden-Württemberg mbH.* http://europa.eu.int/comm/secretariat_general/sgb/state_aids/comp-2004/n181-04.pdf.

([7]) For example State aid N 368/2005 — Spain, *Ayudas a la promoción de obras audiovisuales por Andalucía,* http://europa.eu.int/comm/secretariat_general/sgb/state_aids/comp-2005/n368-05.pdf .

([8]) On the other hand, measures favouring activities not linked to the production of films have been assessed under Article 87(3)(d) EC directly. Furthermore, undertakings in the film and television programme production sector may, depending on the circumstances, also benefit from other aid types granted under national horizontal aid schemes, not aimed directly at cultural activities, but more widely at assisting types of economic activities or regions which happen to also encompass undertakings in the audiovisual sectors (e.g. regional aid, aid for small and medium sized enterprises (SMEs), research and development aid, training aid, employment aid).

([9]) *The economic contribution of the UK film industry* published by Oxford Economic Forecasting, supported by the UK Film Council and Pinewood Shepperton plc, September 2005: http://www.ukfilmcouncil.org.uk/get/?doc=117

California (10) illustrate the economic advantages of attracting and the costs of losing large budget films, respectively. The first analysis concluded that the UK film industry contributed £3.1 billion (EUR 4.5 billion) to UK GDP in 2004. Both analyses stress that this is a highly mobile industry and the Californian analysis begins by noting that "… *a growing number of states and countries have recognized the value of employment and government tax revenues generated by film and television production and are aggressively courting the business with tax credits and other enticements. … [They] have started building their own studio facilities, launched training programs for their residents, and implemented relocation and outreach programs for experienced non-residents. The result has been to create real competition for motion picture production.*"

In view of the fact that the attraction of (foreign) film productions to a certain national territory is driven often by more economic than by cultural considerations, and that these film productions would sometimes receive considerable financial support, the Commission has to ask itself whether the schemes it assesses meet the cultural condition for the application of the cultural derogation. It is for the Member States to define the concept of culture, albeit along the lines of the Cinema Communication, i.e. that *"Each Member State must ensure that the content of the aided production is cultural according to verifiable national criteria"*. The Commission shall thus ensure that the Member States have not committed a manifest error in defining the cultural purpose of their schemes, and that the criteria they have established ensure that this goal will be met. In any event, since the Cinema Communication is based on Article 87(3)(d) EC, any aid that could not be argued to go to cultural activities, cannot be declared compatible with this Communication.

It is in this perspective that the Commission examined the new £ 120 million per year UK and EUR 60 million per year German film schemes at the end of 2006. These schemes apply both points-based cultural tests as part of their eligibility criteria, which were closely analysed by the Commission to see whether they effectively ensure that the aid is directed towards a cultural product. In fact, the approval of the UK film tax incentive (11) was based on a revised UK Cultural Test submitted by the UK authorities in November 2006, rather than on the original UK Cultural Test which they had notified to the Commission.

UK film tax incentive

In the UK film tax incentive case, the aid takes the form of an enhanced tax deduction and a payable film tax credit. The enhanced tax deduction allows a film production company to benefit from a higher deduction for certain production costs than the normal UK tax rules would allow. The payable film tax credit allows the film production company to receive a cash payment of up to 25% of any tax loss.

To select the eligible films, the UK authorities have drawn up a point-based test called the UK Cultural test. The original UK Cultural Test was divided into three sections, two of which referred to certain technical costs (such as studios and visual effets) and the geographic origin of certain categories of cast members. In view of this, only the criteria in the first section of the original UK Cultural Test could be used to ensure that the aid was directed towards a cultural product. However, the first section only accounted for 4 points out of 32 (one of which for the use of English in the film's dialogue). A film could achieve the pass mark of 16 points without picking up any of the points in this section. It therefore was not clear that the original UK Cultural Test would always ensure that the aid would be directed towards a culturally British product.

The revised UK Cultural Test which has subsequently been included in the relevant legislation is substantially different from the original UK Cultural Test:

Section	Revised UK Cultural Test		Original UK Cultural Test	
A — Cultural content	16	52%	4	12%
B — Cultural contribution	4	13%	0	0%
C — Cultural hubs	3	10%	15	47%
D — Cultural practitioners	8	26%	13	41%
Overall maximum	31	100%	32	100%

The Cultural content section comprises four criteria: extent to which the film is set in the UK; what proportion of the main characters are British citizens or residents; whether or not the subject matter or underlying material of the film is British; and extent to which the original dialogue is in English. The new Cultural contribution section comprises three criteria: cultural diversity, cultural heritage and cultural creativity. These

(10) What is the cost of run-away production? Jobs, Wages, Economic Output and State Tax Revenue at Risk When Motion Picture Productions Leave California published by the California Film Commission and the Los Angeles Economic Development Corporation, August 2005: http://www.film.ca.gov/ttca/pdfs/link_overview/cfc/California_Film_Commission_Study.pdf

(11) http://ec.europa.eu/comm/competition/state_aid/register/ii/by_case_nr_n2005_450.html#461

two sections account for 65% of the overall points available (20 out of 31 points). Therefore a film satisfying only these two sections could achieve the 16 points required to pass the test.

In addition, in case of the extreme scenarios of a film obtaining most if not all of the 11 points in Sections C and D and all the four points for the use of English, (as English is widely spoken internationally, it could be argued that the use of English in a film's original dialogue would not necessarily guarantee that the film would be culturally British), a film could not pass the test without fulfilling at least one additional cultural criterion from the first two sections. The Commission therefore concluded that the revised UK Cultural Test ensures that the content of this film could reasonably be found to be cultural, according to the UK definition.

German Film Fund

The new German Film Fund, also approved by the Commission at the end of 2006,12 represents a different model both in its form and in its definition of cultural content. From the point of view of its form, it is a selective scheme which awards direct grants. Moreover, there is a maximum financial limit to the grant available per film, which is as a rule, EUR 4 million, or up to 10 million in exceptional cases. These characteristics make it already inherently less attractive for large budget films than the UK scheme.

In addition, the eligibility test designed by the German authorities respectively for feature films, documentaries and animation films focus not only on German, but also on European cultural content and contain specific criteria for films promoting universal cultural heritage. This test include three different parts: *"cultural content"*, *"creative talents"* and *"production"*, each of which is attributed a number of points..

The *"cultural content"* part contains a number of criteria, including the following:

- Content, motives, film locations, principal characters, storyline are from Germany, the German culture or language area or from Europe or the EEA,
- One of the final versions of the film is in German,
- The film is an adaptation of a literary work or originates from traditional fairy tales or legends,
- The film is about artists, art genres, significant personalities, historical achievements, religious or philosophical questions, issues of socio-cultural relevance, way of living of people and minorities, scientific issues,
- In the case of animation films, the storyline is meant and appropriate for children's or youth film
- The film is made with the contribution of a contemporary artist.

The *"production"* part clearly relates to commercial aspects and attributes points based on the production phases carried out in Germany. The part on *"creative talents"* reflects the participation of creative talents from Germany or the EEA.

In order to qualify for the aid, a film has to first fulfil a minimum number of criteria in the *"cultural content"* part (the "pre-test") (this number varies according to the type of production). Additionally, the candidate film has to achieve a minimum score of the total points available in the test.

In its assessment, the Commission examined in detail the different criteria proposed by the German authorities, the structure of the tests as well as the individual points attributed to the different aspects. Taking into account the pre-test specifically designed to ensure the cultural content of the films financed under the scheme and the truly cultural character of the criteria in the *"cultural content"* part of the tests, the Commission came to the conclusion that aid is indeed directed towards a product with cultural content. In this case, the relevant criteria aimed either at supporting German culture (eg, content, motives, film locations, principal characters, storyline/artworks from the German culture, the German language requirement, etc.), or promoting European culture (eg, European content and motives, film location or principal character), or strengthening cultural heritage in the general sense (eg, adaptations of literary works, films about artists, art genres, significant personalities, historical achievements, etc.).

Extended outlook and the question of territorial conditions

As explained above, the new UK and German schemes were, like any other audiovisual and TV production support system, assessed on the basis of the Cinema Communication. This Communication will expire on 30 June 2007. The Commission had announced that *"in advance of the next review of the Communication, the Commission intends, in addition to further analysing the*

(12) http://ec.europa.eu/comm/competition/state_aid/register/ii/by_case_nr_n2006_690.html#695

arguments of the sector, to carry out an extensive study on the effects of the existing State aid systems. The study should examine in particular the economic and cultural impact of the territorialisation requirements imposed by Member States, in particular taking into account their impact on co-productions." ([13]) This study was launched in August 2006 and is expected to be completed in autumn 2007. The preliminary results will be discussed at a workshop in summer 2007 to which stakeholders such as funding bodies, film producers, exhibitors and distributors will be invited. In order to allow time to complete the study and the subsequent review of the Communication, the Commission will continue to apply the rules of the current Communication until such time as new rules come into effect, or, at the latest, until 31 December 2009. The current Cinema Communication will be prolonged accordingly.

Territorial conditions, which require that a proportion of the film production expenditure is incurred in the territory providing the aid will thus be among the central issues of the review. As noted above, the relevant criterion in the current Communication is that film producers must be able to spend at least 20% of the film budget in other Member States without suffering a reduction in the aid provided for under the scheme. In other words, the Commission accepts that territorial conditions may require expenditure of up to 80% of the production budget of an aided work to be spent in the territory providing the aid.

On the one hand, such conditions may be justified to ensure the continued presence of human skills and technical expertise required for cultural creation. On the other hand, the clauses obliging producers to spend a considerable amount of the film budget in the territory offering the aid are likely to constitute a barrier to the free circulation of workers, goods and services across the European Union. They may also strengthen the fragmentation of the European film sector and some film producers have called for territorial conditions to be removed. Finally it is not at all clear why certain cost categories should be considered to have to have an impact on the expertise needed for cultural creation: for example costs for catering are often considered to be part of the film production budget, hence are subject to territorial conditions.

Indeed, the Communication also states that territorialisation requirements must be limited to the minimum degree required to promote cultural objectives. The maximum territorial requirement of 80% was set in 2001 when few Member States imposed territoriality requirements in order to qualify for aid. However, the recent trend has been for most new schemes to apply territorial conditions and to set them at or close to this limit, as in the UK film tax incentive scheme and the German Film Fund.

In this context, the question arises to what extent should the cultural derogation in Article 87(3)(d) EC allow the Member States to support their 'national cultural industries' to the detriment, for instance, of the Treaty's fundamental freedoms. This question goes to the heart of the relationship between 'culture' as a nationally defined concept and the internal market freedoms. To strike the right balance between these two elements, the new rules that the Commission will adopt will have to consider these issues as reflected in the results of the study concerning territorialisation. The review of the Communication could also take account of other recent trends affecting the sector. These include the growing number of State aid schemes offering aid for aspects such as film distribution and development, the global incentive 'war' to attract large-budget productions, and investment in digital distribution/projection facilities. The Commission will aim at ensuring that its policy is suited to the current environment of the sector.

([13]) Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions on the follow-up of the Commission communication on certain legal aspects relating to cinematographic and other audiovisual works of 26.09.2001 (COM(2004)171 final of 16.3.2004, OJ C 123 of 30 April 2004.

Solving problems at the sources: why telecommunications regulation should focus on wholesale, not on retail, markets [1]

Iratxe GURPEGUI and Przemyslaw KORDASIEWICZ, Directorate-General for Competition, unit C-1

In this article we discuss the key role of wholesale markets (as opposed to retail markets) in the telecommunication sector's regulatory framework. Firstly, we describe the general principles with regard to remedies imposed *ex-ante* in the telecommunication sector. Then, we explain the focus on wholesale regulation in the current regulatory framework and compare it with the proposed new framework. Finally, we provide a practical illustration of the difficulties raised by retail-level regulation, in relation to two recent cases under the Article 7 consultation mechanism.

Introduction

The Regulatory Framework for Telecommunications of 2003 [2] ("2003 Framework") introduced significant changes to the scope and role of *ex-ante* sector specific regulation for the telecommunication industry. The 2003 Framework provides for an *ex-ante* regulatory approach which is based on concepts and principles of competition law. Namely, it requires that the definition of relevant markets and the assessment of significant market power ("SMP") is done in line with competition law principles.

The objective of the 2003 Framework is to create — through regulation — the conditions for effective competition in the telecommunication markets and once effective competition exists, to withdraw all unnecessary sector–specific regulation and apply the general competition rules only.

In line with the above, the Commission proposed in June 2006 a review of the 2003 Framework [3] ("2006 Review") which encourages further deregulation of the sector, leaving large parts of the industry to be governed by competition law only. However, where regulation can not be rolled back entirely, the Commission is of the view that regulation should still occur, but just at the highest possible level of the value chain in order to let competition develop as much as possible in downstream markets.

Focus on wholesale regulation under the 2003 Framework

The 2003 Framework requires National Regulatory Authorities ("NRAs") to ensure that the obligations imposed on operators with significant market power ("SMP") are based on the nature of the problem identified and are proportionate in the light of the objectives specified in Article 8 of the Framework Directive [4]. According to ECJ case-law, a measure is proportionate where it represents the minimum necessary intervention required to achieve a particular aim [5]. Where there is a choice of several appropriate means to achieve a desired result, NRAs are bound to apply the least burdensome remedy which would solve the identified problem [6]. Typically, most of the problems observed on retail markets in the telecommunications sector may be remedied by appropriate remedies imposed at wholesale level [7].

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) The Regulatory Framework consists of the Framework Directive 2002/21/EC and four specific Directives: the Authorisation Directive 2002/20/EC, the Access Directive 2002/19/EC, the Universal Service Directive 2002/22/EC and the Data Protection Directive 2002/58/EC.

(3) The package published in June 2006 includes: (a) a Commission Communication that reports on the functioning of the current regulatory framework and that identifies areas for change; (b) a Commission Staff Working Document in which concrete amendments to the framework are proposed; (c) and Impact Assessment Report on those proposals; and finally (d) a Commission Staff Working Document containing a draft revised Commission Recommendation on relevant product and service markets susceptible to *ex-ante* regulation.

(4) Article 8 of the Framework directive; Article 17.2 of the Universal Service Directive; and Recital 15 and Article 8.4 of the Access Directive.

(5) Case C-331/88; *Fedesa and Others,* ECR I-4023.

(6) Revised ERG Common Position on Remedies ERG (06) 33, p. 55-56.

(7) There may still be a need for combating any remaining anticompetitive issues by the application of ex post antitrust rules.

The focus on wholesale regulation may also be found in the Universal Service Directive. This Directive clearly states that "regulatory controls on retail services should only be imposed where NRAs consider that relevant wholesale measures or measures regarding carrier selection or pre-selection would fail to achieve the objective of ensuring effective competition and public interest" (8).

Focus on wholesale regulation under the 2006 Proposed Recommendation

In June 2006, the Commission published a draft revised Recommendation (9) ("draft Recommendation") on the markets susceptible to *ex ante* sector-specific regulation as part of the package of the 2006 Review. The draft Recommendation proposes substantially reducing the number of markets which are susceptible to ex ante regulation. This reduction has been particularly relevant to retail markets. The Commission proposes deregulating all retail calls markets and the retail market for minimum set of leased lines. The only retail market which the Commission proposes keeping in the list of markets susceptible to *ex-ante* regulation is the market for access to the public telephone network at a fixed location (10).

With regard to retail calls markets, the Commission considers that effective wholesale regulation (Carrier Selection, Carrier Pre-Selection, and in some countries Wholesale Line Rental) has significantly reduced the barriers to entry in these markets. Indeed, large scale market entry of alternative suppliers can be observed across Europe, leading to significant loss of market share by incumbents and to price reductions. Additionally, increasing penetration of broadband has increased competition on the retail calls market by enabling retail customers to take advantage of new calls services based on Voice over IP. Therefore, it is the Commission's view that competition law in combination with effective wholesale regulation is now in general the appropriate tool to challenge potential competition problems, such as anticompetitive bundling, on retail calls markets.

Similarly, the Commission believes that effective wholesale regulation imposed on SMP operators should significantly reduce barriers to entry into the retail market for minimum set of leased lines. New entrants could equally provide retail offers, based on the wholesale access to ubiquitous networks of incumbents (11).

By contrast, when considering the retail markets for access to the public telephone network, the Commission is of the view that even with the imposition of wholesale remedies, the present high barriers to entry would neither be reduced nor disappear. Alternative operators are required to incur significant sunk investments in order to be able to benefit from the most pertinent wholesale remedy — local loop unbundling (LLU) (12). The latter remedy has therefore a limited impact on the removal of barriers to entry (13). Furthermore, the current levels of deployment of alternative access infrastructures such as cable, fibre-to-the-home or wireless local loop are not yet sufficient to represent a competitive constraint so as to push this market towards effective competition.

The focus on wholesale remedies has also been reflected in the sequence that NRAs are required to conduct for the analysis of interrelated markets identified in the draft Recommendation (14). NRAs should analyse first the markets furthest upstream in the vertical supply chain. Taking into account the *ex ante* regulation imposed on such markets, NRAs should then proceed to assess the related downstream market(s) until they reach the stage of the retail market. A retail market should only be subject to *ex ante* regulation if there is still SMP despite the presence of effective wholesale regulation (15).

(8) Universal Service Directive, Recital 26 and Article 17.1(b).
(9) Commission Staff Working Document containing a draft revised Commission Recommendation on relevant product and service markets susceptible to *ex-ante* regulation. SEC (2006) 837 http://ec.europa.eu/information_society/policy/ecomm/doc/info_centre/public_consult/review/recommendation_final.pdf
(10) This is due to particular characteristics of this market which are difficult to tackle purely by regulation at the wholesale level, namely high barriers to entry, economies of scope and no economic justification for infrastructure duplication at the access level.
(11) See footnote 9 above; p. 35.
(12) The local loop is the physical twisted metallic pair circuit connecting the network termination point at the subscriber's premises to the main distribution frame (MDF) or equivalent facility in the fixed public telephone network. Local loop unbundling requires the alternative operator to build its own network to the Main Distribution Frames ("MDFs") and install its own equipment at the incumbent's local exchange in order to interconnect their own network to the copper pair.
(13) Moreover it is questionable if LLU will be successful in remedying the competition problems. It can be anticipated that the transition by incumbents towards Next Generation Networks would make any investment in LLU obsolete.
(14) See footnote 9, p. 13.
(15) This methodology is known as the "modified greenfield approach."

The Polish experience: retail markets for access to the telephone networks at a fixed location and retail calls markets

Two recent notifications by the Polish NRA under the Article 7 procedure ([16]) illustrate the dubious value of retail regulation in this field. One of them led the Commission to adopt a veto decision, while in the other one it expressed its "serious doubts" (subsequently withdrawn).

The Polish retail markets for access to the telephone network at a fixed location

In October 2006 the Polish NRA, Urząd Komunikacji Elektronicznej ("UKE"), notified to the Commission draft regulatory decisions concerning the retail markets for access to the public telephone network at a fixed location for residential and non-residential customers ("markets 1 and 2") ([17]). In its notification, UKE concluded that Telekomunikacja Polska S.A. ("TP") should be designated as having SMP on those markets. The strict remedies proposed by UKE included inter alia retail price regulation and submission of tariffs and other conditions of service for approval.

Failure to define the market in accordance with competition law principles

Departing from the Recommendation ([18]) and the approach followed in other Member States, UKE proposed to include broadband access lines ([19]) (in particular xDSL ([20]) lines) in markets 1 and 2 ([21]).

Market definitions given in the Recommendation are not binding. Different national circumstances may justify NRAs defining a specific market more narrowly or more broadly than it is done in the Recommendation, as long as such definition is in line with competition law principles.

In the present case, however, the Commission observed that, in its notification, UKE did not provide sufficient analysis based on competition law principles in accordance with the Commission's guidelines on market definition and SMP assessment which would justify such a broad market definition.

Markets 1 and 2, as specified in the Recommendation, include the provision of a connection or access (at a fixed location or address) to the public telephone network for the purpose of making and/or receiving telephone calls and related services (such as fax). In the Commission's view, although broadband connections are also capable

([16]) For an overview of the market review and Article 7 consultation mechanism see KRUEGER and DI MAURO, "The Article 7 consultation mechanism: managing the consolidation of the internal market for electronic communications", Competition Policy Newsletter, 2003 — number 3, p. 33-36.

([17]) See UKE's notifications registered under PL/2006/0518 and PL/2006/0524 available at http://forum.europa.eu.int/Public/irc/infso/home/main

([18]) Commission Recommendation 2003/311/EC of 11 February 2003 on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services (the "Recommendation"), OJ L 114, 8.5.2003, p. 45.

([19]) Broadband is one of the main forms of access to data services. Broadband access may be delivered in the form of ADSL connections over the local network or via other access technologies and has the following distinguishing features: (i) it is possible to use both voice and data services simultaneously; (ii) the possibility of always-on connection; (iii) it has a faster download speed than a dial up connection. Narrowband is also one of the main forms of access to data and voice services, but lacks the characteristics of broadband services described above. Among other features, narrowband connections only allow low download speeds and do not allow using voice and data services simultaneously.

([20]) DSL (Digital Subscriber Line) is a technology which makes it possible to use the local loop of the existing network for fixed telephony (PSTN) for high capacity transmission of digital data. DSL technologies make use of existing telephone lines to deliver voice, data and video traffic simultaneously at high speed. There are a number of DSL-based technologies which are collectively referred to as xDSL. All these characteristics have to be present simultaneously for an internet access service to be defined as broadband.

([21]) Three other Member States (Sweden, Malta, Lithuania) included broadband connections in such markets, but in so far as they allow only access to the telephone network, but not internet access.

of facilitating delivery of telephone services, customers generally switch to broadband for the purpose of higher speed internet and not for getting access to voice services. The functional differences (i.e. the possibility of accessing voice service as well as the broader service of internet at high speed) tend to be reflected in higher prices for broadband access compared to narrowband access. Broadband access therefore tends to be only partially substitutable with narrowband access lines.

Another reason for not including broadband access lines in markets 1 and 2 is that so far customers, when purchasing broadband access, have generally kept their narrowband connections, indicating that both access products are from a demand-side perspective complements rather than substitutes. One of the reasons for this phenomenon is the absence in some Member States, including Poland, of DSL-only offers (so-called "naked DSL") ([22]). Other reasons include reliability and quality requirements, simplicity of use, etc. Also supply-side substitution between narrowband and broadband access seems to be limited in view of the different underlying infrastructures ([23]).

In its responses to the Commission's requests for information and serious doubts letter, UKE provided further factual information on the number of xDSL, PSTN and ISDN lines in Poland, pricing information on existing xDSL, PSTN and ISDN offers, and functionalities of the IP telephony service offered by TP in Poland. This additional information, however, confirmed the initial concerns of the Commission as to the lack of substitutability between broadband access and markets 1 and 2. In particular, it showed wide price differences between PSTN/ISDN access and broadband connections. Differences in functionalities were also observed, since TP's IP telephony services enable subscribers to make and receive calls only to/from TP's subscribers. The Commission, therefore, vetoed the Polish draft decision.

It is true that, as argued by UKE, some NRAs had notified decisions including broadband access (e.g. wireless access) in markets 1 and 2 without the Commission vetoing such decisions. In those cases, however, the relevant NRAs proved that broadband access was equivalent in terms of prices and functionality to the access to telephone network for residential and non-residential customers provided through metallic loops. The Commission indicated in its veto decision that over time, it seems likely that the competitive pressure from xDSL access services on PSTN and ISDN access services may increase. Especially when broadband penetration will become more important ([24]), IP telephony services will allow similar functionalities, naked-DSL will become available and the price divergences will further decrease. It considered, however, that the existing market conditions in Poland did not allow, on a forward looking approach, to conclude that xDSL and PSTN and ISDN access services already belonged to the same market. In the event that market conditions would allow such a broader definition of the market, the finding of an undertaking holding SMP on that market and ultimately the imposition of regulation on such undertaking might be less likely than it is now.

Proportionality of remedies proposed

The consequence of adopting a broad market definition would have been the adoption of the same set of remedies for narrowband access and broadband access alike. Even if UKE had submitted a proper market definition on the basis of competition law principles the imposition of retail remedies (specifically retail price control and the obligation to provide naked-DSL) without consideration of the remedies imposed on upstream markets would have been contrary to the principles of the 2003 Framework.

On the basis of the principle of proportionality ([25]), the NRA should have considered if already imposed wholesale regulation was effective in bringing competition to the broadband retail market. If this was not the case, UKE should aim at improving the effectiveness of the wholesale remedies instead of immediately imposing regulation at retail level. Only where the NRA would have established that such improved wholesale remedies would still not be effective and if *ex-post* competition law enforcement would be insufficient, it could consider turning to retail regulation.

([22]) Naked DSL did not exist in Poland at the time of UKE's notification of its draft measures.

([23]) The Court of First Instance has recently upheld, in case T- 340/03 *France Telecom v. Commission,* the market definition of high-speed internet access made by the Commission in its Decision Comp/38.233 — Wanadoo Interactive. In particular, the Court of First Instance established that the Commission was right in concluding that there was not a sufficient degree of substitutability between high-speed and low-speed access as to justify the inclusion of both access markets in one.

([24]) Broadband penetration in Poland (around 10% of households) is below the EU average.

([25]) Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and service: para.117 establishes that *"Community law and, in particular, Article 8 of the framework Directive, requires NRAs to ensure that the measures they impose on SMP operators under Article 16 of the framework Directive are justified in relation to the objectives set out in Article 8 and are proportionate to the achievement of those objectives".*

A careful look at the different actions taken by the Polish authorities with regard to the broadband market, and the remedies already imposed at the wholesale level, seems to indicate that the remedies proposed by UKE were not justified and were therefore disproportionate. In particular, some of the remedies proposed by UKE in its notification to the Commission might not have been necessary in view of the decisions already adopted by UKE, as well as the National Competition Authority ("UOKiK "). For example:

In its notification, UKE proposed to impose on TP the obligation to provide xDSL services separated from the PSTN voice services at the retail level (i.e. naked-DSL remedy). The competition issue which this remedy sought to solve had already been addressed in different decisions:

- In July 2006, UKE adopted a decision on the basis of the Polish Telecommunications Act ([26]) ordering TP to provide DSL offers separately from its fixed telephony subscription. In September 2006, UKE imposed an approximately EURO 25 million fine on TP for not complying with the July decision. TP has committed to providing naked-DSL to its retail customers as from early 2007.
- The Bitstream wholesale offer was amended in September 2006 by UKE in order to mandate wholesale access to naked DSL.
- In its notification to the Commission of the wholesale broadband market ("market 12"), UKE proposes to keep the mandated wholesale access to naked-DSL ([27]).
- A decision with similar effect had also been adopted by Polish competition authority. UOKiK considered that TP was abusing its dominant position ([28]) on the market for retail broadband access by requiring the consumers who purchased broadband access to additionally maintain their subscription to TP's voice telephony services. In its decision ([29]) the Polish NCA imposed a fine on TP and ordered the provision of broadband services separately from the subscription to voice telephony.

In its notification, UKE also proposed to impose price regulation on the broadband retail market. It seems however that the existing regulation at wholesale broadband market would have an impact on retail prices:

- Indeed, the Bitstream wholesale offer in Poland sets the wholesale access charges at retail minus ([30]). The retail minus model calculates the wholesale charge on the basis of a discount of the SMP operator's retail tariff so as to allow alternative operators to compete on the retail market on the basis of the available wholesale access offers.
- UKE has also proposed in its notification to the Commission of the wholesale market for broadband access ("market 12") to maintain wholesale price regulation ([31]).

The decisions described above seem to already address the competition problems observed on the retail market for broadband access. Therefore it seems that further retail regulation (i.e. of the xDSL retail products) would be superfluous and, thus, disproportionate.

The Polish retail calls markets in the public telephone networks at a fixed location

The second notification concerned the retail calls markets in Poland ([32]). The retail calls markets include: local and/or national telephone services provided at a fixed location for residential customers and non-residential customers; and international telephone services provided at a fixed location for residential and non-residential customers (markets 3 to 6). In this case, the Commission decided to withdraw its serious doubts on the basis of additional information provided by UKE in the course of the second phase.

([26]) Article 57 of Polish Telecommunication Act, of 16 July 2004, as amended. English translation is available at http://www.mt.gov.pl/viewattach.php/id/fd2c74add52c01da93b8dd36d0efb1bc (last accessed on 5.02.2007). This article provides that operators of publicly available telecommunication services may not make the provision of such services conditional upon the purchase of any other services.

([27]) UKE notified market 12 to the Commission in August 2006. The remedies proposed in that notification have not been adopted yet.

([28]) TP has a market share exceeding 40% on retail broadband access; UOKiK referred to data collected by UKE and concluded that in 2005 TP had 66% of the market.

([29]) This decision has been formally adopted already after the notification of UKE's draft decision concerning markets 1 and 2, however the fact that UOKiK is conducting such proceedings has been published on UOKiK website in August 2005.

([30]) The discount from TP retail offers has been set at 41% or 51%, depending whether from TP's special or standard offer, respectively.

([31]) See footnote 27. UKE set the wholesale charges at FL-LRIC model, however until the costs are successfully verified by auditors and accepted by UKE, an interim retail minus calculations would be applicable.

([32]) See notification of 6 November 2006 in cases PL/2006/0528-0531, available at http://forum.europa.eu.int/Public/irc/infso/home/main

In its notification, UKE excluded from the definition of the calls markets certain products ([33]) which seemed to be quite popular in Poland, especially as a substitute of international calls and, to a lesser extent, of national long distance calls. In fact, such services were not even mentioned in UKE's notification. The Commission expressed serious doubts with regard to the exclusion of such services from the market definition and the possible impact on the SMP assessment.

Information provided by UKE in response to the Commission's serious doubts letter indicated that such services had only limited impact on the market and TP's market shares would still remain high ([34]) had those services been included on the relevant markets. This in combination with other SMP criteria, such as (i) high entry barriers ([35]), (ii) vertical integration, (iii) TP's advanced sales and distribution network and (iv) limited potential competition, led the UKE to conclude that the inclusion of such services in the calls markets would not have resulted in a different SMP finding ([36]).

The Commission agreed that the information and arguments presented by UKE make it possible to find TP as having SMP on all retail markets. Nevertheless, it also noticed that the information provided suggested the existence of certain competitive dynamics on the Polish calls markets ([37]), in particular on the international calls markets. There were indications of increasing market shares of alternative providers and the availability of various methods of call placing (direct call, call selection and pre-selection, calls via premium rate numbers and emergence of VoIP-based services). Furthermore, in the short to medium term, the wholesale regulation would become effective, beginning with wholesale line rental ([38]) which should become operational in early 2007.

The Commission therefore invited UKE to closely monitor market trends and to undertake a new market analysis within one year following adoption of the final measures.

Conclusion

The 2003 Framework and the 2006 Review promote deregulation where effective competition exists or there is a tendency towards it. The Commission is aware that some telecommunication markets still need to be regulated. In these cases, wholesale regulation is usually preferable over retail regulation. This is explained by the fact that regulation should be proportionate to its objective, i.e. the adopted remedy should be the least burdensome to redress the competition problem identified. In vertically related markets, problems at retail level should primarily be resolved by way of effective remedies imposed at wholesale level leaving the retail market open to the competitive process.

([33]) The excluded services are calls via certain premium rate dial-in numbers and pre-paid calling cards. UKE has also excluded Voice over Broadband, due to low broadband penetration and the fact that the related services are only in the nascent phase in Poland.

([34]) In 2005 TP had following market shares (by volume): 85% in the market for residential local/national calls; 73% in the market for non-residential local/national calls; 68% in the market for residential international calls; and 53% in the market for non-residential international calls. TP's market shares are decreasing over time, in particular in the international calls markets. The remaining part of the markets is fragmented amongst alternative operators, none of which was able to achieve substantial market share.

([35]) UKE considers that there are still significant barriers to entry into the retail calls markets in Poland. New entrants must make significant investments in interconnection points and backhaul networks, infrastructure, billing and invoicing systems and advertising. Also the fact that due to CS/CPS arrangements the customer receives two invoices (one from the access provider and one from the CS/CPS provider) creates a significant barrier.

([36]) In its comments the Commission has invited UKE to include in UKE's final measure the data and arguments developed during the second phase proceedings, in particular to indicate TP's market shares including calls via premium rate numbers and via pre-paid calling cards.

([37]) This however should not be confused with the tendency towards effective competition.

([38]) Imposed as one of the obligations in the measure concerning market 8 (case PL/2006/0380).

The Energy Sector Inquiry: conclusions and way forward (1)

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Introduction

On 10 January 2007, after an 18 month investigation, the Commission published the final report on the sector inquiry carried out by DG Competition into the gas and electricity markets in the EU (Commission Communication COM(2006)851 and a more detailed Commission Staff Working Paper (SEC(2006)1724). This was part of the overall energy package adopted by the Commission as its key policy objective for the rest of its mandate.

The sector inquiry plays a pivotal role in the package. Based on a vast amount of empirical evidence, a large part of which had never been gathered before with that level of detail and accuracy, it gives an in-depth analysis of the way European electricity and gas markets function in practice, and identifies a number of shortcomings in the functioning of these markets. Secondly, it helps DG Competition to identify areas where it needs to focus its competition enforcement and to improve the effectiveness of remedies in competition cases, including merger cases. Since the start of the inquiry (but outside its immediate scope), several energy companies have been inspected and a number of new investigations opened. Finally, the results of the sector inquiry provide a solid, and widely supported, factual basis for the Commission's Strategic Energy Review and the future legislative proposals. This not only allows the Commission to bring forward the most appropriate proposals to address the current shortcomings, but should also ensure that the debates in the Council and the Parliament are as well informed and constructive as possible.

This article (2) presents the wider context of the sector inquiry, the main barriers to competition in the energy sector and then discusses the competition and regulatory remedies that could be used to remove these barriers.

The wider context

The three objectives of the EU energy policy are "competitiveness, security of supply and sustainability", which are closely interlinked and complementary. Competitive markets provide the necessary signals for investment, which leads to supply security in the most cost efficient manner. Similarly, the creation of a competitive internal market will allow the Union's energy companies to operate in a market of a larger dimension, which will improve their ability to contribute to security of supply. At the same time, market forces oblige European operators to use the most cost effective methods of production, which in the appropriate regulatory environment can benefit sustainability. Consumers will be able to choose between different providers and contract schemes, and could thus reduce their electricity costs and adapt their consumption to market developments. Competitive, cost reflective prices will help encourage energy efficiency, which can reduce the dependence on external suppliers and which supports the Union's objective for sustainability and security of supply.

The Final Report concentrates on the competition aspects of Europe's energy policy and the remaining obstacles to creating a single European energy market. This aspect merits a thorough analysis in its own right and also reflects the focus dictated by the procedural framework, in which the inquiry was carried out.

The findings

The findings of the Final Report have been grouped into eight categories. The first five findings have already been presented as part of the Preliminary Report. Therefore these will only be briefly summarised and this article will focus on the results of the public consultation launched in February 2006 and the new findings presented in the Final Report centred on the topics downstream, balancing and LNG markets.

The **first phase results** of the sector inquiry presented in the Preliminary Report can be summarized as follows:

- **Market concentration** is high in the energy sector. In the gas markets, wholesale trading is slow to develop and entrants are dependant on incumbents for services throughout the supply chain. In electricity concentration in generation leads to companies being able to exercise market power on wholesale markets.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) This article follows up on the article in the Competition Policy Newsletter 2006 Number 1, p. 12

- An insufficient level of unbundling between network operation and supply activities results in **vertical foreclosure** by incumbents vis-à-vis entrants which is witnessed both in gas and electricity markets.
- There is a lack of **market integration** primarily due to the control of primary capacity on cross-border pipelines by gas incumbents and to a shortage of interconnection capacity and lack of investment incentives in the electricity sector.
- There is a lack of **transparency** on energy markets leading to an information asymmetry between incumbents and entrants. This is particularly the case for gas transit pipelines and electricity wholesale markets.
- **Price** formation is not effective and transparent on gas or electricity markets, the former being hampered by the oil-price link, while in the latter recent price rises seem to have other causes than just input and CO2 price developments.

After the publication of the Preliminary Report and the close of the first phase of the inquiry in February 2006, a three-month public consultation was launched. Altogether 60 responses were received from a broad range of parties including vertically integrated energy companies, network companies, traders, entrants, national regulators and competition authorities, customers, industry associations and consultancies. In general the respondents welcomed the report and its findings and proposed remedies similar to the ones put forward by the Commission, but of course there were opposing views as well. The main issue on which the views diverged was the success of the existing unbundling provisions. Generally speaking, the incumbents were not in favour of further measures, arguing that the current legislation was sufficient and should be given more time for the results to become clear. But consumers, traders, new entrants and the authorities supported further legislative initiatives. The analysis on unbundling was broadened in the second phase of the inquiry, but is not analysed here (see instead the specific article on this subject in this issue of the Competition Policy Newsletter). It can be concluded that the results of the consultation were reassuring as regards the orientation of the inquiry and suggested that further market opening and integration should be maintained.

Downstream markets

In the second phase of the sector inquiry, downstream markets in electricity and gas were analysed with the conclusion that competition is often limited at the retail level too. The analysis shows a substantial foreclosure effect through long-term contracts, albeit with significant differences between Member States on the degree to which industrial customers are tied to incumbent suppliers on a long-term basis. The number of competitive offers that customers receive is particularly unsatisfactory in some Member States characterised by a high level of concentration and there is a general lack of pan-European supply offers. For gas, restrictions on how customers can dispose of their gas, in combination with restrictive practices by suppliers regarding delivery points, limit competition and prevent the achievement of efficiencies by these customers. In electricity, certain standard contracts contain restrictions, which may also raise competition concerns.

Balancing markets

As regards the balancing markets, the results of the inquiry show that the balancing regimes often favour incumbents while at the same time creating obstacles for newcomers.

In the gas sector, the small size of current balancing zones, the highly complex and divergent rules in each zone, and the obligation to reserve capacity at each border point increases costs of shipping gas within Europe. All these aspects create major obstacles for new suppliers to enter the market, which the vertically integrated incumbents have little incentive to remove. Furthermore, balancing charges, clearing costs and penalty charges are not transparent and often contain unjustified penalty charges, favouring incumbents.

In electricity, the markets on which transmission system operators have to acquire balancing and reserve energy are highly concentrated, giving generators scope to exercise market power. This can result in entry barriers for new suppliers facing a high risk of high imbalance prices and/or high network charges. Furthermore the level of harmonisation of balancing market regimes is inadequate. In some Member States the structural relation between TSOs and their affiliated generation provides an incentive for the TSO to buy excessive reserve capacity and/or to pay high prices, thereby favouring their affiliated generation arm.

LNG markets

LNG supplies widen Europe's potential upstream suppliers and are therefore important for both security of supply and competition between upstream suppliers. Nevertheless the results of a study commissioned by DG Competition show that the potential for LNG supplies to favour less concentrated downstream markets still needs to be realised. Traditionally LNG has been imported by national incumbents who also own LNG terminals, and this situation has prevented LNG imports from increasing downstream competition. Recent trends, however, point to more capacity going to new entrants and to upstream producers themselves. This is likely to have a positive impact on downstream competition unless such effects are frustrated by anticompetitive rules or behaviour.

Remedies

To address the market shortcomings identified, the Commission proposed in its final report both competition law remedies and regulatory/structural remedies.

Competition law enforcement

The Commission noted that it will make full use of antitrust rules, namely Article 81, 82 and 86 EC Treaty, in close cooperation with National Competition Authorities. The Commission also reiterated its intention to ensure pro-competitive outcomes when applying merger rules (Regulation (EC) No 139/2004 ([3])) as was done in important recent energy cases such as GdF/Suez ([4]), DONG/Elsam/Energi E2 ([5]) and E.ON/MOL ([6]). Finally, the Commission also noted in its Communication the importance of State aid control (Articles 87 and 88 EC Treaty) in the energy sector.

The sector inquiry has identified a number of issues that need to be addressed.

The Commission is currently investigating a number of possible antitrust infringements, partly on the basis of inspections carried out in 2006 at the premises of gas and electricity companies in six Member States ([7]). Careful and thorough assessment of the evidence is required in each individual investigation, which is outside the scope of the sector inquiry.

Articles 81 and 82 EC Treaty may be infringed where markets are vertically tied by long-term downstream contracts, unless there are countervailing efficiencies benefiting consumers. Another reason why competition at the downstream level does not take off is that at the upstream level, gas import contracts are concentrated in the hand of a few incumbents. These effects on the downstream market require attention, even if existing and future upstream contracts are not as such put into question. Similarly, in the electricity sector, power purchase agreements can have foreclosure effects which need to be examined ([8]).

Foreclosure can also arise due to lack of access to infrastructure (transmission and distribution networks and/or storage facilities). Long-term contracts and capacity hoarding can prevent access to infrastructure, which is necessary for the development of competition at the supply level. In particular, the compatibility of pre-liberalisation long-term contracts with competition rules needs to be assessed. Transmission companies vertically integrated with supply companies may also have behaved strategically to protect their downstream supply interest when deciding not to carry out some infrastructure investments ([9]).

Collusion, including market partitioning between incumbents, is a serious antitrust infringement that the Commission would address as a priority not least as it directly impedes market integration.

The Commission is also concerned about the distorting effect on competition exercised by regulated tariffs. For this reason it has opened a formal investigation under EC Treaty state aid rules into potential aid to large and medium-sized companies and to the electricity incumbents in Spain in the form of artificially low regulated industrial tariffs for electricity. It also received a complaint with respect to the antitrust rules.

In further competition enforcement action the Commission has carried out unannounced inspections at the premises of electricity companies in Germany in December 2006, based on concerns that companies may have violated EC-Treaty antitrust rules that prohibit restrictive business practices and/or abuse of a dominant market position ([10]). The issues investigated are the alleged withholding of generation capacity and raising rivals' costs in balancing markets.

Remedies arising from competition cases can be behavioural or structural. The Commission and national competition authorities have gathered significant experience in the energy release programmes (electricity Virtual Power Plants and gas release programmes). These need to be well-designed and of a large scale to develop market

([3]) O.J. L 24, 29.1.2004 p. 1.
([4]) Case COMP/M.4180, IP/06/1558.
([5]) Case COMP/M.3868, IP/06/313.
([6]) Case COMP/M.3696, IP/05/1658.
([7]) See MEMO/06/203 and MEMO/06/205 of 17 May 2006 and MEMO/06/220 of 30 May 2006 and MEMO/06/483 of 12 December 2006 available at http://europa.eu/rapid/.
([8]) Case C-41/2005, IP/05/1407.
([9]) The Italian competition authority recently took action against the incumbent gas company, ENI, who refrained from carrying out an expansion of a gas pipeline that would have allowed third parties to bring gas into the country independently of him for the first time.
([10]) MEMO/06/483 of 12 December 2006 available at http://europa.eu/rapid.

liquidity and increase entry opportunities. As market concentration levels are very high in most energy markets, competition authorities are willing to prevent the market structure from further deteriorating. Energy release programmes have been used in the framework of merger control (e.g. E.ON/MOL, DONG/Elsam/Energi E2 ([11])). Far reaching structural measures could also be used as a remedy to competition infringements as was done in the GdF/Suez or the DONG merger cases ([12]). In these cases behavioural remedies would have been less effective at removing the competition concerns. According to Article 7 of Regulation 1/2003 structural remedies can be imposed where there is a substantial risk of a lasting or repeated infringement that derives from the very structure of the undertaking, or where behavioural remedies would be more burdensome on the dominant undertaking than a structural solution ([13]).

Structural remedies

Key structural and regulatory issues identified through the sector inquiry related to the inadequate level of unbundling, regulatory gaps — in particular with respect to cross-border issues — and transparency.

The sector inquiry confirms that it is essential to resolve the systemic conflict of interest inherent in the vertical integration of supply and network activities, which has resulted in discrimination and a lack of investment in infrastructure. It thus highlighted the need for effective **unbundling** of the network activity ([14]).

A clear observation resulting from the sector inquiry is that there is an urgent need **to strengthen the powers of regulators** and to enhance **European co-ordination** between them. Such a regulatory scheme would provide the basis for the transparent, stable and non-discriminatory regulatory framework that the sector needs for competition to develop and for future investments to be made. The main ingredients of such a framework should be (i) enhanced powers for independent national energy regulators; (ii) reinforced coordination between national energy regulators; and (iii) substantially enhanced consistency of regulation in cross-border issues. We also need reinforced cooperation between Transmission System Operators (TSOs).

The findings of the inquiry have also highlighted the need for enhanced **transparency.** It was proposed therefore that relevant information should be published in a timely manner and any exceptions should be very strictly limited to what is required to reduce the risk of collusion. This is to be done through guidelines, monitoring and adaptation of the EC rules. Proposals for transparency are also included in the Commission Communication on "Prospects for the internal gas and electricity market" ([15]).

The final report presented some further issues to be considered towards developing a pro-competitive market environment relating to regulated prices, "legacy contracts", exemption procedures, market design harmonisation, interconnector capacity allocations, gas storage access and market oversight:

- Distortions of competition resulting from regulated supply tariffs should be removed.
- Any exemption to access requirements granted for new investment should not be detrimental to competition.
- Market design should be harmonised, especially regarding issues having an effect on cross border trade.
- The legal position of long term pre-liberalisation contracts, so-called "legacy contracts", should be clarified so that more gas transmission capacity is available.
- Implicit auctions should be the preferred method of allocating limited interconnector capacity.
- Third party access for gas storage should be reviewed so as to strike the right balance between the need for effective access and maintaining incentives for new storage developments.
- There should be stronger regulatory oversight for trading on wholesale markets (e.g. power exchanges)

Conclusion

The European energy sector inquiry is now concluded. It has identified a number of serious shortcomings which prevent European energy users and

(11) See "A combination of gas release programmes and ownership unbundling as remedy to a problematic energy merger: EON/MOL" in the Competition Policy Newsletter of Spring 2006 (page 73) and "DONG/Elsam/E2: Remedying competition problems in an energy merger through infrastructure unbundling and gas release" in the Competition Policy Newsletter of Summer 2006 (page 55).

(12) For a more extensive description of the GdF/Suez case, please see the article on page 83 of this Newsletter. For a more extensive description of the DONG case, see the article referred to in footnote 10.

(13) See Article 7(1) and recital 12 of Regulation (EC) No 1/2003.

(14) The unbundling issue is discussed in detail in a separate article on page 23 of this Newsletter.

(15) COM (2006) 851.

consumers from reaping the full benefits of liberalisation. Much still needs to be done to achieve competitive markets which respond to investment signals and ensure security of supply while taking due account of environmental challenges.

Energy is and will remain high on the Commission's agenda. The focus now turns to individual competition cases in antitrust, mergers and state aid. The Commission will also focus on the third liberalisation package that it intends to bring forward in the summer.

Mergers in the energy sector will be rigorously scrutinised to ensure that they are pro-competitive, but similarly barriers to pro-competitive mergers (for example, attempts to create national champions) will be removed wherever possible. Antitrust and State aid enforcement in the energy sector is a priority and many investigations have been launched since May 2006.

The findings of the sector inquiry have helped the Commission to identify a number of important regulatory changes that need to be made to promote competitive energy markets in Europe, as presented in the Communication on "Prospects for the internal gas and electricity market". The sector inquiry should also provide a solid factual basis for the discussions that will take place in the Council and the Parliament on the Commission's proposals. The sector inquiry should therefore play a key role in the development of an Internal Market for energy that contributes to sustainability, competitiveness and security of supply.

The transformation of monopolised national energy markets into a competitive single energy market is difficult and time-consuming, but it is necessary to enhance consumer welfare and to make Europe a competitive market economy.

Sector Inquiry Identifies Widespread Competition Barriers in Retail Banking ([1])

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On 31 January 2007 the European Commission published the Final Report of its sector inquiry into European retail banking markets ([3]). The inquiry has identified a number of deficiencies in the way these markets work that cause higher cost for consumers and small businesses and deter entry by new players. These deficiencies concern the markets for payment cards, (non-card) payment systems and certain core retail banking products. Particular indicators are large variations in merchant and interchange fees for payment cards, barriers to entry in the markets for payment systems and credit registers as well as obstacles to customer mobility and product tying. On 31 January 2007 the Commission also adopted a Communication summarising the results of the inquiry and describing areas for further investigation and antitrust enforcement to open markets and stimulate competition ([4]).

The decision to open inquiries into certain financial services sectors — namely business insurances ([5]) on the one hand and retail banking on the other — was taken in June 2005 ([6]). Retail banking covers a wide range of activities and markets. Some of these markets and players have been repeatedly under antitrust scrutiny, for instance, payment cards and payment card networks. Others, such as the wide variety of the markets for core retail banking products seemed to be relatively untouched by competition investigations. Against this background, the retail banking inquiry was split into two main parts: first, the markets for payment cards, on which an Interim Report was already published on 12 April 2006 ([7]) and, secondly, the markets for current accounts and related services. Preliminary results of the latter part of the inquiry were published on 17 July 2006 in a separate Interim Report ([8]).

With the publications of the preliminary findings of the sector inquiry the Commission invited market participants to submit comments. This wide and open consultation as well as the public hearing that took place on 17 July 2006 has resulted in extensive and valuable feedback ([9]). All received comments contributed to the elaboration of the final report that covers both parts of the retail banking inquiry.

Main conclusions

The findings clearly confirm that markets remain fragmented along national lines. Fragmentation means that the potential of a 450 million citizen market is not fully exploited, that consumers have limited choices and often pay more than they should for current accounts, loans or payments. Despite all efforts at European level to further integrate the EU financial services markets, access to several product and geographic markets still appears to be difficult. The inquiry has found a great variation of prices, profit margins and selling patterns between countries and, at the same time, a contrasting homogeneity within the individual Member States. This suggests the existence of regulatory or behavioural barriers. Indeed the inquiry has identified a variety of such barriers, be it of the one or the other kind or, most often, a combination of the two. It also indicates that widespread co-operation within markets or networks may lead to the alignment of prices and other parameters.

([1]) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

([2]) Currently Directorate-General for Internal Market, unit B-1 (Policy development and coordination of the internal market).

([3]) http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/sec_2007_106.pdf

([4]) http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52007DC0033:EN:NOT

([5]) Preliminary findings regarding the sector of business insurances were published on 24 January 2007 (see http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/interim_report_24012007.pdf).

([6]) Alongside the decision to open the energy sector inquiry where the final report was published on 10 January 2007 (http://ec.europa.eu/comm/competition/sectors/energy/inquiry/index.html).

([7]) http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/interim_report_1.pdf.

([8]) http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/interim_report_2.pdf

([9]) http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/retail.html

Payment cards

The European payment card industry provides payment means with an overall value of €1 350 billion per year. These payments annually generate an estimated €25 billion in fees for banks. The inquiry has identified several competition concerns in this important sub-sector.

First, the payment card industry is highly concentrated. This results in high fees and high profitability. Moreover, the operative rules of some of the networks also bring about significant entry barriers. It is not only the international networks that cause concerns in this respect. Several national card schemes run by the main domestic banks also raise competition problems in setting a range of discriminatory rules.

Secondly, there are large variations in payment card fees across the EU. The results of the inquiry suggest that retailers in some countries pay fees that are up to four times higher than in other countries for accepting the same major credit card.

Thirdly, the inquiry gathered significant evidence on multilateral interchange fees ("MIFs"), i.e. the fees that are paid by the acquiring bank to the issuing bank for each payment card transaction at the point of sale of a merchant. This evidence rebuts to a large extent the industry's arguments for the economic benefits of high interchange fees. It shows that several card networks can and do operate efficiently with low or even no interchange fees. The report does not condemn the existence of MIFs as such, because any concrete decision concerning interchange fees will have to be taken on a case-by-case basis. The sector inquiry has, however, highlighted the necessity to critically review academic justifications for this pricing mechanism. The present MIF in many of the schemes examined indeed seems problematic.

The publication of the interim report as well as the subsequent consultation with industry and other stakeholders seems to have already yielded positive results in a number of Member States where players have taken initial steps to address the Commission's concerns ([10]).

Finally, the sector inquiry has highlighted several market barriers that need to be addressed by all involved in the Single Euro Payments Area (SEPA), a project driven by the European banking industry and strongly supported by the European Commission and the ECB. In view of the inquiry's results regarding current network structures competition authorities have already engaged to closely monitor the process.

Current accounts and related services

Despite significant growth and diversification that has taken place in the banking industry over the last two decades, traditional retail banking has remained the industry's most important sub-sector, representing over 50% of total EU activity in terms of gross income. Structures of the markets for current accounts and related services are, however, still fragmented. Suppliers rarely offer their services on a cross-border basis, and markets remain divided along national lines. This is due to factors such as cultural differences and historically grown industry structures. However, the report has also identified regulatory and behavioural barriers that are of particular concern from the viewpoint of competition policy.

The inquiry found, for example, access barriers in key infrastructures, particularly in (non-card) payment systems and credit registers. These schemes and platforms are often run by the incumbent banks that have a very limited interest in facilitating third parties' market access. For newcomers, however, non-discriminatory access to these facilities is indispensable to compete.

Another focus of the analysis concerned product tying. This practice that, for instance, ties the opening of a current account to a mortgage or a SME loan, is widespread in most Member States. Depending on the circumstances of the case, tying may reduce customer choice, render price competition intransparent or create obstacles to customer mobility.

Finally, the inquiry also analysed the area of co-operation between banks. Retail banks co-operate to set standards or operate infrastructures such as the above mentioned payment systems and credit registers. Certain types of banks, namely savings and cooperative banks, traditionally have even closer co-operative ties. Co-operation can result in economic and consumer benefits. There are, however, also competition risks. The variety of ownership and company structures, the difference of the scope and scale of the co-operation as well as certain national regulatory provisions render a uniform assessment impossible. The Commission is likely to gather further information to assess whether cooperation between banks that have significant market positions appreciably restrict competition either between themselves or in relation to other actual or potential competitors.

([10]) Report on the retail banking sector inquiry, point B 2.2., page 93 (electronic version): http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/sec_2007_106.pdf.

Sector Inquiry into Business Insurance — Commission seeks comments on Interim Report (1)

Concetta CULTRERA, Christoph EMSBACH, Mourad HADDAD and Antonio Carlos TEIXEIRA, Directorate-General for Competition, unit D-1

On 24 January 2007, the European Commission published the Interim Report on Business Insurance, which presents the preliminary findings of the Sector Inquiry in June 2005.

As pointed out by Commissioner Kroes, *"the preliminary findings of the Commission's inquiry into the business insurance sector have identified factors on all levels of the supply chain that may prevent the markets from working as well as they should. With the help of the comments received during the consultation, the Commission intends to look at these issues in more detail before finalising the sector inquiry report"* (2).

The preliminary findings of the Sector Inquiry are based on a very extensive set of data collected from insurers, reinsurers and intermediaries and from national associations of insurers, intermediaries and risk managers.

The data collected show sustained differences of insurers' underwriting profitability in different Member States. This suggests a significant degree of ***market fragmentation along national lines*** and therefore indicates that the European Union does not yet benefit from a fully integrated market in business insurance.

Moreover, in some Member States, insurance companies tend to display consistently ***higher underwriting profitability in the SMEs' segment,*** compared to the Large Corporate Clients' segment. This may be a sign of a higher degree of competition in the Large Corporate Clients' segment.

The Interim Report also highlights potential ***risks of foreclosure*** in two main areas: ***long-term insurance contracts,*** notably in Austria, Italy, the Netherlands and Slovenia, and ***networks of exclusive agents,*** controlling, in particular in Italy, the vast majority of insurance distribution. These practices could create serious obstacles to the entry of new competitors in the national markets at stake. With the help of the National Competition Authorities, the Commission will assess whether these risks of foreclosure are confirmed. If this is the case, problems will be tackled through antitrust enforcement measures, either at national or Community level.

In the field of reinsurance, the Inquiry has established that some reinsurance companies active in the European Union use so-called ***"best terms and conditions"*** clauses in their contracts with their clients, the direct insurers. These clauses lead to a harmonisation of terms and conditions at the most favourable level for the reinsurers concerned, to the detriment of the direct insurer and, ultimately, of the final business insurance customer. The same practice also appears to exist in co-insurance. The effect of these clauses on the market will be further assessed.

As for the functioning of insurance distribution channels, the Sector Inquiry shows that some insurance intermediaries can be exposed to serious ***conflicts of interest*** when they provide not only advice and services to their clients, but also to insurers, and receive remuneration from these very same insurers. This "double relationship" can compromise the objectivity of their advice to clients and has a potential negative impact on competition.

Contingent commissions (i.e. payments made by insurers to intermediaries, based on the achievement of agreed targets) could create incentives for intermediaries to steer high volume or profitable business to selected insurance companies, regardless of the quality of the insurance product offered and of the level of the premium charged, and therefore not necessarily in the interest of clients. The preliminary results of the Sector Inquiry confirm that contingent commission agreements have been widely spread in many EU Member States and have in some cases represented a source of revenues of considerable magnitude. This issue will be further examined.

Moreover, it appears that the ***lack of transparency of intermediaries' remuneration*** reduces the potential for price competition in the insurance mediation services markets.

Finally, the Inquiry shows that ***horizontal cooperation among insurers,*** normally considered as a very important characteristic of the insurance sector, does not follow consistent and uniform

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(2) See IP/07/74, 24.01.2007.

patterns across Europe. Indeed the degree of horizontal cooperation varies significantly from one Member State to another. Such findings, therefore, legitimately raise doubts about the real need for certain forms of horizontal cooperation among insurers and about the scope of the present Insurance Block Exemption Regulation. These findings, as well as any other input that the Commission will receive on this issue, will shape the debate on the renewal of the present Insurance Block Exemption Regulation, which will expire in 2010.

The Commission has launched a wide and thorough public consultation on the preliminary findings of the Sector Inquiry, ending on 10 April 2007.

Moreover, it has organised on 9 February 2007 a Public Hearing to which industry representatives and business insurance customers have actively participated. On that occasion, the Report's most relevant preliminary findings were discussed in two panel sessions dealing respectively with horizontal cooperation among insurers and with distribution aspects.

Additional investigative steps are also conducted in order to clarify the competition concerns identified in the Interim Report. This new investigative phase is pro-actively involving the customers, which have been encouraged to share with the Commission any competition related concerns regarding business insurance.

A Final Report, reflecting the observations received during the public consultation, the debate in the Hearing and the findings of the additional investigative steps, will be published by September 2007.

Commission fines copper fittings producers € 314.7 million for price fixing cartel (1)

Glykeria DEMATAKI and Rainer WESSELY,
Directorate-General for Competition, units F-3 and F-1

On 20 September 2006, the European Commission fined 30 copper fittings producers a total of € 314.7 million for participating in a cartel. The 11 groups to which these 30 companies belong are Aalberts, IMI, Delta, Advanced Fluid Connections, Legris, Frabo, Mueller, Tomkins, Flowflex, Viegener and Sanha Kaimer. Between 1988 and 2004, they fixed prices, discounts and rebates, agreed on mechanisms to coordinate price increases, allocated customers and exchanged commercially important and confidential information. Four of the groups, namely Aalberts, Delta, Advanced Fluid Connections and Legris had their fines increased by 60% because they continued their illegal arrangements after the Commission's initial inspections. Advanced Fluid Connections' fine was increased by a further 50% for providing the Commission with misleading information. Mueller received full immunity from fines under the Commission's leniency programme, as it was the first company to come forward with information about the cartel.

The product

The product concerned is copper fittings, including copper alloy fittings (e.g. gunmetal, brass and other copper-based alloys). A fitting connects tubes used to conduct water, air, gas, etc. in plumbing, heating, sanitation and other installations. There are various types of fittings known as end-feed, solder ring, compression, press and push-fit which were all covered by the cartel arrangements.

The investigation showed that the cartel covered the whole of the EEA. The EEA market value for fittings was ca. € 550 million.

The infringement

In March 2001, the Commission carried out inspections at the premises of several undertakings following an application for leniency under the 1996 Commission Notice on the non-imposition of fines ("Leniency Notice").

After the inspections several undertakings submitted leniency applications.

The Statement of Objections was adopted in September 2005 and was addressed to 30 legal entities belonging to 11 groups and one association. An Oral Hearing was held in January 2006.

The infringement's main features included: fixing prices, agreeing on price lists, agreeing on discounts and rebates, agreeing on implementation mechanisms for introducing price increases, allocating national markets, allocating customers and exchanging other commercial information.

The investigation showed that the infringement constituted one single, complex and continuous infringement that started in the UK, among the UK manufacturers, in December 1988, continued and grew at European level, with the expansion of the UK producers into continental Europe, from January 1991 until April 2004. The infringement was organised at both national and pan-European level.

Fines

The practices uncovered are a very serious infringement. In fixing the fines, the Commission took account of the size of the EEA market, the duration of the cartel, and the size of the firms involved.

The Commission increased the fines by 60% for Aalberts, Delta, Advanced Fluid Connections and Legris because they continued their cartel arrangements after the Commission's initial inspections. In this regard, there are elements showing that the undertakings concerned not only committed the cartel infringement after the inspections, but also declared their intention to continue their illegal arrangements by agreeing to participate in the collusive meetings in the future.

In addition, another undertaking had its fine increased by a further 50% for providing the Commission with misleading information. In its reply to the Statement of Objections, the company denied that one of its employees had certain contacts with an individual from another company participating in the cartel during a specified period. The Commission, however, had evidence indicating that this undertaking's employee had numerous communications with the particular individual of the competitor company during the period in question.

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Cooperation outside the scope of the 1996 Leniency Notice

Frabo was the first to disclose the continuation of the cartel after the inspections, and, in particular, it was the first to provide evidence and explanations to prove continuity of the infringement post-inspections and until April 2004. Prior to Frabo's leniency application, the Commission could not have established the duration and continuity of the infringement from March 2001 until April 2004. On this basis and in line with past practice the Commission considered that Frabo should not be penalised for its cooperation by imposing on it a higher fine than the one that it would have had to pay without its cooperation. Therefore the basic amount of Frabo's fine was reduced for effective cooperation outside the scope of the 1996 Leniency Notice, by the hypothetical amount of the fine that would have been imposed on Frabo for a three year infringement.

The Commission only found one attenuating circumstance: the minor/passive role claimed by Flowflex. The basic amount for Flowflex was therefore reduced by 10%.

Sufficient deterrence

In order to set the amount of the fine at a level which ensured that it had sufficient deterrent effect and in line with previous practice, the Commission considered it appropriate to apply to one of the undertakings concerned, Tomkins, a multiplication factor to the fines imposed.

Application of the 1996 Leniency Notice

Mueller was the first undertaking to inform the Commission about the existence of a cartel in the fittings sector affecting the EEA market in the 1990s. Mueller's submissions prior to the Commission's investigation, enabled the Commission to establish the existence, content and the participants of a number of cartel meetings and other contacts held in particular between 1991 and 2000 as well as to undertake inspections on 22 March 2001 and thereafter. Mueller immediately put an end to its involvement in the infringement before starting its cooperation with the Commission. It continuously provided the Commission with all relevant information and evidence available, and maintained full cooperation throughout the investigation by numerous submissions. Hence, Mueller benefited from total exemption from any fine.

IMI was the second undertaking to submit a leniency application. This application was submitted after the Commission had carried out inspections and had sent to IMI an Article 18 request for information. The evidence, corporate statements and witness interviews provided by IMI cover a period extending from late 1980s to 2001. IMI provided a description of the cartel including a non-exhaustive list of the multilateral meetings and other contacts as well as a number of additional internal evidence drafted at the time the various anti-competitive activities were taking place. It also described the context and provided narratives explaining a number of handwritten notes and other documents found during the inspections at its employees' offices. These narratives made it possible to connect the evidence submitted to specific cartel events. IMI's submissions were completed by oral explanations given by IMI's employees at interviews conducted at the Commission's premises in Brussels on a number of occasions. On an overall basis, IMI assisted the Commission in many respects and its cooperation was active and complete. Consequently and in accordance with Section D of the 1996 Leniency Notice (10% to 50%), IMI was granted a 50% reduction.

Delta was the third undertaking to submit a leniency application. Delta corroborated IMI's leniency application. The corporate statements and witness interviews provided by Delta covered the period of the UK arrangements and continued during the period of the pan-European arrangements until March 2001. In its corporate statements and witness testimonies, Delta provided a description of the cartel making the distinction between the UK arrangements that started in the late 1980's and the later pan-European arrangements. Although Delta did not provide information establishing continuity between these two arrangements, it nevertheless clarified and confirmed evidence in the possession of the Commission regarding the infringement in late 1988. It thus allowed the Commission to solidify its evidence proving continuity between these two periods. Consequently and in accordance with Section D of the 1996 Leniency Notice (10% to 50%), Delta was granted a 20% reduction.

Frabo was the fourth undertaking to submit a leniency application. Frabo corroborated the facts presented by IMI and Delta. The evidence and corporate statements provided by Frabo covered mainly the period between 1998 and 2004. This evidence allowed the Commission to solidify its evidence for the period ending with the inspections in March 2001.Consequently and in accordance with Section D of the 1996 Leniency Notice (10% to 50%), Frabo was granted a 20% reduction.

Advanced Fluid Connections was the fifth undertaking to submit a leniency application. Advanced Fluid Connections approached the Commission and provided direct evidence of the infringement for the period from June 2003 until April 2004 confirming Frabo's leniency application. However, in its reply to the Statement of Objections, Advanced Fluid Connections only admitted a limited number of facts as to the period after the inspections while contesting the validity of others. In addition, as indicated above, Advanced Fluid Connections misled the Commission. In these circumstances, Advanced Fluid Connections was not granted any reduction of the fine.

Comap was the last undertaking to submit a leniency application, which was part of its reply to the Statement of Objections. Comap's application was thus submitted four and a half years after the Commission's inspections and two and a half years after the Commission had first contacted Comap requesting information. Comap's leniency application was based on the non-contestation of facts for the period between 8 December 1997 and March 2001. Thus, Comap's non-contestation of facts was limited only to three out of thirteen and a half years of the infringement. In these circumstances, Comap was not granted any reduction of the fine.

Conclusion

The total of fines imposed in this case makes it the fifth largest set of fines ever imposed on a cartel.

In this case, the Commission issued a strong warning against undertakings that disregarded the inspections and even, for some of them, continued the infringement for as much as three years thereafter. The fact that these undertakings participated in the infringement even though they were informed that the Commission had launched an investigation targeted at that very infringement led to an increase of the fine, representing a sanction for the additional unlawful energy expended in continuing the infringement. The Commission also issued a strong warning against undertakings that provide it with misleading information.

At the same time, however, by granting full immunity from fines to Mueller, the Commission is offering an incentive to future immunity applicants to come forward and actively cooperate with the Commission's investigations.

Competition Commissioner Neelie Kroes commented on this case by stating *"We will not tolerate cartels and will take all measures to stamp them out. We will not only punish firms severely for cartel behaviour, but also increase the fines for flagrantly continuing after a Commission dawn raid and for providing wrong or misleading information"*.

Commission fines producers and traders of synthetic rubber € 519 million for price fixing and market sharing cartel (1)

Massimo DE LUCA and Bjarke LIST,
Directorate-General for Competition, units F-2 and F-3

On 29 November 2006 the Commission adopted a Decision and imposed fines totalling € 519 050 000 on five groups of companies for participating in a cartel involving price fixing and market sharing for certain types of synthetic rubber. The addressees of the decision are Bayer, Dow, Eni, Shell, Unipetrol and Trade-Stomil. Eni and Shell had their fines increased as they are repeat offenders. Bayer, also a repeat offender, avoided a fine by receiving full immunity under the Commission's leniency regime for being first to provide information about the cartel. The fine of Dow was reduced as a consequence of its cooperation under the leniency regime.

The products

The cartel involved the following two synthetic rubber products:

— **Butadiene Rubber (BR); and**

— **Emulsion Styrene Butadiene Rubber (ESBR).**

Both Butadiene Rubber (BR) and Emulsion Styrene Butadiene Rubber (ESBR) are primarily used in tyre production. Other applications for BR and ESBR are various types of consumer goods such as shoe soles, floor coverings and golf balls. Among the companies involved in the cartel, Bayer, Dow, Polimeri (Eni group), Shell, Kaucuk (Unipetrol group) and Trade Stomil, who traded the production of the Polish company Dwory, were active in the supply of ESBR, while only Bayer, Dow, Polimeri (Eni group) and Shell produced BR.

The investigation showed that the cartel covered the whole, or at least the large majority, of the EEA. The total value of 2001 EEA BR and ESBR sales is estimated to have been at least € 550 million.

The infringement

During the period beginning at least 20 May 1996 and continuing until at least 28 November 2002 the addressees of the Decision agreed on price targets for the products, shared customers by non-aggression agreements and exchanged sensitive commercial information relating to prices, competitors and customers.

In March 2003 the Commission carried out an inspection at the premises of Dow following applications covering BR and ESBR for immunity from fines submitted by Bayer under the 2002 Notice on immunity from fines and reduction of fines in cartel cases ("Leniency Notice").

After the inspection Dow submitted a leniency application.

On 7 June 2005 the Commission initiated proceedings, and adopted a first Statement of Objections.

After having received new information the Commission adopted a second Statement of Objections on 6 April 2006. An Oral Hearing was held on 22 June 2006.

In the margins of some but not all of the meetings of the European Synthetic Rubber Association (ESRA), typically during dinner, at the bar, on the way to dinner, in the hotel room of one of the participants or at a specifically hired conference room, and hence outside the official ESRA meetings and in the absence of the ESRA Secretary General, the companies concerned concluded price agreements for BR and ESBR. The discussions leading to the price agreements could take the form of actual cartel meetings or a series of side meetings between two or three producers and the discussions started typically with a discussion of prices for key raw materials and often led to a decision to increase or stabilise prices, typically by setting a target price for the next quarter or to agree to a roll-over price, that is to say, that the same price as in the previous quarter would apply for the next. The market sharing agreements typically took the form of "non-aggression agreements" or "status quo agreements" whereby the competitors agreed

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to avoid aggressive competition for the main clients of the other players as, if this happened, they could expect an attack on their main clients. This could also take the form of assurances concerning specific clients.

The cartel Decision is based on numerous documents, corporate statements and witness interviews provided by the leniency applicants, together with meeting notes discovered by the Commission during the on-site inspection. The Statements from Bayer were to a large extent confirmed by the statements given by Dow. At a later stage, Shell also admitted to having participated in the cartel.

Fines

The practices uncovered are a very serious infringement. In fixing the fines, the Commission took account of the size of the EEA market (at least € 550 million), the duration of the cartel (up to 6 years and 6 months), and the size of the firms involved. The Commission increased the fines by 50% for Eni and Shell as they are repeat cartel offenders.

In setting the starting amount of the fine for each undertaking, the Commission took into account their combined turnover in the EEA for BR and ESBR in the most recent full year of the infringement in which the undertakings were active in the cartel. As there was considerable disparity between each undertaking's turnovers in the cartelised industry, the undertakings were divided into five groups. In this manner, the Commission takes into account the effective economic capacity of the undertakings to cause significant damage to competition in the cartelised industry.

Shell claimed their co-operation outside the scope of the Leniency Notice as an attenuating circumstance. The Commission decided to evaluate Shell's cooperation within the scope of the leniency notice as if Shell had made a formal application. Another attenuating circumstance claimed was lack of implementation, which was rejected by the Commission.

Repeated infringements

At the time the infringement took place, Bayer, Eni and Shell had already been subject to previous Commission prohibition decisions for cartel activities. This justified an increase of 50% in the basic amount of the fine to be imposed on these undertakings.

Sufficient deterrence

In order to set the amount of the fine at a level which ensured that it had sufficient deterrent effect, and in line with previous decision practice, the Commission considered it appropriate to apply a multiplication factor to the fines imposed on Bayer, Dow, Eni and Shell.

Individual increases of the fine were also applied according to the duration of the infringement by each legal entity. In consideration of the fact that Dow did not own Shell's BR and ESBR business during the first three years of the infringement and that Shell is also liable for the infringement in respect of the same period, the increase linked to duration was reduced for Dow.

Application of the 2002 Leniency Notice

Bayer was the first undertaking to inform the Commission of the existence of a cartel and was granted conditional immunity from fines in accordance with point 8(a) of the Leniency Notice on 5 February 2003. Bayer was granted full immunity from the fine that would otherwise have been imposed on it.

Dow was the second undertaking to approach the Commission under the Leniency Notice, on 16 October 2003, and the first undertaking to meet the requirements of point 21 thereof, as it provided the Commission with evidence which represented significant added value with respect to the evidence already in the Commission's possession a the time of its submission. On 4 March 2005 Dow was informed of the intention of the Commission to grant it a reduction of 30 to 50 % of the fine which would otherwise have been imposed on it. Dow was granted a reduction of 40 % of the fine that would otherwise have been imposed on it.

In its reply to the First Statement of Objections, Shell accepted that the facts, which the Commission was addressing, actually occurred, and pointed to limited additional factual circumstances. Shell did not apply for leniency under the terms of the Leniency Notice. Nonetheless the Commission decided to consider its co-operation under the terms of the Leniency Notice. The Commission found that at the time the information was provided, it did not constitute significant added value with respect to the evidence already in the Commission's possession, as the Commission was already able to prove the infringement in all of its main elements. No reduction was granted to Shell for its co-operation.

Addressees, duration and fines imposed

Addressees	Duration	Fines imposed
Bayer AG	from 20 May 1996 to 28 November 2002	EUR 0
The Dow Chemical Company	from 1 July 1996 to 28 November 2002	EUR 64 575 000
Jointly and severally with **Dow Deutschland Inc**	from 1 July1996 to 27 November 2001	EUR 60 270 000
Jointly and severally with **Dow Deutschland Anlagengesellschaft mbH** and **Dow Europe GmbH**	from 22 February 2001 to 28 February 2001 from 26 November 2001 to 28 November 2002	EUR 47 355 000
Eni S.p.A. and **Polimeri Europa S.p.A,** jointly and severally	from 20 May 1996 to 28 November 2002	EUR 272 250 000
Shell Petroleum N.V., Shell Nederland B.V. and **Shell Nederland Chemie B.V.,** jointly and severally	from 20 May 1996 to 31 May 1999	EUR 160 875 000
Unipetrol a.s. and **Kaucuk a.s,** jointly and severally	from 16 November 1999 to 28 November 2002	EUR 17 550 000
Trade-Stomil Ltd	from 16 November 1999 to 22 February 2000	EUR 3 800 000

The total of fines imposed in this case was the second largest fine that had ever been imposed on a cartel. The fine imposed on Eni was the second largest fine imposed on a single company.

Commission fines fourteen undertakings a total of € 266 million for participating in a cartel for road pavement bitumen in the Netherlands (1)

Jan NUIJTEN and Bertus VAN BARLINGEN,
Directorate-General for Competition, units F-2 and F-1

On 13 September 2006 the Commission adopted a decision and imposed fines totalling € 266 717 000 on eight suppliers and six purchasers of road pavement bitumen in the Netherlands for having participated in a cartel between 1994 and 2002. The bitumen suppliers fined are Esha (Smid & Hollander), Klöckner Bitumen, Kuwait Petroleum, Nynäs, Shell, Total and Wintershall. The bitumen purchasers fined are Ballast Nedam, BAM, Dura Vermeer, HBG (now part of BAM), Heijmans and KWS. Shell had its fine increased because it was found to be a repeat offender and because of its instigating/leading role in the cartel. The fine for KWS was also increased because of the instigating/leading role of this undertaking and because of its attempts to obstruct the Commission in carrying out its investigation. Another participant of the cartel, BP, avoided a fine of € 30 million by receiving full immunity under the Commission's leniency regime for being the first to provide information about the cartel. The fine of Kuwait Petroleum was reduced because it also provided information with significant added value under the Commission's leniency regime.

The product

Bitumen, a by-product of fuel production, is mainly used as an adhesive in the production of asphalt, binding the other materials together. It is also used in a variety of industrial applications such as roofing felts, paints and varnishes etc. The cartel covered all bitumen used for road construction in the Netherlands, a market valued around € 62 million in 2002.

The investigation

The investigation was prompted by an application for immunity of fines from BP in June 2002 under the 2002 Notice on immunity from fines and reduction of fines in cartel cases ("2002 Leniency Notice") (2) that covered several Member States.

In October 2002 the Commission carried out inspections at the premises of several undertakings. When the Commission later continued its investigation by means of sending out requests for information in June 2003, several undertakings submitted leniency applications or provided the Commission with information on a voluntary basis in September/October 2003.

During the investigation it appeared that the cartel in the Netherlands, in which the large buyers were also involved, operated as a distinct cartel. It could not be established that this cartel formed part of any wider collusion covering other Member States and the Commission handled the investigation in the Netherlands in its own right, given that the facts in question constitute a separate infringement.

Proceedings were initiated and a Statement of Objections was issued in October 2004, addressed to 37 legal entities belonging to 15 undertakings. The oral Hearing was held in June 2005 and the final Decision was adopted on 13 September 2006 and addressed to 31 legal entities belonging to 14 undertakings.

The Commission investigation is separate from the investigations the Dutch Competition authority (NMa — Nederlandse Mededingingsautoriteit) has conducted in recent years in the construction sector. The Commission investigated price fixing for sales and purchases of bitumen in the Netherlands whereas the NMa investigated market sharing and bid rigging in downstream asphalt and road building markets in the Netherlands. The players involved are different in the sense that the bitumen cartel included the bitumen suppliers. The behaviour also relates to a different product and different cartel activities.

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(2) OJ C45, 19.02.2002, p. 3-5. It was revised by the entry into force of a new Leniency Notice on 8.12.2006, OJ C298, p. 17-22.

The infringement

The addressees of the Decision participated in a single and continuous infringement of Article 81 of the EC Treaty from at least 1994 to 2002 with respect to road pavement bitumen.

In a series of meetings, called the "bitumen consultation" ("bitumenoverleg"), a delegation of the bitumen suppliers met with the six biggest road construction companies in the Netherlands. These meetings were usually preceded by preparatory meetings of the suppliers and separate preparatory meetings of the six biggest road construction companies (the latter being referred to as "WO5" or "WO6" ("wegenbouwoverleg") ([3]).

In the joint meetings, the bitumen suppliers fixed with the large construction companies the price of bitumen (i.e. the gross price to be invoiced to the asphalt production plants that are owned by the road building companies in the Netherlands). It not only relates to the price of bitumen purchased (via their asphalt plants) by these large construction companies, but for all road pavement bitumen.

The large constructing companies owning these plants appeared not to be particularly concerned about the absolute level of the price of bitumen, as long as they directly received discounts that were higher than the rebates received by their smaller competitors. Therefore, they agreed in these meetings with the bitumen suppliers on two rebates (i.e. the rebates that are usually directly settled between the bitumen supplier and the road builder owning the asphalt production plant): a uniform minimum rebate for themselves and a smaller, maximum rebate for all other construction companies active in the Netherlands. In this manner, they not only limited competition for an important input among themselves, but they also deliberately and artificially disadvantaged smaller construction companies in the Netherlands.

Regular monitoring of the implementation of the agreements took place and sanctions (in the form of retroactive extra discounts) could be imposed on the suppliers if they were found to have granted too high rebates to smaller road builders.

The fixing of prices and rebates formed part of one overall anti-competitive scheme and the Commission considers such behaviour cartel behaviour. It does not accept claims that the behaviour of the large construction companies was a separate and less serious infringement.

([3]) "Wegenbouwoverleg" means road building consultation; the number 5 or 6 refers to the number of large construction companies participating in the system.

Fines

The fines imposed by the Commission have been adopted in application of the 1998 Fining Guidelines ([4]).

The Commission took first into account the gravity of the infringement and in particular the fact that the practices uncovered are by nature a very serious infringement of the EU competition rules. The Commission also took into account the size of the market.

The Commission furthermore took into account the effective economic capacity of the undertakings involved to cause significant damage to competition in the cartelised industry: the undertakings were divided into different groups on the basis of their sales or purchases in the Netherlands of bituminous products for road building and similar applications in the most recent full year of the infringement in which they were active in the cartel.

In order to set the amount of the fine at a level which ensures that it had sufficient deterrent effect the Commission considered it appropriate in this proceeding to apply a multiplication factor, based on the worldwide turnovers in the financial year 2005, to the fines imposed for the undertakings with an annual turnover of more than € 10 000 million. Individual multiplying factors were also applied to all legal entities in function of the long duration of the infringement of each of them.

The Commission increased the fine by 50% for Shell because, at the time this infringement took place, it had already been subject to previous Commission decisions for its involvement in the polypropylene and PVC (II) cartels. The Commission also increased the fine by 50% for Shell and KWS because they were considered to have played an instigating and a leading role in the cartel. Finally, the Commission increased the fine by 10% for KWS for its attempts to obstruct the Commission investigation, in particular by refusing the inspectors access to its premises, forcing them to invoke the aid of the Dutch Competition Authority and the Dutch police.

Several undertakings claimed attenuating circumstances, such as a minor/passive role in implemen-

([4]) Guidelines on the method of setting fines imposed pursuant to Article 15 (2) of Regulation No 17 and Article 65 (5) of the ECSC Treaty, OJ C 9, 14.01.1998, p. 3-5. These Guidelines have been revised by the Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003. OJ C 210, 1.9.2006, p. 2-5, but the 2006 Guidelines will only apply to decisions where a statement of objections is issued after 1.9.2006.

tation of the agreements and absence of benefit, early termination of the infringement, existence of a reasonable doubt as to whether the restrictive conduct constituted an infringement, co-operation outside the 2002 Leniency Notice and the fact of fines imposed by the NMa for related infringements. All these claims were rejected. Voluntary co-operation was assessed under the 2002 Leniency Notice and the fines imposed by the NMa relate to different infringements.

For one undertaking, Esha, the maximum fines threshold of 10% of annual turnover was met and the fine was accordingly limited.

Application of the 2002 Leniency Notice

BP, Kuwait Petroleum and Shell submitted applications under the 2002 Leniency Notice. Other undertakings also claimed to have provided the Commission with information on a voluntary basis. None of the construction companies applied for leniency with the Commission.

BP disclosed the existence of the cartel in June 2002 and otherwise met the conditions of the Leniency Notice. It was therefore granted full immunity from paying a fine which was calculated at € 30 780 000.

Kuwait Petroleum was the second undertaking to approach the Commission with information under the Leniency Notice, on 12 September 2003, and the first undertaking to meet the requirements of point 21 thereof. The Commission considered the evidence submitted by Kuwait Petroleum of significant added value and granted a reduction of its fine, within the bracket of 30%-50%, of 30% (= a reduction of € 7 million). The reduction was not higher because it was only made almost one year after the Commission had conducted inspections. It was also taken into account that Kuwait Petroleum reformulated part of its statements after the Oral Hearing and that this contributed to the withdrawal of the accusations against one undertaking that was still addressed in the Statement of Objections.

Other undertakings voluntary submitted information shortly after Kuwait Petroleum. That time, the information provided did not or no longer constitute significant added value with respect to the evidence already in possession of the Commission and therefore failed to qualify for a reduction of the fines.

Commission re-adopts cartel decisions in the steel sector [1]

Téa Katarina BROMS and Susanne LAGEARD,
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Introduction

In 2006, the Commission corrected procedural errors in cartel cases in the steel sector which had led to the annulment of two cartel decisions by the EC Courts [2]. The Commission's intention is to correct any procedural error to ensure that companies will not escape cartel fines for procedural reasons.

The two cartel decisions re-adopted in 2006 concerned hot-rolled steel beams used in the construction industry (*Steel beams case*) and stainless steel products (*Alloy Surcharge case*). In both cases the Courts had found that the Commission had not explicitly invited one addressee of its final decision to give its views on some parts or the whole of the infringement on which it was held liable. These errors were corrected by reopening the proceedings and addressing new Statements of Objections against companies that had not been fully heard on the original Statement of Objections.

For both decisions, the ECSC Treaty still constituted the substantive law applicable since the infringement was committed whilst the Treaty was still in force (the ECSC Treaty expired in 2002). As regards procedure, the law applicable was the existing EC Treaty.

Steel beams case

In 2003, the Court of Justice annulled the judgment of the Court of First Instance and, on procedural ground, the Commission cartel decision from year 1994 in *Steel beams* case [3] in so far it concerned one undertaking, Arbed SA (Decision of the Commission 94/215/ECSC [4]). The Commission decision imposing fines was addressed to Arbed SA while the Statement of Objections in 1992 had been sent to TradeArbed, Arbed SA's subsidiary.

Following the judgements, the Commission re-opened the procedure as regards Arbed SA and issued a Statement of Objections in March 2006 correcting the procedural error [5] and, on 8 November 2006, re-adopted the decision in *Steel beams* case. The facts and the substance of the decision were based on the findings of the earlier Commission decision with the exception of objections that were dismissed by the Court of First Instance.

In order to avoid discrimination between the companies that were fined on the basis of the old decision in 1994, the Commission set the fine taking into account the ruling of the Court of First Instance. The amount of the fine was € 10 000 000.

Alloy surcharge case

The Commission, in its decision of 20 December 2006 in *Alloy surcharge* case [6], held Thyssen-Krupp Stainless AG (TKS) liable for Thyssen Stahl AG's (TS-AG) conduct during the years 1993 and 1994 after it sent a Statement of Objections to TKS giving it the possibility to defend the allegations raised against TS-AG. The cartel infringement as such — collusion on a price element of stainless steel products — was not at issue in the re-adoption case.

In order to hold TKS liable for the illegal behaviour of TS-AG, the Commission based itself again on the explicit and voluntary statement from TKS given to the Commission during the old investigation procedure (Decision of the Commission 98/247/ECSC [7]) according to which TKS takes over the liability for the behaviour of TS-AG. The Commission highlights that the Courts accepted that such a statement could lead to a transfer of liability. No legal nor economic succession is invoked in this respect.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.
(2) For *Steel beams:* T-137/94 [1999] ECR II-303 and C-176/99 P [2003] ECR I-10687. For *Alloy surcharge:* T-45/98 and T-47/98 [2001] ECR II-3757 and C-65/02 P and C-73/02 P, not yet published.
(3) Case COMP 38.907– Steel beams.
(4) OJ L 116, 6.5.1994, p. 1.
(5) The Statement of Objections and the Commission decision in 2006 were addressed to Arcelor Luxembourg S.A (ex-Arbed SA), Arcelor International SA (ex-TradeArbed SA), the wholly-owned subsidiary of Arbed SA, and to Arcelor Profil Luxembourg S.A. (ex-ProfilArbed SA, the economic successors of the steel beams activities of Arbed SA). Following the creation of Arcelor as a result of the merger between Arbed, Aceralia and Usinor in 2002, TradeArbed SA changed its name to Arcelor International.
(6) Case COMP 39.234 — Alloy surcharge.
(7) OJ L 100, 1.4.1998, p. 5.

In order to avoid discrimination between the companies that were fined on the basis of the old decision in 1998, the Commission set the fine in exactly the same manner as in the 1998 decision taking into account the ruling of the Court of First Instance. This means that the final amount of the fine was € 3 168 000.

Mergers — Main developments between 1 September and 31 December 2006 (1)

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Introduction

Merger and acquisition activity continued at high levels during the four months from September to December with numbers reaching record levels at year end. The Commission received a total of 120 notifications and adopted 132 final decisions during the period. This compares with 125 notifications and 115 decisions adopted in the previous trimester.

The Commission adopted a total of 124 decisions after a Phase I investigation in this trimester with 84 of these qualifying for treatment under the simplified procedure. The Commission also adopted 4 decisions subject to conditions and obligations pursuant to Article 6 (2) ECMR during this period.

The Commission adopted 3 decisions pursuant to Article 8 after in-depth investigation. Two cases were cleared subject to substantial commitments being made (Gaz de France/Suez and Metso/Aker). The remaining case — Glatfelter/Crompton — was cleared without conditions as the Commission was satisfied that there was sufficient competitive pressure coming from other competitors in the market. The Commission also opened 6 Phase II investigations (Article 6(1) (c) ECMR) during this period. One case was withdrawn during Phase II.

The new streamlined referral mechanism introduced in 2004 for cases without Community dimension continues to generate a large number of referrals with the total number of requests for the trimester reaching some 16 cases. There were also two post-notification referrals — one case was referred to the Commission pursuant to Art. 22 and one case was referred by the Commission to a Member State pursuant to Art. 9 (Foster Yeoman /Aggregate Industries — see below for further details).

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

A — Summaries of decisions taken under Article 6

Nokia/Siemens

On 13 November, after an intensive Phase I investigation, the Commission gave its unconditional go-ahead to the proposed merger between the Finnish company Nokia and the network equipment business of the German company Siemens AG.

Nokia is mainly active in mobile telecommunications, i.e. handsets and equipment to run mobile telephony networks. Siemens has activities in the telecommunications sector and is active in a number of other business areas such as automation and control, power and transportation. Both Nokia and Siemens supply telecommunications equipment and related services to operators of communications networks worldwide. Communications networks enable operators to transmit all types of content (voice, data or multimedia) to customers on a global scale. By the proposed concentration Nokia would acquire control of the newly created company, Nokia Siemens Networks, to which Nokia and Siemens would contribute their mobile and fixed-line telecommunications network equipment business.

The main competitive impact of the proposed transaction was in the mobile network equipment sector, since Nokia has few activities in fixed-line telecommunications. The Commission's market investigation revealed that, despite the considerable market shares the merged entity would have in the mobile network equipment sector, the market structure would remain competitive. A sufficient number of credible competitors would remain in the market, inter alia market leader Ericsson and Alcatel-Lucent. Customers (mostly network operators) would still have alternative suppliers.

The Commission's investigation did not reveal any cause for concern with respect to any of the other activities of the parties namely those relating to fixed-line telecommunications network equipment and associated mobile and fixed-line services.

Toshiba/Westinghouse /BNFL

In September the Commission cleared a proposed acquisition by the Japanese conglomerate Toshiba of Westinghouse Electric UK and the BNFL USA Group, both active in the nuclear sector.

As well as being a worldwide supplier of equipment in a number of other sectors, Toshiba supplies nuclear power plants, including instrumentation and control systems and post-installation services, to utilities that operate such plants, mainly in Asia. Toshiba also holds a minority share in the nuclear fuel assembly supplier Global Nuclear Fuels ("GNF"), controlled by the US company General Electric ("GE"), with Hitachi of Japan also holding a minority stake.

Westinghouse Electric UK and the BNFL USA Group (hereafter "Westinghouse"), currently part of British Nuclear Fuels plc, are active worldwide in all aspects of nuclear power plants.

The Commission found that the proposed transaction would combine two suppliers of nuclear power plants and related products whose activities are to a significant extent complementary, both technologically and geographically. Toshiba is focussed on nuclear power plants based on so-called boiling water reactors, mainly in Asia, whilst Westinghouse is active principally in pressurised water reactors. The merged entity would still face competition from a number of suppliers of nuclear products and services after the merger. In particular GE, and the French company Areva would continue to be strong competitors to Westinghouse, since they are active in the nuclear power industry on a world-wide scale, GE being particularly strong in nuclear power plants, and Areva as a market leader in control systems and nuclear post-installation services in Europe.

The Commission investigated in particular the effects of the transaction in the nuclear fuel assemblies markets, in which Westinghouse, Areva, and GNF are the largest suppliers worldwide. During the Commission's investigation, concerns materialised as to possible effects on potential competition in the fuel assembly markets of the combination of Toshiba's stake in GNF with its control of Westinghouse. To allay these concerns Toshiba has submitted to the Commission a commitment to modify its contractual arrangements with its partners in GNF, General Electric and Hitachi, in order to eliminate the risk that Toshiba could impede competition through the joint venture.

The Commission concluded that, subject to full compliance by Toshiba with the commitment submitted, the proposed operation would not raise competition concerns and would not have any negative impact on European customers or on the safety of energy supply in Europe

Veolia /Cleanaway

A conditional clearance was granted to the proposed acquisition of the UK waste management service company Cleanaway by Veolia ES Holdings plc. on 21 September. Veolia, the acquirer, is also in the waste management business.

Veolia ES provides waste management services in the UK, in particular the collection and disposal of municipal, industrial and commercial waste. It is an indirect subsidiary of Veolia Environnement, a global provider of environmental management services. Cleanaway is a provider of waste management services in the UK, including the collection, disposal and treatment of municipal, commercial and industrial waste, as well as a range of related services such as street cleansing.

The Commission's investigation showed that in most segments of the UK waste management sector (collection and disposal of waste) the proposed transaction would not raise competition concerns because the new entity would face competition from several strong waste management service providers.

However, the Commission's market investigation revealed that there could have been an adverse effect on competition in relation to the thermal treatment/incineration of hazardous industrial and commercial (I&C) waste. This is a particular type of service in which both parties were active. The service involves the use of high temperature incinerators ("HTIs") designed principally to incinerate hazardous waste at high temperatures (typically greater than 1000° Celsius). The Commission's investigation indicated that for certain types of hazardous waste, HTI incineration was the only viable alternative. It was likely therefore that there was a separate market for incineration of hazardous waste in HTIs only. Furthermore, in particular due to regulatory barriers to the export of hazardous waste for incineration in HTIs outside the UK, the geographical scope of the market was considered to be national.

In the UK there were at the time of notification only two HTI facilities for large scale hazardous waste treatment — one belonging to Veolia and the other to Cleanaway. Therefore, the proposed transaction as originally notified would have led to a 100% market share on the merchant market for incineration of I&C hazardous waste in HTIs in the UK.

To address the Commission's concerns in the HTI market, Veolia undertook to divest its HTI facility at Fawley in Hampshire. This would allow a second service provider and thus restore the competitive structure existing before the proposed transaction. This would ensure that the merged company will continue to have at least one commercial viable competitor on the market for the thermal treatment/incineration of hazardous industrial and commercial (I&C) waste by HTI.

Fisher/Thermo Electron

On 9 November the Commission approved the proposed acquisition of Fisher Scientific International Inc. by Thermo Electron Corporation. Both Thermo and Fisher are US companies active in the field of manufacturing and supplying a wide variety of analytical instruments, scientific equipment, consumables and services to the scientific community, including clinical, pharmaceutical, environmental and industrial laboratories. Fisher is also active as a distributor of laboratory and life science products.

The Commission examined the competitive effects of the merger in the markets where both companies are active as suppliers. The Commission's investigation showed that the new entity would continue to face strong, effective competitors in the manufacturing of the products involved, with the exception of centrifugal evaporators. Centrifugal evaporators are pieces of equipment that use heat, vacuum and centrifugal force to concentrate laboratory samples by separating the solvent from samples suspended in solutions. However as Thermo undertook to divest all of Fisher's assets related to the production of centrifugal evaporators, the competition concerns that could result from the proposed transaction were entirely removed.

Given that Fisher is active as a distributor, the Commission also scrutinised the market characteristics and the competitive structure at both manufacturing and distribution level and concluded that a significant share of distribution would still be available to other suppliers and likewise that distributors would not have problems in finding alternative sources of supply. Therefore the Commission came to the conclusion that the merged entity would lack the ability to restrict distributors' access to input or to drive competing manufacturers out of the market.

Johnson and Johnson /Pfizer

On 11 December the Commission cleared Johnson & Johnson's ("J&J") proposed acquisition of Pfizer's consumer healthcare business ("PCH") subject to conditions.

J&J is a leading healthcare group active worldwide in three business segments: pharmaceuticals, consumer products and medical devices and diagnostics. PCH is Pfizer's worldwide business division active in over-the-counter ("OTC") pharmaceuticals and personal care products.

The Commission's investigation focused on the few product areas where the activities of J&J and PCH overlap. The investigation revealed that the proposed transaction would not significantly modify the structure of most of the concerned markets and that a number of credible alternative competitors would continue to exercise a competitive constraint on the merged entity.

However, the Commission found that the proposed transaction could significantly impede effective competition for topical dermatological antifungals in Italy and daily-use mouthwash in Greece. In Italy, the combination of the topical dermatological antifungals of J&J (with the brands *Daktarin, Pevaryl* and *Nizoral*) and PCH (with the brand *Trosyd*) would have reduced the number of players on the market from three to two. In Greece, J&J (with the brand ACT) and PCH (with the brand *Listerine*) are the two leading suppliers of daily-use mouthwash.

To resolve these competitive concerns, J&J proposed to divest the OTC topical dermatological antifungal formulations supplied by PCH in Italy under the trademark *Trosyd* and its *ACT* daily-use mouthwash business EEA-wide. The divestitures consist of the sale of the relevant assets for the manufacture and sale of the products. These assets include goods and inventory, marketing authorisations, the trademarks, intellectual property rights and know-how.

The Commission further identified competition concerns in the field of "Nicotine Replacement Therapy" products ("NRT"), due to the vertical relationship between J&J's subsidiary, ALZA, and GlaxoSmithKline ("GSK"), for which ALZA manufactures nicotine patches. Through the proposed transaction, J&J would acquire PCH's *Nicorette* NRT business, which directly competes with GSK's *NiQuitin* NRT business. Post-merger, the combined entity could thus have the ability and the incentive to engage in input foreclosure strategies vis-à-vis GSK and would have access to confidential information from one of its main competitors.

J&J offered to divest ALZA's international nicotine patch business (the global business, excluding the US, Canada and South Korea). In the event that such divestiture has not taken place within a given time, J&J would divest ALZA's global nicotine patch business (including sales in the

US, Canada and South Korea). The main assets to be transferred are the relevant supply agreements, trademarks, technology and, as an option for the purchaser, ALZA's nicotine patch production lines. In addition, J&J undertook to provide manufacturing capacities and technical assistance to the purchaser until the latter had become fully operational. Following the divestiture of ALZA's nicotine patch business, the purchaser would thus be in a position to supply GSK's requirements in the EEA independently from J&J.

These remedies remove all overlaps between J&J and PCH for topical dermatological antifungals and daily-use mouthwash, as well as the vertical relationship between J&J's nicotine patch manufacturing activities and PCH's NRT business.

B — Summaries of decisions taken under Article 8

Glatfelter/Crompton

On 20 December the Commission gave its unconditional approval to the proposed takeover of Crompton's Lydney paper mill by Glatfelter of the US. This approval followed an in-depth Phase II investigation.

Glatfelter is a US manufacturer of specialty papers with production sites in the US, Germany, France and the Philippines. The company manufactures, in particular, wetlaid fibre materials such as tea-bag paper, paper for coffee-filters and coffee-pads, as well as overlay papers for laminates which are used to produce flooring, furniture and work surfaces. The target company Crompton had been a leading manufacturer of specialty papers for the tea-bag and coffee-filter industry with three paper mills in the UK and worldwide sales. It had been placed in court-ordered administration earlier in the year.

The case had been referred to the Commission by the German Bundeskartellamt pursuant to Art. 22 (3) of the Merger Regulation. The Commission's market investigation found that although Glatfelter, together with the Lydney mill, would control a substantial share of both sales and capacity in the European Economic Area (EEA), this would not constitute a significant impediment to effective competition. The new entity would remain constrained by its competitors, such as Ahlstrom and Purico. These companies, along with other potential competitors, would be able to expand their capacity in response to an increase in the price of wetlaid fibre for tea and coffee filtration. Purico's Chinese manufacturing facility had recently become operational and provides the market with new capacity. Purico also acquired two additional plants formerly owned by Crompton, Devon Valley and Simpson Clough, as well as the Crompton brand. These assets, together with the newly opened mill in Shanghai, established Purico as a significant competitor in the wetlaid fibre market.

Gaz de France/Suez

For a more extensive treatment of this case please see the article on page 83 of this Newsletter

On 14 November the Commission gave its conditional approval to the merger of Gaz de France (GDF) and the Suez group. After an in-depth investigation, the Commission initially found that the deal would have anticompetitive effects in the gas and electricity wholesale and retail markets in Belgium and in the gas markets in France. The Commission's concerns related mainly to the removal of the increasing competitive pressure that GDF and Suez had so far exerted (and would have exerted in the foreseeable future) on each other in both Belgium and France. Given the conditions on the markets, including the very high barriers to entry, their respective dominant positions would have been considerably strengthened by the merger. In response to these concerns, the parties offered extensive remedies including the divestiture of Distrigaz and SPE and Suez relinquishing its control of Belgian network operator Fluxys.

Gaz de France is active in the gas sector at all levels, in electricity generation, electricity retail, and in energy services. It operates throughout Europe, but mainly in France and Belgium. In Belgium, Gaz de France, along with Centrica, has joint control over SPE, the second biggest player in the Belgian electricity and gas markets.

The Suez group is active in the gas and electricity sectors, in energy services and in water and environmental services, and operates mainly in Belgium and France. Suez's main energy subsidiaries are Electrabel (electricity and gas), Distrigaz (gas) Fluxys (gas infrastructures), and (in the energy services sector) Suez Energy Services (former Elyo), Fabricom, GTI, Axima and Tractebel Engineering.

The Commission analysed the impact of the proposed operation on the gas and electricity markets in Belgium and France and concluded that, in the absence of the proposed remedies, the transaction would significantly impede effective competition. Conversely, no negative impact would arise in the other countries concerned, i.e. the UK, Luxembourg, the Netherlands and Hungary.

The Commission found that the merger, as originally planned, would have led to very high combined market shares in Belgium and would have removed GDF as the strongest competitor to the incumbents Distrigaz (gas) and Electrabel (electricity and to a lesser extent gas). The removal of GDF's competitive pressure would also have raised competition concerns with regard to the supply of gas to gas-fired power generators competing with Electrabel. Moreover, in view of its specific assets and strengths, no other company would have been able to reproduce the same level of competitive pressure as GDF.

The Commission also found that high barriers to entry would have further strengthened the parties' dominant position in the gas markets. *Inter alia,* the merging parties would have had access to most of the gas imported to Belgium and would have held almost all long-term import contracts. In addition, due to the parties' control over Fluxys, the network operator, they would have had privileged access to supply infrastructure and storage.

The Commission found that the merger would have strengthened GDF's dominant position in France by removing the competitive pressure exerted by Distrigaz, one of its best placed competitors. In France too, barriers to entry, relating to access to gas and infrastructures, would have increased the horizontal effects of the merger.

Finally, competition concerns would also have arisen in the market for district heating in France, where the merger would have combined the largest player (Suez) with its second largest competitor (GDF), thus leading to a further concentration of this market.

To address these concerns Gaz de France and Suez offered a comprehensive and far-reaching package of remedies. Most notably Suez agreed to divest Distrigaz (including its French activities) and to relinquish control over Fluxys. GDF will in turn divest its shareholding in SPE and, to address the concerns in the district heating market, divest its subsidiary Cofathec Coriance. Furthermore, a series of investment projects will be carried out both in Belgium and in France with a view to increasing infrastructure capacities, thereby facilitating the entry of new competitors onto the market and fostering competition. Most notably, the functioning of the Zeebrugge hub will be enhanced through the creation of a single entry point linking all networks converging on Zeebrugge and through the operation of the hub by an independent operator, Fluxys, which will no longer be controlled by Suez.

The Commission carefully assessed the revised remedies in the light of the response by market operators to an initial package of remedies and concluded that the final package would be sufficient to remove all competition concerns in a clear-cut manner.

The remedies are consistent with the preliminary findings of the ongoing energy sector inquiry (2) which emphasise the need for structural solutions, such as ownership unbundling and severing the link between supply and infrastructure to create pro-competitive conditions for the sustainable development of energy markets.

Metso/Aker

On 12 December the Commission gave conditional approval to a proposed acquisition by Metso Corporation Oy ("Metso") of Finland of the pulp and power business of the Norwegian group Aker Kvaerner ASA.

Both Metso and Aker Kvaerner are active worldwide in the development and production of equipment for pulp mills. The Commission's market investigation showed that the proposed transaction could have substantially reduced competition in those markets for pulp mill equipment in which both companies are active, namely equipment for the cooking, brown-stock washing, oxygen delignification and bleaching stages of pulp production.

The Commission's investigation showed that many customers would welcome a partner like the merged entity, capable of supplying all elements of a modern pulp mill, thereby providing customers with a broader product portfolio and a better knowledge of the overall process of pulp production. At present, only the current market leader, the Austrian-based company Andritz, is able to supply equipment for a complete pulp mill.

However, there are currently only three large suppliers that dominate the supply of pulping machinery: Metso, Aker Kvaerner and Andritz. A fourth player, the Canadian-based GL&V, is only active in supplying certain parts of a pulp mill. Due to the high degree of specific know-how required to produce modern pulp mill machinery, as well as the need to have a strong reputation with customers based on past supplies (the so-called "installed base"), there are significant barriers to entry in the markets concerned.

In order to address these competition concerns, Metso offered to divest its business for the cooking stage (including the "SuperBatch" brand) as well as Kvaerner's businesses for brown-stock washing, oxygen delignification and bleaching equipment (including the "CompactPress" wash

(2) See also the articles on page 23 and page 65 of this Newsletter.

press technology) to GL&V. This will eliminate all overlaps between Metso's and Kvaerner's activities in the supply of pulp mill equipment.

The Commission ensured that the divested businesses comprised all assets, such as know-how, intellectual property rights and key personnel that are currently part of the parties' activities in the relevant fields. Moreover, the Commission verified that after acquiring the divested businesses of Metso and Kvaerner, GL&V would have the capability and incentive to become a credible new third player in the pulping equipment industry.

Whilst Metso gave a commitment to entirely divest all assets related to its batch cooking business, it will retain a licence to continue to use the divested "SuperBatch" technology in competition with GL&V. This was necessary, because some customers of cooking equipment rely exclusively on the so-called "batch" cooking process (currently only offered by Metso and GL&V) and cannot purchase cooking equipment based on the so-called "continuous" cooking technology (supplied by Andritz and Kvaerner). For these customers, the licence prevents a market configuration where they are left with only one supplier of batch cooking technology.

Based on this analysis, the Commission concluded that the commitments provided by Metso would remove all competition concerns raised by the proposed transaction.

C — Summaries of decisions taken in accordance with Article 9

Foster Yeoman /Aggregate Industries

In September clearance was given of the proposed take-over of UK company Foster Yeoman by Aggregate Industries. The clearance related only to markets outside the UK. At the same time, at the request of the UK's Office of Fair Trading (OFT), the Commission referred the examination of the impact of the proposed acquisition on the UK aggregates, asphalt and road surfacing market to the OFT

Aggregate Industries is a subsidiary of the Holcim Group (Switzerland), which is active in aggregates, asphalt and road surfacing, as well as in cement and concrete. Foster Yeoman is a privately-owned heavy building materials group. Both Aggregate Industries and Foster Yeoman are active in the markets for aggregates (mostly sand, gravel and crushed rock), asphalt production and road surfacing, but almost exclusively within the UK.

On 11 August 2006 the United Kingdom requested the referral of that part of the proposed concentration relating to UK markets with a view to carrying out its own assessment under UK competition law, pursuant to Article 9 of the EU Merger Regulation. In the request the UK's Office of Fair Trading ("OFT") submitted that the notified transaction affected competition in a number of separate product markets: the production and supply of aggregates and of asphalt and the supply of surfacing services and related activities. The OFT considered that these markets presented all the characteristics of distinct markets where competition is affected. Moreover, according to the OFT, some of these markets did not constitute a substantial part of the Common Market.

The Commission's findings concurred with the submission of the OFT. Given that an examination of the case would require the investigation of local (sub-) markets and supply relations it agreed that the OFT was best placed to assess the impact of the case on the heavy building materials markets in the UK. In addition, the OFT had recently investigated this sector in the UK and thus it had expertise of the sector. The Commission therefore decided to refer the investigation to the UK Competition Authority for further in- depth analysis of the proposed transaction's effects on a number of local UK markets concerning aggregates, asphalt and road surfacing services.

Aggregate Industries and Foster Yeoman also import aggregates into European ports (including Germany, where they use the port of Rostock), where these aggregates are used as an input for local ready-mixed cement production. Holcim has a local ready-mixed cement production of some importance in Rostock. However, the market position of the combined entity in aggregates would be modest and the Commission concluded that the proposed acquisition would not create any risk of aggregate supply problems for other local ready-mixed concrete producers.

Gaz de France/Suez: Keeping energy markets in Belgium and France open and contestable through far-reaching remedies (1)

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1. Introduction

Following an in-depth investigation, the Commission approved under the EU Merger Regulation the merger between Gaz de France ('GDF') and the Suez Group on 14 November 2006.

GDF is active in the gas sector at all levels, in electricity generation and retail, and in energy services. It operates throughout Europe, but mainly in France and Belgium. In Belgium, GDF, along with Centrica, has joint control over SPE, the second biggest player in the Belgian electricity and gas markets.

The Suez group is active in the gas and electricity sectors, in energy services and in water and environmental services, and operates mainly in Belgium and France. Suez' main energy subsidiaries are Electrabel (electricity and gas), Distrigaz (gas), Fluxys (gas infrastructures).

The Commission analysed the impact of the proposed operation on the gas and electricity markets in Belgium and France and concluded that the transaction would significantly impede effective competition, both due to horizontal and vertical effects. Conversely, no negative impact would arise in the other countries concerned, i.e. the UK, Luxembourg, the Netherlands and Hungary.

To avoid such an impediment to effective competition, GDF and Suez offered a comprehensive and far-reaching package of remedies. Most notably, the merged entity will divest Suez's gas supply business Distrigaz (including its French activities) and relinquish control over the Belgian gas transmission network operator, Fluxys. It will further divest GDF's shareholding in the Belgian electricity supplier SPE and, in order to address competition concerns identified by the Commission in the district heating market, it will also divest GDF's subsidiary Cofathec Coriance. Furthermore, a series of investment projects will be carried out both in Belgium and in France with a view to increasing infrastructure capacities, thereby facilitating the entry of new competitors onto the market and fostering competition. Most notably, the functioning of the Zeebrugge hub will be enhanced through the creation of a single entry point linking all networks converging on Zeebrugge and through the operation of the hub by an independent operator, Fluxys, which will no longer be controlled by Suez.

The Commission carefully assessed these remedies and concluded that they would be sufficient to remove all competition concerns in a clear-cut manner.

From a remedies policy viewpoint, this case is interesting because the far-reaching remedy package *inter alia* includes, through the divestiture of Distrigaz, the severing of the link between the Belgian gas network infrastructure and the main supplier of gas in Belgium, thereby bringing about a form of effective unbundling.

It is important to highlight that, in spite of the delay and the uncertainty as regards the closing of the merger (2), the Commission decision still stands. However, the postponement of the closing may have an impact on the calendar of the remedies implementation.

This article will first sketch out the main relevant features of the European, Belgian and French regulatory environments in the energy sector; it will subsequently briefly describe the competitive assessment carried out by the Commission; and it will finally focus on the remedy package.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.
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(2) By means of its decision of 30 November 2006 the French Constitutional Court ("Conseil constitutionnel") effectively delayed the closing of the GDF/Suez transaction until after 1 July 2007, by stating that "*… ce n'est qu'au 1er juillet 2007 que Gaz de France perdra sa qualité de service public national; que dès lors le transfert effectif au secteur privé de cette entreprise ne pourra prendre effet avant cette date*" (Considérant 26).

2. The pre-merger: situation economic context and regulatory framework in Belgium and France [3]

Belgium

Gas

Belgium imports all of the natural gas it consumes, either via gas pipeline or as liquefied natural gas (LNG). The Belgian market is characterised by the coexistence of two networks: an "H" gas network ("high" nominal calorific value of 11.63 kWh/m^3(n)) and an "L" gas network ("low" nominal calorific value of 9.769 kWh/m^3(n)).

Large customers directly connected to the natural gas <u>transmission</u> network have been eligible (i.e. they can choose their supplier) since 1 July 2004. In the Flemish Region, the market has been liberalised completely, i.e. also on the level of the <u>distribution</u> network, since 1 July 2003. In the Walloon Region and in the Brussels Region, large industrial customers have been eligible since 1 July 2004, whereas residential customers have become eligible on 1 January 2007 in both Wallonia and in Brussels.

Fluxys (a subsidiary of Suez) is responsible for managing, maintaining and developing the transmission network. Fluxys has also been managing, on a transitional basis, the two Belgian storage sites for H-gas (Belgium has no L-gas storage).

The Belgian gas network is used for international transit as well as domestic transmission with the transit volume being three times as large as the domestic consumption. Transit reservations are marketed by Suez' subsidiary Distrigaz &Co. Belgium has eighteen entry points (which are part of the transmission/transit network), fifteen for H gas and three for L gas.

The Zeebrugge hub is the largest gas trading place in Continental Europe and was initially designed to route British gas towards the continent ('forward flow') and continental gas towards Great Britain ('reverse flow') via a submarine pipeline ("Interconnector"). The hub is now also connected to the Belgian gas network but still most of the traded volumes are shipped abroad.

In sum, the Suez group controls the incumbent gas supplier (Distrigaz) and the infrastructure operator (Fluxys). Beside through Distrigaz, Suez is also active in retail supply through ECS (Electrabel Customer Solutions).

Electricity

When the operation was notified, all Belgium consumers were eligible with the exception of household customers in the Brussels and the Walloon region. The latter became eligible on 1 January 2007.

The Belgian transmission network is interconnected with those of the Netherlands and France and one of the transmission networks in Luxembourg. There is no interconnection between the Belgian transmission system and the German and UK systems.

Elia is the transmission system operator (for voltages above 70 kV) and the distribution network operator for voltages between 30 and 70 kV. Distribution of electricity at voltages below 30 kV is in the hands of a number of different distribution network operators which take the form of associations of local authorities known as '*intercommunales*'.

Suez holds a minority share of 27.45% in Elia, the transmission system operator, and has stakes in various network operators known as '*intercommunales mixtes*' (as opposed to the '*intercommunales pures*' which are owned entirely by the public sector).

In sum, as regards the activities of the Parties, the Suez group controls Electrabel, the incumbent electricity player and has a large minority participation in Elia, the transmission system operator and in certain distribution system operators. GDF is active in the Belgian electricity sector through its participation in SPE, the second largest electricity player.

France [4]

Gas

France's regulatory framework provides for the eligibility of all gas purchasers, irrespective of their gas consumption threshold, with the exception of residential customers, for whom full liberalisation will become effective on 1 July 2007.

Eligible customers have the option not to exercise their eligibility. In this case they remain subject to regulated tariffs. On the other hand, once they decide to exercise their eligibility, they are irrevocably under the liberalised tariff regime.

There are five gas entry points in France and two natural gas transmission system operators in France: GDF transmission network (GRTgaz) operates most of the gas network, and Total Infra-

(3) The internal market for gas and electricity is regulated by Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003, repealing Directive 98/30/EC.

(4) As to France, only the gas sector was negatively affected by the merger, whereas the electricity markets were not.

structures Gaz France (TIGF) operates the network in the South West of France. GRTgaz and TIGF are 100% subsidiaries of GDF and Total respectively.

The transmission networks currently comprise five balancing zones, within which operators must (with limited tolerance) inject as much gas as they withdraw. The network operated by GRTgaz has four balancing zones (North, West, East and South) while TIGF's network constitutes a single balancing zone (South-West). There are plans to reduce the number of GRTgaz zones down to two (North and South) in 2009, with the current North, West and East zones to be merged into a single North zone. The transmission network carries high calorific value gas (H gas) into each of the five zones. In the North zone there is also a specific network for low calorific value gas (L gas).

There are currently two methane terminals in France, which are owned and managed by GDF. In addition, GDF has begun building a third methane terminal, which should come on stream at the end of 2007.

In addition, there are fifteen gas storage facilities of which thirteen are owned and managed by GDF inside the four GRTgaz balancing zones. The other two, which are located in the South-West zone, are owned and managed by TIGF.

In sum, as regards the activities of the Parties, GDF is the incumbent player in most of the French territory and in most French relevant markets. GDF also owns and operates the vast majority of the French gas infrastructures. The Suez group has recently become active in France through Distrigaz, in each balancing zone, and has built up strong positions in the East and the North.

3. The impact of the merger: the competitive assessment of the Decision

In its decision, the Commission reached the conclusion that the merger would significantly impede effective competition in four areas: gas in Belgium, gas in France, electricity in Belgium and district heating in France (5).

(5) In France and in the Walloon and Brussels regions of Belgium, the markets for the supply of electricity and gas to residential customers were only to be opened only as from 1 July 2007 (in France) and 1 January 2007 (Brussels and Walloon regions). However, the various players were already preparing for this event. In such a situation, the merger would lead to the disappearance of the main potential competitors for the incumbent in the market for these residential customers. The merger was therefore deemed to have effects also on these prospective markets.

Gas in Belgium

As regards the gas sector in Belgium, the Commission identified significant impediments to effective competition on the following (nationally defined) markets for supply of H and/or L gas: to intermediary resellers (i.e. the "intercommunales", "default suppliers" such as ECS (Electrabel Customer Solutions) and newcomers on the gas supply market in Belgium such as Essent and Nuon, to gas-fired electricity power plants; to large industrial customers; to small industrial and commercial customers; to residential customers (the latter market being potentially regional).

In all these markets, the Parties would have very high combined market shares (in most cases above 80%) and the already dominant position of Suez would be strengthened by the merger.

As a matter of fact, the merger would remove the best placed competitor (GDF) of the incumbent (Suez). No other company would be able to reproduce the same level of competitive constraint as GDF. The Commission found that the significant positions of GDF in the various markets are due to a number of specific assets and advantages enjoyed by GDF which no other new entrant would combine to the same extent. In particular, GDF is the historical operator in the only neighbouring country with no capacity constraints at the Belgian border; GDF has access to a large and diversified gas portfolio, including LNG; GDF has priority access to H gas storage in Belgium; it owns L gas storage capacity in France near the border with Belgium; it is co-owner of certain transit pipelines (SEGEO) through Belgium and shares control of certain entry points, with concomitant capacity reservations on entry points. Moreover, for L gas, Suez and GDF are the only sources for new competitors on the Belgian market, such as Nuon and Essent.

Furthermore, the Commission found that the very high barriers to entry existing in the market would further strengthen the horizontal effects caused by the combination of market shares resulting from the merger. These barriers relate to access to gas (the merging parties have access to most of the gas imported into Belgium, and they hold almost all the long-term import contracts), access to infrastructures (including Suez' control over Fluxys, the network operator, management of the transit network by Distrigaz, insufficient entry capacity, network congestion), access to LNG (the only terminal in Belgium, in Zeebrugge, is managed by Fluxys LNG, a Suez affiliate), access to H gas storage in Belgium (the French storage capacity, owned by GDF, is the best alternative outside Belgium), quality specifications and the lack of liquidity on the Zeebrugge hub. While many of these entry barriers pre-existed the merger, a number of them would be strengthened by it (e.g. pipeline ownership, capacity and storage reservations).

Gas in France

As regards gas in France, the Commission assessed the impact of the merger on the basis of the division of the country into five balancing zones, North, West, East, South and South-West as the Commission found that the five balancing zones remain characterized by differing competitive conditions, and congestions occur between the different zones. As already indicated, four of the five transport networks are owned and managed by GDF, the fifth one being owned and managed by Total.

Taking into account this geographic subdivision into five zones, the Commission identified significant impediments to effective competition on the following markets: the supply of H gas to *large customers* who have exercised their eligibility in the zones North, East, West and South, as well as for L gas in the North; the supply of H gas to *small customers* who have exercised their eligibility in each of the five zones, as well as for L gas in the North; the supply of H gas to *intermediary resellers* (*"entreprises locales de distribution"*) who have exercised their eligibility in the zones North and East, as well as for L gas in the Northern zone; the supply of H gas to *gas-fired power plants* in the Eastern and Northern zones as well as the supply of L gas in the Northern zone; the supply of H gas to residential customers as of 1st of July 2007 in each of the five geographical zones, as well as for L gas in the Northern zone.

On most of these markets, already pre-merger GDF enjoyed a dominant position. The disappearance of Suez (Distrigaz) from the market would strengthen GDF's dominant position by removing one of the best-placed and strongest alternative players.

Furthermore, similarly to Belgium, the Commission also found that important barriers to entry, relating to access to gas and infrastructures, would strengthen the horizontal effects of the merger. As far as access to gas is concerned, the merging parties have access to most of the gas imported into France, and they hold almost all the long-term import contracts. As far as infrastructure is concerned, almost all of these (except for the South-West) are owned by GDF, either directly or via its 100% subsidiary GRTgaz, and are essentially booked by GDF. Moreover, although GRTgaz has planned to expand gas transport capacities, these new infrastructures will not be available before the end of 2008 and GDF competitors would benefit from these additional infrastructures only to a limited extent. Finally, as some of GDF's regulated tariffs do not incorporate the totality of gas procurement costs, they constitute a barrier to entry on the liberalised markets.

Electricity in Belgium

The Commission identified significant impediments to effective competition on a number of electricity markets, on which the parties' combined market shares would be above 80% and the already dominant position of Suez would be strengthened by the merger.

On the national Belgian market for production and wholesale of electricity, the Belgian incumbent Electrabel (Suez) would acquire joint control, through the merger, over its largest competitor (SPE), whose power plants are situated on the mid-merit and peak-load section the merit curve. This would further strengthen the merged entity's capacity to determine prices on the Belgian wholesale market for electricity.

On the national market for auxiliary and balancing power, the merger would combine the only two suppliers of these services to the transmission network operator Elia.

On the national market for supply of electricity to large commercial and industrial customers, the existing dominant position of Electrabel (Suez) would be further strengthened by the elimination of one of the two companies (SPE) capable of exercising competitive pressure on Electrabel (the other one being EDF) ([6]).

On the national market for supply of electricity to small commercial and industrial customers (<70kV), the market share of SPE would strengthen the already dominant market position of Suez.

As to the supply of electricity to eligible residential customers, the merged entity would have a dominant position both on the basis of regional definitions of the relevant geographical market as well as on a national basis.

In addition to these horizontal effects, the Commission also found that a number of vertical effects of the merger would strengthen the already dominant position of Suez on the electricity markets in Belgium.

Most notably, since gas is an input for electricity generation, the Commission found that the parties would have the ability and the incentives to increase the cost of gas to other electricity sup-

([6]) RWE, also present in this market, cannot exercise any competitive pressure because the entire output of its sole power plant is committed to a single customer.

pliers and in particular to increase the cost of the flexible supply of gas to gas-fired power plants of their competitors.

The decision also highlights that the parties would have access to detailed information on the cost and usage of its rivals' gas-fired power plants, and, hence, their prices and production policy.

The parties are the prime suppliers of auxiliary services and balancing power to Elia. The decision identifies the ability and the incentives for the parties to increase the cost for auxiliary services and balancing power and, as these costs are passed though by Elia to the parties' rivals, to raise their costs.

Finally, the Commission also found that significant barriers to entry relating to (i) access to electricity generation capacity, (ii) green and combined heat and power (CHP) certificates, (iii) the illiquid nature of the electricity trading market, and (iv) access to transmission and distribution infrastructure would further strengthen the anticompetitive effects of the merger. Also in view of the effects of the merger on the market for supplies to gas-fired electricity plants, the merger would still increase these entry barriers.

District Heating in France

Among the several "energy-related services" in which both parties are active, the Commission concluded that one market would raise competition concerns: the nationally defined market for district heating networks in France ("réseaux de chaleur") ([7]). The long-term contracts (12-24 years) to manage district heating systems are granted by the municipalities concerned, after an official tendering process, in which in practice only a handful of France-based specialised companies participate. These suppliers are: Dalkia (Veolia group), SES-Elyo (Suez group), Soccram (Thion — Ne Varietur group) and Cofathec-Coriance, (Cogac, GDF group). Cogac (GDF group) has a substantial shareholding in, and arguably joint control of, Soccram (Thion — Ne Varietur group). After the merger, the parties would be the largest player in the market. The merger would remove Cofathec-Coriance (GDF group) which has acted as a "maverick" in the market, thus leading to non-coordinated effects. Moreover, the Commission found that the position of GDF as the dominant supplier of gas to anyone participating in a tender to manage a district heating system in France would be a further factor reducing competitive pressures in the market for district heating.

([7]) District heating networks are collective systems for the distribution of heat generated in the form of steam or hot water by centralised generating units.

4. The Remedies: a far-reaching package

In order to remedy the competition concerns identified by the Commission, the parties submitted commitments on 20 September 2006. The market test carried out by the Commission showed that these initial commitments were not sufficient to remove the competition concerns raised by the merger. The parties modified their initial commitments on 13 October 2006 to take into account the results of the market test. These commitments were fine-tuned and submitted again on 6 November 2006.

The commitments offered on 13 October 2006 (re-submitted on 6 November)

The commitments offered by the parties consist of five main elements:

i) divestiture of the Suez group's shareholding in Distrigaz;

ii) divestiture of GDF's shareholding (via Segebel) in SPE;

iii) restructuring of the activities of Fluxys and relinquishing of Suez' control over the company;

iv) a series of additional measures (most notably investments) relating to the gas infrastructures in Belgium and France;

v) divestiture of Cofathec Coriance.

Divestiture of Distrigaz

Suez will divest its holding in Distrigaz to a third party, which must have relevant expertise in the energy sector and in particular in the downstream supply to final customers. The candidate purchaser will be subject to the Commission's approval.

Distrigaz will be divested in is entirety, with all tangible and intangible assets, including the upstream supply contracts currently in its procurement portfolio.

Prior to the divestiture of its stake in Distrigaz, the merged entity will conclude one or more supply contracts with Distrigaz, intended to cover part of Electrabel's needs for its gas-fired power plants and the needs of Electrabel Customer Solutions (ECS) to serve its (mainly residential) customers. These contracts will decrease over time and, after five years, only a small volume will remain in place.

Lastly, the parties undertake to transfer to Distrigaz, immediately upon request, the storage capacity in Belgium and the corresponding volumes being stored, relating to any existing ECS public supply customer in Belgium which might be acquired by Distrigaz or by one of the resellers supplied by it.

Divestiture of SPE

GDF will relinquish its 50% shareholding in the capital of Segebel, a company which itself has a 51% shareholding in SPE's capital.

Reorganisation of Fluxys' activities and loss of control of Fluxys

Fluxys' activities will be reorganised into two entities, Fluxys and Fluxys International. Fluxys International will own the Zeebrugge LNG terminal and the non-regulated Belgian and international assets (BBL, Huberator, Gas Management Services Limited, Belgian Pipe Control, C4Gas and Endex). The other entity (Fluxys) will own the entire Belgian gas transmission/transit system as well as the Belgian gas storage infrastructure. To this end, GDF will transfer to Fluxys its 25% holding in Segeo (natural gas transmission/transit operator) while Suez will transfer Distrigaz & Co (which markets transit capacity on the Troll and rTr routes).

Fluxys will operate all the infrastructures regulated under Belgian law (transmission/transit system, storage, LNG terminal).

The parties have undertaken not to control Fluxys, either *de facto or de jure* or by a shareholders agreement. In order to substantiate this commitment, the parties have undertaken:

a) as regards Fluxys:

— not to hold more than 45% of Fluxys 's capital;

— not to have more than seven representatives out of 21 on the Board, and not to make proposals for the nomination of the seven independent directors of the Board;

— that no Fluxys director will have any responsibility in gas supply activities;

— to set up an executive committee ("comité de direction") within Fluxys with exclusive powers as regards (i) the management (including commercial strategy) of the regulated infrastructures and (ii) the overall investment plan for regulated infrastructures in Belgium. The Board will not be in a position to reject the overall investment plan except on the grounds of the impact any such investment would have on the company (financial interests of shareholders acting as investors). In the latter case the parties will vote to allow the investments to be financed by a third party and if necessary to allow the capital of Fluxys to be opened to third parties with the specific objective of financing these investments;

— not to control the executive committee, either *de facto or de jure* or by a shareholders agreement.

b) as regards Fluxys International, the parties have undertaken that:

— the merged entity will hold not more than 60% of the company's capital;

— Fluxys's executive committee, referred to above, will draw up an overall investment plan for the LNG terminal and the Zeebrugge hub, which the Board of Fluxys International will not be in a position to reject except on grounds of its financial impact on the company (financial interests of shareholders acting as investors). On its own initiative, the executive committee of Fluxys will also be able to propose additional investment in the regulated and unregulated assets owned by Fluxys International or its subsidiaries. Should these investments be rejected by the Board of Fluxys International, the representatives of the merged entity will vote to allow the financing of such investment by a third party and if necessary to allow the capital of Fluxys International to be opened to third parties with the specific objective of financing these investments.

Additional measures relating to gas infrastructure

The parties have committed to put in place a number of additional measures relating to gas infrastructure. Most importantly, the parties have undertaken to create a single point of entry at Zeebrugge bringing together the pipeline hub, the LNG terminal, the point of arrival of the Interconnector Zeebrugge Terminal (IZT) and the point of arrival of the Zeepipe Terminal (ZPT).

Moreover, the parties have also undertaken to carry out a number of investments in the gas infrastructure in France, with a view to enhancing the capacity and the functioning of the network ([8]).

([8]) The parties have undertaken, inter alia, to develop new storage capacity (80 Mm3 at the Trois Fontaines site, available at the end of 2009, and 60 Mm3 at the Alsace site, available at the latest in 2018) and new capacity at the Montoir terminal (available as from 2007), and to offer this new capacity on the market prior to their availability, partly already before end of 2007. The parties have undertaken to adopt a variety of measures designed to improve the operation of the 'use it or lose it' mechanisms and the returnable capacities of the GRTgaz network.
Moreover, GRTgaz will install a deodorisation plant at the Taisnières H entry point which will be able to provide a physical flow towards Belgium of 300,000 m3 per hour.

District heating networks

The parties have undertaken to divest Cofathec Coriance (excluding its holding in district cooling networks) and the five district heating networks operated by Cofathec Services, as well as the staff associated with the operation of these networks.

The Commission's assessment of the commitments

On the basis of the assessment of the information obtained through the investigation, and, in particular, of the results of a market test, the Commission concluded that the modified commitments were sufficient to remove in a clear-cut manner the competition concerns raised by the merger, both in Belgium and in France.

It must be stressed that these commitments go far beyond the removal of the sheer horizontal overlaps arising from the merger. This proved necessary, in the light of the results of the investigation, to compensate for the major impact that the merger would have had, in the absence of remedies, owing to the removal not only of an actual competitor of the incumbent in both Belgium and France, but also of one of the best placed (if not the best placed) potential competitor in both national markets. This removal of potential competition, combined with the very high barriers to entry (due essentially to the vertical integration of the two merging groups) called, in the opinion of the Commission, for a far-reaching package of commitments, including the divestiture of the incumbent Distrigaz and the restructuring of Fluxys, accompanied by infrastructure — related measures. Moreover, it was indispensable to ensure the viability of any divested business so as to enable it to exert competitive pressure on the merged entity. The Commission concluded, in this respect, that Distrigaz would be the only divested business capable of ensuring the necessary long term viability.

Competitiveness and viability of Distrigaz

The Commission concluded that Suez' divestiture of its majority shareholding in Distrigaz constitutes an appropriate remedy to the loss of competitive pressure on the French and Belgian gas markets and the foreclosure problems on the Belgian electricity markets resulting from the merger. Distrigaz is a going concern which possesses all the requisite assets (in particular supply contracts with producers, gas infrastructure reservations and an existing customer base) to be able to compete effectively with the merged Suez/GDF entity in both countries.

Distrigaz' viability will not be jeopardised by the supply contracts to be stipulated with Electrabel and ECS. These contracts concern the supply of gas to Electrabel and to ECS. The volumes covered by the supply contracts would amount to about a third of the total volume supplied by Distrigaz in 2005 and less than 45% of its current supplies under contracts, i.e. excluding spot purchases. The volumes of gas available to Distrigaz will be sufficient to supply all its existing customers in France and Belgium, including SPE and to meet rising demand. Distrigaz will be able to meet such additional demand through its existing contracts and through purchases on the Zeebrugge hub, as it does today. Furthermore, the buyer of Distrigaz must possess proven experience in the energy sectors and therefore be capable of extending existing contracts or concluding new ones with producers.

Finally, the volume of the supply contracts will be gradually decreasing, owing to the expiry of Distrigaz' upstream contracts and ECS' foreseen loss of residential customers in the wake of the liberalisation in Brussels and Wallonia.

While it is true that most of Distrigaz' current customers are industrial customers, Distrigaz will, however, keep its contracts for the supply of dealers such as Nuon and Essent and continue to cover part of the gas needs of Electrabel and SPE power stations under back-to-back contracts. Moreover, Distrigaz will also be able to compete on the markets for gas supply to household customers and small industrial and commercial customers. This will be facilitated by the retention of the 'Distrigaz' brand, which is well known in Belgium and France. Distrigaz will therefore be able to put together a balanced customer portfolio.

In sum, the Commission concluded that Distrigaz will remain a viable business and be able to compete effectively with the new GDF/Suez entity in Belgium and France. Its competitiveness will be enhanced by the proven expertise in the energy sector required of the purchaser. Moreover, the commitments relating to access to infrastructure will lower the barriers to entry and thereby allow Distrigaz to operate in a viable and competitive matter.

Divestment of SPE

The Commission considered that the divestment of GDF's holding in SPE was necessary to eliminate the problems identified in the Belgian gas and electricity markets, as it would eliminate a clear horizontal overlaps in those markets.

However, as also highlighted by the market test, the Commission considered that the effectiveness of the divestment of SPE in restoring competition to the electricity sector and to the supply of gas to small customers — by eliminating the current horizontal overlaps — must be assessed not in isolation, but in conjunction with the other remedies in the other affected gas markets in Belgium.

As a matter of fact, thanks to the implementation of the commitment to divest Distrigaz, SPE will be able to benefit from the competition between the merged entity and Distrigaz so as to obtain supplies of gas and flexibility for its gas-fired power plants and its own customers at competitive terms. In the light of this, the Commission concluded that SPE will be able to compete with the parties in the Belgian electricity markets as effectively as it did with Suez prior to the merger.

Fluxys

The Commission considered that the commitments concerning Fluxys and Fluxys International will contribute to lowering the barriers to entry to the Belgian gas markets, barriers which were very high already before the merger and some of which would have been exacerbated by the merger.

The restructuring of Fluxys, in line with the commitments and the parties' undertaking not to control Fluxys and its management committee, will contribute to ensuring the independent management of the regulated gas infrastructure. Moreover, the divestment of Distrigaz will lead to the effective unbundling of the transport operator (Fluxys) from the main gas supplier (Distrigaz). The remedies will therefore lower the barriers to entry in the gas supply business and will contribute to creating a level playing field for all competitors as regards access to infrastructure.

As regards the commitment not to control Fluxys, while the merged entity and Publigaz are currently the main shareholders of Fluxys, it must be stressed that joint control by the merged entity and Publigaz by means of shareholders agreement would be in breach of the commitments. In addition, the merged entity will not have a majority on the board of directors of Fluxys, but will only appoint one third of its directors (7 out of 21). This creates the possibility of shifting majorities. Moreover, the parties have undertaken that the merged entity will relinquish the right to appoint independent directors for the board. This will also ensure the genuine independence (before and after nomination) of the seven independent directors. It is also provided that the CREG will certify the independence of candidates for the post of independent director. As a consequence, only one third of the directors will represent the merged entity on the board of directors, opening the way to shifting majorities and preventing the merged entity from exercising any veto power.

As a further guarantee of their commitment not to control Fluxys either in law or in fact or by shareholder agreement, the parties offered to set up a "comité de direction" within the meaning of Article 524bis of the Belgian Company Code. It is provided that this "comité de direction" will have exclusive powers to manage all aspects of the company's activities in Belgium regarding transport/transit infrastructure, storage and the LNG terminal. As already pointed out above, the "comité de direction" will also draw up the investment plan. The system proposed by the parties for appointing members of the "comité de direction" will guarantee its independence from the board of directors. The appointment procedure will contain four successive safeguards to ensure the committee's independence from the parties: proposal by the remuneration committee; opinion from the corporate governance committee; approval by the CREG; and abstention of the merged entity in the vote.

This system of governance in Fluxys will in practice remove from the board of directors any powers over matters entrusted to the "comité de direction". As a result, the merged entity will have no right of veto over the commercial strategy of Fluxys and no decisive influence in matters that fall within the responsibility of the "comité de direction".

The Commission concluded that the set of measures regarding the governance of Fluxys described above will guarantee that the merged entity will not control Fluxys.

As regards Fluxys International formed from the present Fluxys LNG, which will own the LNG terminal in Zeebrugge and the non-regulated Belgian and international assets, The merged entity will own no more than 60% of its share capital.

Nevertheless, according to the commitments, Fluxys International will grant Fluxys all the requisite rights to use installations and equipment regulated under Belgian law and delegate to Fluxys all the tasks necessary for it to perform its role as manager of the LNG terminal in Zeebrugge. The system of governance proposed for Fluxys will therefore also apply to Fluxys International, which will in practice be managed independently of the parties, as decisions by Fluxys concerning the management of Fluxys International on the above-mentioned issues, which are the sole responsibility of the "comité de direction" of Fluxys, will not be subject to the control of the merged entity.

Moreover, the parties will not be able to block investment decisions relating to infrastructure controlled by Fluxys and Fluxys International. The commitments provide that decisions on investments concerning the infrastructures owned by Fluxys and Fluxys International will be delegated to the "comité de direction" of Fluxys. The commitments also provide a further procedure whereby any investments deemed necessary can be financed by opening up the capital of Fluxys and Fluxys International to third parties.

Finally, the commitments relating to transit (the transfer to Fluxys of Distrigaz &Co and of GDF's stake in Segeo and the commitment by Fluxys to apply the code of conduct, currently applicable to transmission, to new transit contracts) will strengthen the legal framework for the transit of gas in Belgium (the importance of this aspect was stressed by many third parties throughout the proceedings).

Commitments on investments

As indicated, the parties undertook to make a series of investments to increase Belgian and French gas infrastructure capacity.

Most importantly, these include the creation in Zeebrugge of a single entry point, thereby making it possible to link the hub, the LNG terminal, the arrival point of the Interconnector Zeebrugge Terminal ('IZT) and the arrival point of the Zeepipe Terminal ('ZPT'). This will help solve the difficulties resulting from the lack of access capacity at the hub. The single entry point will make it possible to transfer volumes within this area from any point bordering the Zeebrugge zone, at a 'commodity' tariff and without having to reserve capacity. This connection will improve liquidity at the hub, since all operators active on the other terminals will be able to negotiate on the hub without having to overcome existing barriers to entry.

In addition, Fluxys has committed to making the necessary investments to improve the interconnection of the three terminals (Interconnector Zeebrugge Terminal, Zeepipe Terminal and LNG terminal) by October 2010 at the latest. Such interconnection will increase liquidity on the Belgian and French markets.

District heating

The commitment proposed for eliminating the problems identified in the market for district heating in France (by divesting GDF's subsidiary, Cofathec Coriance) would remove the horizontal overlap created by the transaction. The number of networks and the volume of heat production to be divested will ensure the viability of the divested business. The divested entity will therefore be able to play a credible role in tendering procedures. Since this commitment entirely eliminates the horizontal overlap in a structural and well defined manner, the Commission concluded that it would be sufficient to eliminate the concerns identified in this market.

5. Conclusion

The Commission concluded that the commitments submitted by GDF and Suez were sufficient to address all competition concerns raised by the concentration and therefore declared the transaction compatible with the common market and the functioning of the EEA Agreement pursuant to Article 8 (2) of the Merger Regulation.

The experience and knowledge acquired with this case will undoubtedly prove useful in future merger cases and beyond. The results of the energy sector inquiry ([9]) have provided indications that the gas and electricity markets are still not working as they should. While the Commission supports European integration and restructuring of the energy sector, it must ensure that any competition concerns are remedied, and that consumers are protected. The remedies of this case are consistent with the findings of the energy sector inquiry which emphasise the need for i) structural solutions, such as ownership unbundling, aiming at severing the link between supply and infrastructure and ii) greater investment in infrastructure capacities to secure pro-competitive conditions for the sustainable development of energy markets.

([9]) On 10 January 2007, the Commission published its final report on the energy sector competition inquiry, concluding that consumers and businesses are losing out because of inefficient and expensive gas and electricity markets. Particular problems include high levels of market concentration; vertical integration of supply, generation and infrastructure leading to a lack of equal access to, and insufficient investment in infrastructure; and, possible collusion between incumbent operators to share markets.
The final report is available on DG Competition's website at: http://ec.europa.eu/comm/competition/sectors/energy/inquiry/index.html

Empirical estimation of a discrete choice model for filler calcium carbonates in the paper industry (1)

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1. Introduction

This paper presents the econometric work carried by the members of the Chief Economist (CET) for the merger decision M.3796 — Omya / JM Huber. The merging companies produce and sell calcium carbonate, an industrial mineral largely used in the paper manufacturing. We use customer level data to estimate the substitution pattern between the different suppliers of calcium carbonate filler for the paper industry. The dataset consists of detailed information on annual shipments from the major suppliers to paper mills in the EEA. The data was collected by the European Commission for the investigation of the transaction involving Omya and JM Huber.

One of the major issues the Commission faced during this merger investigation was to determine whether ground calcium carbonate (GCC) and precipitated calcium carbonates (PCC) belong to the same relevant market. The notifying party claimed that sales of PCC form a distinct market, a market definition that produces a minimal overlap, while third parties argued that GCC and PCC are considered interchangeable by customers. Using the data collected during this merger review, the CET estimated an econometric model that was used in conjunction with other pieces of evidence to allow the Commission to take a view on the delineation of the relevant market.

PCC and GCC are both used for various applications in the paper industry, in particular for "filling" applications. This industrial procedure consists in adding the mineral to the cellulose slurry before it is formed into the sheet. The filling application improves the quality of paper in terms of whiteness, opacity, brightness and colour; furthermore, it increases its dimensional stability and bulkiness.

GCC is produced from the different types of the raw material $CaCO_3$, which is commonly found in nature throughout the world and mined by both opencast and underground methods. The main types of $CaCO_3$ used for producing ground calcium carbonate (GCC) are sedimentary (limestone or chalk) or metamorphic (marble). GCC derived from these sources differs in terms of the level of brightness of the paper produced, higher for marble, which is the preferred type for paper industry, and lower for limestone and chalk.

PCC is a synthetic industrial mineral obtained from burnt lime or its raw material, limestone, through a chemical precipitation process. Unlike other industrial minerals, PCC can be shaped and modified to offer differing properties to the paper produced. Despite the major benefits deriving from this property, PCC can reduce the fibre strength and on average requires a longer production process for paper than GCC.

Because logistic and transportation costs are important considerations in this industry, paper mills purchase filler requirements from mineral plants that are sufficiently close. In principle, if customers bear the transportation costs, when choosing between two identical sellers, they will always prefer the one closer to their location. In this particular case, transaction records show that transportation costs were not always invoiced as a separate service, but rather included in the overall price. However, this did not make much of a difference, since the costs in question are in practice perfectly transparent and understood by every actor in the industry (3). It follows that a plant will face less competition if its rivals are located at greater distance in comparison to a plant that has many plants in its vicinity. Spatial differentiation appears to be therefore an important consideration for market definition and the competitive effect of the transaction.

A large portion of PCC is supplied through on-site plants, that is to say, plants producing PCC that are built directly on the site of the paper mill that is their (main) purchaser. Contracts between an on-site plant and the host paper mill tend to run

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

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(3) In phone conversations with various customers about their different choice of suppliers, all quoted the cost of transportation that they would have to pay for each alternative. Ultimately, it made little difference to them whether they bear directly such costs or these are included in the final price.

for a minimum of five years at least, though recent contracts have been awarded for ten years ([4]). Although the major part of an on-site plant production is normally sold to the host paper mill, on-site plants also ship PCC to other paper mills. On-site PCC plants are thus considered to be a source of supply for the merchant market. We focus on the interaction between merchant GCC and merchant PCC, that is, PCC that is supplied by an on-site operator to mills other than its host mill. Because of data limitations, we do not consider the interaction between supply of GCC and selection of on-site PCC delivery ([5]).

The empirical study applies a discrete choice approach to estimate the substitution patterns between the various producers of carbonates filler. The purpose of this exercise is to determine to what extent GCC and PCC are choice substitute and furthermore to what extent the merging parties, Omya and Huber, were close competitors prior to the transaction. The results of econometric model should shed light on the post-merger competitive effect of the transaction. However, this study does not pretend to estimate the price effect of the transaction.

2. A Choice Model

The model adopted in this study assumes that each paper mill will select a supplier of filler calcium carbonates that is located within a certain geographic distance. This assumption is born by the reality of the marketplace. In principle, no physical hurdle nor any regulation prevent a paper mill from importing GCC or PCC from mineral plants located very far from it. However, transportation of PCC and GCC involves a host of logistic problems that increase shipping costs. Not only suppliers and customers have indicated that transportation costs constrain the ability of shipping GCC and PCC, but also the set of transactions provided by the suppliers to the Commission reveals that shipments are limited in their geographic scope. The choice model will predict the probability that a paper mill choose a particular supplier within its relevant geographic zone.

In a discrete choice model the decision maker must select only one alternative between mutually exclusive alternatives ([6]). For this industry, each paper mill chooses between different mineral plants for its requirement of filler calcium carbonate. The fact that each paper mill tends to be supplied by a single plant for its filling requirements of calcium carbonates makes the discrete choice framework highly appropriate.

2.1. *Customer's Choice Set*

The transaction data shows that a few paper mills are served by more than one plant. But in principle, paper mills have only one primary source of filler calcium carbonate for each paper machine and often for the entire mill. For the few paper mills that purchase filler calcium carbonates from more than one plant, these mills have several paper machines, but no paper machine is fed with calcium carbonates from two different plants ([7]). The choice is then made at paper machine level. For the purpose of this study, when a paper mill is served by more than one plant we consider only the main supplying plant. But for a few cases where there is no clear main source of supply, we include the different shipments and assume that the choice of supplier for each paper machine is independent.

To delineate the choice set of each customer, we apply a rule based on a maximum distance between each paper mill and all mineral plants located within the EEA. All plants located beyond that maximum distance are excluded from the choice set. In other words, we assume that the probability that a plant located beyond that distance serves a customer is simply zero. However, we account for the fact that transportation costs vary depending on the product (GCC or PCC), the water content, and the mode of transportation ([8]).

The maximum distance will vary depending on the mode of transportation. When the mode of travel is trucking, it is assumed that plants located

([4]) Because logistics and transportation costs are an issue, some paper mills that have large carbonate filler requirements have opted to host a satellite plant on their premises. In principle, the operator of the on-site plant is selected through a tendering process. The winning bid builds an on-site plant and delivers PCC to the host mill for a few years.

([5]) This is due in part to the lack of information on the number and the type of plants that could serve these paper mills at the time when they opted for a long-term on-site contract.

([6]) McFadden (1974) introduced the conditional logit to estimate a choice model. For a thorough introduction of discrete choice model, their properties and estimation techniques we refer the interested reader to Train (2002) and Greene (2003) chapter 21.

([7]) Because the operator will adjust the various technical parameters of the paper machine to the specificities of the calcium carbonate filler, such technical fine tuning prevents dual sourcing for any paper machine.

([8]) Note that although the size of the quantity requirements of a customer may have an effect on the possible travelling distance because of economies of scale in shipping, generally the maximum distance is taken so that it is unlikely that any volume size will be shipped beyond such distance.

farther than 700 km from a paper mill cannot be included in the choice set of that particular customer (9). Although shipments travelling beyond 700 km occur once in a while, they usually correspond to trials, when a customer is fitting a new product on a paper machine. However, the rule of 700 km is altered for PCC merchant (that is to say, not "on-site") plants. Unlike on-site PCC plants, merchant PCC plants have the capability of shipping PCC with much less water content, which substantially lowers the costs of transportation. The maximum distance for these alternatives is thus higher, and is set at 1,000 km. The probability that a customer selects a plant located beyond this distance is negligible. When nearby seaport facilities are available, plants can ship calcium carbonates by sea. This mode of transportation is more economical, and the average distance travelled is longer than that achieved by trucks. In this study the maximum reasonable distance is set at 1,700 km for PCC and 2,000 km for GCC. Finally, the study considers the possibility of shipping filler carbonates via rail with a maximum distance of about 800 km. As a result of these assumptions each paper mill has a unique choice set. The probability of a paper mill selecting a plant beyond these maximum distances is sufficiently close to zero that these alternatives can be discarded.

The choice set of each individual paper mill contains PCC or GCC plants owned by different firms. In terms of volume shipped, the number one producer of GCC in the EEA is Omya, and Imerys is second. There are also some minor producers with only a few small plants such as Provençale and Reverté. However, because the number of shipments collected was few for these two producers, they were dropped entirely. In the EEA PCC for the paper industry is supplied by JM Huber, Omya, SMI, Solvay and Schaeferkalk. Note that Solvay and Schaeferkalk operate on-site plants for specialty paper, they also make some off-site sales but their presence is relatively small in comparison with the other producers. Again, because the dataset contains very few observations for Solvay and Schaeferkalk, observations for these two producers were also dropped.

2.2. Customer Behaviour

The study models the probability that a paper mill selects a supplier of filling mineral as a function of the producer plant characteristics and the customer's (paper mill's) own characteristics while allowing for unobserved heterogeneity in preferences over the producers' offer. Customer n's utility from being supplied by plant j can be written as:

$$U_{nj}=V_{nj}(z_j, x_{nj}, \theta) + \varepsilon_{nj},$$

where

n denotes a paper mill, $n=1,\dots,N$ and

j denotes alternatives, $j=1,\dots,J$.

$V_{nj}(z_j, x_{nj}, \theta)$ represents a systematic component of utility in which zj is a vector of observable plant/product characteristics, x_{nj} a vector of observable attributes specific to the customer as well as to the choices and θ is a vector of parameters to be estimated. ε_{nj} is the random component of utility that represents the unobserved customer n's idiosyncratic taste for being supplied by plant j. Each paper mill will choose the calcium carbonate plant that provides the highest utility level. Therefore, the probability that customer n selects plant j as its major supplier of its calcium carbonate filler is written as:

$$\begin{aligned} P_{nj} &= \Pr(U_{nj} > U_{ni}) \text{ for any } j\neq i,\ i,j \in J_n \\ &= \Pr(\varepsilon_{ni} - \varepsilon_{nj} < V_{nj} - V_{ni}) \text{ for any } j\neq i,\ i,j \in J_n \end{aligned}$$

where J_n is the subset of plants that constitutes the choice set of paper mill n.

Assuming that the error term is i.i.d and follows a Type I extreme-value distribution, the formula above yields the multinomial logit formula. However, the logit model imposes the IIA assumption that restricts the pattern of substitution between alternatives. The nested logit is a less restrictive model in which the i.i.d assumption is replaced with a variance component structure. The distribution of the unobserved component of utility is a type of generalised extreme value that allows the unobserved portion of utility to be correlated for alternatives that are grouped within the same nest, but still to remain uncorrelated with alternatives that belong to different nests. The error structure of the nested logit implies that the IIA assumption holds within each nest, but for any two alternatives that belong to different nests, the ratio of probabilities depends on the attribute of other alternatives in the corresponding nests. The substitution pattern is thus derived from a priori segmentation. Daly and Zachary (1978) and McFadden (1978) have shown that the nested logit model is consistent with utility maximisation. One advantage of using the nested logit model is that it yields closed-form equations for the plant choice probabilities, thus easing estimation while allowing for varied correlation patterns among the different alternatives.

PCC and GCC share similar characteristics that enable paper makers to increase the paper quality.

(9) GCC or PCC are transported by trucks each carrying a load of 14 to 20 dry metric tons.

These calcium carbonates allow the production of paper at lighter weights but with added bulk and with better brightness and opacity. Yet PCC and GCC also differ in various respects. Unlike GCC, PCC is a synthetic product that can be shaped and modified to offer differing properties to the paper produced. PCC offers higher brightness, opacity and bulk in comparison to GCC. But employing PCC brings some disadvantage such as the reduction in the fibre strength to a point which limits the filler loading levels. Because the properties of PCC and GCC are not directly observable by the econometrician, it is likely that the unobserved portion of utility of PCC products are correlated, and similarly for GCC products. We postulate that PCC products are more similar than GCC products, and combine these alternatives together in one nest. For the nested logit, the probability that a paper mill n select plant j in nest k is commonly presented as the product of two probabilities:

$$P_{nj} = P_{nj|k} \cdot P_{nk} \quad \text{for} \quad k = PCC, GCC$$

where $P_{nj|k}$ is the probability of selecting alternative *j* conditional on choosing any alternative in nest *k*, and P_{nk} is the probability that paper mill *n* selects any alternative in nest *k*. Formally, these probabilities are written as:

$$P_{nk} = \frac{e^{\lambda_k I_{nk}}}{\sum_{l=1}^{K} e^{\lambda_l I_{nl}}}, \quad \text{where} \quad I_{nk} = \ln \sum_{j \in B_k} e^{V_{nj}/\lambda_k}$$

$$P_{nj|k} = \frac{e^{V_{nj}/\lambda_k}}{\sum_{j \in B_k} e^{V_{nj}/\lambda_k}}$$

I_{nk} is called the inclusive value and represents the expected utility for all the alternatives included in nest *k*. The inclusive value parameters λ_k also known as the dissimilarity parameters should be within the unit interval for the model to be globally consistent with utility maximisation ([10]). And $(1 - \lambda_k)$ is a measure of correlation of unobserved component of utility within each nest. When $\lambda_k = 1$, there is zero correlation, and the model is equivalent to a standard conditional logit.

3. Empirical Specifications

The indirect utility function of customer *n* is assumed to take the following linear form:

$$V_{nj} = \beta_1 P_{nj} + \beta_2 T_{nj} + \theta Z_{nj} \quad (1)$$

The indirect utility depends not only on the price charged by each alternative *j*, P_{nj}, but also on the logistic costs of shipping calcium carbonates, T_{nj} and other exogenous variables included in Z_{nj}.

The price variable used in the estimation is the price ex-work that plant j charges to paper mill *n*. However, the price of alternatives that are not actually chosen is not directly observable. Unlike consumer good industries suppliers do not offer uniform prices. In fact, they tend to charge prices that are relatively different from one customer to another ([11]). As a result, the price that a mineral plant could charge to a new customer may not be the same as the one that it already charges to its current customers. This fact makes it difficult to attribute a price for alternatives that were not selected.

Because the price of alternatives that are not chosen is not observable, this study resorts to constructed hypothetical prices for each paper-mill-alternative pair. A simple OLS regression is used to make out-of-sample prediction. The ex-work price is likely to depend on the quantity required, the type of mineral, whether PCC or GCC, and if GCC whether it is chalk, limestone or marble based GCC, the type of paper for which the filler pigment is being used as well as the cost of operating the supplying plant. Using actual 2004 transaction data, the estimated price equation is described below:

$$price_{ij} = \varphi_0 + \varphi_1 quantity_{ij} + \varphi_2 mineral_j + \sum_{l=1}^{L} \lambda_l\, papertype_j + \sum_{i=1}^{J} \gamma_j\, paperdummies_j + \upsilon_{ij} \quad (2)$$

The plant dummies will capture unobserved plant characteristics that are likely to be associated with larger or lower prices. To check the robustness of our results, we implement two other specifications of equation (2) without the quantity variable. One of them is similar to the above equation without the quantity variable. The second specification includes labour costs and energy prices. Using the OLS regression coefficient estimates, we predict the prices of these non-selected alternatives.

As already mentioned, logistics is an important consideration when selecting a supplying plant. Interviews with customers confirm that, also for

([10]) For more on the global conditions for the nested logit model to be consistent with utility maximisation see Daly and Zachary (1979) and McFadden (1978). For value of λ greater than one, Börsch-Supan (1990) derives conditions for which the model is locally consistent with utility maximisation. For an empirical application see Kling and Herriges (1995).

([11]) Large paper companies own several mills, and in this case it is rather unlikely that a calcium carbonate supplier can charge different ex-works price to paper mills belonging to the same paper company. As a result, the price of non-selected alternatives would be the same as that of paper mills actually selecting the product at issue. However, not all paper companies own several paper mills, and not all paper companies deal with all suppliers.

plants within the actual choice set of a given mill, it remains an important decision factor. Moreover, the logistic costs vary depending on the means of transportation: the most frequent mode of transport is trucking, but shipping across water is also used by some mineral plants. Because the data on transportation costs as provided by the different suppliers are inconsistent (e.g. because it does not appear as such in the invoicing), distance is an objective measure that is taken as a proxy for transportation and logistic costs. However, since transportation costs also vary with the water content of the calcium carbonate product (the higher the water content, the larger the transportation cost), distance is adjusted for the solid content. Merchant plants ship filler PCC with dry content of 50% and sometimes 70%. Alternatively, on-site PCC plant ship up to 35% dry content. In addition, filler GCC is made drier than filler PCC.

Dummy variables for each supplier are also included in most of the empirical specifications of the model. These variables should capture unobserved attributes for this producer such as customer relationship, image etc. The model also includes dummy variables for the types of GCC. The raw material for GCC is chalk, limestone and marble. Chalk GCC is usually cheaper and provides lower brightness levels.

4. Data

The data was collected for the European Commission investigation of the acquisition of twelve JM Huber on-site plants by Omya, six of which are located in Europe. The merging parties provided annual shipments to paper mills for the years 2002-2004. For many shipments the data also contained the price with and without transportation costs, the distance (in km) between the mineral plant and the paper mill, slurry form, and the mode of transportation, road, sea vessel or rail. In addition, the Commission requested the annual capacity of each plant.

Third parties active in GCC and PCC also provided similar data. Imerys is the only other firm active in both GCC and PCC. SMI, Solvay and Schaeferkalk provided data on PCC shipments. Finally, two small producers of GCC, Provençale and Reverte also supply similar data.

Each producer provided the distance for all of their shipments. The distance of all alternatives included in each customer choice set was computed using web-based software at www.mappy.com. The zip code of each plant and each paper mill were used to locate their respective geographic position, which enabled the software to provide an estimated distance using available roads and highways.

Because of the necessary investments in logistics, the study assumes that shipping via sea vessel is an alternative restricted to only a few plants and customers. Only a handful of plants use sea vessel to deliver their products to a number of customers. This study therefore considers that only plants that have already shipped their product by sea can realistically do so for other customers. Similarly, only customers who are currently served by sea vessel could consider switching to a plant using that same mode of transportation. The same assumption is made for shipments *via* rail.

After eliminating outliers such as trials, small quantity shipments (less than 500 dmt annually), and ex-works prices that are too high to be realistic (above Euro 200 per dmt) ([12]), the final database contains 139 annual transactions for 2004 for 4 suppliers of calcium carbonates. Omya supplies both PCC and GCC. Imerys only supplies GCC, as it started its Husum PCC operation in 2005, and Huber and SMI supply only PCC.

5. Estimation Results

Nested logit model can be estimated either in two steps, by first estimating the conditional probability and then the marginal probability, or by estimating the entire probability model using standard maximum likelihood. The latter procedure is the most commonly employed. Greene (2003) in chapter 21 specifies a nested logit model without dividing V_{nj} by λ. The estimation of such a model may lead to different results from the other version. Unfortunately some software packages such as STATA implements the Greene formulation while this version may not be consistent with utility maximisation ([13]). One way to circumvent the problem is to constrain the dissimilarity parameters of all nests to have the same value. In this case, the only concern is the scaling of the coefficient estimates ([14]).

The CET have estimated different specifications of the nested logit model imposing the constraint $\lambda_l = \lambda_k$. The different specifications are used to test the robustness of the coefficient estimates, in particular of β_1, and the predicting power of the model. In this paper we will present only one set of results.

([12]) Shipments whose prices are unusually high are likely to be trials.

([13]) For more on this discussion see Henscher and Greene (2002) and Heiss (2002). Note that NLOGIT, companion software of LIMDEP, estimates the two versions of nested logit model. But the European Commission does not possess this software, and the procurement rules would delay any acquisition.

([14]) For more on this topic see Heiss (2002).

Table 1 reproduces the estimation results when the price equation (2) includes quantity, the types of calcium carbonates, the types of paper and a set of dummy variables for each plant. Columns 1, 2 and 3 present the results for three basic specifications. In summary:

The coefficient estimate on price has the expected sign and is statistically significant at the 1% level. This result is consistent throughout the different specifications presented in Table 1.

Transportation costs are proxied by the variable distance, which is itself interacted with the mode of transportation ([15]). Column 1, 2 and 3 show that longer distance affects negatively the chance of a plant to supply customers. However, when transportation is done via ships, this tends to annihilate the distance factor. In fact, the coefficient estimate on the interacted variable is always slightly greater for these three specifications, though that difference is not statistically significant. Column 4 presents the results when the distance variable is interacted for all three modes of transportation. Two of these coefficient estimates are not statistically significant.

Column 5, 6 and 7 present the results of a model specification that is similar to that presented in column 3 but including another relevant variable. In column 5, the empirical model specification includes the interaction between the price variable and a dummy variable for paper-mills that belong to large paper companies. Arguably the price sensitivity of these paper mills could be different given that, for example, negotiations with suppliers could take place at the group levels and include deals covering several paper mills. Although the coefficient estimate indicates that these mills are less price sensitive, the estimate is not statistically significant. Column 6 presents a specification where a variable is included that accounts for the amount of spare capacity of each alternative relative to each customer's requirement. Note that there is no clear theoretical prediction how this variable should affect customers' choice: the presence of spare capacity with respect to the requirements of a given customer may indeed indicate that the plant can readily deliver the product to the customer, which should influence price positively; alternatively, it may also signal that the plant is not reaching an optimal utilisation rate, or, for PCC, is an older generation plant that is being less used — which should influence the price negatively. The estimation results support the latter interpretation, with a negative coefficient, although the magnitude of the coefficient estimates on the distance variables casts some doubt on the sensibility of this specification.

Finally, column 7 presents a specification where a variable accounting for customer loyalty is introduced. When a paper mill belongs to a paper company that already deals with the supplier that owns the plant the dummy variable "customer loyalty" is equal to 1, otherwise it is zero. The coefficient estimate is positive as expected and statistically significant. This result suggests that paper-mills would prefer selecting a supplier with whom their paper company already does business with.

6. Choice Elasticities

The nested logit specification adopted in this study models the choice probabilities as function of observed variables. Once such a model is estimated it is useful to know the extent to which these probabilities vary in response to a change in price. The coefficient estimate of the price variable is not directly interpretable. We present the changes in terms of semi-elasticities. That is, by how much the choice probabilities are altered for a 1% change in price. To compute the own price elasticities we restrict our attention to customers who are actually selecting the alternative in question. Table 2 presents the elasticities for the model specifications presented in column 1 of table 1. The elasticities for the other specifications of table 1 follow very similar patterns.

The first cell indicates by how much the probability of selecting an Omya GCC plant would decrease following a price increase of 1%. The figure indicates that current Omya customers would on average rapidly switch to another supplier should Omya raises its price too much. A 5% price increase would certainly leave Omya with no customers as the probability cannot decrease by more than 1.

The cross-price elasticities are provided in the diagonal cells of table 2. When Omya increases its price, its current customers are more likely to switch on average to Imerys than to other suppliers. Note that not all Omya customers would have Imerys as an alternative in their choice set. As a result, this change in probability only applies to these customers for whom Imerys is a realistic alternative. The cross-price elasticities for Imerys's current customers reveal that following a price increase these customers are more likely to switch to Omya GCC than to other suppliers. This result tends to indicate that GCC customers would prefer first another GCC supplier. Focusing on Huber's customers, the difference in cross-elasticities is much less pronounced in this case.

([15]) Other specifications not presented here include distance divided by solid content.

Following a price increase, Huber's customers are more likely to switch to Omya PCC, although the probabilities of switching to the other alternatives are not much lower.

7. Conclusion

We use the data collected by the Commission to estimate a discrete choice model to shed light on the substitution pattern between GCC and PCC. The purpose of this work is to check and possibly complement other evidence about market definition collected by the Commission during its investigation. In particular, contrary to the notifying party's claim, interviews with customers and switching evidence pointed toward a broad market including both filling PCC and GCC. The elasticities results of the choice model support the existence of a broad market.

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Table 1 — NLM estimation results

(Variables used to predict price: quantity, pcc, gcc_limestone, gcc_chalk, Speciality, UWF, CWF, UMP, CMP, Board, Plant_dummies)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Price	-.0095*** (0.003)	-.0161*** (.003)	-.0133*** (.003)	-.01196*** (.003)	-.01496*** (.003)	-.01274*** (.003)	-.01505*** (.003)
Large Customer Price ([1])					.0041 (.005)		
Distance	-.0029 *** (0.001)	-.0039*** (.001)	-.0037*** (.001)		-.0038*** (.001)	-.0049*** (.001)	-.0040*** (.001)
Distance for Ship Shipments	.0030*** (0.001)	.0039*** (.006)	.0037*** (.001)	-.0001 (.0003)	.0037*** (.001)	.00814*** (.001)	.0039*** (.001)
Distance for Road Shipments				-.0039*** (.0007)			
Distance for Rail Ship-ments				-.0001 (.0009)			
GCC Chalk	1.1110*** (0.562)		.3069 (.517)	.4779 (.590)	.2963 (.514)	-.5670 (.776)	.1623 (.481)
GCC Limestone	1.7534 *** (0.578)		1.2652** (.528)	1.3328** (.635)	1.2559** (.524)	2.1592** (.996)	1.2587** (.490)
GCC Marble	.8856** (0.533)		.3483 (.503)	.5002 (.581)	.3167 (.503)	.7984 (.765)	.2625 (.467)
Imerys		-.8923*** (.269)	-.7941*** (.294)	-.7067*** (.298)	-.7704** (.297)	-2.324*** (.547)	-.6800** (.302)
SMI		-2.2792*** (.422)	-1.5991*** (.552)	-1.2179** (.580)	-1.5913*** (.550)	-3.0320*** (.769)	-1.7307*** (.548)
Huber		-1.3705*** (.462)	-.8742 (.592)	-.6136 (.628)	-.8534 (.595)	-2.7103*** (.838)	-.4492 (.597)
Spare Constraint						-.0979*** (.015)	
Customer Loyalty							1.1721** (.568)
ICV	.7394*** (.20)	1.1199*** (.224)	1.0206*** (.273)	.8661*** (.240)	1.0245*** (.276)	1.0521*** (.359)	1.1097*** (.292)
Log-likelihood	-189.9250	-187.3531	-182.8319	-175.8821	-182.5698	-75.7761	-180.9856
Observations (Groups)	993 (139)	993 (139)	993 (139)	993 (139)	993 (139)	992 (139)	993 (139)
Predictive Power ([2])	74	83	80	81	79	119	81
Nests	2	2	2	2	2	2	2

Standard Errors are presented in parenthesis. * , **, *** = significance level at 10%, 5% and 1% respectively.

([1]) Dummy variable Large Customer is equal to 1 when a paper mill belongs to one of the top five paper companies: IP, Stora Enso, Sappi, Upm, M-real.

([2]) Number of observed choices predicted by the model.

Table 2 — Weighted semi-elasticities of probability with respect to prices.

(Variables: Distance, Distance for Ship, GCC Chalk, GCC Limestone, GCC Marble)

	Effect on the probability of selecting				
%price change	Omya GCC	Omya PCC	Huber PCC	Imerys GCC	SMI PCC
Omya GCC	**-0.1948**	0.0225	0.0296	0.0630	0.0296
Omya PCC	0.0952	**-0.1762**	0.0092	0.0296	0.0540
Huber PCC	0.0325	0.0505	**-0.1090**	0.0422	0.0421
Imerys GCC	0.1304	0.0114	0.0046	**-0.1867**	0.0390
SMI PCC	0.0599	0.0188	0.0115	0.0060	**-0.1080**

ECJ Judgement of 5 October 2006 Commission v. France: A major step forward for the recovery policy (1)

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On 5 October 2006, the Court of Justice issued an important judgement for the State aid recovery policy (2). The article below summarises the facts that gave rise to the case before the Court and gives an overview of the reasoning followed by the Court. Finally, it highlights the importance of this judgement for the execution of Commission recovery decisions.

1. The facts

On 12 July 2000, the Commission found that the aid granted by France to Scott Paper/Kimberly Clark (3) was incompatible with the common market and took a final negative decision ordering its recovery. The aid amounting to €12.3 million consisted of a preferential price of land and of a preferential water treatment levy.

Following the Commission decision, the French authorities issued the assessments ordering the recovery of the aid and the relevant interests to the beneficiary. These assessments were challenged by Scott Paper before the "tribunal administratif" of Orléans. Under French law, the challenge of these assessments leads to an automatic suspension to their execution. In addition Scott Paper contested the Commission decision before the Court of First Instance of the European Communities (4).

After several exchanges of correspondence between France and the Commission with a view to speed up the recovery procedure, the Commission decided to sue France before the Court of Justice for failure to execute the Commission decision. Despite the two-month deadline set by the Commission decision, only a minor part of the aid (5) had been reimbursed four years after the adoption of the recovery decision by the Commission. On that basis, the Commission considered that the French State did not fulfil its obligation to achieve an immediate and effective execution of the Commission decision as defined by Article 14(3) of the Council Regulation 659/1999 of 22 March 1999 ("the Procedural Regulation") (6).

2. The judgement

The judgement brings very interesting clarifications on two essential points of the state aid field. It makes clear that the measures taken by the Member State must lead to the immediate and effective execution of the Commission recovery decision and clarifies the principles governing the actions by the beneficiary against the Commission decision both at Community and national levels.

2.1. The national measures chosen to execute the Commission decision must lead to an immediate and effective execution

In its action for failure to comply with the Commission's recovery decision before the Court, the Commission argued that the French procedure which provides for an automatic suspensory effect of actions brought against demands for payment issued in order to recover aid did not fulfil the criteria of an "immediate and effective" execution of the Commission decision as contained in the Commission decision and in Article 14(3) of the Procedural Regulation.

The French government counter-argued that it had taken all necessary steps to implement the Commission decisions and that the national procedure applied did not preclude the execution of the Commission decision. Besides, the French authorities submitted that the expression "immediate and effective" execution of the Commission decision contained in article 14(3) of the Procedural regulation did not mean that the aid must be effectively recovered immediately, but that it was sufficient for the recovery procedure to be initiated without delay.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) Case C-232/05, *Commission v France,* (2006), not yet reported.

(3) OJ, 15.01.2002, L 12, p. 1-32.

(4) Case T-366/00 *Scott v Commission,* (2007), not yet reported. On 23 March 2007, the Court of First Instance annulled part of the decision that concerns the aid granted in the form of a preferential price for the property.

(5) One part of the aid linked to the preferential water treatment levy was repaid by the company Procter and Gamble who took over the assets of the Scott plant in June 1998.

(6) Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty (OJ L 83, 27.03.1999, pp 1-9).

The Court refuted the arguments put forward by the French authorities. The Court stated that a national law providing for an automatic suspensory effect of actions brought against recovery orders failed to have regard to the objectives pursued by the Community rules on State aid, in particular the immediate restoration of the previously existing situation on the market.

By delaying the recovery of the aid, this national provision goes against the principle of effectiveness, which is embedded in art. 14(3) of the Procedural Regulation ([7]). Consequently, the Court ruled that the national law is contrary to article 14(3) of the Procedural regulation and should have been left unapplied.

The Court thereby also emphasised the need for an immediate execution of the Commission recovery decisions, by stressing that the delays caused by the national procedures did prevent the immediate restoration of the previously existing situation and prolonged the unfair competitive advantage resulting from the aid. Therefore, to achieve its objective of an effective restoration of competition, it is necessary that the recovery of the aid is effected immediately.

2.2. *Appeal of Commission decisions*

The Court also clarifies the remedies and procedures available to the aid beneficiary acting against the Commission decision or the measures taken by the Member State with a view to execute the decision. The Court recalls that a recipient of aid, acting against the measures taken by the national authorities to implement a Commission recovery decision, cannot call into question the Commission decision without challenging this decision before the Community Court.

The Court repeats that, unless interim measures are taken by the CFI, the challenge of a Commission decision before the CFI does not have suspensory effect. The judicial protection offered by the EC Treaty to the beneficiary is therefore sufficient, so that the suspensory effect of actions brought before national courts can not be considered to be essential to protect the aid beneficiary.

By saying that only the Community judge can grant interim measures to suspend execution of a Community decision in the frame of an application for annulment before the Community courts, the Court seems therefore to exclude any possibility of forum shopping by the beneficiary of the aid between the national judge and the Community judge as far as interim measures are concerned.

3. *The conclusions of the judgement in the wider context of the recovery policy*

The European Courts have consistently confirmed, that "recovery of unlawful aid is the logical consequence of the finding that it is unlawful" ([8]). Recovery has not been conceived as a penalty but as a way to restore the ex-ante situation on the market. The "re-establishment of the previously existing situation is obtained once the unlawful and incompatible aid is repaid by the recipient who thereby forfeits the advantage which he enjoyed over his competitors in the market, and the situation as it existed prior to the granting of the aid is restored ([9])".

In the Olympic Airways judgement ([10]), the ECJ has insisted that in order for a Commission recovery decision to be fully executed, the actions undertaken by a Member State must produce concrete effects as regards recovery. The Scott judgement takes this one step further, by insisting that the repayment of the aid has to take place without delay and that recovery must be immediate ([11]). It stresses that the time-frame within which the aid must be recovered is indeed essential in order to ensure the re-establishment of the ex-ante situation on the market. National procedures that prevent the immediate restoration of the previously existing situation and prolong the unfair competitive advantage resulting from unlawful and incompatible aid do not fulfil the conditions laid down in Article 14(3) of the Procedural Regulation.

From a recovery policy point of view, it is essential that the principle of immediate and effective recovery be reaffirmed. The reality shows that until now the recovery of illegal and incompatible

([7]) '[…]Recovery shall be effected without delay and in accordance with the procedures under the national law of the Member State concerned, provided that they allow the immediate and effective execution of the Commission's decision.[…]'

([8]) Case C-183/91 Commission v Greece [1993] ECR I-3131, paragraph 16.

([9]) Case C-348/93, Commission v Italy [1995] ECR I-673, paragraph 26.

([10]) Case C-415/03, Commission v Greece, [2005] ECR I-03875.

([11]) Case C-232/05, Commission v France [2005] nyr.

aid, based on the use of national procedures, is a very lengthy process (12). The study carried out in 2006 on the application of state aid law at national level (13) confirmed that the excessive length of the national recovery proceedings constituted an obstacle for an immediate and effective recovery. One of the reasons for this delay is the length of national proceedings. By emphasising that it is not sufficient for the Member State to take all necessary steps in their national law to recover the aid, but that these steps must also lead to concrete and immediate outcomes in term of recovery, the Court sets up clearly the objective to be followed by the Member States in the exercise of their procedural autonomy.

The State aid action plan (14) presented in 2005 by Neelie Kroes stressed that the effectiveness and credibility of state aid control presupposed a proper enforcement of the Commission's decision, especially as regards the recovery of illegal and incompatible state aid. The landmark judgement in the Scott case may contribute to a better enforcement of state aid discipline and to the establishment of a level playing field for all economic actors throughout the European Union.

(12) The spring 2006 update of the State Aid Scoreboard shows that 16 of the recovery decisions still pending at the end of June 2005 were adopted before the year 2000. For more details, please refer to Report, State Aid Scoreboard — spring 2006 update http://ec.europa.eu/comm/competition/state_aid/scoreboard/2006/spring_en.pdf

(13) Study on the enforcement of state aid law at national level, coordinated by Thomas Jestaedt, Jones Day, Jacques Derenne, Lovells, Tom Ottervanger, Allen & Overy, Competition studies 6, Luxembourg, Office for Official Publications of the European Communities. http://ec.europa.eu/comm/competition/state_aid/studies_reports/studies_reports.html

(14) State Aid action plan: Less and better targeted state aid: a roadmap for state aid reform 2005-2009

Recent training aid cases in the car industry (1)

Andrés GARCIA BERMUDEZ and Christophe GALAND, Directorate-General for Competition, unit G-2

In recent years the car manufacturing industry in Europe has been through difficult times. Some large car manufacturers have announced and undertaken major workforce reductions and plant closures. It has also become clear that large car manufacturers put their plants in competition, where the production of new models is to be allocated. The plants have to "bid" for those models, and the mother company compares the total production costs, including potential state aid, of the different plants. In view of these sector developments, authorities may be encouraged to grant operating aid in order to limit the size of the workforce reduction in their country, to retain existing activities, or to attract new ones. In the assessment of the compatibility of large training aid projects with the common market, the Commission has recently adopted a more careful approach, taking into account this changing economic reality. In particular, it has verified in more detail that the aid indeed covers training activities which would not be undertaken by the firm without aid, and thereby contributes to the European common interest by increasing the pool of skilled workers and improving the competitiveness of Community industry. [1]

In the State Aid Action Plan, the Commission has committed itself to make use of a refined economic approach in order to achieve on the one hand *"a more transparent evaluation of distortions to competition and trade associated with State aid measures"*, and on the other hand *"to investigate why the market by itself does not deliver the desired objectives and evaluate the benefits of state aid measures in reaching these objectives"*. The refined economic approach is therefore expected to increase the efficiency and effectiveness of State aid, by means of a careful balance between clear ex-ante rules and precise methodology for assessment of more complex cases. The more cautious approach adopted by the Commission in recent training aid cases in the car industry should be seen in this context.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

1. Recent training aid cases in the car manufacturing industry

In the course of the last year, the Commission has adopted three final decisions concerning training aid in the car industry. In addition there is a fourth case, for which the formal investigation procedure was opened, where the Commission has not yet taken a final decision.

Ford Genk

The planned aid to Ford in Genk (2) was notified in June 2005. The Belgian authorities envisaged granting training aid of EUR 12.28 mio. for eligible costs of EUR 33.84 mio., covering a period of 3 years (2004-2006). In November 2005 the Commission opened a formal investigation procedure, which was subsequently closed by means of a partially negative decision in July 2006 (3).

Among the training aid measures notified by Belgium, two are of particular interest for the present purposes. They concerned aid in support of "launch costs" training expenses (training the workforce for the production of new models), and of training deriving from the company's restructuring (4). The Commission's assessment of these measures established the pattern under which subsequent (similar) cases are to be analysed, and will be explained below in further detail.

(2) The Ford Genk plant, part of the Ford Motor Company, was opened in 1964, and has since then produced more than 12 million vehicles. At the end of 2003, it underwent — in the context of a general restructuring of Ford Europe — a significant reduction of staff, involving about 3,000 employees, out of a total workforce of 9,000. At the same time, the company announced an investment programme of about EUR 700 mio., primarily devoted to a new flexible manufacturing system. As a result, the existing production of the *Mondeo* model would be complemented with the next generation *Galaxy* and with a third vehicle. In 2005, the plant employed 5000 people and produced 207,163 vehicles.

(3) Case C 40/2005, OJ L 366, 21.12.2006, p.32.

(4) In order to guarantee continuity of production and quality after the restructuring implemented between December 2003 and April 2004, a number of experienced employees were requested to stay for some additional weeks or months, to train their successors.

General Motors Antwerp

Belgium notified in December 2005 the intention of the Flemish region to grant EUR 5.33 million to GM Antwerp ([5]), for a training programme costing EUR 19.95 mio. The supported training activities would take place in the context of GM Antwerp's EUR 127 mio. investment programme for the period 2005-2007, that will allow the production of an additional version of the Astra ([6]) and a doubling of the plant's press activity ([7]).

In April 2006 the Commission decided to open a formal investigation procedure ([8]), which was subsequently closed by means of a partially negative decision in February 2007 ([9]).

Auto Europa

The Portuguese authorities notified the planned training aid to Auto Europa ([10]) in December 2005.

Auto Europa planned investments for the launching of new vehicles in several market segments (cabrio/coupé, Multi Purpose Vehicle, etc.). In this context, the Portuguese authorities proposed to grant (ad hoc) training aid amounting to EUR 3.55 mio., for a period of 3 years (2004-2006). The total eligible costs of the training project were EUR 10.90 mio.

In May 2006 the Commission opened a formal investigation procedure ([11]).

Webasto

The training aid to Webasto ([12]) was notified by Portugal in December 2005. The Portuguese authorities proposed to grant training aid amounting to EUR 3.43 mio., for a period of 3 years (2004-2006). Eligible costs were EUR 6.85 mio. The training programme intended to prepare the newly recruited personnel for Webasto's start of activities ([13]). 96% of the training effort (in volume) was allocated to general training.

In May 2006 the Commission endorsed the aid ([14]). The particular circumstances leading to that approval are analysed below in further detail.

2. Necessity of the aid

The necessity of the aid is a general requirement for compatibility of State aid under Art 87(3)(c) of the Treaty. An aid is necessary when it induces undertakings to do something that otherwise they would not do under normal market conditions. Only under these circumstances the aid might allow the company to "internalize" positive externalities ([15]).

Where the aid does not lead to additional activities being undertaken by the beneficiary, it cannot be deemed to have any positive effect for the common interest. It is then considered to be only distortive operating aid, and cannot be authorised. Using the wording of Article 87(3)(c) of the EC Treaty, the aid does not "*facilitate the development of economic activities*" if the company would have undertaken the supported activities in any event, and notably in the absence of aid.

([5]) General Motors Belgium NV in Antwerp is part of the General Motors Corporation. The plant, which was opened in 1924, employs 5,000 people and produces the Opel Astra.

([6]) In addition to the 3 versions already produced, the plant will manufacture the Astra TwinTop with retractable hardtop (the "cabrio"). Until now, the "cabrio" version was not produced by GM Europe, but outsourced to the Italian company Bertoné.

([7]) The extension of the press activity is part of GM Europe's strategy to have a better match with local needs. The higher grade of self-supply in bodywork parts and the more efficient logistic between different subsidiaries of the group allow to reduce the transport of parts between plants.

([8]) Case No. C 14/2006, OJ C 210, 1.9.2006, p.6.

([9]) Not yet published.

([10]) Auto Europa- Automóveis, Lda. ("Auto Europa") was established in 1991, as a joint venture between Volkswagen and Ford. In 1999 Volkswagen acquired the totality of the company's capital. Auto Europa has a single production plant in Setúbal (a region falling under Article 87(3)(c)), where it currently produces several models (VW Sharan, SEAT Alhambra, Ford Galaxy and the VW Eos), and employs 2,790 people.

([11]) Case No. C 17/2006, OJ C 177, 29.07.2006, p. 25.

([12]) Webasto Portugal- Sistemas para Automóveis, Lda. ("Webasto") is a component supplier for Auto Europa. The company was established in 2003, also in the Setúbal area, in order to provide Auto Europa with convertible tops for the new "Eos" model. Webasto's capital is shared between Webasto AG (Germany) and Webasto France SAS. In 2004, the company had no turnover, since the "Eos" has not started production yet.

([13]) According to the information provided by Portugal, the retractable hardtop produced by Webasto is characterised by the use of state-of-the-art technology, that is new in the country. Because of the complexity of this product, the Webasto group has opted for the construction of a brand new plant in Portugal in order to supply Auto Europa. This plant represents the group's main investment outside of Germany. For this purpose, the Portugal plant recruited 273 workers.

([14]) Case N 653/2005, OJ C 306, 15.12.2006, p. 14.

([15]) NB- the necessity of the aid is a necessary condition for compatibility of the aid, but of course not a sufficient one.

Although the Training aid Regulation ([16]) does not mention explicitly the incentive effect/ necessity of the aid as a stand-alone criterion for compatibility, it refers to the question in an indirect manner by stressing, in point 11 of the preamble, that:

"In order to ensure that State aid is limited to the minimum necessary to obtain the Community objective which market forces alone would not make possible, the permissible intensities of exempted aid should be modulated according to the type of training provided, the size of the enterprise and its geographical location" (emphasis added)

In this context, point 10 of the preamble refers to the specific community objective and to the market failure that the training aid is meant to address:

"Training usually has positive external effects for society as a whole since it increases the pool of skilled workers from which other firms may draw, improves the competitiveness of Community industry and plays an important role in employment strategy. In view of the fact that enterprises in the Community generally underinvest in the training of their workers, State aid might help to correct this market imperfection and therefore can be considered under certain conditions to be compatible with the common market and therefore exempted from prior notification" (emphasis added)

In this light, the market failure acknowledged by the Regulation is that firms *"underinvest in the training of their workers"*, as compared to what would be optimal for the total welfare of the Community. Indeed, when planning new training activities, a company will usually compare the cost of those activities with the benefits it can draw from them (such as increased productivity or the ability to produce new products). The company will generally not take into account the benefits for the society as a whole, which it is not able to capture for itself. It will also consider whether there are (cheaper) alternatives to training, such as for instance the hiring of already skilled workforce (possibly at the expense of existing employees). Therefore, in certain cases training aid effectively addresses a specific market failure. Under these circumstances, aid is *"necessary to obtain the Community objective which market forces alone would not make possible"*.

In the past, the Commission has not analysed in detail the necessity of training aid ([17]). This, however, does not deprive it from doing so once it notices that the economic conditions in the sector concerned have evolved.

In this light, it is with the *Ford Genk* case — and, more generally, with the recent cases in the car industry — that the Commission has for the first time carried out a specific scrutiny of the necessity of training aid. This scrutiny has focused, at a first stage, on training related to activities that belong to the normal running of a car company, such as the launching of new models.

3. Launch of new models

Over the last two years, the Commission has accumulated evidence that, for the production of new models, large car manufacturers often put their production plants, located in different Member States, in competition with each other. They first consider the comparative advantages of several plants for the launching of the new product, and then decide on the location to be retained on the basis of total costs, including government support such as training aid. This increased competition between plants seems to result form the higher flexibility of production lines, which can now accommodate more easily the production of additional models. Thus, it is less difficult for car companies to shift the production of model from one plant to another.

In view of this economic reality, there is a risk that certain training aid does not contribute to the objective of common interest laid down in paragraph 10 of the Regulation –inciting the companies to undertake additional training activities-, but simply constitutes distortive operating aid aimed at retaining or attracting the production of certain models at a certain site, and to cover training expenses that the company would have incurred anyway. Consequently, the Commission scrutinized more carefully the necessity of aid "*in order to ensure that State aid is limited to the minimum necessary to obtain the Community objective which market forces alone would not make possible*". Such assessment is even more justified in view of the current market situation in the motor vehicle sector, characterised by significant overcapacities.

([16]) Commission Regulation (EC) No. 68/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to training aid (OJ L10 of 13.01.2001, p. 20).

([17]) See, for example, C77/2002, Volvo Cars NV, 13.5.2003, OJ L235 of 23.9.2003, p. 24 and C78/2002, 13.5.2003, Opel Belgium NV, OJ L201 of 8.8.2003, p. 21.

In this light, the Commission observed in the *Ford Genk* case that automotive products become obsolete quite rapidly. The frequent introduction of new models is necessary to maintain competitiveness. Therefore, the production of a new model is a normal and regular feature of this industry. In order to produce new models, car manufacturers need to train their workforce on the new techniques to be adopted. Consequently, the training expenses associated with — and necessary for — the launching of the new model are normally incurred on the sole basis of the market incentive. The Commission thus considered that the training activities in question would have been undertaken by the company in any event, and notably in the absence of aid, and that therefore the aid was not necessary and thus not justified.

4. Further operational expenses

Other than for the launching of new models (perhaps the clearest example in the car industry of an activity which is undertaken on the basis of the market forces alone), the Commission has applied the reasoning mentioned above to the assessment of training aid linked to other activities that also belong to the core business of the companies. Such kind of aid, in the Commission's view, might be covering normal operating costs, and therefore constitutes distortive operating aid.

In the *Ford Genk* case, the Commission had to assess aid for training in the framework of the restructuring of the plant. The Commission concluded that the expenses to train the employees that will occupy a new function following the reorganisation of the plant are a normal and indispensable part of the restructuring costs: once the company has decided to lay off a significant part of its personnel (in order to save costs), temporary training in favour of replacing employees is indispensable for ensuring the continuity of production and quality. Consequently, a training aid in this context would only subsidise restructuring costs that the company would incur anyway, even without aid. The Commission thus considered that the aid was not necessary and, in any event, would not result in additional training18.

Likewise, in *GM Antwerp,* the Commission observed, in relation to the extension of the press activity, that the related training expenses seemed necessary for (increasing) the production of car parts, which is a normal activity in the automobile industry. Car parts constitute an important and indispensable input to the assembly plant, and represent a significant part of the cost of the car. Thus, market forces alone seemed sufficient to encourage the company to incur the corresponding trainings cost.

5. The case of Webasto

In contrast to the prior examples, in the *Webasto* case the Commission has explicitly acknowledged that the new — higher — standard on necessity of the aid has been complied with.

However, the reasoning in the decision makes clear that the Commission has founded this conclusion on the specific characteristics of the Webasto project, namely:

1. The training programme seemed to exceed the basic work needs of the beneficiary. This was reflected by the fact that the large majority of training courses (96% in terms of volume) concerned the transmission of transferable skills, i.e., general training which might potentially also benefit other firms, and not skills which are specific and limited to the operation of Webasto;

2. The training sought preparation of employees that were newly recruited, for the beginning of activities in a brand new plant. In particular, it is likely that the aid had played a role in overcoming the competitive disadvantage resulting from the weak qualification of workforce in the region;

3. The technology involved in the production of this type of retractable hardtops was not available in Portugal, and had to be imported from the German mother company. The new know-how would arguably contribute to raise the technical qualifications of the workers concerned, and thus improve their degree of employability.

Implicit in the two last arguments is the conclusion that the firm had the possibility not to incur these training expenses by locating in a country where the requested skills were already available. Therefore, the aid seems necessary to offset the higher training costs resulting from the weak qualification in the region. In addition, the aid contributes to increase the pool of skilled workers at the European level.

It results from *Webasto* that factors such as the predominance of general training, the beginning of activities in a new plant in a region with weak

(18) The Commission also noted that, contrary to the rationale of training aid as described in paragraph 10 of the Regulation, the restructuring at stake had led to a reduction of the pool of skilled workers available, and therefore seemed against the explicit objective of the Regulation.

qualification of workforce and the introduction of new know-how, are of a nature — when taken together — to facilitate the Commission's recognition of the aid's incentive effect. However, by referring so clearly to the specific circumstances of that particular project, the *Webasto* decision explicitly avoids any attempt of generality, and points to a case-by-case analysis of the conditions attached to each aid proposal.

6. Conclusion

In the context of training aid, the observation of changes in the economic reality of the car manufacturing industry have led the Commission to undertake a stricter verification of the necessity of the aid, and of its contribution to the objective of common interest. In recent cases concerning the car industry, the Commission has concluded that training activities which are normally undertaken by companies on the basis of market incentives (such as those relating to the launching of new models) cannot be considered eligible for aid. The Commission based its assessment on the specific circumstances of each case, in consistence with the principles of economic analysis.

Of course, this stricter verification of the necessity of training aid will not be limited in the future to the car manufacturing industry, in order to increase, in line with the State Aid Action Plan, the efficiency and effectiveness of State aid.

Regional investment aid to the shipbuilding industry: How to deal with capacity increases? — Experience with the Volkswerft Stralsund and Rolandwerft cases (1)

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1. Introduction

In November and December 2006, the Commission adopted final decisions in the cases *Volkswerft Stralsund* (2) and *Rolandwerft* (3). Volkswerft Stralsund and Rolandwerft are two German shipyards located in assisted areas where State aid can be authorised to promote regional development. Germany had notified regional investment aid to these two yards.

Regional aid measures aim at increasing the economic strength of a certain region whose living standard is below average. Among others, this can be achieved through investments involving the setting up of new companies or increasing the production capacity of a company which is already present. Both types of investment are seen to create jobs and to contribute to the economic development of the region.

However, these general rules on regional aid do no apply to the shipbuilding sector. The shipbuilding sector is a cyclical market which regularly faced periods of over-capacity and depressed prices in the past, and also for the future over-capacity issues can be expected. Because of the sector's high sensitivity, State aid to shipbuilding is governed by a special set of rules, the Framework on State aid to Shipbuilding ("Framework") (4). This Framework is more restrictive than the general rules on regional investment aid as it allows aid for investments only into upgrading and modernisation and only to improve the productivity of existing installations.

But the Framework does not provide a straightforward answer to the question whether aid for investments which will lead to a capacity increase is under all circumstances prohibited or whether there is a certain degree of flexibility. The previous few cases on regional aid to shipbuilding (5) involved only single investments for which it was apparent that they would have no impact on the capacity of the yard. The Commission could therefore approve the aid without further assessing this point in depth. Volkswerft Stralsund and Rolandwerft were the first cases which involved a higher number of different kinds of investments and for which the impact of the investments on the yards' capacities and, ultimately, on the outcome of the Commission's assessment, was not clear.

This article has the purpose to describe the line of assessment which was developed in the context of the two cases. First, the question was analysed whether the Framework prohibits regional aid for investments entailing any form and degree of capacity increases. It was concluded that this was not the case but that a certain degree of flexibility was given.

Second, as concerns the application of this flexibility in practice, the Commission had to define a coherent pattern of analysis which would respect the purpose of the Framework and the realities of the shipbuilding sector. It was decided to structure the assessment into three steps. In a first step, it has to be ascertained that the measure constitutes a modernisation or upgrading aiming at increasing the productivity of the existing installations, as prescribed by the wording of the Framework. In a second step, the effects of the investment on the capacities of the yard have to be evaluated. Finally, in the last step, any detected increase of capacities has to be balanced against the increase of productivity and should be found not to be disproportionate.

The article will end with a brief description of how the developed line of assessment was applied on the two cases Volkswerft Stralsund and Rolandwerft.

(1) The content of this article does not necessarily reflect the official position of the European Commission. Responsibility for the information provided and the views expressed lies entirely with the authors.

(2) Case C6/2006, decision of 06.12.2006, available on the European Commission Competition website: http://ec.europa.eu/comm/competition/state_aid/register/ii/by_case_nr_c2006_000.html#6

(3) Case C 5/2006, decision of 20.12.2006, available on the European Commission Competition website: http://ec.europa.eu/comm/competition/state_aid/register/ii/by_case_nr_c2006_000.html#5

(4) OJ C 317 of 30.12.2003, p.11.

(5) See cases C 23/2001 — *Flender Werft AG,* OJ L 203 of 01.08.2002, p. 60; N 306/2002 — *Flensburger Schiffbaugesellschaft mbH & Co. KG,* OJ C 277 of 14.11.2002, p.2; N 383/2002 — *Neorion Shipyard,* OJ C 6 of 10.01.2004, p. 21; N 617/2003 — *Lamda Shipyard,* OJ C 24 of 29.01.2005, p. 5.

2. No strict prohibition of capacity increases

The central provision for the assessment of regional aid to shipbuilding is Point 26 of the Framework which stipulates that *"Regional aid to shipbuilding, ship repair or ship conversion may be deemed to be compatible with the common market only if it fulfils the following conditions: (a) the aid must be granted for investment in upgrading or modernising existing yards, not linked to a financial restructuring of the yard(s) concerned, with the objective of improving the productivity of existing installations […]"*.

How is that provision to be read against the background of point 3 of the Framework, following which *"[…] the Commission recognises that certain specific factors affecting the shipbuilding sector should be reflected in the Commission's policy of State aid control: (a) over-capacity, depressed prices […]"?* Does this imply that no aid can be authorised for investments that lead to a capacity increase?

Point 3(a) is systematically located in Section 1 of the Framework entitled "Introduction". Point 26 is part of Section 3.3, which contains the specific provisions applying to the shipbuilding industry, i.e. the provisions which deviate from the normal rules. The chapter on the specific provisions is introduced by point 13, which explains that *"The general principle outlined in Section 3.2 is subject to the following exceptions, which are justified by the specific factors presented in Section 1."*

It can thus be concluded that the fact that the sector, according to Section 1, suffers from overcapacities, finds its expression in the specific rules, among others point 26. Point 26 thus contains all conditions for the granting of regional investment aid to this specific industry. Point 3(a) does not contain an additional condition but merely justifies the restricted rules in point 26 and serves as an interpretation guideline.

This interpretation is further supported by the wording of point 3 which stipulates that it is the Commission's "policy" which reflects the listed specific factors, in the sense of "policy" as opposed to "the Commission's case by case decision practice". Also no express strict prohibition to increase capacities is laid down in point 26. In addition, a strict prohibition to increase capacities would probably not well serve the actual aim of the Framework, namely to strengthen the European yards in the fierce worldwide competition by encouraging productivity increases without encouraging capacity increases.

Finally, a number of investments into productivity automatically lead to an increase of capacity. Where investments aim at producing faster, it is obvious that they may give the yard the opportunity to produce more. However, the Commission should not hinder Community yards from becoming more efficient. On the contrary, point 5(a) of the Framework explicitly mentions as one of the objectives of the Framework to encourage greater efficiency and competitiveness of Community yards.

While the prohibition of any form of capacity increase did not seem justified, it was on the other hand also clear that capacity increases could not be disregarded altogether. It emanates from the wording of point 26 that investment aid should be restricted to measures which improve what already exists. As stated above, point 3 (a) serves as an interpretation guideline for point 26. Point 3 thus provides a justification for the limitation in point 26 by referring *inter alia* to overcapacities.

The Commission therefore concluded that the Framework does not exclude capacity increases as such. Nevertheless, as required by the wording of point 26, the Commission must ascertain that the investments are for the modernisation and upgrading of an existing yard with the objective of improving the productivity of existing installations. Investments which have as sole objective to increase the capacity of the yard are therefore excluded. For all other investments, the Commission concluded that, where investments led to a capacity increase, it would be necessary to balance this capacity increase against the productivity increase.

3. Eligibility of measures leading to a capacity increase

After having concluded that the Framework did not strictly prohibit the subsidising of measures also leading to capacity increases, but that a balanced approach was the most appropriate way to proceed, the next question was how this balancing would be carried out in practice. To this end, the first crucial step is to make sure that the purpose and the effect of the investment is to strengthen the competitiveness of the yard by improving its productivity. In the second step, the effect of the investment on the capacity of the yard has to be evaluated. And, quite logically, in the third step, both have to be weighed against each other.

a) Improving the productivity of existing installations

Point 26 prescribes that only "*investment […] with the objective of improving the productivity of exist-*

ing installations" can be eligible. The background to this criterion is the sensitivity of the world market for shipbuilding where competition, in particular from Asia, is fierce and recurrent overcapacities regularly lead to a sharp drop in prices. Until today, the strength of the European shipbuilding industry lies in its high degree of quality and specialisation. To maintain its competitiveness the European shipbuilding industry should further build up on quality (instead of quantity). Therefore only investments into further modernisation and upgrading which improve the productivity of the yards should be encouraged through State support and not the mere setting-up of additional capacity. As a first assessment step, the Commission must therefore ascertain that each investment notified fulfils this condition.

To be able to analyse whether this precondition is fulfilled, it was first necessary to clarify the notion of "installation", or more precisely, to define at which level "installations" should be considered. At a level of greater detail, an installation would be for instance some machine in a production line, a crane or a rail track. At a broader level, an installation could be a panel production line or a fitting quay etc. It was concluded that a narrow approach would not be justified. Adopting a narrow approach could result in excluding from eligibility investments that increase the productivity of the production process as such but are no investments in the single installations already existing on the yard. An example would be the purchase of an automatic welding machine to replace manual welding which would have no impact on the productivity of the other machines. Such limitation would put an unjustified obstacle to these investments even if they had the effect to render the yard concerned more competitive. However, considering installations at an even broader level than explained above would not make sense because it would practically mean to equal "existing installations" with "existing yards", whereas the Framework clearly makes a difference between the two. It was thus concluded that the most appropriate level would be the aggregate intermediate level of an installation as serving a specific production step.

Second, it should be noted that the regional aid provision of the Framework does not explicitly require that, in order to be eligible, investments have to concern directly existing installations. Instead the requirement is that the investments have to be into existing yards and the objective of the investments has to be an increase of the productivity of existing installations. One could imagine a situation where investments into new installations do increase the productivity of other, existing installations. This can happen in case of installations with idle capacities because of other bottlenecks in previous production steps. An example would be a panel construction line with a capacity of x, with a subsequent section construction line of a capacity of 2x. The section construction line would only work at half capacity. The construction of a second panel construction line would be considered a new installation (at an existing yard). It would however enable the yard to use its section construction line at full capacity and thus increase the productivity of this existing installation.

Where an investment in a new installation has no positive impact on the productivity of the existing installations, the situation is clear: a regional investment aid would not be covered by the Framework.

b) Assessment of capacity increases

If the condition of the improvement of productivity is fulfilled, the Commission will look more closely at the effect of the measure on the yard's capacity. However, assessment experience shows that capacity measurements in figures are no straightforward exercise. It should therefore be clarified in which cases an in depth assessment of capacity changes is really required.

A first conclusion which was drawn in this respect concerned capacity increases which are the direct result of productivity increases. As already explained above, investments which enable specific installations to produce faster may have as direct consequence that the yard can produce more ([6]). However, since the main aim of the Framework is to increase the productivity of the yard, such type of directly linked and "unavoidable" capacity increases do seem acceptable. Therefore, this type of capacity increases is not normally further evaluated and balanced against the productivity increase (unless there would be indications hinting at a disproportionality of the capacity increase).

Second, the assessment of the single investments in the two cases Volkswerft Stralsund and Rolandwerft showed that a distinction can normally be made between investments into existing installations and investments into new installations.

An investment into an existing installation, which has the aim to increase the productivity of this installation, is normally less likely to increase the yard's capacity (apart from capacity increases which are a direct result of the productivity

([6]) This requires that there are no other bottlenecks in the yard which would hinder an overall speeding up of the production.

increase). The production facility already exists and it is merely "modernised" or "upgraded". This is precisely what the Framework aims at. It thus appears that no in depth balancing test would normally be necessary for investments into existing installations either, unless there are doubts on the proportionality of the capacity increase.

The case is different for an investment into new installations. Even if such an investment increases the productivity of existing installations, it consists in setting up new facilities and is more likely to enable the yard to (significantly) increase its production. In how far these new facilities will additionally increase the capacity of the yard in general can only be assessed on a case by case basis. As experience in the Rolandwerft case shows (see below), the assessment here can go quite into the details of the yard's technical possibilities to increase its activities.

c) Balancing of capacity increase against productivity increase

It should always be excluded that the capacity increase of the yard would be disproportionate in relation to the productivity increase. In practice, as a consequence of the explanations above, no in depth balancing will normally be necessary where the capacity increase is the direct result of the productivity increase or where the investment is done in an existing installation.

A substantial balancing should normally be carried out where the investment sets up new installations on the yard. However, in the existing decision practice, the Commission so far did not need to fully apply such a proportionality test. For the most controversial investment in the Rolandwerft case — the construction of an additional fitting quay — an increase of capacity could be excluded, such that proportionality did not have to be assessed anymore. In the Volkswerft Stralsund case no capacity increase measured in annual output of ships (taking into account the size of the ships) was found. Only the steel processing capacity of the yard increased slightly. No experience is thus so far available concerning the precise determination of "disproportionate".

4. What does this approach mean in practice: the Volkswerft Stralsund and Rolandwerft cases

Volkswerft Stralsund

The investment project of Volkswerft Stralsund concerned the modernisation and rationalisation of the yard to allow the yard to efficiently build a larger type of vessels, the so-called "panamax vessels". It comprised investments into existing installations (prolongation of the existing ship lift to be able to lift larger ships, enlargement of two of the four already existing cells of the conservation facilities) as well as investments into new installations (construction of a new production line for panels and for section parts and construction of four additional sites for section construction).

The Commission concluded that the project would improve the productivity of the yard and its existing installations as it would enable the yard to assemble panamax vessels from larger sections than before, thus increasing efficiency and competitiveness of the yard.

Nevertheless, as the investment project also comprised investments into new installations, in a second step it was necessary to assess the impact of the investments on the capacity of the yard and to balance any potential capacity increase against the productivity increase. It was found that the capacity of the yard measured in annual output of ships (taking into account the larger size of the ships) would not increase. The capacity of the yard measured in tons of steel processed per working hour would increase. However, the Commission concluded that this increase in steel processing capacity was a side effect of the productivity improvements and that it would not be disproportionate to the achieved productivity increases.

Rolandwerft

In the case Rolandwerft, most of the investments concerned existing installations, they increased the productivity of the installations and any potential capacity increase would have been the direct result of the productivity increase. The measures could therefore be approved without any deeper assessment.

A much more detailed analysis was required for an investment into the construction of a new equipping quay. Before the implementation of the investment project, Rolandwerft had equipped two ships in parallel on the same fitting quay. The first ship was berthed directly at the quay side and equipped by using the quay equipment. The second ship, which was berthed alongside the first ship, was equipped from the water side by using rented swimming cranes and from the quay side by crossing the first ship. The notified investment foresaw the construction of a new equipping quay so that it would not be necessary anymore to equip two ships berthed in parallel on the first fitting quay.

The Commission concluded that the second quay would increase the productivity of the first quay and that the condition of improving the productivity of an existing installation would be fulfilled ([7]).

As regards the question whether the investment concerned an existing installation, Germany brought forward the argument that the second berth should be qualified as an existing second equipping quay which would merely be *relocated*. However, as there were hardly any existing physical installations for this second "quay", the Commission concluded that it could not be considered as an existing installation. A second argument brought forward was that the investment into the installations for equipping a second ship on this quay merely constituted a *prolongation* of the existing quay. In the end, it was not necessary to determine whether the investment should be regarded as an investment into an existing installation or into a new installation as it was concluded that the investment in any event would not result in a capacity increase.

As regards the analysis of the effects of the investment on the capacities of the yard, the Commission carried out a separate analysis for each type of shipbuilding activity of Rolandwerft, i.e. newbuilding, ship repair/conversion and equipping of prefabricated hulls. The question was assessed against the specific history of the yard, which has always equipped two ships at the same time. Originally, two smaller ships were equipped at the quay, but when the yard began to build bigger ships, the quay became too short and the second ship was shifted on the "parallel" berth. The Commission therefore concluded that the equipping of a second ship was not only an occasional activity, and that the capacities of the yard before the investments also include the equipping of a second ship. On this basis, it could be excluded, for each of the shipbuilding activities, that the yard would be able to use the second quay to increase its capacity: the construction installations in preceding stages were already used at full capacity and therefore represented a bottleneck for an increase of the activities on the quays. Outsourcing with the aim to equip prefabricated hulls was not possible for technical reasons either. It was also verified that the yard would not be able, through a simple further investment, to remove the bottleneck. The aid could therefore be approved without having to carry out a balancing exercise.

5. Conclusion

The cases Volkswerft Stralsund and Rolandwerft obliged the Commission to reflect upon its assessment line when dealing with cases where investments increase the yard's capacities. An essential conclusion was that it is, as a general principle, necessary to see any capacity increase in relation to the productivity increase achieved through the investment and to assess whether a capacity increase would be disproportionate in relation to the productivity increase. The aid would then not be allowed. In practice however such detailed analysis seems only necessary in a limited number of cases. For investments in existing installations it is normally possible to assume that they will not lead to a disproportionate capacity increase as no new facilities will be set up. But, as Rolandwerft showed, as soon as there are doubts as to the qualification of an installation as existing or new, a more detailed assessment of the impact of the investments on the yard's capacity cannot be avoided.

([7]) One crane system for both ships was set up, the new crane would facilitate the lifting of charges also on the first quay and works on the first ship would not be impeded anymore by having to cross it for works on the second ship.

State aid to an electronics cluster in Poland: Assessing regional investment projects in the context of spatial agglomeration ([1])

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Introduction

On 19 July 2006, the Commission adopted ([2]) nine separate decisions relating to a series of initial investment projects undertaken by eight different companies. Eight of these projects are part of an electronics cluster set up to develop flat panel display technologies in the South-West of Poland (Dolnośląskie region).

The endorsed projects were assessed in the light of the rules of the Guidelines on national regional aid ([3]) (RAG). In addition, those projects for which eligible costs were above EUR 50 million were assessed under the Multisectoral framework on regional aid for large investment projects ([4]) (MSF).

In its decisions, the Commission has for the first time provided for an extensive analysis and interpretation of the concept of a single investment project and the respective criteria stipulated in point 49 of the MSF ([5]).

The assessment of the Commission focused in particular on the question whether the separately notified investments to be undertaken in the same geographic location, with purchase/sale dependencies and links between the investors in the cluster over the concurrent period of time would not constitute a single investment project.

As a result of the assessment of the inter-relationships between the different investment projects, the Commission found that MSF rules were not circumvented for the current group of investments, and that the projects were not artificially divided to avoid the application of the scaling down mechanism of maximum aid ceilings foreseen in point 21 of the MSF for projects with eligible costs above EUR 50 million.

Accordingly, the eight investment projects making up the electronics cluster were examined separately which led to the approval of an aid package of close to EUR 200 million in present value for total eligible costs amounting to about EUR 650 million in present value.

The issue of discerning whether the eight investment projects constituted a single investment project was a key aspect to address in the assessment of these cases since the MSF foresees a significant reduction in aid intensity for large investment projects ([6]). In this respect, Soltesz (2005) has argued that the approach followed in the MSF represents in essence an attempt of the Commission to significantly reduce the allowable aid intensities for large investment projects in assisted regions. This could have undesirable effects on the capacity of Europe to attract foreign large investment projects. However, Cavallo and Junginger-Dittel (2004) note that the automatic scaling down mechanism for maximum aid intensities in the MSF could counterbalance the strong incentives for delocalisation of large investment projects that result from EU enlargement. In case this cluster would have been considered to be a single investment project and without prejudice to the results of the compatibility assessment, given the size of the eligible costs involved, the allowable aid amount would have needed to be reduced by an amount in excess of EUR 50 million due to the automatic scaling down mechanism in the MSF.

Facts of the case: the electronics cluster

In spring 2006, Poland notified a package of nine investments projects to be undertaken by a group of Korean-based companies in Kobierzyce,

([1]) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

([2]) State Aid N 245/2006 — "Aid to LG.Philips LCD Poland Sp. z o.o.- MSF 2002"; State Aid N 246/2006 — "Aid to Ohsung (Dong Seo) Display Poland Sp. z o.o."; State Aid N 247/2006 — "Aid to Lucky SMT Sp. z o.o."; State Aid N 248/2006 — "Aid to Dong Yang Electronics Sp. z o.o."; State Aid N 249/2006 — "Aid to Heesung Electronics Poland Sp. z o.o."; State Aid N 250/2006 — "Aid to LG Chem Poland Sp. z o.o."; State Aid N 251/2006 — "Aid to LG Innotek Poland Sp. z o.o."; State Aid N 256/2006 — "Aid to LG Electronics Wrocław Sp. z o.o." (Household Appliances) and State Aid N 257/2006 — "Aid to LG Electronics Wrocław Sp. z o.o." (TV sets) (not yet published).

([3]) OJ C 74, 10.3.1998, p. 9 as amended.

([4]) OJ C 70, 19.3.2002, p. 8 as amended.

([5]) Schütte (2005) has criticized the ambiguity of the definition of single investment project embedded in the MSF.

([6]) The part of eligible costs of a large investment projects above EUR 100 million would have to be reduced to approximately 1/3 of the applicable aid intensity for the region concerned.

near the city of Wrocław, Dolnośląskie region in Poland, an area eligible for regional aid under Article 87 (3) (a) of the EC Treaty.

Eight of these investments, led by an anchor investor, form part of an electronics cluster for the production of LCD modules used in the production of flat panel display (FPD) TV sets.

The anchor investor of the cluster, LG.Philips LCD Poland Sp. z o.o. (LPL), plans to set up an assembly plant of large LCD TV modules. The LCD TV module production process is the last step in the production of Flat Panel TV displays. The initial stage of fabrication of an LCD panel (the so called "cell") is carried out in Korea. It requires the fabrication of a back glass substrate and a front glass which are then joined together after injecting liquid crystal materials between the two glasses. In a second stage, the module assembly takes place, where various electronic components are fitted into the LCD panel. The finalized module is then ready for incorporation in the downstream product, the television set.

Currently, virtually all LCD production in the world (including the stage when LCD panels are turned into LCD modules) takes place in Asia. The modules are then shipped to manufacturers of TVs, PC monitors, notebooks, mobile phones and PDAs around the world. The plant of LPL in Poland will be the first of its kind in Europe and thus represents the entry point of the LCD producers in the EU. The plant will supply LCD modules for flat-screen TVs to the European industry (including Turkey), for which demand is growing very rapidly in Europe.

Six other Korean companies comprising Ohsung (Dong Seo) Display Poland, Lucky SMT Poland, Dong Yang Electronics Poland, Heesung Electronics Poland, LG Chem Poland and LG Innotek Poland will carry out investments to establish production plants in the Kobierzyce site. These investments aim at producing a series of components that can be used in LCD TV modules (like printed circuit boards, backlight units, polarizers, and inverters) as well as other products such as TV tuners, power supply units and filters for plasma display panels which can be used as part of stand alone electronic products which are not related to LCD module production.

A further company carrying out investment in the same site will be LG Electronics Wrocław. The company will manufacture LCD TV sets, the downstream product in the supply chain. The company also intends to produce refrigerators and washing machines in a separate plant. Given the type of product manufactured, the investment concerning the production of refrigerators and washing machines is not considered to be part of the electronics cluster.

The economics of clusters: A short overview

Eight of the investments assessed adopt a cluster strategy. Companies reap economic benefits from grouping together in a specific geographical location ([7]).

Firstly, the setting up into clusters allows companies to have access to a better and cheaper variety of inputs provided by specialized suppliers. Clustering leads to productivity advantages by reducing transportation and information costs as well as by enabling the building up of trust relations between the firms operating in the cluster. Additionally, the geographical proximity between suppliers and clients allows to reduce the inventory requirements of companies.

Secondly, clustering leads to innovation advantages. The proximity between customers (downstream companies) and suppliers (upstream companies) leads to innovation gains by facilitating the transfer of knowledge between the companies in the cluster. In other words, by working in a cluster, firms can mutually benefit from the knowledge spillovers generated by each other. Moreover, clustering allows the companies to access a larger pool of skilled workers. This pool benefits both the companies that have access to a larger supply of specialised workers and the workers who have more opportunities to valorise their own skills/competences.

In high technology industries, and particularly during the early stage of the life cycle of a product, geographical clustering facilitates the use and transfer of tacit knowledge. This knowledge is transferred via informal mechanisms and is acquired through practical experience, learning by doing and social interaction. The transfer of this type of uncodified knowledge requires personal contact as well as physical proximity. This is arguably the case of flat TV screen production, a technology which is in a relatively early stage of

([7]) There has been a recent surge in analytical and empirical models aiming to capture and explain the processes of spatial agglomeration and clustering. These models incorporate some sort of increasing returns and imperfect competition to explain spatial agglomeration and urban growth phenomena. Marshall (1890) already signalled the large advantages of industrial clustering deriving from external economies of scale achieved though knowledge spillovers, user-supplier connections and labour market interactions. See Henderson and Thisse (2004) for a broad and authoritative review of recent contributions to this literature.

market penetration. In the more mature sectors, the process of learning and innovation takes place fundamentally through codified knowledge taking the form of blueprints, patents and academic publications.

Aid package

The aid package offered by the Polish authorities to the nine investment projects concerns a mix of different types of *ad hoc* aid as well as aid granted under existing aid schemes. Depending on the case, the financial assistance offered included: capital investment grants; grants for job creation; local real estate tax exemptions; (partial) free transfer of land; exemptions from Special Economic Zone (SEZ) management fees; exemptions from corporate income tax in SEZ; exemptions from de-agriculturization fees; labour market incentives; interventional jobs; financing of workplace equipment and training aid.

Assessment

After establishing that each of the individually notified measures constitute State aid within the meaning of Article 87(1) of the EC Treaty, the Commission assessed the compatibility of the aid package in accordance with the provisions of the RAG and where applicable the MSF.

This assessment was carried out in three steps: In a first step, the Commission verified whether the overall cluster had to be considered as a "single investment project" in the meaning of the MSF. In a second step, the compliance with the standard compatibility criteria of the RAG was assessed, and in a third step, the conformity with other MSF rules was considered.

The aid measures were found to be compatible with Article 87(3) (a) of the EC Treaty since they promote the economic development of a region where the standard of living is abnormally low and where there is serious underemployment. The detailed description of the Commission's assessment is provided in the sections below.

Single investment project

Point 49 of the MSF establishes that for the purposes of the framework an investment project includes all the fixed investments on a site, made by one or more undertakings, in a period of three years. In turn, a production site is an economically indivisible series of fixed capital items fulfilling a precise technical function, linked by a physical or functional link, and which have clearly identified aims, such as the production of a defined product. Where two or more products are produced from the same raw materials, the production units of such products will be deemed to constitute a single production site.

Recently, new Guidelines on national regional aid for the period 2007-2013 ([8]) have been adopted by the Commission. As a result of the revision, the MSF rules have been incorporated as an integral part of the regional aid guidelines. Junginger-Dittel (2006) indicates that the changes introduced in the rules do not concern the definition of single investment project. In consequence the assessment below is still valid for the period of applicability of the new guidelines 2007-2013.

In the case of this electronic cluster of eight projects, despite the geographical proximity of the individual investments and the indirect relationships between some of the beneficiaries, the Polish authorities provided evidence that the investments are not to be considered a single investment project within the meaning of point 49 of the MSF 2002. In particular, to establish the independence of the current projects, the Commission took into account the following considerations:

No artificial subdivision of the projects

- The decision-making processes of LPL and the other investors are independent from each other. The business rationale underlying the planned investments is achieving overall economic efficiency, not the avoidance of State aid rules. For the reasons indicated previously, the investments to be carried out are likely to experience major gains from clustering. Evidence that similar clusters for the fabrication of LCD TV modules have developed in Asia, where no state aid rules apply, confirms that there has not been an artificial subdivision of project to escape MSF rules. Moreover, LPL also acts as the anchor investor in one of the Asian clusters. The fact that in Asia there has been no vertical integration between the companies belonging to the cluster provides evidence that the companies find it profitable to remain independent.

Economic divisibility

- For the current cluster, there is no indication that any of the investments would be impossible without the other seven investments which are carried out in close geographical and temporal proximity.
- The divisibility of the investments is also confirmed by the observation of the business reality of the companies operating in this market

([8]) OJ C 54, 4.3.2006, p.13.

in Asia. In the case of Asia some suppliers have decided to locate in close proximity to LPL for efficiency reasons, while others sell their products to LPL although being located far away from LPL's plant, sometimes even in another country.

- The geographical proximity of the investments in the cluster was essentially influenced by the Polish authorities offer to locate in Kobierzyce.
- The investment decisions have been taken independently by each of the companies and subsequent agreements entered into between each individual investor and the Polish authorities are not mutually dependent on each other.

No one single technical function

- The components manufactured by the investors in the cluster are not linked technically. They constitute separate and stand alone products in their own right that can be (and often are) produced separately from a wide variety of raw materials. Moreover, the fixed capital items of the different investments do not fulfill a precise technical function since all manufactured products can be sold and marketed separately.
- The overall purchasing policy of the investors requires alternative sources of supply other than the companies forming the cluster. This ensures that companies can obtain better prices on the intermediate goods they buy from their suppliers.

Lack of functional and physical link

- The projects are not linked by any preferential supply or exclusivity agreements. The various investors are free to set prices according to prevailing market conditions. As indicated before, LPL and the other investors in the cluster, already procure or sell the products in question in Asia (to each other, but also to and from third parties). Therefore they have a frame of reference for determining market prices even if no market for the products in question has yet developed in Europe.
- Within the cluster, a company's output does not rely exclusively on the supply by other companies. In fact, the companies have based their calculations on return on investment on projections to supply components to clients outside the cluster. In addition, companies in the cluster will also manufacture products to be sold solely outside the cluster (e.g. PDP filters, power supply units and TV tuners).
- In a first period (also since LPL will be the only manufacturer of LCD TV modules in Europe), dependence on sales within the cluster will be important, but never exclusive. LPL aims to eventually have several sources of supply just like other investors in the cluster aim to supply customers other than LPL. Two of the component producers, Lucky SMT and Dong Yang electronics will be selling to companies outside the cluster already from the start of production. The dependence of the remaining component producers in the cluster on sales to LPL will significantly diminish overtime.
- The projects do not share a physical link. The various goods and components are being produced in separate, discrete processes in each project. In particular, there is no "back and forth" process by which a product would be semi-finished by one company, provided to another for further processing and returned to the first company for completion.
- Transportation of materials and merchandises occurs by over public roads and not through private means such as internal conveyor belts. Each of the companies will operate their own warehouses for raw materials and products, not sharing storage facilities. Each of the companies will independently manage and decide on its production processes and capacity usage.

No common aim

- The investments do not have a clearly identified common aim. The suppliers' follow a profit maximisation objective by selling their own products. These may eventually be used for a variety of applications such as the development of other end products.
- The products manufactured by each individual investor are to be viewed as unique products that are sold and marketed separately on the market. The objective of each investor in the cluster is not aimed at producing the same end product.

Consequently, given the evidence provided by the Polish authorities, the eight investments forming the cluster were assessed separately. Cases where the eligible costs of the project were below EUR 50 million, were assessed solely under the provisions of the RAG. For the rest of the cases above this threshold, compliance with the automatic scaling down of the allowable aid intensity ceiling had to be evaluated (point 21 of MSF). Furthermore, for the project where the aid amount was higher than the maximum amount of aid that a hypothetical investment of EUR 100 million could receive in the region concerned, a further assessment under MSF rules concerning market share and capacity created had to be performed.

Compliance with the RAG

As a general rule the Commission does not favour the award of aid that is not based on an earlier approved scheme or is sector specific. However, in the present cases, it was concluded that the projects (in many instances, the first of their kind in Europe), will produce substantial positive spillovers which should provide a major contribution to the development of an EU disadvantaged region and outweigh the potential distortion of competition.

The electronics cluster will have a positive contribution to the development of Dolnośląskie, a region which suffers from large socio-economic handicaps. The region has about half the GDP per capita of the EU-25 ([9]) and an unemployment rate which is three times higher than the EU- 25 average ([10]).

From a dynamic perspective, the project will lead to the establishment of a completely new activity in a high tech sector, which will attract additional investors, supporting the creation of new jobs and economic development in the Dolnośląskie region. This could lead to a path dependence pattern helping the region to develop a critical mass and specialisation in the production of technology driven consumer goods electronics.

In terms of employment, the investments concerning LPL and the other investors are expected to create around 12,000 direct jobs and a significant number of indirect jobs.

The project will also have a positive effect by facilitating structural change in the Dolnośląskie region by shifting economic activity from coal mining towards a rapidly expanding market.

The Commission also found that the projects complied with all the remaining provisions of the RAG. Accordingly, the notified measures aimed at initial investment and aid for job creation; the beneficiary's own contribution to the eligible costs for each project was above the required 25% threshold; the aid applications were submitted before the work started on the respective projects; the costs of buildings and plant/machinery were considered eligible; the investments and new jobs created will be maintained for at least 5 years after completion of the investment and finally, the rules on cumulation of aid were respected.

([9]) GDP per capita 47.5% of EU-25 average for the period 2000-2002 (EU-25=100). GDP per capita measured in purchasing power standard.

([10]) 280.8 % of EU-25 average and 131.3% of the Polish average. Average for the period 2001-2003 (EU-25=100).

Market share and capacity considerations

As already indicated the Commission had to carry out a detailed market analysis in the LPL case to establish the compliance of this investment with points 24 (a) and (b) of the MSF (market share and capacity increase).

Examining compliance with these conditions calls first for the definition of the relevant product and geographic market(s).

Relevant market

The investment project by LPL Poland concerns the production of LCD TV modules of screen size 22-inches and above ([11]). Therefore, to define the relevant product market the Commission had to examine what other products could be considered as substitutes from a demand and supply-side point of view.

LCD TV modules are used in TV displays, which in turn are divided into two categories: cathode ray tube (CRT) and flat panel displays (FPD). Flat panel technology is a clearly distinct market from that of CRT in the light of prices, customer preferences and supply-side substitutability (i.e. equipment, production lines and technology differ significantly). Moreover CRT TV is an obsolete technology which is rapidly being replaced by FPD.

As regards FPD, although there are several competing display technologies (e.g. digital light processing, organic light emitting diode), several reasons led the Commission to restrict market analysis to the most common LCD and plasma display panel (PDP) technologies. Firstly, this constitutes a narrow definition of the FPD technology and represents thus a worst case scenario for the purpose of assessing market share and capacity increase. Secondly, from a customer perspective (i.e. the perspective of TV set manufacturers), the LCD and PDP modules are roughly similar. For both technologies, the module contains not only the display but also important electronic functions, facilitating the assembly of the finalized TV. This also means that there are no significant impediments for a TV set manufacturer to switch from PDP to LCD TV production and vice versa.

In its analysis, the Commission defined the relevant product market for FPD TV modules according to two distinctive criteria, the underlying technology (i.e. LCD and PDP considered together or

([11]) Although there are no technical constraints to produce modules below this size in the Polish site, it would be economically unprofitable for the company to do so.

separately) and the dimension (display size of the panel). Accordingly four possible relevant markets were identified:

(A) LCD and PDP TV modules (broad market definition)

(B) LCD TV modules

(C) LCD and PDP TV modules equal or above 22-inches

(D) LCD TV modules equal or above 22-inches (narrow market definition)

The Commission also analysed the need to adopt an even narrower market definition for FPD TV modules, distinguishing between the medium segment (screen size between 22-inches and 37-inches) and the large segment (screen size above 37-inches) but concluded that such further segmentation is not warranted for supply and demand side substitutability reasons.

As regards the geographic market, data submitted with the notification pointed in the direction of defining the market as worldwide. Both manufacturing and sales are highly globalised, there are no impediments to trade in TV display units in terms of technical requirements and there are no significant price differences between regions. The main component of the LCD TV module to be produced in LPL Poland, the LCD cell, is imported from Korea.

Assessment under point 24 (a) of the MSF

In order to prevent that a company benefiting from a substantial amount of State aid has or acquires a dominant position in the market that could impede effective competition, point 24 (a) of the MSF requires that the market share of the aid beneficiary at group level is below 25 % before and after the investment.

The Commission checked compliance with point 24 (a) of the MSF on the relevant product markets both at EEA-level and at the worldwide-level, to make sure the analysis covers all possible demarcations of the geographical market.

To establish the market share of LPL in the relevant markets before and after the investment, the Commission compared the sales, in value and in volume terms, of the relevant products by LPL to the overall sales on the market concerned. The figures on overall sales were based on publicly available data as well as projections made by an independent company specialised in market research. Data on LPL's own sales were based on the company's own calculations which were coherent with independent estimates.

The calculations confirmed that the market share of the beneficiary is and will remain below 25 % in all possible product and geographic markets.

Assessment under point 24 (b) of the MSF

In order to avoid aid being granted to a significant capacity increase which is not matched by a corresponding increase in demand for the product concerned, point 24 (b) of the MSF provides that aid is incompatible if it concerns a capacity increase exceeding 5% on an underperforming market (i.e. where sectoral growth is below EEA GDP growth). The Commission has to assess the production capacity created by the project and the relevant sectoral growth on the basis of the apparent consumption of the product concerned in the EEA market.

On the basis of the available data, the Commission was able to establish that, whatever market segmentation referred above is used; the apparent consumption of the market analysed in the EEA has been growing much faster than the EEA's GDP. In fact, due to the rapid development of this newly created market, growth figures have been in the triple-digit area, and this expansion is also expected to continue in the years to come. Consequently, the assessment of the relative increase in capacity due to the investment project was not necessary and the Commission concluded that the investment of LPL Poland is compatible also with point 24 (b) of the MSF.

In case the project carried out by LPL had been found to exceed one of the two applicable thresholds in points 24(a) and (b) of the MSF, the project would not be eligible for any regional aid. Junginger-Dittel (2006) notes that under the new regional guidelines, the compatibility criteria for the assessment of large investment projects focusing on these two tests have been abandoned and redefined into procedural thresholds triggering an in-depth investigation based on the merits of the measure.

Conclusion

In the current set of decisions, concerning a cluster of parallel investments taking place in the same geographical location, the Commission has applied for the first time the concept of a single investment project.

The group of decisions sets a precedent of the elements the Commission may take into consideration when assessing the issue of single investment project in the context of economic clusters. The assessment of these cases also provides an example of how the Commission can support State aid for a group of investment projects when it can rely on strong economic reasoning and factual evidence.

By excluding the existence of a single investment as defined by MSF, the Commission assessed the projects separately and adopted eight independent decisions concerning the cluster.

In a framework of increased globalisation and economic integration, clustering is likely to become an even more relevant factor of investment in sectors driven by innovation and knowledge in which Europe is building its comparative advantage.

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Poste Italiane: a market fee can fulfil the Altmark criteria (1)

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On 22 November 2006, the Commission has decided that the remuneration fee paid by *'Cassa Depositi e Prestiti'* (CDP) to *'Poste Italiane'* (PI) for the distribution of postal savings books as of 2004 does not constitute State aid (2) because this remuneration is in line with the principles established by the European Court of Justice in its Altmark ruling of 24 July 2003 (3).

Background

CDP is a state-controlled financial body, whose mission is to foster the development of public investment, local utility infrastructure works and major public works of national interest.

PI is the universal postal service provider in Italy, which fulfils the universal postal service obligation. PI also exercises financial activities through an integrated business division named 'Bancoposta'.

BancoPosta can be considered as a deposit institution and a financial intermediary. While it does not hold a bank license, it uses the 13881 post-office outlets (4) of PI to operate and provide banking and financial products.

PI is remunerated by CDP for distributing postal savings products, i.e. postal savings books and postal bonds on behalf of CDP.

Postal savings books are fund-raising instruments, with a low risk profile, as reimbursement is State-guaranteed. The deposits may be either registered or bearer (5). The main operations are money deposits and withdrawals. The current interest rate is 1.40%. Interests are paid yearly on 31 December and are subject to 27% withholding tax. The opening and closing of postal savings books have by law to be cost free for savers.

Existence of State aid

The Commission has established that there is trade between Member States in the postal and financial services sectors. The remuneration for postal savings products strengthens the position of PI in relation to postal and banks undertakings competing in intra-Community trade. Therefore, the measure is liable to affect such trade and distort competition.

The key issue in the case has therefore been whether the remuneration paid for the collection of postal savings books would confer an advantage to PI.

Existence of an advantage

The collection of postal savings is a service of general economic interest

While financial services as a whole are not included within the remit of universal postal service PI is entrusted with, the collection of postal savings through PI on behalf of CDP has been qualified as a service of general economic interest by the Italian authorities since October 2004. This means that PI is entitled to receive remuneration for the distribution of postal savings books as compensation for the provision of this public service obligation.

The Altmark framework

It is apparent from the case-law of the Court of Justice of the European Communities that public service compensation does not constitute State aid within the meaning of Article 87(1) of the Treaty if it fulfils certain conditions. In its judgment in Altmark, the Court laid down the conditions under which public service compensation does not constitute State aid as follows:

- '(…) First, the recipient undertaking must actually have public service obligations to discharge and those obligations must be clearly defined (…).

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.
(2) Not yet published in the Official Journal. At the same time, the Commission has also opened the procedure pursuant to Article 88(2) on the remuneration paid by CDP for the distribution of postal bonds.
(3) Judgements in Case C-280/00 Altmark Trans GmbH and Regierungspräsidium Magdeburg v Nahverkehrsgesellschaft Altmark GmbH (2003) ECR I-7747.
(4) This figure corresponds to at least one outlet per municipality on average. PI has thus the biggest banking retail network in Italy.
(5) Registered postal savings books represent 99% of the total.

- (…) Second, the parameters on the basis of which the compensation is calculated must be established in advance in an objective and transparent manner (…).
- (…) Third, the compensation cannot exceed what is necessary to cover all or part of the costs incurred in the discharge of the public services obligation, taking into account the relevant receipts and a reasonable profit (…).
- (…) Fourth, where the undertaking which is to discharge public service obligations, in a specific case, is not chosen pursuant a public procurement procedure, which would allow for the selection of the tenderer capable of providing those services at the least cost to the community, the level of compensation needed must be determined on the basis of an analysis of the costs, which a typical undertaking, well run and adequately provided within the same sector would incur, taking into account the receipts and a reasonable profit from discharging the obligations.'

Where these four criteria are met, public service compensation does not constitute State aid and Article 87(1) and 88 of the Treaty do not apply.

In its decision of 22 November 2006, the Commission has considered that PI, the recipient undertaking, has had public service obligations to discharge and these obligations have been clearly defined. The parameters on the basis of which the compensation is calculated have been established in advance in an objective and transparent manner, notably by means of conventions between CDP and PI.

The Commission has therefore had to check whether the compensation has not exceeded what is necessary to cover all or part of the costs incurred in the discharge of the public services obligation, taking into account the relevant receipts and a reasonable profit, while (in the absence of a public procurement procedure) the level of compensation needed must be determined on the basis of an analysis of the costs, which a typical undertaking, well run and adequately provided within the same sector would incur, taking into account the receipts and a reasonable profit from discharging the obligations.

Definition of a market reference

A study aiming at identifying market remuneration fees for the distribution of postal savings books has been assessed by the Commission.

The methodology of the study develops six successive steps:

i) the identification of the main characteristics of the postal product,

ii) the identification of a comparable financial instrument for the postal product,

iii) the definition of a reference sample,

iv) the identification of the economic component to be compared,

v) the research of the remuneration rate, and

vi) the comparison of the remuneration rate with the rate paid to PI by CDP.

The Commission has considered that the methodology of the study, aiming at identifying for CDP and PI market remunerations for the distribution of postal savings books, is appropriate.

Regarding the definition of the comparative product used in the study, the banks savings books, only one difference with the postal savings books has been identified: the guarantee offered to subscribers, as postal savings books enjoy a State guarantee while banking saving books benefit from a guarantee provided by means of a dedicated fund with a ceiling of 103 291 euros. Referring notably the height of the ceiling, the Commission has considered that the difference between both products is not material for subscribers. Consequently, after having compared the characteristics of both savings books, the Commission has concluded that banks savings books are a financial instrument comparable to postal saving books.

As detailed information for estimating the costs of distributing the similar financial products, i.e. bank savings books, could not be gathered, a proxy has to be used. It has been considered that the rate spread, i.e. the difference between borrower and lender rates ([6]), is an appropriate proxy for assessing the distribution costs of bank savings books, considering that the organization CDP/PI could be regarded as similar for this purpose to the organization of a bank headquarter (producing the investment/savings vehicles) and its subsidiary managing the retail network, in charge of distributing the products.

([6]) Using the Euribor-6 months, or similar, as lender rate is cautious, notably when referring to the liquidity risk linked to postal savings books.

Comparison of the remuneration with market rates

The fee rates paid to PI for the distribution of postal savings books and the historical rate spreads have been the following: [7]

(%)	Historical rate spreads (7)	Distribution fee rates
2000	1.90	1.40
2001	1.59	0.92
2002	1.36	1.08
2003	1.10	0.89
2004	1.10	0.95
2005	1.25	0.89

The rate spreads applicable to banks savings books have been higher than the fee rates paid to PI for the distribution of postal savings books. Therefore, the fees paid to PI are market-conform.

The market fee identified above is an appropriate estimate of the level of the costs, which a typical undertaking, well run and adequately provided within the same sector would incur, taking into account the receipts and a reasonable profit from discharging the obligations.

Conclusion

Since the implementation of the service of general economic interest in 2004, the four Altmark criteria have been fulfilled. The Commission has therefore concluded that yearly remunerations paid to PI on postal savings books in 2004 and 2005 are not State aid.

Moreover, before the entrustment of the service of general economic interest, the yearly remunerations paid to PI on postal savings books were also market conform. As there was no advantage granted to PI, the remunerations were not State aids.

(7) The table represents the lowest of the spread values communicated by the Italian government, using various sources.

Utilisation d'avances remboursables pour aider la R&D: mise en ligne du régime belge en faveur du secteur aéronautique [1]

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Le 6 décembre 2006, la Commission européenne a exigé que le régime belge d'aide pour la recherche et le développement dans le secteur aéronautique soit mis en ligne avec les règles du traité CE sur les aides d'Etat. Ce régime, représentant un budget total de 82,581 millions d'euros, avait été illégalement mis en œuvre entre 2002 et 2006. Conformément à la demande de la Commission, la Belgique a modifié toutes les conventions attribuant les aides incriminées.

Contexte

La Belgique a notifié le 13 février 2004 un régime d'aide à la R&D dans le secteur aéronautique en même temps qu'une aide individuelle en faveur de la société Techspace Aero. Cette dernière constituait un cas d'application de grand montant du régime nécessitant une notification individuelle. En effet, le point 4.7 de l'encadrement communautaire des aides d'Etat à la recherche et au développement de 1996 [2] (ci-après «l'encadrement R&D») alors en vigueur, prévoyait que tout projet individuel de recherche dépassant un coût de 25 millions d'euros et bénéficiant d'une aide dépassant l'équivalent-subvention brut de 5 millions d'euros, soit préalablement notifié à la Commission. L'aide à Techspace Aero d'un montant de 41,274 millions d'euros pour un projet de […] [3] d'euros entrait effectivement dans cette catégorie.

Le régime en objet a été mis en place suite à une décision du Conseil des Ministres belge du 1er décembre 2000. Les aides ont été octroyées par l'Etat fédéral selon un accord conclu le 20 novembre 2001 entre l'Etat et les Régions, sur la base de la loi budgétaire de 2001 [4]. Dans le cadre de ce régime, des avances ont été attribuées à dix bénéficiaires entre 2002 et 2006. L'aide à Techspace Aero a été accordée en 2003. L'Etat belge a soutenu des activités de recherche industrielle (RI) et de développement préconcurrentiel (DPC) au sens de l'annexe I de l'encadrement R&D. Les coûts admissibles répondaient aux définitions de l'annexe II de l'encadrement R&D. L'effet incitatif des aides était vérifié par les autorités belges: tout projet éligible devait comporter un degré de risque technique et/ou financier qui empêchait son financement complet par le bénéficiaire.

Les aides ont pris la forme d'avances dont les remboursements à l'Etat étaient indexés sur le chiffre d'affaires généré par la commercialisation des produits développés dans le cadre des projets de R&D. Le montant maximal des avances atteignait 75% des coûts de RI (base de 60%, majorée d'éventuelles bonifications mais ne pouvant jamais excéder 75%) et 50% des coûts de DPC (base de 40%, majorée d'éventuelles bonifications mais ne pouvant jamais excéder 50%). Ce type d'avances remboursables uniquement en cas de succès, est classique dans le secteur aéronautique. Cet instrument se caractérise par une intensité d'aide plus élevée que celle classiquement autorisée pour des subventions. Cette intensité supérieure est la contrepartie de l'obligation pour les bénéficiaires de rembourser les avances reçues si le projet de R&D débouche sur un succès commercial (le succès commercial du projet étant atteint si les ventes prévues au moment de l'octroi de l'aide sont effectivement réalisées).

Analyse de la Commission

En premier lieu, la mesure remplit les critères cumulatifs constitutifs d'une aide d'Etat au sens de l'article 87, paragraphe 1, du traité CE. Les avances, financées par les fonds de l'Etat fédéral belge, sont remboursées uniquement en cas de succès commercial du produit faisant l'objet de la recherche. Cela constitue un avantage par rapport à des prêts selon des conditions de marché. La mesure confère cet avantage à des entreprises du secteur aéronautique implantées en Belgique, ces entreprises ayant des concurrents dans d'autres Etats membres. Aussi, le régime est susceptible de fausser la concurrence et d'affecter les échanges entre les Etats membres.

En deuxième lieu, en contradiction avec l'article 88, paragraphe 3, du traité CE, la mesure a été mise en œuvre avant son autorisation par la Commission. Elle est donc considérée comme illégale au sens de l'article premier, points b) et f), du

(1) Le contenu du présent article ne reflète pas nécessairement la position officielle des Communautés européennes. Les informations et les opinions qui y sont exposées n'engagent que leurs auteurs.
(2) JO C 45 du 17.2.1996, p. 5.
(3) Secret d'affaires.
(4) Loi concernant le premier ajustement du budget général des dépenses de l'année budgétaire 2001 — Loi du 27.7.2001, Moniteur belge du 14.5.2002.

règlement (CE) n° 659/1999 du Conseil du 22 mars 1999 portant modalités d'application de l'article 93 du traité CE ([5]). Les aides individuelles attribuées dans le cadre du régime ont fait l'objet de conventions entre l'Etat et les entreprises bénéficiaires. Ces conventions ne prévoyaient pas de clause suspensive relative à l'analyse par la Commission au titre des règles communautaires concernant les aides d'Etat.

En troisième lieu, la Commission a émis des doutes sur la compatibilité des modalités de remboursement des avances attribuées dans le cadre de ce régime.

Le point 5.6 de l'encadrement R&D prévoit la possibilité de ce type d'avances remboursables uniquement en cas de succès. L'encadrement indique tout d'abord que l'intensité de l'aide acceptable, en équivalent-subvention brut, est celle fixée par l'encadrement pour les divers stades de recherche. L'encadrement ajoute ensuite qu'en cas d'échec de la recherche en cause, la Commission, conformément à sa pratique décisionnelle, pourra accepter une intensité d'aide plus élevée étant donné que l'échec du projet réduit le risque de distorsion de la concurrence et des échanges. L'encadrement précise enfin que les modalités précises du remboursement seront appréciées par la Commission au cas par cas.

Plusieurs aides sous forme d'avances remboursables en cas de succès ont été notifiées à la Commission depuis l'entrée en vigueur de l'encadrement R&D ([6]). A cette occasion, la Commission a développé une pratique d'interprétation du point 5.6 de l'encadrement. Dans les cas analysés à ce jour par la Commission, les modalités de remboursement des avances prévoyaient, en cas de succès du programme, le remboursement non seulement du principal de l'avance, mais aussi d'intérêts, calculés en application du taux de référence et d'actualisation prévu par la Commission pour l'Etat membre concerné au moment de l'octroi de l'aide ([7]). Le remboursement était même supérieur en cas de succès particulièrement marquant du programme. Dans ces circonstances, la pratique de la Commission a été de limiter l'avance, exprimée comme un pourcentage des coûts éligibles, à un maximum de 60% pour les activités de RI et de 40% pour les activités de DPC, ces taux de base pouvant éventuellement faire l'objet des bonifications prévues au point 5.10 de l'encadrement R&D.

Or, dans le cas du régime en examen, les autorités belges ont appliqué ces taux de 40% et 60% (plus d'éventuelles bonifications en ligne avec le point 5.10 de l'encadrement R&D), alors même que les modalités de remboursement de l'avance ne prévoyaient le versement d'aucun intérêt. Le remboursement ne visait que la récupération de l'avance en cas de succès du programme. Aussi, les modalités de remboursement étaient considérablement plus favorables pour les entreprises belges bénéficiaires du régime que pour leurs partenaires et concurrents, bénéficiaires des aides examinées jusqu'à ce jour par la Commission. En effet, l'absence de remboursement d'intérêts conduit à la certitude de bénéficier d'un élément d'aide dans tous les cas, alors que, selon des modalités de remboursement classiques, cet élément d'aide peut être complètement absent en cas de succès (et peut même devenir négatif en cas de grand succès, l'entreprise faisant gagner de l'argent à l'Etat).

Adaptation de la mesure

La Commission a décidé le 22 juin 2006 d'ouvrir la procédure prévue à l'article 88, paragraphe 2, du traité CE à l'encontre du régime et de l'aide individuelle à Techspace Aero. Lors de cette procédure, la Commission n'a reçu d'une part aucune observation des parties intéressées. La Belgique a accepté d'autre part de modifier chaque aide attribuée selon une des deux alternatives suivantes.

La première alternative consiste à récupérer une partie de l'aide attribuée afin de ramener son intensité au niveau de celle prévue par l'encadrement R&D pour une subvention (50% pour les activités de RI et 25% pour les activités de DPC, majorée d'éventuelles bonifications). Les autorités belges recouvrent la partie excédentaire de l'aide au plus tard le 31 mars 2007 en appliquant un taux d'intérêt égal au taux de référence et d'actualisation de la Commission en vigueur au moment de l'octroi de l'aide. Cette modification supprime l'avantage indu concédé initialement aux bénéficiaires.

En plus de ce recouvrement, les autorités belges demandent en cas de succès du projet, le remboursement sans intérêt de la part de l'aide conservée par l'entreprise. Cette condition va au-delà des exigences de l'encadrement R&D. Les aides ainsi adaptées deviennent donc compatibles avec cet encadrement. L'aide à Techspace Aero est revue ainsi, ce qui implique une récupération avec intérêts de 8,397 millions d'euros pour réduire l'avance finalement attribuée à Techspace Aero à 31,979 millions d'euros.

([5]) JO L 83 du 27.3.1999, p. 1.

([6]) Voir par exemple le cas N 234/01 (France — Aide à la R&D à la société SNECMA — JO C133 du 5.6.2002, p. 10) et le cas N 120/01 (Royaume-Uni — Aide à la société Rolls-Royce pour les projets TRENT 600 et 900 — JO C 67 du 16.3.2002, p. 33).

([7]) Communication de la Commission concernant la méthode de fixation des taux de référence et d'actualisation — JO C 273 du 9.9.1997, p. 3.

La deuxième alternative maintient l'avance remboursable uniquement en cas de succès, et aligne son remboursement sur la pratique de la Commission. La Commission a été vigilante sur les modalités de remboursement finalement retenues par les autorités belges. La Commission a exigé que les conditions suivantes soient satisfaites:

- Lorsque le succès est atteint, le nominal et les intérêts calculés sur la base du taux de référence et d'actualisation de la Commission en vigueur au moment de l'octroi de l'aide, sont récupérés.
- Le remboursement doit être progressif afin de ne pas favoriser un abandon prématuré de la commercialisation des produits issus du programme.
- Le succès commercial des projets est défini sur la base des ventes prévisibles au moment de l'octroi de l'aide. Si le succès n'est pas établi sur la base d'une hypothèse prudente et raisonnable mais que sa définition est trop optimiste, le bénéficiaire aura peu de chance d'atteindre le succès. L'avance ne sera alors vraisemblablement pas remboursée dans sa totalité et le bénéficiaire conservera quasi systématiquement un avantage.
- L'ensemble des ventes réalisées (y compris celles qui n'étaient pas prévues dans le cadre du programme d'aide) est pris en compte pour le remboursement de l'avance car l'impact de l'aide sur la concurrence au sein du marché affecté demeure, quelle que soit la destination des produits vendus.

La Belgique a proposé plusieurs modalités de remboursement répondant à ces critères. Le remboursement lié à chaque vente peut être fixe ou variable. Dans ce deuxième cas, le paiement peut varier selon les critères suivants:

- Les paiements peuvent inclure une part variable calculée au fil des ventes, qui couvre les intérêts correspondant au principal de l'avance restant dû.
- Les paiements peuvent être déclenchés par paliers. La Commission a exigé que dans le cas où le programme s'interrompt avant le succès, le bénéficiaire effectue un ultime paiement au prorata des ventes réalisées depuis le dernier palier atteint.
- Les paiements peuvent être exponentiels, leur montant augmentant au fil de phases successives de remboursement.

Les modifications proposées par la Belgique ont levé les doutes qui ont conduit la Commission à ouvrir la procédure. A ce titre, le régime et l'aide à Techspace Aero peuvent finalement bénéficier de la dérogation prévue par l'article 87, paragraphe 3, sous c), du traité CE. Dans sa décision finale du 6 décembre 2006 sur le régime, la Commission a soumis son approbation à la condition que la Belgique modifie la mesure comme elle s'y est engagée. La Belgique a effectivement réalisé ces adaptations avant le 31 décembre 2006, comme elle l'avait annoncé.

Codification de la pratique communautaire

Le point 5.1.5 du nouvel encadrement communautaire des aides d'Etat à la R&D et à l'Innovation [8], adopté par la Commission le 22 novembre 2006 et applicable depuis le 1er janvier 2007, codifie la pratique de la Commission en termes d'aides au projet de R&D prenant la forme d'avances remboursables uniquement en cas de succès du projet.

Le nouvel encadrement offre tout d'abord la possibilité aux États membres de notifier une méthodologie de calcul de l'équivalent-subvention brut d'une telle aide, cet équivalent-subvention brut devant respecter les intensités maximales prévues pour les subventions.

Le nouvel encadrement indique ensuite qu'à défaut, l'intensité de l'avance, exprimée comme un pourcentage des coûts éligibles, peut atteindre au maximum 60% des coûts admissibles pour la recherche industrielle et 40% pour le développement expérimental [9], à quoi peuvent s'ajouter des primes, sous les conditions suivantes:

- L'issue favorable des activités de recherche doit être définie clairement, de manière prudente et raisonnable.
- En cas d'issue favorable du projet, l'avance est remboursée à un taux d'intérêt au moins égal au taux de référence et d'actualisation de la Commission.
- Dans l'hypothèse d'une réussite allant au-delà de l'issue favorable définie précédemment, l'État membre doit pouvoir continuer d'exiger des versements au-delà du remboursement du montant de l'avance et des intérêts.
- En cas d'échec du projet, l'avance ne doit pas être intégralement remboursée. En cas de succès partiel, la Commission demandera généralement que le remboursement soit proportionnel au degré de réussite du projet.

(8) JO C 23 du 30.12.2006, p. 1.
(9) Remplace et élargit le développement préconcurrentiel dans le nouvel encadrement.

Clarification of the procedure for terminating rescue aid where the presentation of a restructuring plan does not justify the prolongation — comment on the decisions in case of rescue aid to CIT and Ottana (1)

Max LIENEMEYER, Directorate-General for Competition, unit G-2

Introduction

In 2004 the Commission issued new 'Community Guidelines for rescuing and restructuring firms in difficulty' (hereinafter 'the guidelines') (2), which tightened the rules for rescue aid.

Rescue aid is per definition a short time liquidity support (in the form of a guarantee or a loan) until the company has drawn up a restructuring or liquidation plan. It offers, similar to interim measures, a respite to keep a company in business for a limited period. This period is limited to six months. Different to what was laid down in the old guidelines, no extra time is granted to terminate the rescue aid (i.e. reimburse the loan, this was formerly 12 months (3)). In fact, point 25 of the guidelines stipulates that the Member State must provide an undertaking that the aid is terminated after six months or in case of an illegal rescue aid that it must be terminated six months after the disbursement of the first instalment to the firm.

Point 27 of the guidelines lays down a mechanism to strictly enforce this rule. It obliges the Commission in case the aid is not terminated to open a formal investigation immediately. The only exception to this rule is laid down in point 26 of the guidelines, which envisages that such follow up can only be avoided in case a restructuring plan (or a liquidation plan) is presented "unless the Commission decides that such an extension is not justified".

In a decision of 26 September 2006, concerning rescue aid provided by Italy to Compagnia Italiana Turismo S.p.A (hereinafter referred to as "*CIT*"), the Commission applied the rule in point 26 of the guidelines for the first time. It thereby amended a first decision of 7 July 2006 and reiterated that it will not accept any misuse of the prolongation of a rescue aid by presenting a restructuring project without substance. In another decision of 12 December 2006, concerning another rescue aid provided by Italy in favour of *Ottana Energia,* the Commission followed the same approach.

Compatibility of the rescue aid for six months — the first CIT decision

In 2005, Italy has established by so called *decreto competitivita* (Decree no 35 of 14/3/2005) a fund for providing rescue aid guarantees, which were granted to six companies, which have all been notified to the Commission after the aid had been granted and disbursed.

In February 2006, Italy notified to the Commission a rescue aid guarantee for loans amounting to € 75 million in favour of *CIT,* an Italian tourism operator. The company was in serious difficulty. A first loan of € 10 million of the aid was paid out already on 19 January. The guarantee was limited to six months and accompanied by an undertaking to terminate it six months after disbursement. Moreover, the aid amount could be considered as the minimum necessary to keep the firm in business for six months, as the cash flow needs for the preceding year remained below the results obtained by applying the formula set out in Annex I of the guidelines.

Therefore, the rescue aid fulfilled all criteria laid down in point 25 of the guidelines, so that on 7 July 2006, the Commission raised no objection against the rescue aid of € 75 million in favour of *CIT* for the period from 19 January until 19 July 2006 (4).

No Prolongation beyond six months — the second CIT decision

On 20 July 2006, Italy notified a restructuring project to the Commission. However instead of submitting a restructuring plan Italy informed in the notification that a restructuring plan will only be presented in December 2006.

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and views expressed lies entirely with the authors.

(2) Community Guidelines on State aid for rescuing and restructuring firms in difficulty, OJ 2004 C 244, page 2. In case points are cited without further reference they refer to these guidelines.

(3) Cf. Commission Decision in Case C29/2002 *Bull,* OJ 2003 L 209, page 1; and Commission Decision in Case NN37/2004 *Lloyd Werft* of 8.9.2004.

(4) Case NN 16/06, Commission decision of 7 July 2006, OJ C 244 page 14 of 11.10. 2006.

The Commission indicated in a second decision that the period of six months for the rescue aid has expired on 19 July 2006 and that Italy did not terminate the guarantee but notified on 20 July 2006 a restructuring project.

This gave the Commission the opportunity to outline its understanding of point 26 of the guidelines: It first noted that point 26 spells out the principle that in such case, where the Commission receives a restructuring plan within six months after the granting or disbursement of a rescue aid, this aid is presumed to be prolonged on the basis of the rescue aid decision until a decision on the restructuring plan is reached.

Second, the Commission made clear that this presumption may be rebutted if the prolongation is not justified according to point 26 at the end. This rebuttal is required even if a restructuring plan is not credible and sustainable, as point 26 does not, contrary to point 27, limit the presumption to such a case. The aim of such a decision is to terminate the rescue aid. However, as the presumption of point 26 provides expectations, the rescue aid would remain legal until the rebuttal takes effect. Thus, the decision should only have effect *ex nunc*. If the Member State does thereafter not terminate the rescue aid in due course there is ground for initiating proceedings under Article 88(2) of the Treaty for the misuse of aid under point 27.

Third, the Commission clarified that such decision would not require a formal investigation procedure. In fact, point 26 does, contrary to point 27, not require an opening of the procedure. Indeed, as the rebuttal of the presumption must be taken rather swiftly, only a simply Commission decision can serve this purpose.

The Commission applied this rationale to the case at hand and explained that it considers that documents submitted by Italy do not qualify as a restructuring plan because they do not allow the Commission to perform a serious assessment provided for in points 35 to 37 of the restructuring guidelines and to conclude that the aid proposed will restore long-term viability. For this reasons it could have even been argued that the rescue aid was never prolonged. Nevertheless, the Commission considered, for reasons of legal certainty, to adopt a decision pursuant to point 26 and to terminate any possible presumption of prolongation. Therefore, the Commission held that the rescue aid period in the present case cannot, unlike what was originally stated in the decision, be prolonged and the decision must be amended in that respect.

With the decision the Commission provides further clarification that a decision under point 26 is to be distinguished from a procedure as stipulated in point 27. Only if Italy does not adhere to the amended decision and does not terminate the guarantee, a procedure under point 27 would be the next step.

Notwithstanding this, the Commission did not exclude that it could have opened directly proceedings under point 27 given that Italy failed to provide a substantive restructuring project. This could have spared the Commission to go through the additional 26 decision making procedure. However, it was believed that in this case a decision was needed to set aside the legal presumption created in point 26 which, in particular in the absence of an established practice, could have been able to create legitimate expectations. Moreover, a decision under point 26 was also considered more effective, as even if such decision might also, implicitly or explicitly, be taken within the point 27 procedure, it would take until the final decision to rebut the presumption.

The present case, where Italy indeed terminated the guarantee after the second decision was taken, illustrates that it is not in every case necessary that a procedure under point 27 must follow the procedure to terminate the rescue aid. Only, if the Italian authorities were not to terminate the guarantee the aid should then be considered as illegal. If the rescue aid is followed by a restructuring project, the illegal rescue might then also be assessed as restructuring aid, and eventually would need to be recovered if the restructuring cannot be justified on its own merits.

Compatibility only for six months — The Ottana decision

In its next decision where the Commission had to assess a rescue aid in favour of Ottana Energia Srl (*Ottana*), a local utility company situated in Sardinia dealing with electricity generation, the Commission followed the rationale of the *CIT* decision. The facts of the case are very similar. Also here the rescue aid could be held compatible for six months but its prolongation was in view of a too poor restructuring plan not justified.

Moreover, because the Commission had not taken a decision on compatibility within six months it was able to combine the compatibility decision with the decision indicating that no prolongation was justified ([5]).

([5]) Case NN 14/06, Commission decision of 12 December 2006. http://ec.europa.eu/comm/competition/state_aid/register/ii/by_case_nr_nn2006_000.html#14

Conclusion and outlook

The Commission strict approach in not accepting a prolongation of a rescue aid in case of the presentation of a restructuring plan, which is not apt to comply with the conditions set out in the guidelines outlining how viability of the company is to be restored, is justified, by the change of the guidelines which would otherwise remain meaningless. The Commission will soon have further chance to develop its practice on the application of point 27 of the guidelines, as in the *Ottana* case Italy has not terminated the rescue aid [6].

(6) In the meantime the Commission has opened proceedings under point 27. See case C11/27 *Misuse of rescue aid and compatibility of restructuring aid to Ottana,* Commission Decision of 4 April 2007.

Two Dutch cases on State aid and soil rehabilitation (1)

Saskia DIRKZWAGER-DE RIJK, Directorate-General for Competition, unit G-4.

Introduction

In 2002 the Commission approved the Dutch aid scheme N 520/01 the Soil Protection Agreement (2). The basic principles of this covenant are currently incorporated in the "Soil Rehabilitation Decree". At the moment the Soil rehabilitation Decree contains two State aid measures: one subsidy scheme related to the support of non-liable landowners for the rehabilitation of their sites, the other one is a subsidy scheme for situations where the enforcement of the remediation obligation would lead to serious financial difficulties for the involved enterprise. This article describes some of the modifications introduced with the implementation of the covenant into the Soil Rehabilitation Decree and aims to give a brief overview of some developments in aid schemes for soil rehabilitation in the Netherlands.

Background

It is estimated that 15.000 industrial sites in The Netherlands are seriously polluted. According to the Dutch law on soil protection, the obligation for the rehabilitation of these polluted industrial sites rests in principal on the owners of these sites (3), regardless of whether the owner is liable for the pollution of the site.

Regarding the national law applicable on liability, the Dutch Supreme Court ruled in several cases that undertakings could not be held liable if the pollution took place before 1-1-1975, even if they had polluted the sites themselves. The Dutch Supreme Court decided that undertakings that caused the pollution of industrial sites were not able to judge the economic and environmental consequences of that pollution before 1-1-1975. This means that although these enterprises are technically responsible for the pollution, they can not be held liable under Dutch Law for the cost of the rehabilitation of the polluted industrial sites.

This led to the implementation of two aid schemes for the rehabilitation of polluted sites in the Netherlands: the first one is related to the liability for the pollution of the sites and access to subsidy for the rehabilitation, the second one is related to the legal obligation to rehabilitate for the owners of polluted sites. Below a description of the two aid schemes.

Description of the measures

Related to liability for the pollution

The Soil Protection Agreement of June 2001 was a covenant between the national authorities, the provincial executives, the association of Netherlands municipalities, the confederation of Netherlands Industry and Employers and the Royal Association MKB-Nederland (organisation of SME employers). In this covenant the participating parties agreed on a scheme to partly support rehabilitation of Dutch polluted industrial sites, for those cases where no private party can be held liable for the pollution. This covenant was approved as aid scheme N 520/01 the Soil Protection Agreement (4) on 27 February 2002.

Meanwhile the basic principles of the above mentioned covenant are incorporated in the "Soil Rehabilitation Decree" (5) and this State aid scheme was approved with decision N 85/05 (6), Soil rehabilitation of polluted industrial sites.

Some adjustments were also implemented, for example the application of the pro rata temporis principle (7) was introduced. Before the introduction of this principle it had to be established whether the pollution took place before 1-1-1975, in this context the Dutch authorities distinguished two types of cases: obvious and non-obvious cases. In obvious cases it is clear when the industrial site was polluted. In so called non-obvious cases the Dutch authorities have set up criteria to determine what part of the pollution was caused before 1-1-1975 and what part was caused after that date. To this end a so called "age protocol" entered into force on 11 June 2001. This age protocol includes

(1) The content of this article does not necessarily reflect the official position of the European Communities. Responsibility for the information and the view expressed lies entirely with the author.
(2) OJ C 146, 19.06.2002, p. 8.
(3) Artikel 55b Wet bodembescherming, Staatsblad 1986, 374.
(4) An article by Melvin Koenings about this case was published in the Competition Policy Newsletter, no. 2, June 2002 p. 65.
(5) Besluit Financiële bepalingen bodemsanering, Staatsblad 2005, 681.
(6) OJ C 228, 17.09.2005, p. 9.
(7) Liability in proportion to the moment of causing the pollution.

a calculation method which gives as a result the percentage of the pollution caused before 1-1-1975. The aforementioned covenant limited the access to the scheme because enterprises could only apply for a grant if 80% or more of the pollution dated from before 1-1-1975.

The "age protocol" was modified and made it possible to apply for a grant also in cases where less than 80% of the contamination dates from before 1-1-1975. In the approved measure when for example only 79% dates from before 1-1-1975, the grant would be refused. However, in the new measure the aid can only be granted in relation to the part of the pollution caused before 1-1-1975. This is the application of the pro rata temporis principle: liability in proportion to the moment of cause. For example if 78 % of the contamination dates prior to 1-1-1975, the grant will be allowed at the applicable subsidy rate only with respect to 78% of the decontamination costs ([8]).

Other modifications introduced were: the different classes of beneficiaries where simplified, the aid intensities where adjusted and a uniform SME ([9]) bonus was introduced ([10]).

Obligation for the rehabilitation

The other aid scheme is designed for situations when polluted sites have not been rehabilitated because the owner does not have the financial resources to finance the rehabilitation. As described above article 55b of the Soil Protection Act contains an obligation upon the owner of an industrial site to rehabilitate the site, regardless of whether the owner is liable for the pollution on the site. In return, a subsidy is possible in so far as the owner cannot be held liable for the pollution, and provided that the other conditions for the subsidy are fulfilled.

However, the enforcement of the rehabilitation obligation could result in situations where some businesses become insolvent because of disproportionately high rehabilitation costs in relation to a relatively low turnover or cash flow. In such situations no soil rehabilitation will be carried out for quite a long time and in the end the government will have to include the rehabilitation in its own governmental rehabilitation programme.

To avoid such situations, a "Financial Strength Support Instrument (FSSI)" is developed by the Dutch authorities. This instrument can be offered to 'otherwise healthy' businesses who are in the circumstance where — as a result of enforcement of the obligation to rehabilitate — the viability of a business is put in such jeopardy that the continued existence of the business is uncertain. In this context the enterprise may request the competent authority to carry out the rehabilitation against payment of a contribution by the enterprise itself. The owner will pay a contribution to the authority for the execution of the rehabilitation. This so called 'buy-off sum' is determined according to the ability to pay.

In order to determine the payment of an enterprise according to its capability to pay, a financial strength test has been developed. This test intends to serve as an objective examination of the capability to pay for a business owner of polluted ground who is obliged to rehabilitate. The exact amount of the payment (buy-off sum) by an owner to the authority for taking over the execution of the rehabilitation is calculated on the basis of five different steps ([11]).

For establishment of the minimum payment by the authorities point 38 of the Community guidelines on State aid for environmental protection (hereafter the environmental aid guidelines) ([12]) is taken into account and the payment made by the enterprises to the competent authority determined in the different steps must not be lower than the outcome from the calculation of the following formula:

Minimum payment of the company to the competent authority:

= the increase in value
from decontamination of the site concerned
minus 0,15 x the rehabilitation costs

If the payment by the business to the competent authority is determined according to the above described formula, the procedure is as follows. The competent authority carries out the rehabilitation and the business pays the 'buy-off sum'. For determination of the buy-off sum account has already

([8]) For example: An enterprise exists since 1960. The application of the age protocol shows that 78% of the contamination dates prior to 1-1-1975. Assuming that the applicable subsidy rate is 30%, the enterprise gets a grant equal to 78% of 30% (= 23,4%) of the rehabilitation costs.

([9]) OJ L 124, 25.5.2003, p. 36. SMEs are defined in accordance with the Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises, replacing the Recommendation 96/280/EC as from 1 January 2005

([10]) For a detailed description of the modifications see the text of decision N 85/05, see footnote 6.

([11]) For the description of these steps, see point 16 of decision N 501/05.

([12]) OJ C 37, 3.2.2001, p. 3.

been taken of any right to other subsidies for the soil decontamination of operational and permanent industrial sites [13]. The remaining rehabilitation costs are borne by the competent authority.

The maximum gross aid intensity cannot be expressed in amounts [14] or percentages, but it can be expressed in the formula below:

Maximum contribution of competent authority:

= 115% of the decontamination costs minus the increase in value as a result of rehabilitation of the site concerned

The increase in value of the land will be established by means of an independent valuation.

The use of the FSSI is directly linked to the enforcement of the obligation upon the owner or leaseholder of an industrial site under the Soil Protection Act to rehabilitate. One of the conditions for access to the FSSI instrument is that there is a need of rehabilitation of the site in the short term and the authorities have established that there is serious pollution that urgently needs to be rehabilitated.

Where the company is liable under the national liability regime, the support of the government can in no circumstances go above the ceilings of Commission Regulation (EC) No 69/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to de minimis aid [15] (hereafter the de minimis Regulation).

Application of point 38 of the environmental aid guidelines

As regards the rehabilitation of polluted industrial sites, point 38, second paragraph of the environmental aid guidelines states that "where the person responsible for the pollution is clearly identified, that person must finance the rehabilitation in accordance with the 'polluter pays' principle, and no State aid may be given. By 'person responsible for the pollution' is meant the person liable under the law applicable in each Member State, without prejudice to the adoption of Community rules in the matter". This point refers to the polluter pays principle which is a leading principle in European environmental law [16].

Community rules have been adopted in the field of environmental responsibility: "Directive 2004/35/CE of the European Parliament and of the Council of 21 April 2004 on environmental liability with regard to the prevention and remedying of environmental damage [17]". However, according to its Article 17, this directive shall not apply to damage caused by an emission, event or incident that took place before 30 April 2007. Therefore the Commission had, in the two cases, still to rely on the national law.

As described above, the Dutch Supreme Court ruled in several cases that undertakings could not be held liable if the pollution took place before 1-1-1975, even if they had polluted the sites themselves. These judgements should be seen as the national law applicable on liability for the pollution [18].

According to the third paragraph of point 38 of the environmental aid guidelines "where the person responsible for the pollution is not identified or cannot be held liable to bear the cost, the person responsible for the work may receive aid".

Paragraph four of point 38 of the environmental aid guidelines stipulates further that "Aid for the rehabilitation of polluted industrial sites may amount to up to 100% of the eligible costs, plus 15% of the cost of the work. The eligible costs are equal to the cost of the work less the increase in the value of the land."

For the application of the pro rata temporis principle the Commission decided that the fact that now also cases where less than 80% of the pollution is caused before 1-1-1975 can apply for this scheme, will undoubtedly lead to a higher number of beneficiaries. However, the eligible costs remain the same. Only the rehabilitation cost of the part of the pollution caused before 1-1-1975 is taken into account.

As far as the other notified modifications concerned: they were in line with the thresholds of the guidelines [19].

(13) E.g. Decision N 85/05, see footnote no. 6.

(14) This applies to situations where company is not liable. Otherwise the ceiling of the de minimis must be respected.

(15) OJ L 10, 13.01.2001, p.30 and recently adapted; Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of Articles 87 and 88 of the Treaty to de minimis aid, OJ L 379, 28.12.2006, p. 5.

(16) Article 174 (2), EC Treaty.

(17) OJ L 143, 30.4.2004, p. 56.

(18) This approach was also accepted in the decision in the State aid case N 520/01.

(19) For a detailed assessment see decision N 85/05, footnote 6.

With the application of the FSSI the maximum contribution of the authorities falls within the thresholds set by the aforementioned point 38 of the environmental aid guidelines. The possible cumulation with other subsidy schemes is taken into account in the determination of the buy-off sum so that the total amount of State aid always respects the ceilings allowed under the environmental aid guidelines.

As regards the cases where the pollution took place on or after 1-1-1975 and the owner or long term leaseholder is liable under the national liability regime, the financial strength support instrument may only apply under the conditions of the de minimis Regulation. Under these conditions, such support is not considered State aid. Should the support of the government go above the ceilings of the de minimis Regulation then such support would constitute State aid which cannot be approved under the environmental aid guidelines because it is not in line with the polluter pays principle.

Therefore, in both cases the Commission has decided not to raise objections to the notified measures as the State aid could be found compatible with the common market pursuant to Article 87(3)(c) of the EC Treaty, since it respects the conditions laid down in the environmental aid guidelines.

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DIRECTORATE A Policy and Strategic Support	***Emil PAULIS***	02 29 65033
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Deputy Head of Unit	*Céline GAUER*	02 29 63919
2. Merger policy and scrutiny	*Carles ESTEVA MOSSO*	02 29 69721
3. European Competition Network	*Kris DEKEYSER*	02 29 54206
Deputy Head of Unit	*Donncadh WOODS*	02 29 61552
4. International Relations	*Blanca RODRIGUEZ GALINDO*	02 29 52920
DIRECTORATE B Energy, Basic industries, Chemicals and Pharmaceuticals	***Herbert UNGERER***	02 29 68623
1. Energy, Water	*Lars KJOLBYE*	02 29 69417
Deputy Head of Unit	*Dominik SCHNICHELS*	02 29 66937
2. Basic industries, Chemicals and Pharmaceuticals	*Georg DE BRONETT*	02 29 59268
3. Mergers I	*Dan SJOBLOM*	02 29 67964
Deputy Head of Unit	*John GATTI*	02 29 55158
4. Mergers II	*Olivier GUERSENT*	02 29 65414
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1. Telecommunications and post; Information society Coordination	*Michael ALBERS*	02 29 61874
Deputy Head of Unit	*Reinald KRUEGER*	02 29 61555
— Liberalisation directives, Article 86 cases	*Christian HOCEPIED*	02 29 60427/02 29 52514
2. Media	*Arianna VANNINI*	02 29 64209
Deputy Head of Unit	*Gerald MIERSCH*	02 29 96504
3. Information industries, Internet and consumer electronics	*Per HELLSTROEM*	02 29 66935
Deputy Head of Unit	*Nicholas BANASEVIC*	02 29 66569
4. Mergers	...	
Deputy Head of Unit	*Johannes LUEBKING*	02 29 59851

DIRECTORATE D		
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Adviser	*Fin LOMHOLT*	02 29 55619/02 29 57439
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2. Transport	*Linsey Mc CALLUM*	02 29 90122
Deputy Head of Unit	*Maria José BICHO*	02 29 62665
3. Distributive trades & other services	*Zsuzsanna JAMBOR*	02 29 87436
Deputy Head of Unit	*Rüdiger DOHMS*	02 29 55984
4. Mergers	*Joachim LUECKING*	02 29 66545
Deputy Head of Unit	*Helena LARSSON HAUG*	02 29 69338
DIRECTORATE E		
Industry, Consumer goods and Manufacturing	***Paul CSISZAR***	02 29 84669
1. Consumer goods and Foodstuffs	*Yves DEVELLENNES*	02 29 51590/02 29 52814
Deputy Head of Unit	*Andrés FONT GALARZA*	02 29 51948
2. Mechanical and other Manufacturing industries including transportation equipment	*Paolo CESARINI*	02 29 51286/02 29 66495
3. Mergers	*Maria REHBINDER*	02 29 90007
Deputy Head of Unit	*Guillaume LORIOT*	02 29 84988
DIRECTORATE F		
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Deputy Head of Unit	*Tea MÄKELÄ*	02 29 54430
2. Cartels II	*Dirk VAN ERPS*	02 29 66080
3. Cartels III	*Jaroslaw POREJSKI*	02 29 87440
Deputy Head of Unit	*Flavio LAINA*	02 29 69669
4. Cartels IV	*Ewoud SAKKERS*	02 29 66352
Deputy Head of Unit	*Sari SUURNÄKKI*	02 29 91828
DIRECTORATE G		
State aid I: Cohesion and competitiveness	***Humbert DRABBE***	02 29 50060/02 29 52701
1. Regional aid	*Robert HANKIN*	02 29 59773/02 29 68315
Deputy Head of Unit	*Klaus-Otto JUNGINGER-DITTEL*	02 29 60376/02 29 66845
2. Industrial restructuring	*Karl SOUKUP*	02 29 67442
Deputy Head of Unit	*Mehdi HOCINE*	02 29 94646
3. R&D, innovation and risk capital	*Wouter PIEKE*	02 29 59824/02 29 67267
4. Environment and Energy	*Jorma PIHLATIE*	02 29 53607/02 29 69193
Deputy Head of Unit	*Brigitta RENNER-LOCKENZ*	02 29 54569
DIRECTORATE H		
State aid II: Network industries, liberalised sectors and services	***Loretta DORMAL-MARINO***	02 29 58603/02 29 53731
1. Post and others services	*Joaquin FERNANDEZ MARTIN*	02 29 51041
Deputy Head of Unit	*Daniel BOESHERTZ*	02 29 66437
2. Financial services	*Jean-Louis COLSON*	02 29 60995/02 29 62526
3. Telecommunications and Media	*Eric VAN GINDERACHTER*	02 29 54427
Deputy Head of Unit	*Sandro SANTAMATO*	02 29 93447
DIRECTORATE I		
State aid policy and strategic coordination	***Marc VAN HOOF***	02 29 50625
1. State aid policy	*Alain ALEXIS*	02 29 55303
2. Strategic support and decision scrutiny	*Nicola PESARESI*	02 29 92906
3. State aid network and transparency	*Wolfgang MEDERER*	02 29 53584/02 29 65424
4. Enforcement and monitoring	*Dominique VAN DER WEE*	02 29 60216
Deputy Head of Unit	*Anne FORT*	02 29 69182

Reporting directly to the Commissioner		
Hearing officer	*Serge DURANDE*	02 29 57243
Hearing officer	*Karen WILLIAMS*	02 29 65575

New documentation

European Commission Directorate-General Competition

This section contains details of recent speeches or articles on competition policy given by Community officials. Copies of these are available from Competition DG's home page on the World Wide Web at http://ec.europa.eu/competition/speeches/

Speeches by the Commissioner, 1 September 2006 — 31 December 2006

30 November: **Securities markets — the post-trading Code of Conduct and competition** — Neelie KROES — Brussels (City & Financial / ICMA conference)

30 November: **20th anniversary of the UK-France electricity interconnector — introductory remarks** — Neelie KROES — Calais, France (Interconnector France Angleterre (IFA))

16 November: **Competition Policy and Consumers** — Neelie KROES — Brussels (Bureau Européen des Unions de Consommateurs (BEUC))

30 October: **A new energy policy for a new era** — Neelie KROES — Lisbon (Conference on European Energy Strategy — the Geopolitical Challenges)

13 October: **Delivering on the crackdown: recent developments in the European Commission's campaign against cartels** — Neelie KROES — Fiesole, Italy (European Institute)

5 October: **EC antitrust rules: an overview of recent developments** — Neelie KROES — Athens (Hellenic Competition Commission)

28 September: **The need for a renewed European energy policy** — Neelie KROES — London (OFGEM seminar on Powering the Energy Debate: Europe — Competition and Regulation)

25 September: **Market developments and future perspectives in the automotive sector** — Neelie KROES — Brussels (European Council for Motor Trades and Repairs (CECRA))

21 September: **The refined economic approach in state aid law: a policy perspective** — Neelie KROES — Brussels (GCLC/College of Europe)

15 September: **Developments in anti-trust policy in the EU and the US** — Neelie KROES — New York, USA (The Council on Foreign Relations)

14 September: **Industrial policy and competition law & policy** — Neelie KROES — New York City (Fordham University School of Law)

2 September: **Cross-border mergers and energy markets** — Neelie KROES — Cernobbia, Italy (Villa d'Este Forum on "Intelligence 2006 on the world, Europe and Italy")

Speeches and articles, Directorate-General Competition staff, 1 May 2006 — 31 August 2006

15 December: **Delivering the State Aid reform** — Lowri EVANS — Brussels (Concurrence — revue des droits de la concurrence)

13 December: **Opening address to conference "The economic case for professionals services reform"** — Philip LOWE — Brussels (Finnish Presidency Conference)

30 November: **Opening remarks to the Energy Day 2006** — Philip LOWE — Brussels (European Commission)

28 November: **Wettbewerb und europäischer Strom- und Gasmarkt** — Herbert UNGERER — Köln, Germany (Innovation Congress GmbH)

17 November: **State Aid reform: modernising the current framework** — Lowri EVANS — London (King's College & European State Aid Law Institute)

9 November: **The liberalisation of EU Energy Markets** — Philip LOWE — London (The Beesley Lectures, Institute of Economic Affairs)

7 November: **State Aid reform: where do we stand? Status of the State Aid Action Plan** — Lowri EVANS — Brussels (IBC Global Conferences)

31 October: **Energy Competition Policy — Short overview** — Herbert UNGERER — Brussels (Stockholm Network)

14 September: **The burden of proof in Article 82 cases** — Emil PAULIS — New York, USA (Fordham Conference)

11 September: **Remarks on Unilateral Conduct** — Philip LOWE — Washington D.C., USA (Federal Trade Commission and Antitrust Division Hearings on Section 2 of the Sherman Act)

5 September: **International Cooperation between competition agencies: Achievements and challenges** — Philip LOWE — Seoul, Korea (4th Seoul International Competition Forum)

Community Publications on Competition

New publications and publications coming up shortly

- ***Report on Competition policy 2005***
- ***Competition policy newsletter, 2007, Number 2***

Information about our publications as well as PDF versions of them can be found on the DG Competition web site:
http://ec.europa.eu/competition/publications

The annual report is available through the Office for Official Publications of the European Communities or its sales offices. Requests for free publications should be addressed to the representations of the European Commission in the Member states and to the delegations of the European Commission in other countries, or to the Europe Direct network.

All publications can be ordered via the EU bookshop on this address:
http://bookshop.europa.eu/

Press releases
1 September 2006 — 31 December 2006

All texts are available from the Commission's press release database RAPID at: http://europa.eu/rapid/ Enter the reference (e.g. IP/06/14) in the 'reference' input box on the research form to retrieve the text of a press release. Note: Languages available vary for different press releases.

Antitrust

IP/06/1851 — 20/12/2006 — Competition: Commission re-adopts "alloy surcharge" cartel decision and fines ThyssenKrupp Stainless AG €3 168 000

IP/06/1811 — 14/12/2006 — Competition: Commission refers Hungary to Court for failure to abolish restrictions on cable TV services

IP/06/1705 — 07/12/2006 — Competition: Commission adopts revised Leniency Notice to reward companies that report cartels

IP/06/1647 — 29/11/2006 — Competition: Commission fines producers and traders of synthetic rubber €519 million for price fixing cartel

IP/06/1527 — 08/11/2006 — Competition: Commission re-adopts steel beams cartel decision and fines Arcelor €10 million

IP/06/1411 — 17/10/2006 — Competition: Commission takes Sweden to Court for failure to end broadcasting services monopoly

IP/06/1401 — 16/10/2006 — Competition: Commission requests Greece to adopt new framework for broadcasting services

IP/06/1391 — 13/10/2006 — Competition: Commission opens infringement procedure against Malta for maintaining import monopoly for petroleum products

IP/06/1311 — 04/10/2006 — Competition: Commission renders commitments by music publishers and collecting societies legally binding

IP/06/1294 — 02/10/2006 — Competition: Commission revises Block Exemption for IATA passenger tariff conferences

IP/06/1288 — 29/09/2006 — Competition: Commission and other ECN members co-operate in use of leniency to fight cross border cartels

IP/06/1283 — 29/09/2006 — Competition: Commission calls for comments on effects on competition of information exchange in liner shipping markets

IP/06/1249 — 25/09/2006 — Competition: Commission welcomes Council agreement to end exemption for liner shipping conferences

IP/06/1222 — 20/09/2006 — Competition: Commission fines copper fittings producers €314.76 million for price fixing cartel

IP/06/1179 — 13/09/2006 — Competition: Commission fines 14 companies a total of €266.717 million for price fixing of road bitumen in the Netherlands

State aid

IP/06/1874 — 21/12/2006 — State aid: Commission endorses €17.3 million aid to Polish machinery company Huta Stalowa Wola

IP/06/1870 — 21/12/2006 — State aid: Commission concludes that award of third Czech 3G mobile phone licences not an aid

IP/06/1869 — 21/12/2006 — State aid: Commission decides Swedish digital terrestrial platform operator Teracom received no aid

IP/06/1857 — 20/12/2006 — Commission approves aid for anti-pollution filters on heavy duty vehicles

IP/06/1856 — 20/12/2006 — The Commission launches a formal investigation procedure with regard to Germany for presumed State aid payments to the firms Bahnen der Stadt Monheim and Rheinische Bahngesellschaft

IP/06/1852 — 20/12/2006 — State aid: Commission concludes that the French tax scheme for "fiscal economic interest groupings" (EIGs) constitutes state aid

IP/06/1850 — 20/12/2006 — State aid: Commission approves €2.03 million investment aid for German shipyard Rolandwerft

IP/06/1849 — 20/12/2006 — State aid: Commission opens formal investigation into sale of Bank Burgenland to Grazer Wechselseitige in Austria

IP/06/1848 — 20/12/2006 — State aid: Commission endorses specific economic and fiscal regimes in Canary Islands worth €7.135 million for period 2007-2013

IP/06/1847 — 20/12/2006 — State aid: Commission authorises under conditions restructuring aid to Polish car manufacturer FSO

IP/06/1846 — 20/12/2006 — State aid: Commission opens in-depth inquiry into proposed restructuring aid to Bison-Bial in Poland

IP/06/1845 — 20/12/2006 — State aid: Commission endorses €76 million aid to Conergy for production plant of solar energy modules in Frankfurt (Oder), Germany

IP/06/1765 — 12/12/2006 — State aid: Commission adopts new de minimis Regulation, exempting aid notification below €200 000

IP/06/1755 — 12/12/2006 — Commission authorises increase in Dutch aid for the European Train Control System

IP/06/1719 — 11/12/2006 — State aid: latest Scoreboard reveals continuing shift towards horizontal objectives

IP/06/1707 — 07/12/2006 — State aid: Commission authorises aid scheme by French Agence de l'innovation industrielle for BioHub R&D programme

IP/06/1706 — 07/12/2006 — State aid: Commission opens investigation into restructuring aid to Polish company Odlewnia Zeliwa ŚREM

IP/06/1704 — 07/12/2006 — State aid: Commission authorises German regional investment aid scheme 'Investitionszulagengesetz 2007'

IP/06/1696 — 06/12/2006 — State aid: Commission approves €4.2 million investment aid to German shipyard Volkswerft Stralsund

IP/06/1695 — 06/12/2006 — State aid: Commission launches probe for possible misuse of restructuring aid to Polish steel company Arcelor Huta Warszawa

IP/06/1694 — 06/12/2006 — State aid: Commission asks Belgium to amend its aid scheme for R&D in the aeronautical sector

IP/06/1617 — 23/11/2006 — State aid: Commission endorses public service compensation for Swedish Posten AB

IP/06/1611 — 22/11/2006 — State aid: Commission approves revised UK film tax incentive scheme

IP/06/1606 — 22/11/2006 — Commission allows Malta to aid the creation of new air routes

IP/06/1605 — 22/11/2006 — State aid: 'Poste Italiane' — Commission endorses remuneration for distribution of postal savings books; opens investigation into distribution of postal bonds

IP/06/1603 — 22/11/2006 — State aid: Commission opens investigation into financial support to DHL and Leipzig/Halle airport

IP/06/1602 — 22/11/2006 — State aid: Commission opens investigation into a French tax credit scheme for video game creation

IP/06/1601 — 22/11/2006 — State aid: Commission opens investigation into 2006 state guarantee for BAWAG-PSK

IP/06/1600 — 22/11/2006 — State aid: Commission adopts new state aid Framework for Research, Development and Innovation

IP/06/1532 — 09/11/2006 — State aid: Commission concludes Czech steel producer Třinecké železárny received no illegal aid

IP/06/1528 — 08/11/2006 — State aid: Commission approves regional aid map 2007-2013 for Germany

IP/06/1525 — 08/11/2006 — State aid: Commission investigates proposed new Swedish CO2 tax reductions

IP/06/1471 — 25/10/2006 — State aid: Commission refers France to Court of Justice for failure to recover illegal aid

IP/06/1461 — 24/10/2006 — Commission authorises two aid measures for Air Caraïbes to improve regional services

IP/06/1456 — 24/10/2006 — State aid: Commission opens inquiry into France's guarantee to Finnish electricity producer TVO

IP/06/1453 — 24/10/2006 — State aid: Commission simplifies procedures for approving regional aid with new block exemption Regulation

IP/06/1452 — 24/10/2006 — State aid: Commission prolongs specific state aid rules for shipbuilding

IP/06/1451 — 24/10/2006 — State aid: Commission approves regional aid maps 2007-2013 for the Czech Republic, Ireland and Lithuania

IP/06/1449 — 24/10/2006 — European Commission authorises rescue aid for Polish company C. Hartwig

IP/06/1412 — 17/10/2006 — State aid: Commission to propose to the Council simplification of exemption procedures for certain types of state aid

IP/06/1393 — 13/10/2006 — State aid: Commission approves regional aid maps 2007-2013 for Luxembourg and Malta

IP/06/1392 — 13/10/2006 — State aid: Commission endorses Dutch state guarantees scheme worth up to €900 million for equity financing and loans to SMEs

IP/06/1388 — 13/10/2006 — Commission approves Belgian aid scheme for inland waterway transport

IP/06/1387 — 13/10/2006 — Commission approves a prolongation of UK aid encouraging movement of intermodal containers by rail

IP/06/1386 — 13/10/2006 — Commission approves Slovak aid scheme for combined transport

IP/06/1365 — 12/10/2006 — State aid: Commission endorses support of up to €45 million for Bavarian ethylene pipeline

IP/06/1363 — 12/10/2006 — State aid: Commission concludes BT and Kingston have received no aid through UK property tax

IP/06/1361 — 12/10/2006 — State aid: Commission opens an investigation into the proposed reform of the French Post Office workers' pension fund

IP/06/1305 — 04/10/2006 — State aid: Commission recommends that France withdraw the unlimited state guarantee for the French Post Office

IP/06/1274 — 28/09/2006 — State aid: Commission investigates proposed new Danish CO2 tax reductions

IP/06/1261 — 26/09/2006 — Commission authorises Czech state aid for research and development in transport

IP/06/1260 — 26/09/2006 — Green light for Czech state aid to compensate inland waterway transport operators

IP/06/1256 — 26/09/2006 — State aid: 'Poste Italiane' — Commission endorses €2.4 billion public service compensation for 2000-2005; opens investigation into interest rates for funds collected as of 2005

IP/06/1220 — 20/09/2006 — State aid: Commission presents for consultation new draft rules on de minimis subsidies

IP/06/1191 — 14/09/2006 — State aid: Commission endorses French public funding of €100 million for Eurocopter R&D project for new Franco-Chinese helicopter

IP/06/1189 — 13/09/2006 — Commission authorises Slovak state aid to the Hornonitrianske Bane Prievidza a.s. mining company

IP/06/1188 — 13/09/2006 — Green light for Slovak state aid to the Bana Dolina mining company

IP/06/1185 — 13/09/2006 — European Commission approves Austrian aid scheme for combined transport

IP/06/1183 — 13/09/2006 — Aid for restructuring SNCM: Commission extends investigation procedure

IP/06/1180 — 13/09/2006 — Commission approves changes to social aid for Martinique

IP/06/1176 — 13/09/2006 — State aid: Commission approves regional aid maps 2007-2013 for a first group of Member States

Merger

IP/06/1904 —22/12/2006 — Mergers: Commission opens in-depth investigation into proposed take-over of SIG by financial investment groups CVC and Ferd

IP/06/1894 —22/12/2006 — Mergers: Commission approves proposed acquisition of Münchsmünster Cracker and associated assets by Basell

IP/06/1893 —22/12/2006 — Mergers: Commission clears proposed acquisition of Corus by Tata Steel

IP/06/1868 —20/12/2006 — Mergers: Commission approves proposed acquisition of Scania by MAN

IP/06/1867 —20/12/2006 — Mergers: Commission opens in-depth investigation into Ryanair's take-over of Aer Lingus

IP/06/1865 —20/12/2006 — Mergers: Commission approves proposed acquisition of Huntsman Petrochemicals (UK) by Sabic

IP/06/1864 —20/12/2006 — Mergers: Commission approves proposed acquisition of KION by KKR and GOLDMAN SACHS

IP/06/1863 —20/12/2006 — Mergers: Commission closes inquiry after Thule abandons acquisition of control over Schneeketten

IP/06/1859 —20/12/2006 — Mergers: Commission approves Glatfelter take-over of Crompton's Lydney paper mill

IP/06/1853 —20/12/2006 — Mergers: Commission decides that Spanish measures in proposed E.ON/Endesa takeover violate EC law

IP/06/1819 —15/12/2006 — Mergers: Commission approves proposed acquisition of Berliner Bank by Deutsche Bank

IP/06/1803 —13/12/2006 — Mergers: Commission approves proposed acquisition of Altana Pharma by Nycomed

IP/06/1762 —12/12/2006 — Mergers: Commission approves acquisition of Aker Kvaerner's pulp machine business by Metso, subject to conditions

IP/06/1726 —11/12/2006 — Mergers: Commission approves proposed acquisition of Pfizer's consumer healthcare business by Johnson & Johnson, subject to conditions

IP/06/1717 —08/12/2006 — Mergers: Commission approves proposed acquisition of Danka by Ricoh

IP/06/1716 —08/12/2006 — Mergers: Commission opens in-depth investigation into Universal's take over of BMG's music publishing business

IP/06/1710 —08/12/2006 — Mergers: Commission approves proposed acquisition of AOL's UK internet access business by Carphone Warehouse Group

IP/06/1688 —05/12/2006 — Mergers: Commission approves proposed acquisition of BST by WLR

IP/06/1687 —05/12/2006 — Mergers: Commission clears proposed joint venture between Fiat Group and Crédit Agricole

IP/06/1674 —04/12/2006 — Mergers: Commission opens in-depth investigation into proposed take-over of automotive starter battery business of the FIAMM group by VB Autobatterie

IP/06/1664—30/11/2006— Mergers: Commission approves proposed acquisition of GE Advanced Materials by the Apollo Group

IP/06/1663 —30/11/2006 — Mergers: Commission approves proposed acquisition of joint control of F Group by DSG International and FR Invest

IP/06/1649 —29/11/2006 — Mergers: Commission informs Spain of preliminary assessment that Spanish Minister's measures in proposed takeover E.ON / Endesa violate EC law

IP/06/1645 —28/11/2006 — Mergers: Commission opens in-depth investigation into acquisition of Alcatel Alenia Space and Telespazio by Thales

IP/06/1644 —28/11/2006 — Mergers: Commission approves proposed acquisition of AOL's German internet access business by Telecom Italia

IP/06/1614 —23/11/2006 — Mergers: Commission approves proposed acquisition of Saurer by Oerlikon

IP/06/1596 —21/11/2006 — Mergers: Commission approves acquisition of Schwarz by UCB

IP/06/1558 —14/11/2006 — Mergers: Commission approves merger of Gaz de France and Suez, subject to conditions

IP/06/1552 —13/11/2006 — Mergers: Commission approves proposed merger between Nokia and Siemens

IP/06/1547 —10/11/2006 — Mergers: Commission approves proposed acquisition of joint control over Oy Ovako AB and Ovako Swenska AB by Hombergh, De Pundert and Pampus Industrie

IP/06/1536 —09/11/2006 — Mergers: Commission clears acquisition of Fisher by Thermo, subject to conditions

IP/06/1520 —07/11/2006 — Mergers: Commission approves proposed acquisition by Thales of Alcatel's rail and systems integration activities

IP/06/1519 —07/11/2006 — Mergers: Commission approves planned acquisition of Intermagnetics by Philips

IP/06/1518 —07/11/2006 — Mergers: Commission approves proposed acquisition of Mazeikiu refinery by PKN Orlen

IP/06/1503 —31/10/2006 — Mergers: Commission clears planned acquisition of Bayer Diagnostics by Siemens

IP/06/1492 —30/10/2006 — Mergers: Commission approves planned acquisition of Inopart by Plastic Omnium

IP/06/1464 —24/10/2006 — Mergers: Commission approves proposed acquisition of Schleipen & Erkens by Mondi

IP/06/1444 —20/10/2006 — Mergers: Commission approves proposed acquisition of Mercury by Hewlett Packard

IP/06/1438 —19/10/2006 — Mergers: Commission approves planned acquisition of Eneco Energia by Edison

IP/06/1426 —18/10/2006 — Mergers: Commission opens infringement procedure against Spain for not lifting unlawful conditions imposed by CNE on E.ON's bid for Endesa

IP/06/1418 —18/10/2006 — Mergers: Commission sends preliminary assessment to Italy on measures to block Abertis-Autostrade merger

IP/06/1339 —09/10/2006 — Mergers: Commission approves proposed acquisition of joint control by Arcelor Profil Luxembourg and SNCFL of newly created CFL Cargo

IP/06/1298 —02/10/2006 — Mergers: Commission approves planned acquisition of O.Y.L by Daikin

IP/06/1292 —29/09/2006 — Mergers: Commission approves proposed acquisition of Banksys and Bank Card Company by Atos Origin

IP/06/1273 —28/09/2006 — Mergers: Commission launches public consultation on consolidated guidance concerning jurisdiction in merger control

IP/06/1246 —22/09/2006 — Mergers: Commission approves proposed acquisition of Cardinal Health by Alliance Boots

IP/06/1245 —22/09/2006 — Mergers: Commission approves proposed acquisition of ALL3Media by Permira

IP/06/1239 —21/09/2006 — Mergers: Commission clears planned acquisition of Cleanaway Holdings Limited by Veolia ES, subject to conditions

IP/06/1228 —20/09/2006 — Mergers: Commission opens in-depth investigation into Glatfelter take-over of Crompton's Lydney paper mill

IP/06/1227 —20/09/2006 — Mergers: Commission approves proposed acquisition of Spectra by Linde

IP/06/1215 —19/09/2006 — Mergers: Commission clears Toshiba's planned acquisition of Westinghouse Electric UK and BNFL USA Group subject to conditions

IP/06/1214 —19/09/2006 — Mergers: Commission approves planned creation of joint venture by Lactalis and Nestlé

IP/06/1212 —19/09/2006 — Mergers: Commission clears proposed acquisition by voestalpine of Profilafroid and Société Automatique de Profilage

IP/06/1174 —12/09/2006 — Financial sector: Commission acts to improve supervisory approval process for mergers and acquisitions

IP/06/1168 —08/09/2006 — Mergers: Commission approves proposed acquisition of ICA Meny by Nordic Capital

IP/06/1157 —07/09/2006 — Mergers: Commission clears proposed acquisition of Foster Yeoman by Aggregate Industries; refers review of UK local aggregates markets to Office of Fair Trading

IP/06/1156 —06/09/2006 — Merger: Commission approves proposed joint acquisition of Casema and Multikabel by Cinven and Warburg Pincus

Cases covered in this issue

Antitrust rules

Mergers

State aid

Competition DG's address on the world wide web:

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