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Legislation

Contents

I Acts whose publication is obligatory

.....

II Acts whose publication is not obligatory

Commission

1999/674/CE:

- ★ **Commission Decision of 3 February 1999 relating to proceedings under Council Regulation (EEC) No 4064/89 (Case No IV/M.1221 — Rewe/Meinl)** [notified under document number C(1999) 228] ⁽¹⁾ 1

1999/675/CE:

- ★ **Commission Decision of 8 July 1999 on the state aid implemented by Germany in favour of Kvaerner Warnow Werft GmbH** [notified under document number C(1999) 2266] ⁽¹⁾ 23

1999/676/CE:

- ★ **Commission Decision of 20 July 1999 concerning presumed aid allegedly granted by France to Sécuripost** [notified under document number C(1999) 2537] ⁽¹⁾ 37

⁽¹⁾ Text with EEA relevance.

II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 3 February 1999

relating to proceedings under Council Regulation (EEC) No 4064/89

(Case No IV/M.1221 — Rewe/Meinl)

[notified under document number C(1999) 228]

(Only the German text is authentic)

(Text with EEA relevance)

(1999/674/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area, and in particular Article 57(2)(a) thereof,

Having regard to Council Regulation (EEC) No 4064/89 of 21 December 1989 on the control of concentrations between undertakings⁽¹⁾, as last amended by Regulation (EC) No 1310/97⁽²⁾, and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 28 September 1998 to initiate proceedings in this case,

Having given the undertakings concerned the opportunity to make known their views on the objections raised by the Commission,

Having regard to the opinion of the Advisory Committee on Concentrations⁽³⁾,

Whereas:

- (1) On 25 August 1998 REWE Internationale Beteiligungsgesellschaft mbH and REWE-Verkaufsgesellschaft mbH, both members of the Rewe group, notified pursuant to Article 4 of Regulation (EEC) No 4064/89 ('the Merger Regulation'), a proposed operation within the meaning of Article 3(1)(b) of that Regulation whereby they were to acquire the entire share capital of Julius Meinl AG.

- (2) On 28 September 1998 the Commission, in accordance with Article 6(1)(c) of the Merger Regulation and Article 57 of the EEA Agreement, decided to initiate proceedings in this case.

- (3) The Advisory Committee discussed the draft of this Decision on 19 January 1999.

I. THE PARTIES

- (4) The Rewe group ('Rewe') forms a uniformly directed group of companies consisting of Rewe-Zentralfinanz eG and Rewe Zentral AG together with their respective direct and indirect subsidiaries. Rewe's activities comprise the acquisition, financing and management of wholesale and retail companies, in particular companies in the food-retailing sector. Most of Rewe's turnover is achieved in Germany. Rewe has been active in Austria since 1996 through its subsidiary BML ('Billa'). Billa operates a food-retailing chain of hypermarkets (Merkur), supermarkets (Billa), smaller self-service outlets (Emma), discount stores (Mondo) and non-dispensing drugstores (Bipa), and is the market leader in food retailing.

- (5) Julius Meinl AG ('Meinl') is a trading group active almost exclusively in Austria, although a few shops are operated in Italy. The overall turnover is achieved mainly through retailing daily consumer goods. Meinl operates hypermarkets (PamPam), supermarkets (Julius Meinl and Meinl Gourmet) and discount stores (Jééé).

⁽¹⁾ OJ L 395, 30.12.1989, p. 1; corrigendum, OJ L 257, 21.9.1990, p. 13.

⁽²⁾ OJ L 180, 9.7.1997, p. 1.

⁽³⁾ OJ C 306, 23.10.1999.

II. THE PROJECT

- (6) Rewe proposes to acquire all the shares in Meinel [...]*. The notified operation encompasses seven Meinel subsidiaries. A total of 341 shops, including supermarkets, discount stores, hypermarkets and a chain of delicatessens, are to be taken over. The business activities and subsidiaries of the Julius Meinel International AG group and Meinel's shops in Italy are not covered by the notified operation.

III. CONCENTRATION

- (7) The operation constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation, in that Rewe is acquiring sole control of Meinel.

IV. COMMUNITY DIMENSION

- (8) The companies concerned have a combined worldwide turnover of more than EUR 5 000 million⁽⁴⁾ (Rewe: EUR [...] million, Meinel: EUR [...] million) and a Community-wide turnover of more than EUR 250 million (Rewe: EUR [...] million, Meinel: EUR [...] million). The parties do not achieve more than two thirds of their Community-wide turnover within one and the same Member State. The operation therefore has a Community dimension and is not a case of cooperation under the EEA Agreement.

V. ASSESSMENT UNDER ARTICLE 2 OF THE MERGER REGULATION

- (9) The proposed operation will have an impact above all on the food-retailing trade in Austria. In accordance with previous Commission decisions⁽⁵⁾, a distinction must in principle be drawn, from the point of view of possible effects on competition, between two separate markets in the food-retailing sector:

(*) Parts of this text have been edited to ensure that confidential information is not disclosed, those parts are enclosed in square brackets and marked with an asterisk.

⁽⁴⁾ The turnovers were calculated in accordance with Article 5(1) of the Merger Control Regulation and with the Commission notice on calculation of turnover (OJ C 66, 2.3.1998, p. 25). Where turnover figures for the period before 1 January 1999 are mentioned, they were calculated on the basis of the average ECU exchange rates and converted into ecus on a one-for-one basis.

⁽⁵⁾ For example IV/M.803 — Rewe/Billa (OJ C 306, 15.10.1996, p. 4); IV/M.1071 — Spar/Pro (OJ C 49, 14.2.1998, p. 13).

- the distribution market, in which food retailers act as suppliers to final consumers,
- the procurement market ('demand market'), in which retailers act as buyers vis-à-vis producers of products forming part of the food-retailing trade's range.

A. DISTRIBUTION MARKET

1. Relevant product market

- (10) There are, within the food-retailing trade, various forms of distribution which differ according to, among other things, the width and depth of the range carried and the size of the sales outlet (such as supermarkets with 5 000 to 10 000 articles, a fresh-food department and a sales area of 400 to 1 000 m², and hypermarkets with a sales area of at least 1 000 m²). Owing to the existing competitive relationships between these different forms of distribution, it will be assumed below, however, as in previous Commission decisions⁽⁶⁾, that there is a separate market in food retailing which embraces all retailers, and in particular supermarkets and hypermarkets, carrying a range of food and non-food products which is typical of the food-retailing trade (excluding, that is, specialised outlets such as butchers and bakers).

- (11) The parties, by contrast, take the view that the relevant product market comprises all sources of supply of foodstuffs accessible to consumers, including all types of local outlet such as, for example, weekly street markets, farmers' markets, butcher's shops, baker's shops, petrol stations, 'bioshops', etc. (specialised trade). They base this view on an analysis by the GfK institute (Gesellschaft für Konsumforschung), of overlap between different forms of distribution for January to October 1998, according to which, although supermarkets, for example, reach out to 97 % of all consumers, 60 % of supermarket customers also go to the butcher's, 75 % to the baker's and 18 % to the greengrocer's. A similar proportion of hypermarket and discount store customers regularly shop at the butcher's, baker's and greengrocer's. Butcher's and baker's shops cater for 60 % and 72 % of all consumers, and of these, 98 % also shop at supermarkets, 78 % at hypermarkets and 85 % at discount stores.

⁽⁶⁾ For example Decision 97/277/EG — Kesko/Tuko (OJ L 110, 26.4.1997, p. 53, paragraphs 18 et seq. of the recitals); Rewe/Billa and Spar/Pro, see footnote 5; IV/M.1303 — Adeg/Edeka, (OJ C 385, 11.12.1998, p. 5).

- (12) The Commission investigations have established, however, that in Austria there are no special features such as might justify departing from the Commission's standard practice. What is more, the market definition used by the Commission was taken as a basis by the parties in their notification of the Rewe/Billa merger.
- (13) As in other Community countries, consumers in Austria expect from the food-retailing trade a specific distribution service, consisting in the supply of a particular range of food and non-food articles. From the Austrian consumer's point of view, also, shopping at specialised outlets such as butcher's and baker's shops is not interchangeable with the broader experience of shopping at a supermarket or other type of food-retailing outlet where he can find all the goods he needs on the spot (one-stop shopping). According to a survey by the GfK (household panel), a total turnover of some ATS 11,7 billion is achieved in the space of a month in perishable consumer goods throughout Austria, only 10 % of which is accounted for by the specialised trade. The specialised trade typically supplies only a particular product or category of product and, in terms of product type, sales area and average price, is not in direct competition with the food-retailing trade in its various guises. Supplies by the specialised trade therefore serve first and foremost to supplement supplies by the food-retailing trade.
- (14) The parties' data do no more than indicate that, besides shopping at a supermarket or other food-retailing outlet, the consumers surveyed also go to butcher's or baker's shops. From the parallel purchasing behaviour as thus measured, it cannot, however, be determined whether consumers go to specialised outlets instead of, or in addition to, food-retailing outlets. The overlap analysis submitted by the parties is not therefore capable of proving that there is any interchangeability between the food-retailing trade and the specialised trade. On the contrary, the figures suggest that specialised outlets are no substitute for food-retailing outlets. This can be seen from the fact that 98 % of the specialised trade's customers also shop at supermarkets, coupled with the fact that supermarkets cover 97 % of all consumers. If specialised outlets were capable of satisfying consumer needs in the same way as food-retailing outlets, then a much smaller number of customers of the specialised trade could be expected to shop additionally at food-retailing outlets.
- (15) Since the parties also wish to include petrol-station shops in the relevant market, it must be pointed out that the size of the sales area of such shops is on average only between 40 m² and 70 m² and that they carry only a limited range centred on beverages and impulse articles. In the case of petrol-station shops, moreover, there is generally a price differential of some 25 to 30 % compared with the food-retailing trade. The consumer is prepared, owing in particular to the more flexible opening hours, to pay higher prices (50 % more for beverages, for instance). Because of the disparate reasons for shopping at petrol stations and at food-retailing outlets, the two distribution channels are not interchangeable in the eyes of the consumer. Since the parties wish to include cash-and-carry stores in the market, it should be pointed out that cash-and-carry stores form a separate marketing stage which mainly provides distribution services to small food-stores, businesses in the service sector, small retail outlets, the hotel and restaurant trade, etc. Access to cash-and-carry stores are limited, moreover, to holders of a special permit (as a rule tradesmen and business people). In past decisions the Commission has accordingly not included cash-and-carry stores in the food-retailing trade's relevant market⁽⁷⁾. The parties have not submitted any arguments which might justify departing from these precedents.
- (16) The results of the Commission's enquiries show that limiting the market to sales outlets which carry the typical range of the food-retailing trade is also appropriate in this case. The competitors who were surveyed all stated that specialised outlets, petrol-station shops and cash-and-carry stores are not in direct competition with food retailers. The market share data for Austria in the statistical yearbook of AC Nielsen are also based on the food-retailing trade market minus the specialised trade, petrol-station shops and cash-and-carry stores. The same goes for the study by Regioplan of the food-retailing trade in Austria.
- (17) The question whether discount stores are to be included in the relevant market in this case for purposes of the competitive assessment of the proposed operation can remain open. The average number of articles stocked by discount stores in Austria is very small compared with supermarkets. And the poorer service and critical lack of branded goods point to there being
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- ⁽⁷⁾ See Footnote 6, Kesko/Tuko, paragraphs 24 et seq. of the recitals.

only a limited competitive relationship⁽⁸⁾. In the last analysis, however, the question can be left undecided, as even if discount stores were included in the relevant market the competitive assessment of the present operation would be the same.

2. Relevant geographic market

(18) The Commission has already considered the question of the definition of the relevant geographic market in the Rewe/Billa decision⁽⁹⁾, where it found that, from the direct viewpoint of the consumer, the geographic markets affected by a concentration in the food-retailing trade are the local markets in which the firms involved run shops. These local markets can be defined as a circle with a radius of approximately 20 minutes by car centred on the individual sales outlet. The Commission has, however, also stated in this connection that an examination limited to such local markets would not reflect the competitive impact of a concentration in the food-retailing trade, at least not where a large number of local markets affected by the concentration are connected in such a way as to overlap and seamlessly cover a larger area or even a whole Member State. It must be borne in mind in particular here that the competitive relationships between major retail chains are not limited to local competition but rather exist in a far wider geographical dimension. This is clear, for example, from the fact that in the case of major retail chains the range of goods carried is to a large extent centrally controlled, and hence at least as far as the basic range is concerned is the same in every local market, and that nationwide advertising is the norm. For the competitive assessment of the Rewe/Billa proposal the Commission, in its decision of that time, proceeded in this respect on the basis that the food-retailing trade in Austria formed an overall market. It found in this connection that a study of local or regional markets was unnecessary, if only because Rewe had not been active in Austria before and hence there could be no question of any additional market share in any conceivable geographic market.

(19) In this case, the Commission's investigations have revealed nothing that might justify a regional market delimitation. The sales outlets both of Rewe/Billa and of Meinl cover the whole inhabitable part of Austria. The same goes for their Austria-wide competitors Spar, ADEG and Löwa. Spar, on the one hand, and Rewe/Billa and Meinl, on the other, have, it is true, historically different regional centres of gravity. While Spar has

a stronger presence in western Austria, Rewe/Billa occupies, as is explained in greater detail in recitals 31 to 36, a strong position in eastern Austria. This fact does not, however, in itself justify creating regional markets for geographic market delimitation purposes. All three firms are present in every Austrian province and hence throughout Austria. The competitors surveyed by the Commission have confirmed, moreover, that in each case they carry an identical or similar core range throughout Austria and that they advertise their products country-wide on national television and in the national press. Furthermore, the Commission has established that prices do not differ appreciably from one part of Austria to another, especially as between western Austria and eastern Austria.

(20) The parties have also submitted that the market is to be delimited nationally and comprises the whole of Austria. For the above reasons, the Commission will now proceed, for purposes of the competitive assessment of the operation, on the premise that the food-retailing market in Austria constitutes an overall market.

3. Competitive assessment

(21) It is to be assumed that the operation will lead to the creation of a dominant position on the part of Rewe/Billa/Meinl in the Austrian food-retailing market.

(a) Competitive assessment

(22) (aa) Rewe/Billa is already the leading supplier in the Austrian food-retailing trade, having strengthened its market position in recent years. Austria is one of the European countries with the highest levels of concentration in the food-retailing trade. The five largest firms together control over 80 % of the market, with the top two alone accounting for nearly 60 %. With the exception of Finland, this is the highest concentration in the EU.

(23) The following firms are active in the Austrian food-retailing market:

Rewe/Billa, a centrally managed chain-store company, has over 1 071 shops across the whole of Austria, including 66 hypermarkets (Merkur), 809 supermarkets (Billa), 28 smaller self-service outlets (Emma) and 168 discount stores (Mondo). Meinl, also a chain-store company, operates 40 hypermarkets (PamPam), 274 supermarkets (Julius Meinl), 20 Meinl Gourmet supermarkets and nine discount stores (Jééé). Meinl currently belongs to the ZEV-Markant purchasing association, but it will leave it after the operation. The Spar group

⁽⁸⁾ IV/M.179 — Spar/Dansk Supermarked (OJ C 29, 6.2.1992, p. 18).

⁽⁹⁾ Rewe/Billa, see footnote 5.

is likewise active throughout Austria, with 1 560 shops, 1 103 of which are, however, operated by independent retailers. The next largest countrywide competitor, ADEG, has a cooperative structure. ADEG has 1 246 shops throughout Austria, very few of which, however, it owns itself. Löwa, a member of the Tengelmänn group, has 285 shops across Austria. The Aldi-owned chain of discount stores, Hofer, is also active throughout Austria with 199 outlets. Apart from these firms, only regionally active competitors (such as M-Preis, Tirol, and Pfeiffer, Linz) are present.

- (24) The Commission's investigations have revealed the following breakdown of market shares in the Austrian food-retailing market, varying according to whether or not discount stores are included in the market:

(%)

Firm	Market share with discount stores	Market share without discount stores
Rewe/Billa	[27 to 33]*	[33 to 38]*
Meinl	[5 to 10]*	[5 to 10]*
Spar	[23 to 28]*	[27 to 32]*
ADEG	[8 to 13]*	[10 to 15]*
Hofer	[< 15]*	
Löwa	[< 10]*	[< 10]*
Others	[< 10]*	[< 10]*

- (25) The market shares worked out by the Commission are based on turnover figures which the Commission has itself ascertained and do not differ much from the data set out in the statistical yearbook of AC Nielsen (for the food-retailing market minus discount stores), a GfK study, a market survey by M+M Eurodata and a study by Regioplan.

- (26) In their notification the parties claim considerably smaller market shares (Rewe/Billa [...]*%, Meinl [...]*%). These market shares are based, however, on the parties' market definition, which the Commission regards as incorrect (see recitals 10 to 17).

- (27) Since the takeover of the Billa group by Rewe in 1996, Billa's market share (including discount stores) has increased from 25 % to approximately 30 % now. This is due to above-average domestic growth (opening of an average of 50 new shops a year, (more than 50) in 1997 alone).

- (28) (bb) As a result of the operation Rewe-Billa will increase its market share yet again by a considerable amount, and in so doing will further widen the gap between it and its

competitors. Rewe/Billa's market share will increase as a result of the operation from approximately [27 to 33]*% (including discount stores) to approximately [32 to 43]*%, or without discount stores from [33 to 38]*% to [38 to 48]*%. The number of shops will increase by one third from 1 071 to 1 414. The total sales area will increase by at least 30 %.

- (29) The closest competitor, Spar, has by contrast an approximately [9 to 15]*% smaller market share. Although after the operation Spar will have all told, a slightly larger sales area than the parties, the turnover per square metre of sales area achieved by Rewe/Billa is a great deal higher than that of the other competitors (see below). Moreover, in the key region of eastern Austria, where the parties are particularly strong, Spar is distinctly less well represented than the Austrian average. Even before the operation, Spar had only about one-third of Rewe/Billa's market share there.

- (30) Following the merger, Rewe/Billa/Meinl will have a market share advantage over all other competitors of at least 25 %. Although ADEG possesses a large number of shops, a substantial proportion of them are small foodstores (up to 150 m²).

(b) Specific strengths of the parties

- (31) (aa) Rewe/Billa and Meinl are by far the leading suppliers in the key regions of eastern Austria (Vienna, Lower Austria, northern Burgenland). The Commission's investigations have revealed the following market share breakdown for eastern Austria and Vienna:

(%)

Firm	Vienna	Eastern Austria
Rewe/Billa	[47 to 53]*	[42 to 47]*
Meinl	[13 to 18]*	[7 to 12]*
Spar	[8 to 13]*	[15 to 20]*
Löwa	[< 15]*	[< 10]*
Others	[< 15]*	[< 20]*

The above figures do not include the Hofer discount chain. If it were included, the market shares would not be significantly smaller.

- (32) Eastern Austria may be regarded as the key region of the Austrian food trade. In eastern Austria, which makes up less than a quarter of the country's surface area, the high population density means that, with over 40 % of all Austrian sales outlets, 41 % of total food-retailing trade turnover in Austria is achieved

there. Within the eastern Austrian region, the federal capital Vienna is of particular importance to the retail food trade. According to Nielsen, the Viennese have by far the highest purchasing power in Austria⁽¹⁰⁾. This is clear, *inter alia*, from the turnover achieved in Vienna.

(33) In eastern Austria Rewe/Billa/Meinl will have almost four times the market share of its closest competitor, Spar, and almost three times as many shops. What is more, Spar has achieved this market share only by taking over former outlets of the Konsum retail chain in 1995. Before that, Spar's market share was only about 5 %. Following Meinl's departure from ZEV-Markant⁽¹¹⁾, the latter will no longer be present in Vienna and will have only a minor presence in the rest of eastern Austria. Löwa has only [< 150]* shops in Vienna, including a mere seven hypermarkets and 38 supermarkets, compared with Rewe/Billa/Meinl's total of [< 500]* shops, including 277 supermarkets and 60 hypermarkets. This large number of shops which Rewe/Billa/Meinl will have at its disposal after the operation will give the firm a decisive competitive advantage inasmuch as, according to the competitors surveyed and the authorities, there are, in Vienna and eastern Austria, only a few sites available for new outlets. The parties rejoin that in Vienna the total operational floor space limit is, at 2 500 m², by far the highest and that there are therefore no substantial barriers to market entry in Vienna. The fact that in Vienna the relevant regulations permit a larger overall operational floor space than in other provinces merely implies, however, that, for physical planning and legal reasons, larger operational floor spaces are more justified in a city with over a million inhabitants than in small or medium-sized towns or in rural areas. It cannot lead to the provision of any extra floor space for new shops.

(34) The exceptionally strong position which Rewe/Billa will occupy after the operation in Austria and especially in Vienna will have a considerable impact on Rewe/Billa's market position in the Austria market as a whole. If Rewe/Billa clearly dominates a region of Austria which is by far the biggest in terms of turnover, the firm will be able to earn increased profits from its activities there. This is especially true of Vienna, where Rewe/Billa/Meinl will, with a total of some 475 shops and a 65 to 70 % market share, rising to over 80 % in eight of the capital's 23 districts, face hardly any competition worth mentioning. The advantages of this dominant position in eastern Austria are therefore likely to provide the firm with additional resources compared with its competitors which can be employed by the firm in areas where its market share is relatively low. The dominant position in eastern Austria accordingly affords Rewe/Billa additional scope for further

squeezing its competitors in other regions and hence also for further consolidating its own market position in those regions as well.

(35) In the opinion of consumer representatives, consumer choice between different suppliers in the food-retailing trade providing a comparable service is already restricted by the high density of the Rewe/Billa shop network in eastern Austria and especially in Vienna. At present there is, however, still some competition, above all between Meinl and Billa shops. The consumer representatives consider that, after the operation, there will be the prospect, not only of a less varied range of goods on the shelves owing to Meinl's becoming a carbon copy of Billa, but also of a substantial limitation, if not total exclusion, of consumer choice.

(36) The parties rejoin that Spar is the market leader in five out of nine Austrian provinces and that, at 64 %, it has a market share in Vorarlberg which is far bigger than Rewe/Billa's market shares in eastern Austria. Moreover, Spar has, they say, a market share of 100 % in many rural areas of Austria because it operates the only food shop in the district. The latter argument is irrelevant as the competitive assessment is based, not on individual local markets, but on the overall market of the food-retailing trade in Austria. As to Spar's market share in Vorarlberg as referred to by the parties, it should be pointed out that, at fewer than 350 000, the population of Vorarlberg is only about a 10th of that of the key region of eastern Austria. Spar's relatively high market share in Vorarlberg accordingly does not confer on that firm anything like the same strength as that which Rewe/Billa possesses as a result of its strong position in the key region of eastern Austria.

(37) (bb) Compared with their competitors, Rewe/Billa and Meinl have a particularly well developed network of highly productive, large shops. Whereas the number of shops engaged in the Austrian food-retailing trade has fallen by half over the last 30 years, the number of supermarkets (400 to 999 m²), and in particular of hypermarkets ($> 1\,000$ m²), has grown considerably (from 706 in 1980 to 1 907 in 1995). This corresponds to an increase in their share of the total number of shops from 5,3 % to 24 %. The share of turnover accounted for by supermarkets and hypermarkets is as high as 66 % of which approximately 27 percentage points are accounted for by hypermarkets⁽¹²⁾. The growing competitive importance of large shops is due primarily to consumers' changing shopping habits (weekly shopping trips, each covering a month's needs) and

⁽¹⁰⁾ See AC Nielsen, *Statistical yearbook 1998 Austria*, p. 37.

⁽¹¹⁾ Meinl is by far the largest member of ZEV, accounting for some two thirds of ZEV's procurement volume.

⁽¹²⁾ See AC Nielsen, *Statistical yearbook 1998 Austria*, p. 46.

increased urbanisation of the population. A further factor is the ever-greater variety of goods on offer by the food-retailing trade, which necessitates adequate storage and shelf space. Large shops are *prima facie* placed at an advantage by this.

(38) Even before the operation takes place, Rewe/Billa controls far more hypermarkets (Merkur, 66 in all) than its largest competitor Spar (44 Interspar shops). As a result of the operation the gap will become even wider, as Rewe/Billa will take over 40 PamPam hypermarkets from Meisl. Löwa controls 17 Magnet shops, and ADEG 47 Contra hypermarkets⁽¹³⁾. Hofer does not have any hypermarkets.

(39) Compared with its competitors (apart from the Hofer discount chain, which is not altogether comparable), Rewe/Billa already achieves on average for all forms of marketing the highest turnover per square metre (Rewe/Billa ATS 86 000, Meisl ATS 53 000, Spar ATS 54 000, ADEG ATS 60 000, Löwa ATS 45 000). Hypermarkets achieve a particularly high turnover per square metre. Rewe/Billa achieves in its Merkur shops by far the highest turnover per square metre, at ATS 103 700. Interspar shops, on the other hand, achieve only ATS 56 235/m², and Magnet shops ATS 86 700m². PamPam's turnover per square metre is, however, only ATS 44 000⁽¹⁴⁾.

(40) The parties contend that, because Interspar shops have larger sales areas, Spar carries a much wider range in those shops than do Rewe/Billa's Merkur shops. Spar is, they claim, able to subsidise the food sector through the better conditions obtained in the non-food sector. If this argument is correct and Spar actually enjoys considerable competitive advantages, it is hard to understand why, as indicated above, the productivity per unit area of Merkur shops is almost twice as high as that of Interspar shops.

(41) As a result of the operation, Rewe/Billa's already considerable lead over its competitors in terms of number of hypermarkets will increase even further.

(42) (cc) Compared with their competitors, Rewe/Billa and Meisl occupy a strong position in conurbations and have especially favourable locations, which they can use flexibly thanks to the Bipa drugstore chain. The Commission's investigations have shown that, even before the operation,

Rewe/Billa has a particularly strong presence in conurbations. As a result of the operation, the density of Rewe/Billa shops in such areas will be further increased. This holds true, for instance, for seven of the nine provincial capitals, where more than 210 (that is to say, over 60 %) of the Meisl shops to be taken over are situated.

(43) Like the dominant position in eastern Austria and Vienna, this concentration on conurbations strengthens the position of Rewe/Billa/Meisl in the Austrian market as a whole. It must be borne in mind in particular here that in conurbations the turnover achieved in the food-retailing trade is higher than the purchasing power of the population resident there as, in such areas, commuters living elsewhere purchase considerable quantities of daily consumer goods. A food-retailer in a conurbation likewise enjoys considerable advantages from a logistical point of view in that it can supply a correspondingly large number of outlets there. This holds true despite the drawbacks inherent in delivering goods in conurbations, such as high traffic density and officially regulated delivery times. These drawbacks lead to a substantial increase in the logistical costs of food retailers who have only a relatively sparse distribution network in conurbations. Bearing in mind, moreover, that the competitors of Rewe/Billa and Meisl have distribution networks which extend for a large part to rural areas and even to remote Alpine valleys, it can be assumed that their logistical costs are on the whole much higher than those of Rewe/Billa/Meisl.

(44) It is already apparent from the sharply above-average productivity of Billa shops that Billa holds particularly favourable sites. This is borne out by the findings of the Commission's investigations and by what competitors say. The favourable location of a site is one of the essential parameters of a food retailer's market position. This holds true all the more as, owing to restrictive official authorisation practices, few new sites are available for food-retailing outlets. Especially in favourable city-centre locations, but also in outlying areas suited to hypermarkets, the construction of new outlets is subject to tight restrictions.

(45) A site may be considered favourable, *inter alia*, where it is centrally located (such as in an inner-city shopping street) or where it is located in a shopping centre or specialised supermarket centre easily accessible by car. The attractiveness of shopping centres lies in their broad mix of businesses offering customers a wide range of goods under one roof, often combined with eating, sports and leisure facilities ('shopping as an enjoyable experience'). Specialised supermarket centres

⁽¹³⁾ See market survey, *Der Lebensmittelhandel in Österreich* 1998, RegioPlan Consulting, p. 90.

⁽¹⁴⁾ See market survey, *Der Lebensmittelhandel in Österreich* 1998, RegioPlan Consulting, p. 49.

are to be found mainly on the outskirts of small towns with their own catchment area, being especially suited to bulk buying by car-owners.

- (46) The Commission's analysis on the basis of the RegioPlan study shows that, together with Meinl, Rewe/Billa will have 160 shops in the 181 key locations covered by the RegioPlan study, of which 66 for Rewe/Billa and 40 for Meinl. Spar, the closest competitor, has 62 shops in key locations, followed by Hofer with 47 and Löwa with 20, while ADEG has only five shops and the smaller competitors number 14 altogether. The 181 key locations consist of the 98 shopping centres, 63 specialised supermarket centres and 20 inner-city shopping streets covered by the RegioPlan study. Taking these three types of key location together, it is clear that, by acquiring Meinl, Rewe/Billa will more than triple its hitherto weak presence in inner-city shopping streets in all provincial capitals (apart from Innsbruck and Bregenz). An analysis of the regional breakdown in Austria shows that Rewe/Billa/Meinl is overrepresented in key locations in every province compared with its average regional presence.

- (47) The following table shows, for each retailer, the number of shops in shopping centres, specialised supermarket centres and inner-city shopping streets, together with the total number of such shops:

Firm	Shopping centres	Specialised supermarket centres	Inner-city shopping streets	Total
Rewe/Billa	24	34	8	66
Meinl	18	3	19	40
Rewe/Billa + Meinl	46	37	27	106
Spar	44	17	1	62
Hofer	4	42	1	47
Löwa	5	13	2	20
ADEG	1	4	0	5
Others	4	8	2	14

- (48) It may be assumed that, after the takeover, Rewe/Billa will no longer operate all the 343 Meinl shops in Austria and the approximately 150 Meinl shops in the Vienna conurbation, as food-retailing outlets. The necessary restructuring would normally be carried out by closing or selling off shops, with the result that their business could be carried on by competitors. But Rewe/Meinl will, even after Meinl has been restructured, not necessarily sell the shops on the market, being able instead to use them, say, for its Bipa drugstore chain. The merger will thus prevent Rewe/Billa's competitors from getting their hands on the shops.

- (49) (dd) *Unlike its main competitors, Rewe/Billa is a centrally managed chain-store company.* As already indicated in recital 23, there are in the Austrian food-retailing trade both pure chain-store companies and hybrid companies. The latter are mainly voluntary trading chains and retailers' purchasing associations, the first of which operate their own shops, and the second of which have distribution agreements with independent retailers. The ratio between the turnover of chain-store companies, including shops owned by voluntary trading chains and retailers' purchasing associations, and that of independent retailers is approximately 75:25. A large proportion of the sales outlets of independent retailers are smaller than 250 m².

- (50) Pure chain-store companies are able to take important business decisions (e.g. assortment policy, price policy, advertising campaigns) centrally and implement them in all affiliated shops immediately. According to suppliers, it takes Rewe/Billa [...] on average to list or delist a product, whereas it takes Spar [...] to reorganise its range in affiliated points of sale. Moreover, in the case of all other organisation forms, full compliance by all affiliated retailers is never to be expected as the owners of affiliated retail outlets enjoy a much greater measure of independence than do branch managers of a centrally organised company. It follows that chain-store companies can react more quickly and more effectively to competitive challenges.

- (51) It is also easier for chain-store companies to introduce own brands and pursue a purposive own-brand policy than it is for less tightly organised food-retailing chains. Rewe/Billa has at its disposal in several product categories an above-average proportion of own brands (see recital 111) and is the only Austrian food retailer so far to have successfully introduced an own-brand range in the upper price segment. Own brands can increase traders' profitability. The prices of well-known branded goods are often used by consumers as a yardstick by which to assess the value-for-money to be obtained from a particular shop. Traders therefore tend to price such goods keenly so as to appear in the consumer's eyes to be offering good value-for-money. This leads to somewhat narrow margins for well-known branded articles. In the case of own brands, however, the consumer is unable to make any direct price comparison. This can be used to achieve a higher margin than in the case of branded goods. Such a

strategy is particularly easy to implement in the case of chain-store companies, as the head office has firm control over all branches.

(52) Both Rewe/Billa and Meinl are straightforward chain-store companies. Their main competitor Spar, on the other hand, is organised to only a relatively small extent along chain-store lines. Of 1 560 Spar shops, 1 103 are run by independent traders. Rewe/Billa/Meinl will thus be further consolidating its existing structural advantages over Spar. Nor is the next-largest competitor ADEG a chain-store company. Although Löwa is organised along chain store lines and is a subsidiary of the Tengelmann group, it has market share of only about [< 10]* %. The only other straightforward chain-store company, M-Preis, is on the whole active only in the Tirol.

(53) (ee) *As a result of its tie-up with Rewe, Billa has considerable resources to fall back on.* Since 1996 Billa has belonged to the Rewe group. Rewe is the leading food retailer in Germany and the third largest in Europe. In 1997 the Rewe group achieved an aggregate turnover of EUR [...] billion. The parties have submitted that Billa has so far not had to resort to the Rewe group's financial resources. This does not rule out the possibility, however, that those resources might be placed at Billa's disposal. By contrast, Billa's main competitor, Spar, is exclusively Austrian and achieves an aggregate turnover of the order of EUR [...] billion. Although Hofer and Löwa are also subsidiaries of international trading groups with a large turnover, they both have only a relatively small market share. And although ADEG and the German Edeka group recently forged ties, the impact is not the same for both, simply on account of their cooperative structure.

(54) (ff) *The dominant position to which the operation will give rise in the procurement market will give Rewe/Billa/Meinl a considerable competitive advantage in the distribution market.* As will be explained below, the merger will lead to the creation of a dominant position in a number of procurement markets which are of decisive importance to the food-retailing trade. And as will also be explained below, the position in the procurement market is of decisive importance as far as the position in the distribution market is concerned.

(55) The more a food retailer buys in, the more favourable as a rule are his buying conditions and hence the more chance he has of gaining a bigger share of the distribution market. This leads in turn to a further strengthening of his purchasing power. If a firm acquires a dominant position both in the distribution market and in the procurement markets, the combination of these two forms of market power enables it

to squeeze existing competitors in the distribution market or to oust them completely from the market.

(c) *Future developments*

(56) (aa) *The existing barriers to entry to the Austrian food-retailing market will be further increased by the merger.* The Austrian food-retailing market is already characterised by high entry barriers. This holds true especially for large-surface stores. Firstly, the land-use planning laws and building regulations of the nine provinces and the Shopping Centre Order adopted pursuant to the Federal Trade Regulations make the opening of food-retailing outlets subject to official authorisation or, above a certain sales area, to tight restrictions going as far as a ban on new shops over a certain size. Secondly, apart from already existing shops, especially in conurbations, suitable plots for additional food-retailing outlets very rarely become available. Both factors constitute a considerable barrier to entry to the Austrian food-retailing market. Moreover, the Austrian food-retailing market already has a high level of concentration.

(57) The parties dispute the existence of the above market entry barriers, pointing out that Rewe/Billa has succeeded in recent years in opening on average 50 new shops a year in Austria and in increasing its market share from 25 % to 30 % through internal growth. This can be answered firstly by saying that no competitor of Rewe/Billa has managed to expand as much in terms of new outlets. Secondly, the new shops were supermarkets and not large-surface stores. Thirdly, as far as Rewe/Billa's internal growth in general is concerned, the parties have themselves stated that many smaller Billa shops have been closed and replaced by larger ones. It follows from all this that, compared with its competitors, Rewe/Billa enjoys strategic advantages thanks to which it can to some extent offset the difficulties standing in the way of expansion in the Austrian market.

(58) In view of the existing market entry barriers, it is not surprising that past attempts by foreign firms to enter the Austrian market have failed. A survey of the past years shows that even internationally active chains have been unable to gain entry to the Austrian market (Denner of Switzerland and Carrefour of France in the 1970s, the German firm Hurler, with Huma, in the 1980s, and Migros of Switzerland in the 1990s). Even the Tengelmann subsidiary Löwa, which has been active in Austria since the 1970s, is having difficulty retaining a foothold in the market. Its market share is

still well below 10 %. Before it acquired a stake in ADEG, Edeka of Germany operated, with moderate success, only two food-retailing outlets in Austria. Although the German trading company Lidl is now becoming active in the Austrian food-retailing market, its activity has so far been confined to a few shops and became possible only after many years of trying. Apart from Rewe in 1996 and the recent entry by Lidl, in the past 20 years or so there has been no new market entry by a large trading chain.

(59) As a result of the merger, the level of concentration in the Austrian food-retailing market will be increased further by a considerable margin and it will be even more difficult for newcomers to enter the market in the future. It cannot therefore be supposed that the room for manoeuvre of Rewe/Billa/Meinl will be restricted by potential competition.

(60) (bb) *The market position of Rewe/Billa/Meinl achieved through the merger can be expected to be further enlarged in the foreseeable future.* The total number of shops in the Austrian food-retailing trade has been falling steadily for years (between 1996 and 1996 and 1997, for example, by 3,7 %). Even before the operation is scheduled to take place, Rewe/Billa is the only supplier to be expanding rapidly, opening on average 50 new shops a year on its own resources. The other large suppliers have, by contrast, been carrying out closures.

(61) If Meinl's shops are fully integrated into the Rewe/Billa group, they can be expected to further enlarge their market position. If after the operation Meinl's volume of purchases is combined with the much larger one of Rewe/Billa, the former Meinl shops will be able to benefit from more favourable purchasing conditions.

(d) **Causality**

(62) In their reply to the Commission's Statement of Objections, the sellers submitted that the operation would not lead to the creation of a dominant position on the part of Rewe/Billa/Meinl in the Austrian food-retailing market. In its present form, and given its present rate of growth and size, Meinl suffered from major competitive disadvantages vis-à-vis other, much larger, competitors. If Meinl were to quit the market or if it had to downsize, the market shares would, owing to the historical and geographical distribution of Meinl's shops, accrue mainly to Rewe/Billa. Nor was there any less anti-competitive alternative to the sale, as the only other potential buyer was Spar. Spar occupied a similar position to Rewe/Billa in terms of market share in the Austrian market as a whole, was especially strong in western Austria and had a larger sales area than Rewe/Billa.

(63) The Commission acknowledged in the Kali and Salz/MdK/Treuhand decision⁽¹⁵⁾, which has since been upheld in this respect by the Court of Justice⁽¹⁶⁾, that a merger which should normally be considered to lead to the creation or strengthening of a dominant position on the part of the acquiring firm can be regarded as not causing such a position on the market if, even in the event of the merger's being prohibited, the acquirer would inevitably achieve or strengthen a dominant position. Accordingly, a merger generally is not the cause of the deterioration of the competitive structure if it is clear that:

- the acquired firm would in the near future be forced out of the market if not taken over by another firm,
- the acquiring firm would take over the market share of the acquired firm if it were forced out of the market,
- there is no less anti-competitive alternative purchase.

(64) At the same time, the Commission made clear in the Kali and Salz decision that such a situation occurs only in exceptional cases. Normally, there would be a presumption that an operation which results in the creation or strengthening of a dominant position is the cause of this deterioration of the competitive structure. Consequently, the burden of proving that there is no causal link lies with the merging firms.

(65) It should be pointed out first of all that, in contrast to the situation underlying the Kali und Salz decision, in this case there is no question of the possible forcing of a whole firm out of the market. The group was split into two back in 1996 when the sub-group Julius Meinl Austria Industrie GmbH was formed. This sub-group includes the production division, which comprises the firms Julius Meinl Kaffee- und Tee Vertriebs GmbH (roasted coffee and tea), Julius Meinl Nahrungsmittelproduktion GmbH (predominantly marmalade, fruit juice, distillery products and wine), Julius Meinl Fleischwerke GmbH (meat and sausages) and Julius Meinl Grosshandels GmbH (distribution of own-label products). Julius Meinl Austria Industrie GmbH also holds 33,3 % of the shares in Meinl Bank AG and all the shares in Copem Compagnie de Participation Européenne Meinl BV, which holds 49 % of the shares in Julius Investment NV. The latter controls Julius Meinl International AG, which acts as holding company for the Meinl group's activities in central and eastern Europe. The retailing division retained by Meinl therefore accounts for only part of the business activities and subsidiaries of the Meinl group. Meinl's withdrawal

⁽¹⁵⁾ OJ L 186, 21.7.1994, p. 38, paragraphs 70 et seq. of the recitals.

⁽¹⁶⁾ Judgment of the Court of Justice in Joined Cases C-68/94 and C-30/95 French Republic and Others v Commission [1998 ECR I-1375.

from the Austrian food-retailing market will accordingly take the form of a management decision to abandon a business activity whose development has not lived up to the expectations of the firm's managing board. In such a case of a 'failing-division defence' and not of a 'failing-company defence', the burden of proving that the defence of lack of causality is valid must be especially heavy. Otherwise, every merger involving the sale of an allegedly unprofitable division could be justified under merger control law by the seller's declaring that, without the merger, the division would cease trading.

(66) The parties' submission is not such as to justify applying the defence of lack of causality. Apart from the general consideration outlined above, the parties have done nothing to prove that, in the absence of a takeover by another firm, Meisl will in any event withdraw from the market in the near future. While it is true that Meisl's financial situation has deteriorated in recent years, the parties have not submitted any evidence to suggest that Meisl is already, or is about to become, insolvent. It must be assumed, rather, that the intended divestiture of the Meisl group's food-retailing activities in Austria is based on a strategic decision of the group's top management. The restructuring of the Meisl group in 1996 suggests that, with the splitting of the group into two sub-groups, steps were already being taken to facilitate the subsequent sale of Meisl's food-retailing activities. As is clear from the 1996 annual report, the loss-making Meisl activities in Austria were being separated from the profitable, essentially more highly capitalised and strategically more important activities, which were being brought together within the sub-group Julius Meisl Austria Industrie GmbH. Against this background, merely proving that, in its present form and given its present rate of growth and size Meisl suffers from major competitive disadvantages vis-à-vis other, much larger, competitors does not suffice to show why Meisl's food-retailing activities must in any circumstances be terminated.

(67) In the Commission's view, the parties' contention that Meisl's market shares will, owing to the historico-geographical distribution of Meisl shops, accrue mainly to Rewe/Billa is likewise not valid. The parties themselves say in the same breath that Spar is a potential buyer. On the strength of the parties' own admission, it cannot therefore be assumed that Meisl's market shares would come what may, accrue to Rewe/Billa. The competitive situation which would arise with or without the proposed operation is therefore by no means the same.

(68) The parties' contention that there is no less anti-competitive alternative to the sale to Rewe/Billa, Spar

being ineligible owing to its market position, is equally unsubstantiated. It is clear from the Commission's exposition in the Kali and Salz/MdK/Treuhand decision that the burden of proving that there is no alternative potential buyer apart from the acquiring firm is, in the Commission's opinion, a heavy one. This view has been upheld by the Court of Justice⁽¹⁷⁾. The parties' argument does not discharge this burden. The parties have neither indicated with which potential buyers the Meisl group has negotiated nor for what reasons the negotiations failed. In saying that Spar is excluded from the outset as a less anti-competitive alternative buyer, the parties have pre-empted the competitive assessment by the competent competition authority. In view of the abovementioned differences between Rewe/Billa and Spar, such a finding is by no means a foregone conclusion.

(69) The parties have therefore satisfied none of the Commission's three tests in the Kali and Salz/MdK/Treuhand decision for sustaining the defence of lack of causality. The proposed operation gives rise for this reason also to the creation of a dominant position on the part of Rewe/Billa/Meisl in the Austrian food-retailing market.

(e) Conclusion

(70) For the above reasons, it is to be expected that the proposed operation will place Rewe/Billa/Meisl in a dominant position in the food-retailing market in Austria.

B. PROCUREMENT MARKET

(71) The exercise of buyer power which leads to the securing of a more favourable purchase deal is not to be considered per se detrimental to the economy as a whole. Especially where the supplier side is itself highly concentrated and powerful, buyers are faced with effective competition in their own selling market and hence are compelled to pass on any savings to their own customers, buyer power can prevent monopoly or oligopoly profits from being earned on the supply side⁽¹⁸⁾. However, if the powerful buyer himself occupies in his selling market a strong position which is no longer kept sufficiently in check by the competition, any savings can no longer be expected to be passed on to customers.

⁽¹⁷⁾ See footnote 15.

⁽¹⁸⁾ See, for example, *The welfare consequences of the exercise of buyer power*, study by Paul Dobson, Michael Waterson and Alex Chu for the Office of Fair Trading, September 1998, p. 17 et seq.

(72) In the retail trade there is a close interdependence between the distribution market and the procurement market. Retailers' shares of the distribution market determine their procurement volume: the bigger the retailer's share of the distribution market, the larger the procurement volume. And the larger the procurement volume, the more favourable as a rule are the buying conditions which the trader obtains from his suppliers. Favourable buying conditions can in turn be used in various ways to improve one's position in the distribution market (sometimes through internal or external growth, but also through low-price strategies targeted at competitors). The improved position in the distribution market is itself reflected in a further improvement in buying conditions, and so on.

(73) The spiral described above leads to ever-higher concentration both in distribution markets and in procurement markets. In the short term, final consumers may benefit from the process, as there may be a period of intense (predatory) competition in the distribution market during which the powerful buyer/trader is forced to pass on his savings to consumers. But this will last only until such time as a structure (as in this case, an individual dominant position) is arrived at in the distribution market which leads to a clear reduction in competitive intensity. At this stage, any consideration for the final consumer goes by the board, as he is left with few alternatives.

(74) Buyer power also gives a trader considerable influence over the choice of products which come to market and hence are obtainable by consumers. Products which are not bought by a dominant buyer have practically no chance of reaching the final consumer as the supplier lacks alternative outlets. Lastly, the dominant buyer determines the success or otherwise of product innovations.

1. Relevant product markets

(75) These markets comprise the sale of daily consumer goods by producers to customers such as wholesalers and retailers and other firms.

(76) The consistent practice of the Commission and the approach of the Court of Justice has been to define the market primarily from the viewpoint of the the

consumer. True, the products or products-categories which are typically bought in by a food retailer are not, as far as the end consumer is concerned, totally interchangeable: even so, at a commercial level the specific distribution service offered by the food-retailing trade is, as was explained in recital 13, of great importance to the consumer, and that service entails a definite range of food and non-food products ('one-stop shopping'). The position is different, however, when it comes to defining procurement markets. Here, the critical factors are the producers' flexibility in changing output and the alternative outlets open to them. Producers generally produce a single product or category of products (such as dairy products, bread and pastries) and are unable to switch readily to making other products. A dairy producer, for instance, cannot produce bread and pastries without substantial investment and additional know-how. It is not possible, therefore, to speak of a uniform procurement market for the food-retailing trade. Although the food-retailing trade exerts demand for a complete range of goods inasmuch as its customers likewise demand variety (see recitals 10 et seq.), it cannot obtain this complete range from one and the same producer. It cannot therefore be accepted that there is a single procurement market.

(77) The Commission's investigations have confirmed that a market definition broken down by product category is generally considered meaningful and that a distinction can be drawn essentially between the following categories:

- meat and sausages,
- poultry and eggs,
- bread and pastries (fresh and packaged bakers' wares, excluding frozen ones),
- dairy products (milk, butter, yoghurt, puddings, fresh milk-based desserts, all types of cheese),
- fresh fruit and vegetables,
- beer,
- wines and spirits,
- soft drinks (including mineral water),
- hot beverages (coffee and tea),
- confectionery,
- basis foodstuffs (including flour, sugar, noodles, rice and spices),
- preserved foods (non-perishable foodstuffs in tins or other packaging, with the exception of frozen foods),

- frozen foods (including ice cream),
- baby foods,
- pet foods,
- body-care products (creams, lotions, etc., the purpose of which is primarily preventive) and cosmetics (make-up and perfumes),
- detergents, polishes, cleaning products,
- other drugstore products (apart from the above, medicinal products available over the counter, health foods, personal hygiene products, and so on),
- other non-food products normally found in supermarkets (for example, clothing, newspapers and magazines, entertainment).

(78) Supplier structures also differ between the various product categories. In the fresh-product sector, and especially in the case of meat and sausages, dairy products and bread and pastries, there is a highly fragmented supplier structure consisting mainly of small and medium-sized businesses. In the non-food field (such as detergents, body-care products and pet foods), on the other hand, large international producers predominate. The remaining product categories display a hybrid supplier structure, although it is normally⁽¹⁹⁾ characterised by a lower level of concentration than the trader side. Buying-in by the food-retailing trade is likewise organised as a rule along the lines of the above product-categories.

(79) As a rule, the food-retailing trade is not the only sales channel open to producers of retail-food products. Other possible sales channels are, for example, the specialised trade, cash-and-carry stores and other wholesalers, delicatessens, drugstores and the export trade. Although the importance of the various sales channels differs depending on the product category (see table at recital 95), the food-retailing trade is, with a share of more than 50 %, by far the most important sales channel for most product categories. The disparate distribution of the sales channels also militates in favour of a delimitation of the procurement market according to product categories.

(80) It must be borne in mind that from the producer's point of view different sales channels are not readily interchangeable. Different container sizes, get-up and packaging (for which special machines or other production requisites may be needed), different sales

strategies (as in the food-retailing trade and in delicatessens), the need for variety of knowledge and contacts for different distribution channels and different logistics make it difficult to switch between sales channels. The Commission has information in its possession which indicates that entry into a new sales channel is sometimes possible only after lengthy canvassing of the market. Numerous products (in particular impulse and branded goods) are expressly designed for direct sale to final consumers. For such products, there are, outside the food-retailing trade, few marketing alternatives (as a rule the specialised trade, for non-food products the drugstore trade, cash-and-carry stores). The Commission's investigations have disclosed that an immediate, smooth substitution of a lost food-retailing trade customer by selling through other sales channels is impossible in most product categories. A change of sales channel would instead, where it is at all possible, require considerable investment and adaptation of the firm's production and sales organisation and cost structure. This points to there being, at least in certain product categories, a pure food-retailing procurement market.

(81) The Commission therefore proceeds on the assumption that the procurement market may be objectively subdivided into the abovementioned product categories. This does not rule out the possibility that some of these markets may have comparable structures and can be lumped together in the analysis. Moreover, there are, for the reasons set out above, strong arguments in favour of subdividing the procurement market according to sales channels, so that procurement for the food-retailing trade may constitute a separate market. This matter does not have to be decided, however, as competition problems already arise in procurement markets covering all sales channels.

2. Relevant geographic markets

(82) According to the parties, the procurement market is EEA-wide. Following Austria's integration into the EU, both suppliers and retailers have concentrated increasingly on the European market. This can be seen from the growth in actual foodstuff exports, especially to Germany. At the same time, however, the parties concede that, more than two years after the takeover of Billa by Rewe, the joint procurement volume of both firms comes to less than 2 % of the total procurement volume of Billa for food and non-food. The parties point out, moreover, that Austrian brands and hence Austrian producers are an essential feature

⁽¹⁹⁾ There are a number of exceptions, including very minor product categories without much importance in Austria, e.g. fish.

of the Rewe/Billa range, there being increased demand from consumers for Austrian and regional products. Rewe/Billa therefore works, they argue, very closely with regional and local suppliers, such as bakeries, mills, sausage and ham producers and water-bottlers. In fruit and vegetables, Rewe/Billa attaches great importance to freshness and hence, owing to the shorter carrying distances, to Austrian goods. As a direct result of the takeover of Billa by Rewe, many customers pay more attention to Austrian quality, Austrian products being preferred in many instances to those of international suppliers, precisely because of their high quality.

- (83) The Commission's investigations have established that the procurement markets for all the product categories referred to below are to be regarded as national. This is due, first, to consumer preferences for Austrian products and a product range tailored accordingly. Secondly, the Austrian food-retailing trade buys predominantly from Austrian suppliers. According to data supplied by AC Nielsen, in the product categories⁽²⁰⁾ of meat and sausages, dairy products, soft drinks, beer, bread and pastries, fruit and vegetables and coffee, the Austrian food-retailing trade obtains more than 80 % of its supplies from purely national suppliers. Even where supplies are procured from internationally active producers (such as branded-goods manufacturers), the procurement is effected almost exclusively through their Austrian establishments. Austrian producers (especially producers of foodstuffs) sell the bulk of their output in Austria, concentrating on the Austrian market with its 8 million inhabitants and special consumption habits. Only 8,4 % of the foodstuffs produced in Austria are sold abroad.

- (84) A further pointer to there being Austrian procurement markets is the existence of higher prices for a number of, in particular, fresh products in Austria compared with Germany. According to the notifying parties, buying Austrian fruit and vegetables costs Billa [...] % more than buying comparable goods elsewhere in Europe. Pork costs ATS [...] * per kilo more in Austria than the EU average. All told, according to the notifying parties, the prices of Austrian products are up to 20 % higher than comparable European market prices.

- (85) Even international branded goods in both the food and the non-food sector are as a rule procured from Austrian establishments/subsidiaries of the relevant firms, and are not imported. This is due primarily to the fact that the food-retailing chains expect from producers, services such as shelf maintenance and market research, which can be provided only through a presence on the spot. This package of products and services, which is tailored specifically to the Austrian market, is negotiated by international producers in the annual rounds of talks with the Austrian food-retailing trade. An additional pointer to there being a national procurement market even in international branded goods is the fact that, especially in the food sector, international brands are often only collective brands. The content of the products differs from country to country according to different tastes. The Commission has determined, for example, that coffees, prepared dishes and even pet foods produced for Germany, are, in spite of identical packaging, not saleable in Austria, and vice versa. The opening-up of the procurement market anticipated in the decision of 27 August 1996 in case M.803-Rewe/Billa⁽²¹⁾ has yet to manifest itself. It is also worth noting in this connection that, even more than two years after the takeover of Billa by Rewe, the joint procurement volume of both firms, according to their own estimates, amounts to less than 2 % of the total procurement volume of Billa for food and non-food. The parties themselves have, moreover, conceded that buying abroad continues to be difficult owing to red tape, for example, formal declaration and packaging.

- (86) Lastly with regard to international branded goods, it is appropriate to define the geographic markets with reference to the ability of suppliers to switch to other means of channelling goods to final consumers⁽²²⁾. Here, access may be had to the consumer only through the corresponding distribution channels in Austria, of which the food-retailing trade is the most important.

- (87) Owing to the abovementioned structural peculiarities, the Commission accordingly proceeds on the basis that there are national Austrian procurement markets.

3. Competitive assessment

- (88) It is to be assumed that the operation will lead to the creation or strengthening of dominant positions on the part of Rewe/Billa/Meinl in nine Austrian procurement markets.

⁽²⁰⁾ The product categories mentioned here do not correspond fully to the product categories set out above.

⁽²¹⁾ See footnote 5.

⁽²²⁾ See Decision 92/227/EC, footnote 6, recital 37.

(a) **Market structure**

(89) (aa) *In the Austrian procurement markets the supply side is much less concentrated than the demand side, especially as far as the food-retailing market as a demander is concerned. The supply structure differs from one product category to another. In almost all product categories (with a few exceptions especially in the non-food sector, such as pet foods), the producer side is much less concentrated than the demand side. In the Cash Almanach⁽²³⁾, which, according to the trade, is the most comprehensive catalogue of, among others, foodstuff suppliers in Austria, on average for all product categories, 22 producers are listed per product category. In the product categories dairy products, meat/sausage and basic foodstuffs, there are 40 to 50 suppliers each, for confectionery, wines/spirits and preserved foods around 30 to 40 each, and for beer and bread/pastries about 20 each⁽²⁴⁾. A large proportion of the producers are, moreover, small firms with a turnover of less than EUR 7 to 8 million.*

(90) The suppliers/producers of dairy products, meat and sausages, poultry and eggs, bread and pastries and beer in Austria are, with few exceptions, Austrian firms which concentrate on the domestic market and which, when compared with their foreign counterparts, are small and medium-sized enterprises. A few German firms (particularly from southern Germany) also supply the Austrian market. Big international firms are the exception (in the case of dairy products, for example, above all Danone, and to a lesser extent KraftJacobsSuchard, for which dairy products are more of a sideline).

(91) In the categories confectionery, soft drinks, coffee and tea, wines and spirits, basic foodstuffs, preserved foods and frozen foods, international groups (such as Nestlé, KraftJacobsSuchard, Masterfoods) and Austrian producers (such as Inzerdorfer, Felix Austria, Darbo, Mautner Markhof, Manner) are equally well represented in each case.

(92) Non-food products especially (body-care products, cosmetics, personal hygiene products, detergents, polishes and cleaning products), but also baby foods and pet foods, are supplied mainly by international suppliers. In these sectors also there are, however, a few (fairly small) Austrian producers.

(93) In the food-retailing trade sales channel, these producers stand opposite fewer than 10 food-retailing chains, of which only five (Rewe/Billa, Meinl, Spar, ADEG, Löwa) are active throughout Austria. According to the information in the Commission's possession, the buyers in other sales channels are, apart from cash-and-carry stores, not very highly concentrated. They are predominantly small and medium-sized enterprises, especially in the specialised trade and delicatessen sales channels. In the cash-and-carry sector, Metro is the only buyer in Austria worth mentioning, but the importance of this sales channel is on the whole minor (the share across all product categories being approximately 10 %). In the export field, although a few large buyers are present, this sales channel is also of much lesser importance than the food-retailing trade (the share across all product categories being approximately 13 %).

(94) (bb) *The food-retailing trade is by far the most important sales channel for the foodstuffs suppliers. The importance of the various sales channels differs depending on the product category. The relative importance of each sales channel to the various product categories as determined by the Commission's investigations, based on the answers of the producers surveyed, weighted according to their turnover, can be seen from the following table:*

Product category	Food-retailing trade share	Specialised trade share	Delicatessen share	(%) Other sales channels share
Dairy products	64	3	3	30
Bread and pastries	33	35	2	30
Soft drinks	50	6	17	27
Hot beverages	62	0,5	19	18,5
Basic foodstuffs	65	5	10	20
Baby foods	31	0	0	69 [of which 66 % SDs ⁽¹⁾]
Pet foods	52	7	0	41 (of which 32 % SDs)
Detergents, polishes and cleaning products	70	0	0	30 (of which 19 % SDs)
Body-care products and cosmetics	40	0	0	60 (of which 44 % SDs)

(¹) SDs = specialist drugstores.

(²³) *Cash Almanach für Handel, Gewerbe und Industrie '98*, published by the trade magazine Cash, Manstein Zeitschriften Verlagsges.m.b.H, Perchtoldsdorf.

(²⁴) In the case of bread/pastries, small producers producing products exclusively or almost exclusively for sale in their own bakeries or as local suppliers to the food-retailing trade are not included.

(95) These percentages show that, for all the product categories indicated apart from baby foods and body-care products/cosmetics, the food-retailing trade is the most important sales channel. The other sales channels are, by contrast, of far less importance.

(96) The Commission's investigations have determined that switching between different sales channels is extremely difficult. Differences in packaging, get-up and container size from sales channel to another are a bar to a speedy, smooth switch-over. More important, however, are differences in logistics and distribution structures from one sales channel to another, which place different demands on a firm. A different vehicle fleet, for example, is needed if, instead of having to supply a few central warehouses for the food-retailing trade, numerous smaller customers have to be supplied direct. The number, knowledge and contacts of the distribution staff also necessarily differ from one distribution channel to another. And different distribution channels call for different advertising messages aimed at final consumers.

(97) For these reasons and because of the large role played by the food-retailing trade in the sale of products in the above categories in Austria, it follows that a 'lost' food-retailing trade customer is as a rule difficult for producers to replace. The producers surveyed stated that they could replace without difficulty only small food-retailing trade customers (accounting on average for less than 5 % of turnover). Even food-retailing customers accounting for 5 to 10 % of turnover are, according to the same source, not easy to replace. Switching to other sales channels is normally out of the question owing to the difficulties referred to above. And the larger producers, both international and Austrian, especially already have as a rule, attained a very high degree of distribution through all sales channels and in particular through all the major food retailers. This shows clearly that in Austria the opportunities for producers to switch to other buyers are much more limited than the opportunities for buyers to switch to other producers.

(98) (cc) *Even prior to the merger, Rewe/Billa has the highest market shares in the procurement markets and will increase them substantially as a result of the operation.* It is difficult to determine precise market shares in the procurement market. The Commission asked some 300 foodstuff manufacturers predominantly in Austria⁽²⁵⁾, what share of their turnover was accounted for by Rewe/Billa and Meidl. On the basis of that survey, producers can be deemed to achieve on average per product category with Rewe/Billa and Meidl the percentages of turnover shown in the following table. The table covers some

200 evaluated answers. The data are based on procurement markets covering all sales channels, although, as indicated above, there are strong arguments in favour of there being separate markets for each sales channel.

Product category	Rewe/Billa	Meidl	Rewe + Meidl
Dairy products	[15 to 25]	[< 10]	[25 to 35]
Bread and pastries	[20 to 30]	[< 10]	[30 to 40]
Soft drinks	[20 to 30]	[< 10]	[25 to 35]
Hot beverages	[25 to 35]	[< 10]	[25 to 35]
Basic foodstuffs	[20 to 30]	[< 10]	[25 to 35]
Baby foods	[25 to 35]	[< 5]	[30 to 40]
Pet foods	[25 to 35]	[< 5]	[25 to 35]
Detergents, polishes and cleaning products	[20 to 30]	[< 5]	[25 to 35]
Body-care products and cosmetics	[25 to 35]	[< 5]	[30 to 40]

(99) As a result of the operation, the average shares of suppliers' turnover in the stated product categories accounted for by Rewe/Billa will increase appreciably, as therefore will the dependence on Rewe/Billa as a customer. As far as the food sector is concerned, these product categories account for a share of nearly 40 % of total turnover in the food-retailing trade and in the specialised trade⁽²⁶⁾. Of the three non-food product categories listed in the table, the two categories detergents/polishes/cleaning products and body-care products/cosmetics belong to the categories with the highest relative turnover share in the non-food sector. It can therefore be assumed that these two procurement markets are of considerable importance.

(100) Apart from these average figures, it must be borne in mind that a considerable proportion of suppliers are even more dependent on Rewe/Billa and Meidl than the averages show. In the case of dairy products, for example, a good third of suppliers transact more than [...] % of their turnover with Rewe/Billa alone. After the operation, this will be true, assuming that procurement behaviour does not change, of nearly half of all suppliers.

(101) The Commission asked producers above what proportion of turnover, with a given customer could not be switched to other sales channels without difficulty.

⁽²⁵⁾ Including both Austrian firms and Austrian establishments of international firms. Producers from other European countries were also surveyed.

⁽²⁶⁾ Source: market survey, *Der Lebensmittelhandel in Österreich 1998*, RegioPlan Consulting, pp. 24 et seq.

It transpired that on average 22 % of turnover is the figure above which a customer can be replaced only at the cost of very heavy financial losses, if at all. The parties have contended that a producer behaving in an economically realistic manner must be able to withstand turnover reductions of up to about 20 %. The Commission proceeds in this case, having regard to supplier structures in the indicated procurement markets and assuming the existence of a dominant position in the distribution market, on the premise that the position which Rewe/Billa will occupy in the procurement markets after the operation takes place will be of an order of magnitude such that either a dominant position is created or an existing dominant position is strengthened.

(102) It must be borne in mind here firstly that, when they lose a major customer, producers do not have much in the way of alternatives. In the food-retailing trade, especially if the firm concerned is already on the list of the leading competitor Spar, only small competitors are left, and they are hardly in a position to take up a large share of turnover. Switching to other sales channels is difficult, costly and, in the short term at least, generally impossible. Switching to exports, mentioned by the parties as an alternative, is likewise not feasible in the short term. To build up export markets, an on-the-spot presence and an intensive, costly canvassing of the market are normally necessary. The Commission has information in its possession which indicates that it can take about five years to attain a satisfactory level of exports, to Germany for example. The upshot is that already on the supplier side there is a strong dependence on Rewe/Billa/Meinl, a dependence which will grow as a result of the merger.

(103) Rewe/Billa and Meinl, on the other hand, are not dependent on individual suppliers. The leading supplier to the Rewe group (the Nestlé group) covers, according to the notification, only about [...] % of the volume of purchases. In the case of Meinl, the leading supplier covers approximately [...] % of the volume of purchases. The result is a much heavier dependence of the supplier side on Rewe/Billa/Meinl than the other way round. This is the norm, moreover, with large food retailers⁽²⁷⁾. Range flexibility in the trade is far greater than the flexibility of producers in production and distribution. Hence it is much easier for the trade not to buy something than it is for the producer not to produce it. This puts the market share study well and truly into context.

(104) The parties argue, by contrast, that they, for their part, are dependent on certain producers. This is true, they

say, of one branded goods producer who makes 'must carry'/products, as Rewe/Billa and Meinl risk losing customers if those products are not on their shelves. They add, moreover, that, in view of the strong preference of Austrians for Austrian products, there is for the same reason a dependence on Austrian producers. The latter argument is not valid, however. While it may be true that Rewe/Billa and Meinl cannot do without Austrian products, especially in the fresh produce sector (such as dairy products and bread), a dependence on individual suppliers cannot be deduced from this. The Commission's investigations have established that there are in the fresh produce sector a large number of Austrian suppliers potentially at the parties' disposal. If individual suppliers drop out, there are sufficient alternatives for the parties to turn to.

(105) The answer to the question as to the extent to which a trader is dependent on branded goods producers depends on what consequences the non-availability of certain brands has for the trader. What matters here is how the trader's customers react to the absence of a product. In the case of foodstuffs purchases, the duration of a shopping trip is an essential consideration to customers. One-stop shopping, meaning buying everything needed from one shop, is preferred. If a branded product which the customer wants is not stocked by such an outlet, the risks have to be weighed up that the customer might: (1) stop shopping or put off making the purchase till later, (2) go to another shop to look for the desired article, but otherwise remain faithful to 'his' trader, (3) take his business elsewhere in the longer term, or (4) buy another brand⁽²⁸⁾.

(106) The answer depends first on the importance of the product to the customer, and secondly on the availability of alternative sources of supply. In the case of foodstuffs which are purchased frequently and for which the convenience of shopping as a rule outweighs other aspects such as price and quality, the importance of the product is somewhat slight. This is all the more true if the customer finds in his shopping environment almost nothing but outlets of one and the same trader. It can accordingly be assumed that, in the event of a delisting of branded goods, the trader suffers less than the producer, especially since he will usually have more alternative possibilities open to him⁽²⁹⁾.

⁽²⁷⁾ See the interim report by Dobson Consulting for the study, *Buyer power and its impact on competition in the food-retailing distribution sector of the European Union*, p. 27.

⁽²⁸⁾ OECD background paper 'Round table on buying power', 1998, pp. 9 et seq.

⁽²⁹⁾ OECD background paper, pp. 11 et seq.

(b) *The parties' particular strengths*

(107) (aa) *Rewe/Billa has structural competitive advantages in the procurement markets which none of its competitors has.* Rewe/Billa is a centrally managed chain-store company which can decide centrally about important factors in competition such as the composition of the range it carries. If the decision is taken at Rewe/Billa head office to include a certain product in the range, according to the information in the Commission's possession only two weeks or so go by before the product is available in every Billa shop in the country.

(108) The closest competitor, Spar, on the other hand, is much less centralised, the majority of Spar outlets (71 %) being run by independent retailers. When launching a new product at Spar, the producer has to deal with three separate levels within the Spar group, namely the head office, regional Spar organisations and individual Spar traders. It accordingly takes much longer ([...]^{*}) before a new product is available in a large number of Spar outlets. A 100 % availability rate, which is attainable at Billa without any difficulty, is normally impossible at Spar. Rewe/Billa cannot be bypassed in Austria when it comes to launching new products, and this places Rewe/Billa at a competitive advantage *vis-à-vis* producers as far as any modifying of the range is concerned.

(109) (bb) *The dominant position in the eastern Austrian/Vienna region strengthens the position of Rewe/Billa/Meinl in the Austrian demand markets.* In order for a firm/product to be present throughout Austria, it is essential, according to the information in the Commission's possession, in all the product categories listed in recital 98 to be represented in the eastern Austrian/Vienna region. As was stated in recitals 32 et seq., it is in this region that the centre of gravity of the Austrian economy lies. According to AC Nielsen, 41 % of Austrian food-retailing trade turnover is achieved there (of which 20 % is in Vienna alone). And a national advertising strategy makes sense only if a product is actually obtainable throughout the country.

(110) With the exception of a few firms⁽³⁰⁾, all the producers of goods in the abovementioned categories who were surveyed told the Commission that an adequate presence in eastern Austria and especially in Vienna was

impossible without a listing with Rewe/Billa/Meinl. Before the merger, Meinl offered firms not listed with Rewe/Billa an alternative, especially through its strong presence in the Vienna area. This alternative has now disappeared. The remaining competitors are too weak in eastern Austria and above all in Vienna to represent a viable alternative to the parties (market shares of at most [< 20] % [Spar] or [< 12] % [ADEG, Löwa]. Similarly, for the reasons given above, neither Hofer nor sales channels outside the food-retailing trade are alternative outlets for producers.

(111) (cc) *Rewe/Billa is using own brands strategically to further reduce its already limited dependence on suppliers.* On average the own-brand share in Austria amounts, according to the notifying parties, to approximately [< 10] % (minus Hofer, which stocks almost nothing but own brands, but which cannot use them strategically against branded-goods producers in the manner described below). Billa's own-brand share is well above average in some product categories:

(%)					
Product category	Billa	Merkur	Mondo	Emma	Bipa
Dairy products	[...] [*]	[...] [*]	[...] [*]	[...] [*]	
Fruit and vegetables	[...] [*]	[...] [*]	[...] [*]	[...] [*]	
Wines and spirits	[...] [*]	[...] [*]	[...] [*]	[...] [*]	
Pet foods	[...] [*]	[...] [*]	[...] [*]	[...] [*]	[...] [*]
Personal hygiene	[...] [*]	[...] [*]	[...] [*]	[...] [*]	[...] [*]

(112) The growth and increasing importance of own brands are having the effect of shifting the balance of power between traders and producers in favour of traders. A trader has own brands produced to his own requirements and under his own logo. The actual producer is no longer visible to the customer and is therefore exchangeable almost at will. This can be illustrated by the example given to the Commission of Billa's own brand 'Heidi Teebutter', which, using almost identical packaging, was produced, first by an Austrian producer, then by a Dutch one. The trader thereby enters *de facto* into direct competition with branded goods producers. The effect is that of a backwards integration into the producer stage⁽³¹⁾.

(113) The presence of own brands endangers in particular weaker brands which do not number among the must-carry products. Such brands are quite easily

⁽³⁰⁾ Namely small producers of fresh produce who deliver only locally in western Austria, firms which have opted for supplying Hofer, and a few firms which supply products mainly through sales channels other than the food-retailing trade.

⁽³¹⁾ See OECD background paper, p. 13.

replaceable by own brands. The presence of own brands therefore makes delisting threats against the producers of such brands even more credible than against producers of must-carry brands.

- (114) The Commission's attention has been drawn to specific instances where, in various product categories, Billa has selectively delisted secondary brands or weaker producer's brands (not only of international branded goods producers but also goods of Austrian producers) and replaced them with own brands. Although must-carry products are as a rule not delisted, as they continue to be needed on the shelves as eye-catchers, their share is reduced to the extent necessary for them to perform their eye-catching function, for example by limiting the range. By the same token, the own-brand share can be considerably increased.

- (115) (dd) *The dominant position to which the operation will give rise in the distribution market will further strengthen Rewe/Billa/Meinl's position in the procurement markets.* As indicated above (recitals 21 to 70) the operation will lead to the creation of a dominant position in the Austrian food-retailing market. The increased market shares in the distribution market achieved by Rewe/Billa as a result of the operation will increase the parties' volume of purchases. The higher Rewe/Billa's volume of purchases, however, the more dependent producers will be on this customer and the easier it will be for it to secure further improvements in its buying conditions.

(c) **Causality**

- (116) As was explained in recitals 63 to 69, the parties have satisfied, in respect of the food-retailing market, none of the Commission's three tests in the Kali and Salz/MdK/Treuhand decision for sustaining the defence of lack of causality. The proposed merger therefore results *a fortiori* in the creation of a dominant position on the part of Rewe/Billa/Meinl in the Austrian procurement markets mentioned below.

(d) **Conclusion**

- (117) It is accordingly to be assumed that, as a result of the operation, dominant positions on the part of Rewe/Billa will be created or strengthened in the procurement markets for dairy products, bread and pastries, soft drinks, hot beverages, basis foodstuffs, baby foods, pet foods, detergents, polishes and cleaning products, and body care products and cosmetics.

C. UNDERTAKING OFFERED BY THE PARTIES

1. **Undertaking**

- (118) In order to meet the Commission's objections to the proposed operation, the parties have made the following commitments.

Meinl will transfer to Rewe/Billa for operation as food-retailing outlets only those shops which are mentioned in the list attached to the letter of 26 January 1999 (Annex 1) as being sites to be transferred. The sites mentioned in Annex 1 are Meinl shops situated outside the territory of eastern Austria (Vienna, Lower Austria and northern Burgenland). Rewe/Billa undertakes to take possession of these shops alone with a view to operating them as food-retailing outlets.

Meinl will transfer to Rewe/Billa the shops listed in Annex 2, which shops will be converted into Bipa shops within three months of the Rewe/Billa merger being authorised and will continue to be operated as such indefinitely. Rewe/Billa undertakes in this respect not to operate, pending the completed conversion, as food-retailing outlets of Rewe/Billa any of the 45 Meinl sites intended for Bipa. Rewe/Billa undertakes for an unlimited period not to reconvert into food-retailing outlets, once they have been converted, any of the 45 Meinl sites intended for Bipa. Should Rewe/Billa not wish to continue to operate as drugstores the shops listed in Annex 2, it undertakes to offer them for sale to third parties independent of Rewe/Billa. If a transfer to third parties is not possible, these sales outlets may be closed or sub-leased to competitors active independently of Rewe/Billa both in the distribution market and in the procurement markets and to firms active in markets other than the food-retailing market.

Rewe/Billa will submit to the Commission, every six months until 28 February 2001 and thereafter every 12 months until 28 February 2004, a written report on the current status of the Meinl shops which are to be run as Bipa shops. These reports will contain in particular all the information which the Commission needs in order to verify whether the sites listed in Annex 2 are being operated by Rewe/Billa as drugstores.

Meinl will, as part of its own business operations, itself continue to operate the sites listed in Annex 3 and undertakes for an unlimited period not to transfer any of the shops listed in Annex 3 to Rewe/Billa or to any of its group member companies. Meinl is free, moreover, to sell shops listed in Annex 3 to firms independent of Rewe/Billa, subject if necessary to examination by the competent competition authority.

Meinl and Rewe/Billa undertake for an unlimited period to remain independent of one another when operating in the distribution and procurement markets. (At this point in the confidential version of the decision, further details are given of the parties' respective undertakings.)

Meinl will submit to the Commission, every six months until 28 February 2001 and thereafter every 12 months until 28 February 2004, a written report on the current status of the shops operated by it. These reports will include all the information which the Commission needs in order to verify whether the commitments entered into by Meinl are being adhered to.'

2. Assessment

- (119) On the basis of the undertaking offered by the parties, Rewe/Billa will acquire 162 out of a total of 341 Meinl shops. The annual gross turnovers of the shops to be acquired total ATS [...] million, which would correspond to an acquisition of 41 % of the total turnover of Meinl's shops. It must be borne in mind in this connection, however, that, of the 162 shops, 45 will be converted into Bipa drugstores. The food-retailing turnovers of these shops correspond to a 7 % share of Meinl's aggregate food-retailing turnovers. Rewe/Billa will therefore in fact acquire only 34 % of Meinl's aggregate food-retailing trade turnovers. The increase in Rewe/Billa's share of the Austrian food-retailing market will accordingly amount to approximately 2,5 %, as opposed to 7 % on the basis of the proposal as originally notified.
- (120) Meinl will remain active in the food-retailing distribution market in Austria as an ongoing competitor with 179 shops. It will concentrate its food-retailing activities on eastern Austria, where it is already in a stronger position than elsewhere. With the proceeds from the sale of 162 shops to Rewe/Billa, Meinl will also be able to carry out much-needed restructuring and above all it may be able to build on and improve its position in eastern Austria.
- (121) The 117 Meinl shops which Rewe/Billa can acquire and continue operating as food-retailing outlets are located outside the key region of eastern Austria. The increase in market share will therefore occur in areas where Rewe/Billa has so far been in a weaker position. In the key region of eastern Austria, on the other hand, the already strong position of Rewe/Billa will not be further strengthened, as Rewe/Billa will not be acquiring there, any shops earmarked for operation as food-retailing outlets. What is more, Meinl will be active in eastern Austria with 179 shops.
- (122) As regard large-surface stores, the increase in the number of PamPam hypermarkets is being limited to 16 instead of 40 as originally notified. The increase is

taking place, moreover, outside the key region of eastern Austria, in areas where Rewe/Billa's Merkur hypermarket chain is not so strongly represented. As far as the key locations covered by the RegioPlan study are concerned Rewe/Billa will acquire half the sites occupied by Meinl in shopping centres, specialised supermarket centres and inner-city shopping streets. Here too, however, the increase will be limited to locations outside the key region of eastern Austria.

- (123) In the procurement markets, the sharply reduced market-share increase in the distribution market will mean that the dependence of suppliers on Rewe/Billa as buyers in the product categories referred to in recital 99 will be hardly any greater. The purchasing potential which will accrue to Rewe/Billa as a result of the amended operation will have no noticeable influence on the position of Rewe/Billa in the procurement markets. Nor will Rewe/Billa further strengthen its strong position in eastern Austria. In addition, Meinl will be active as a purchaser in the procurement markets, albeit to a lesser extent, and will remain an alternative outlet for suppliers, owing especially to its strong presence in the Vienna area. It is accordingly to be assumed that the position which Rewe/Billa will occupy in the procurement markets after the operation takes place will be of an order of magnitude such that no dominant position is created and no existing dominant position is strengthened.
- (124) Third parties have argued, on the other, hand, that, through the acquisition of 45 Meinl sites which are to be converted into Bipa shops, the position of Rewe/Billa in four non-food procurement markets, baby foods, pet foods, detergents/polishes/cleaning products and body-care products/cosmetics, will be strengthened in a way which at least compares with the original proposal.
- (125) It should be pointed out first of all that, looked at from a competition angle, the operation relates to the takeover of Meinl's present position in the distribution market and the various procurement markets. When considering the procurement markets, only the volume of demand which is attributable to the acquired Meinl sites can therefore be taken into account. In a merger review context, however, theoretically higher demand volumes which might arise following conversion of these sites cannot be taken as a criterion. Nor can any safe assertion be made in this respect. A total of at most 41 % of Meinl's demand volume in the procurement markets is to be assigned to Rewe/Billa, assuming that the position in the procurement markets is proportional to that in the distribution market. It follows from this, however, that the position of REWE/Billa in three of the said non-food procurement markets is being strengthened by less than 1 % and

in the market for detergents, polishes and cleaning products by less than 1,5 %. Bearing in mind, moreover, that in these markets, unlike in the food sector, large multinational groups are predominantly active, it is not possible to infer from an increased demand potential of the above order of magnitude any strengthening of Rewe/Billa's position of relevance from a merger-control point of view.

(126) Third parties have also argued that the takeover of a total of 45 Meinl shops which are to be converted into Bipa shops will cause competition problems in the specialised drugstore trade in Austria.

(127) In its decision of 28 September 1998 the Commission reserved the right to examine the market for drugstore products more closely in the course of the proceedings to be initiated. On the basis of the investigations that it carried out, the Commission has come to the conclusion that the concentration in the specialised drugstore trade in Austria gives rise to no objections under competition law. Since Meinl operates no drugstores, there was on the basis of the proposed operation as originally notified no market-share addition on the supply side. As regards the growth, likewise established on the basis of the proposed operation as originally notified, in the four non-food procurement markets of baby foods, pet foods, detergents/polishes/cleaning products and body-care product/cosmetics, this was, in view of the unchanged position on the supply side, not likely to strengthen the position of Rewe/Billa in the specialised drugstore trade in such a way as to affect merger control considerations.

(128) Nor can a different view be taken on the basis of the undertaking offered. This holds true even if one focuses only on drugstores. The current market volume for the Austrian specialised drugstore trade is estimated at just under EUR 1 billion (ATS 13 billion). In the drugstore field, three main suppliers with comparable market shares are active in Austria:

— dm-Drogeriemarkt GmbH, in which Spar has a 33 % holding, is the strongest supplier with a market share of 39 to 43 % and [...] shops,

— Rewe/Billa-owned Bipa is, with 33 to 35 % and, according to it, 340 shops⁽³²⁾, is the second-largest supplier,

— the Schlecker drugstore chain has a market share of 22 to 28 % and operates some 550 shops.

Pursuant to the undertaking, Rewe/Billa would acquire 45 shops which are currently operated by Meinl as food-retailing outlets and which may no longer continue to be operated as such by Rewe/Billa. Assuming that Rewe/Billa converts all 45 shops into Bipa shops and that all 45 shops achieve the average turnover for drugstores in Austria of EUR 727 000 (ATS 10 million)⁽³³⁾, Bipa would achieve additional sales of EUR 32 million (ATS 450 million). This purely hypothetical increase in Bipa's turnover would correspond to a share of less than 3,5 % of the Austrian specialised drugstore trade. Even if the average turnover per Bipa shop were taken as a basis, this would result in only a slightly higher share of just over 4 %. The conversion of 45 Meinl shops into Bipa shops would therefore at most enable Rewe/Billa to catch up with the current market leader dm-Drogeriemarkt GmbH, assuming that the shops that are acquired and converted can be run as successfully as the existing Bipa shops.

(129) The Commission is accordingly of the opinion that the proposed undertaking is such as to avert the creation or strengthening of a dominant position in the Austrian food-retailing market and in the Austrian procurement markets referred to in recital 117.

VI. SUMMING-UP

(130) For the above reasons, it may be accepted that, on condition that the undertaking offered by the parties is carried out, the planned operation will not lead to the creation or strengthening of dominant positions as a result of which effective competition would be significantly impeded in a substantial part of the Community. Subject to this condition, the operation is therefore to be declared, pursuant to Article 2(2) of the Merger Regulation and Article 57 of the EEA Agreement, compatible with the common market and with the functioning of the EEA Agreement,

HAS ADOPTED THIS DECISION:

Article 1

The notified operation whereby Rewe Internationale Beteiligungsgesellschaft mbH and REWE-Verkaufsgesellschaft mbH are to acquire sole control over the entire share capital of

⁽³²⁾ As many as 370 according to other sources.

⁽³³⁾ Nielsen's countrywide estimate.

Meinl is, on condition that the undertaking offered by the parties and reproduced in recital 118 of this Decision is carried out, hereby declared compatible with the common market and with the functioning of the EEA Agreement.

REWE-Verkaufsgesellschaft mit beschränkter Haftung
Domstrasse 20
D-50668 Köln

Article 2

Done at Brussels, 3 February 1999.

This Decision is addressed to:

REWE Internationale Beteiligungsgesellschaft mit beschränkter
Haftung
Domstrasse 20
D-50668 Köln

For the Commission

Karel VAN MIERT

Member of the Commission

COMMISSION DECISION

of 8 July 1999

on state aid implemented by Germany in favour of Kvaerner Warnow Werft GmbH

[notified under document number C(1999) 2266]

(Only the German text is authentic)

(Text with EEA relevance)

(1999/675/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

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

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

Having regard to Council Directive 90/684/EEC⁽¹⁾ of 21 December 1990 on aid to shipbuilding and Council Directive 92/68/EEC⁽²⁾ of 20 July 1992 amending Directive 90/684/EEC on aid to shipbuilding,

Having called on interested parties to submit their comments pursuant to the provisions cited above⁽³⁾ and having regard to their comments,

Whereas:

I. Procedure

- (1) By receiving on 4 September 1998 the regular monitoring report of 30 June 1998 on the shipbuilding capacity of Kvaerner Warnow Werft GmbH (hereinafter referred to as KWW), the Commission was informed that KWW would exceed its annual new-building capacity limitation of 85 000 cgt in both 1998 and 1999. The foreseen production indicated in the report was 106 945 cgt for 1998 and 104 560 cgt for 1999. The Commission services sent a letter to the German authorities on 25 September 1998 requesting them to take the necessary measures to make the undertaking comply with the capacity limitation and to inform the Commission of the contents and the result of these measures. Germany replied with its letter dated 20 October 1998.
- (2) By letter dated 16 December 1998, the Commission informed Germany of its decision to initiate the procedure laid down in Article 93(2) of the EC Treaty in respect of this exceeding of the capacity limitation.

- (3) The Commission decision to initiate the procedure was published in the *Official Journal of the European Communities*⁽⁴⁾. The Commission invited interested parties to submit their comments on the matter.
- (4) The Commission has received comments from interested parties. It has forwarded them to Germany, which was given the opportunity to react. Germany submitted its comments with a letter dated 18 February 1999.
- (5) The Commission services conducted a regular monitoring visit to the yard with an external expert on 14 January 1999. It was discovered that the actual production of KWW in 1998 was much greater than indicated in the monitoring report of 30 June 1998. The Commission requested Germany to comment on the findings of the visit in a letter dated 4 February 1999. Germany submitted its comments with a letter dated 18 February 1999.
- (6) On the further request of the Commission with the letter of 1 March 1999, Germany confirmed the findings of the Commission as regards the production figures of 1998 in its letter of 19 March 1999 and indicated a revised production figure of 122 414 cgt.
- (7) The Commission services conducted a further monitoring visit to the yard on 25 March 1999 with an external expert in order to verify the amount of excess production in 1998. It was confirmed that the production of KWW in 1998 was 122 414 cgt and its production in 1997 was 93 862 cgt, also exceeding the capacity limitation. The foreseen production for 1999 was indicated to be 109 134 cgt.
- (8) This decision concerns only the exceeding of KWW of its capacity limitation in 1998. The Commission intends to open the procedure pursuant to Article 88(2) of the EC Treaty as regards the exceeding of the capacity limitation in 1997. This opening of procedure is subject to a separate Commission decision.

⁽¹⁾ OJ L 380, 31.12.1990, p. 27. Directive as last amended by Directive 94/73/EC (OJ L 351, 31.12.1994, p. 10).

⁽²⁾ OJ L 219, 4.8.1992, p. 54.

⁽³⁾ OJ C 41, 16.2.1999, p. 23.

⁽⁴⁾ OJ C 41, 16.2.1999, p. 23.

II. Detailed description of the aid

(9) The Commission approved restructuring aid in accordance with Directive 90/684/EEC on aid to shipbuilding and Directive 92/68/EEC amending Directive 90/684/EEC on aid to shipbuilding, to allow the comprehensive restructuring of the former East German shipyard Kvaerner Warnow Werft GmbH with its decisions communicated to Germany with the letters of 3 March 1993 (N 692/D/91), 17 January 1994 (N 692/J/91), 20 February 1995 (N 1/95), 18 October 1995 (N 637/95) and 11 December 1995 (N 797/95). The aid was approved subject to a capacity restriction of 85 000 cgt per year, the compliance of which the Commission monitors.

(10) The shipyard Warnow Werft, situated in Rostock-Warnemünde in Mecklenburg-Vorpommern, Germany, was sold by the Treuhandanstalt to the Norwegian industrial group Kvaerner a.s. in October 1992. According to paragraph 27 of the sales contract, sent to the Commission for scrutiny and approval by Germany with a letter dated 30 October 1992, Kvaerner undertook until 31 December 2005, with regard to Warnow yard, not to exceed its annual building capacity of 85 000 cgt unless the requirements based on the EC Treaty became less restrictive.

(11) Directive 92/68/EEC amending Directive 90/684/EEC contains a derogation from the rules on operating aid applicable to other Community yards for the shipyards in the former GDR in order to create the possibility for these yards to undergo urgent and comprehensive restructuring and to become competitive. After the privatisation of Warnow Werft the Commission approved the restructuring aid for the yard in four tranches in accordance with the provisions of Directives 90/684/EEC and 92/68/EEC. The total amount of aid approved by several decisions was as follows:

N 692/D/91 — Commission letter of 3 March 1993 (SG (93) D/4052)

- DEM 45,5 million operating aid,
- DEM 82,4 million operating aid in the form of an exemption from previous liabilities,
- DEM 127,5 million investment aid,
- DEM 27,0 million closure aid;

N 692/J/91 — Commission letter of 17 January 1994 (SG (94) D/567)

- DEM 617,1 million operating aid;

N 1/95 — 20 February 1995 (SG (95) D/1818)

- DEM 222,5 million investment aid;

N 637/95 — Commission letter of 18 October 1995 (SG (95) D/12821)

- DEM 66,9 million investment aid;

N 797/95 — Commission letter of 11 December 1995 (SG (95) D/15969)

- DEM 58,0 million investment aid.

Consequently, the total amount of aid concerned by these decisions was EUR 372,5 million operating aid (DEM 745 million) EUR 237,45 million investment aid (DEM 474,9 million) and EUR 13,5 million closure aid (DEM 27,0 million). This results in total aid of EUR 623,45 million (DEM 1 246,9 million).

(12) The aid was approved on the condition that the yearly newbuilding capacity does not exceed 85 000 cgt. The capacity limitation is included both in the notified sales contract (paragraph 27) concerning the privatisation of Warnow Werft and in the above mentioned Commission decisions authorising the aid. In the Commission decisions communicated to Germany by the Commission letters of 17 January 1994, 20 February 1995, 18 October 1995 and 11 December 1995 it was clearly stated that the Commission will be obliged to demand the recovery of the aid if the restriction of capacity is not complied with.

(13) In the opening of the procedure the Commission noted that the main condition for the approval of the aid was an annual capacity limitation of 85 000 cgt. Such a limit was set in order to offset the distortive effect of the aid on the shipbuilding industry. According to the regular monitoring report of 30 June 1998 on the shipbuilding capacity of Kvaerner Warnow Werft GmbH, the yard would exceed its annual newbuilding capacity limitation of 85 000 cgt in 1998, by producing 106 945 cgt and in 1999, by producing 104 560 cgt. This information indicated that an essential condition under which the aid was approved, was not being complied with.

(14) For this reason the Commission doubted whether the aid approved by the Commission to allow the restructuring and the continued operation of the former East German shipyard Warnow Werft by its decisions communicated to Germany with the letters of 3 March 1993 (N 692/D/91), 17 January 1994 (N/692/J/91), 20 February 1995 (N 1/95), 18 October 1995 (N 637/95) and 11 December 1995 (N 797/95) was any longer compatible with the common market.

III. Comments from interested parties

(15) The Commission has received comments from KWW, a Member State (Denmark), The Federation of Danish Industry (Dansk Industri) and the Association of Danish Shipbuilders (Foreningen af Jernskibs- og Maskinbyggerier i Danmark).

- (16) The comments of KWW concentrate on five main arguments. The first argument of KWW is that an annual production limitation of 85 000 cgt was never imposed on it. The only condition imposed on KWW when the aid was approved was that the new yard to be built would allow a possible production of 85 000 cgt at 31 December 1995 and that certain lay-out-related criteria (bottle-necks) of the yard which limit the production should not be changed. These bottle-necks in the course of production were considered decisive for the production possibilities of the yard.
- (17) Only in its decision of 18 October 1995 does the Commission refer for the first time to the production of the yard as follows: 'Further monitoring will be necessary to ensure, as evidenced by the two production monitoring reports received so far by the Commission, that the actual and planned production respects the capacity limit. The German Government gave an undertaking that the yard will comply with the capacity limitation'. According to KWW, the first sentence implies that during the capacity limitation the lay out of the yard cannot be changed. That sentence also mentions for the first time the actual and planned production that shall respect that capacity limit. KWW understood at the time the undertaking of the German Government, according to which the yard will comply with the capacity limitation, in a sense that only the compliance with the investments plans is ensured. In any case, this first reference to the monitoring of production is not worded as a condition.
- (18) Consequently, according to the first two Commission decisions the concept of capacity limitation means that the lay out and facilities of the yard should be designed in a certain way and that they could not be changed. Such a construction of the yard leads to limited production of the yard. In addition, it is not correct that the capacity limitation of 85 000 cgt was a condition for the approval of the aid. A condition for the approval was only that the approved and examined production facilities would be kept in accordance with the investment plans.
- (19) Secondly, KWW argues that according to the wording of Article 10a(2)(c) of Directive 90/684/EEC⁽⁵⁾ and the Commission decisions approving the aid, the capacity gains due to productivity increases above the level foreseen by the Commission expert as until the end of the restructuring period, should be possible and permitted to the yards.
- (20) Article 10a(2) of the Directive 90/684/EEC lays down conditions for the compatibility of operating aid granted to former GDR shipyards with the common market. Its provision (c) provides that the German government shall carry out a genuine and irreversible reduction of capacity of 40 % net of the capacity existing on 1 July 1990.
- (21) The Court of First Instance has interpreted the notion of 'irreversibility' in its judgment of 22 October 1996 in Case T-266/94⁽⁶⁾, *Skibsværstforeningen and others v. Commission*, as meaning that, with the Commission's agreement, capacity may be increased five years after the end of restructuring and in the absence of such agreement, it may be increased ten years thereafter. In the opinion of KWW this interpretation means that the production facilities which were agreed and defined together with the Commission and the technical bottle-necks approved by the Commission, as well as the production bottle-necks resulting from them can only be changed after the defined periods of time. According to KWW the Court did not consider and decide on the legal situation where the productivity is increased due to the general economic and technical progress so that capacity gains are created on top of the existing, by 40 % reduced production capacities.
- (22) It is the opinion of KWW that irreversible reduction of capacity in the meaning of Article 10a(2)(c) is only to be understood as a prohibition to change the approved investment arrangements and not as a limitation of production possibilities of the yard.
- (23) According to KWW, capacity limitation and production limitations are different concepts that should not be equated. Whereas production limitation concerns the product, the production of which is limited, the capacity limitation is a more open concept, which allows, with the same facilities, a higher production when productivity is increased due to general economic and technical progress. Especially when looked at in the time period of 10 years, it is possible that the productivity develops in a way which allows that more can be produced with the same facilities than at the beginning of this period. Using pre-prepared parts produced by subcontractors with delivery 'just in time' has lead in the last couple of years to productivity increases world-wide in the shipbuilding sector. In 1995 this progress was not yet available to KWW, which has after this date increased its productivity through internal reforms and its own efforts.
- (24) The production capacity of KWW at 31 January 1995 was established in 1992 by an independent expert commissioned by the Commission (A. & P. Appledore International Ltd) who concluded that the yard would achieve a good or even very good European productivity level by 31 December 1995.

⁽⁵⁾ As amended by Directive 92/68/EEC.

⁽⁶⁾ Case T/266/94, *Skibsværstforeningen and others v. Commission*, ECR 1996 II, p. 1399.

- (25) In 1992 KWW could understand and have in fact understood the Commission approval of the aid in a sense that capacity gains based on increased productivity above the good/very good European productivity level can benefit KWW. This assumption was based among others on the following:
- the wording of the Commission decisions approving the aid does not mention production limitation;
 - the Commission commissioned an independent expert to examine the investment plans and the production volumes of the yard at 31 December 1995 under certain productivity assumptions, which would not have been necessary if the Commission intended to impose a production limitation;
 - Germany explained in 1993 that it will ensure that the investment plans for the yards would not be changed, which would not have been necessary if the Commission intended to impose a production limitation from 1995 onwards. The capacity gains following the increased productivity when maintaining the approved investment and construction plans were not subject to the 'capacity limitation'.
- (26) In its third argument, KWW explains that the high production volume of KWW in 1998 is caused by acceptance of offers to build three large 5 000 TEU container ships and a drilling rig. KWW acquired these offers in competition with Asian competitors; no other European yard applied for these offers. This indicates that KWW's exceeding of its production limitation, as the Commission sees it, does not as such mean a disadvantage to other yards. Moreover, carrying out these offers would mean that KWW will not compete in the European market and bid for contracts on products, which other European yards build for a time period of almost two years. The switching of KWW to a special market segment in which other European yards were not active in fact promotes the European state aid policy and should not be punished.
- (27) The fact that KWW proves its competitiveness on the world market and thereby improves the position of the EU-shipbuilding industry without thereby impairing in any apparent way intra-Community competition, indicates that this is not a behaviour that would be incompatible with the common market. As far as other European yards do not compete with KWW for certain specific contracts, like in this case, there is no Community interest at stake. On the contrary, the behaviour of KWW fortifies the position of the EU-shipbuilding industry as a whole in the world market.
- (28) The fourth point raised by KWW in its comments is that the capacity limitation, if it is seen as production limitation, should be considered as an average production of several years. According to KWW, the three large container ships (production with cgt-value) and the drilling rig (production with no cgt-value) cannot be built in parallel because of the time needed for occupation of the dock for both projects. Consequently, the production with cgt-value will remain considerably under 85 000 cgt during the construction of the drilling rig whereas it will exceed this limit during the previous years. On the average, anyway, the limit of 85 000 cgt will not be exceeded during these years. This technical aspect was not taken into consideration when the Directive was adopted and the decisions on approval of the aid were taken. For this reason it seems appropriate to consider the capacity limitation, if it is seen as production limitation, as a long-term average production. This would take into account the fact that KWW, as a recipient of aid, entered successfully into competition in the world market and also entered into a new market segment, thereby proving that it has become a competitive yard. This would be in line with the European state aid policy and its objectives. Considering the capacity limitation as an average of several years would also be meaningful due to the changed economic situation and technical requirements in the shipbuilding sector and would correspond to the reality and circumstances of this sector much better than annual limitation.
- (29) The fifth argument of KWW is that there is no legal basis for laying down the maximum capacity limit for individual yards. The German Government is, according to Article 10a(2) of the Directive 90/684/EEC, only obliged to carry out, before 31 December 1995, a genuine and irreversible reduction of capacity of 40 % net of the capacity existing at 1 July 1990. This has led to the maximum capacity of 327 000 cgt for all yards active in the new German *Länder* per 31 December 1995. KWW refers to the already abovementioned judgment of the Court of First Instance of 22 October 1996⁽⁷⁾ and concludes that according to this judgment, allocation of the capacity between the East German yards is purely an internal German matter that cannot be made a prerequisite for permissibility of a decision on approval of aid. The Commission did not qualify this matter as such in its decisions either.
- (30) Denmark explains in its comments that in the context of adoption of Directive 92/68/EEC Germany committed itself to reduce in a genuine and irreversible way the shipbuilding capacity of yards situated in former East Germany to 327 000 cgt. The state aid now in question was granted to KWW under a condition that it complies with an annual capacity limitation of 85 000 cgt.
- (7) Case T/266/94, *Skibsværftsforeningen and others v. the Commission*, ECR 1996 II, p. 1399.

- (31) Since 1990 the global shipbuilding capacity has increased much more than originally anticipated, which is mainly due to increase of capacities of Japanese and Korean yards. This has led to a world-wide overcapacity and a considerable fall in prices in the world market. This development has affected also Denmark strongly so that many yards have been obliged to cut their activities in a way which has led to a considerable loss of workplaces in the sector. This development took place in Denmark without any state aid having being paid in this context.
- (32) It is emphasised that the production programmes of German shipyards are comparable with Danish shipyards since these are more or less identical as regards location, state of technological development and competition in the world market. It is noted that three TEU 5 000 container ships that have partly caused the exceeding of the capacity limitation are the kind of ships also being built by Danish yards. The actual contract won by KWW has therefore had a direct impact on the market in which also Danish yards operate. The considerable amount of aid received by KWW has thus created a competitive advantage for the German yards and affected the competitiveness of Danish yards.
- (33) The Commission states in the opening of the procedure that according to Germany, the exceeding of capacity shall be compensated in years 2000 and 2001 when the building of the drilling rig will reduce the possibilities of KWW to bid for new contracts. Denmark supports the position of the Commission according to which the existing rules do not foresee any possibility of relaxing the capacity limitation and that such flexible application of them is thereby not possible. Making concessions in this respect would mean a danger of creating a constantly increasing production and the capacity limit exceeding production without ever compensating it with lower production.
- (34) Further, it referred to the German comments on the opening of the procedure according to which the capacity limitations should be re-examined. The German Government stipulates that in 1992 the development of the world capacity was not foreseen and consequently the flexible application of the existing limitations is the only way to increase the international competitiveness of former East German yards. Denmark states that the international development with a considerable increase of capacity above all in the Asian market makes it necessary to consider the maintenance of the existing rules. Nevertheless, this is a problem that concerns the whole European shipbuilding industry and therefore it should not be solved on the basis of problems of one individual yard. It is essential that the EU actively seeks for a global solution to the capacity problem since this is the only way the EU can maintain its credibility internationally. Unilateral increasing of capacity of yards in certain regions would not only be harmful for European shipbuilding but would also destroy the possibilities to achieve results in the international forum in the long run.
- (35) Both the Federation of Danish Industry and the Association of Danish Shipbuilders state in their comments that they support fully the Commission position and remarks as expressed in the opening of the procedure.
- (36) In addition, the Association of Danish Shipbuilders explains in its comments that the container ships being built by KWW and partly causing the excess are ships also being built by Danish yards. The contract of KWW has consequently a direct impact on the market, which is very important for Danish yards. It also refers to the development since 1992 which has led to closure of many yards and to a loss of a considerable amount of jobs in the sector. Therefore it is decisive for the European yards that effective steps to reduce the negative effects of the overcapacity are taken globally. Since such are not possible without an active support from the EU, it is important that the EU maintains its international credibility. An international initiative to reduce overcapacities would not be coherent with a simultaneous accepting of a considerable exceeding of the EU's own capacity limitation, like in this case.
- (37) According to the Association of Danish Shipbuilders, the capacity limitations of the former East German yards are, among other factors, a basis for investment and production planning of other yards. Consequently, the dispositions of other yards are affected by the exceeding of the capacity limitations. These limitations should stay in place ten years and a flexible application of them was never foreseen.
- (38) The German Government stipulates that the capacity limitation should be re-examined in order to be able to react to the special situation in world shipbuilding, the unforeseeable increase of productivity. The Association of Danish Shipbuilders comments on this point that the considerable amounts of state aid were supposed to contribute exactly to increased productivity. If the East German yards have not become internationally competitive under the conditions laid down in 1992 and in spite of productivity increases exceeding all expectations, the restructuring of the yards must be considered as failed. Yet this should not lead to the conditions being adapted to the disadvantage of the rest of the European shipbuilding industry.

- (39) The German Government also explained in the opening of the procedure that it was necessary for KWW to accept the contracts that have led to the excess in order to secure jobs and to be able to conduct business. The Association of Danish Shipbuilders notes that a state based on the rule of law cannot refrain from its legal obligations only on the grounds that economic advantage is gained or economic loss avoided. Accepting this argument of the German Government would mean that each Member State could grant state aid and even contrary to Community law, if it considered this necessary under these circumstances.
- (40) The German Government has known and accepted since 30 June 1998 that KWW would exceed its capacity limitation both in 1998 and 1999. There was a lot of time to take the appropriate measures to change the production plans to avoid the exceeding of the capacity limitation. Yet nothing was done in due time.
- (41) According to the Association of Danish Shipbuilders, it is clear that both the German Government and KWW are bound to respect the capacity limitation. The maximum capacity limit was set by the Council as a condition for approval of the aid and according to Directive 92/68/EEC. The Commission shall monitor that the capacity limitations set for the former East German yards are respected. In this context the Commission established in 1997 that two yards had exceeded their capacity limitations in 1996, the MTW yard by 1 637 cgt and KWW by 92 cgt. Consequently, a corresponding reduction of production was imposed on both yards in 1997. Therefore there is no doubt about the fact that the management of KWW knew very well that it cannot without any consequences accept orders that would lead to exceeding of the capacity limitation.
- sub-contracted. This results in 34 000 cgt having in fact being produced by the sub-contractors and not by the yard.
- (43) Secondly, Germany contests the Commission's observation that an annual capacity limitation of 85 000 cgt was the main condition for approval of the aid. Germany explains that the basis of the approval was much more the restructuring concept linked with the privatisation, which is meanwhile successfully carried out by KWW. The successful execution of the restructuring has led to a considerable increase of productivity, which in general will also be achieved worldwide by other yards.
- (44) Germany stipulates that in its decisions on releasing the tranches of aid, the Commission only imposed on the yard restrictions as regards the layout of the new yard. The Commission examined which new building capacity according to the restructuring plans was possible for the new yard. The expert opinion that the Commission commissioned showed that the capacity of the future yard would not exceed 85 000 cgt. The yard was constructed according to these plans and its layout has not been changed afterwards. The unforeseeably high increase of productivity during the last couple of years cannot change this assessment.
- (45) An exclusively formal position as regards the capacity limitation would mean, taking into account the unforeseeably high increase in productivity, that the yard could not operate the whole year. An artificial idle running of the undertaking would question the economic success of the restructuring. Due to the productivity and the production mix (large container ships), a temporary exceeding of the capacity limitation is unavoidable, but this excess will be equalised during the period of several years.

IV. Comments from Germany

- (42) Germany concentrates in its comments on four main arguments. Firstly, it states that the method of cgt-calculation served originally the purpose of collecting national data comparable in economic terms. It is an inadequate method for measuring a capacity limitation of an individual yard. This becomes particularly evident when the production of KWW is looked at more closely. To the disadvantage of the yard, the so-called serial-effect is not taken into account in the conventional cgt-calculation. Building sister-ships uses in fact less capacity than calculated, since less working hours are needed to build the second, similar ship. In the years 1997 to 1999 KWW built among others two series of ships and altogether the serial-effect reduced the actual working hours in a way, which reduced the cgt-values considerably. In addition, in the context of the restructuring a considerable amount of work was
- (46) The third argument of Germany is that the successful bidding of KWW for the offshore contract (drilling rig) has caused the temporary exceeding of capacity limitation, since building the rig would block the dock for a long time and the ships under construction would therefore need to be built ahead of schedule. This exceeding of the capacity limitation, though, has no negative effect on the European shipbuilding market since KWW has achieved the offshore contract without any European competition. In addition, the capacity limitation concerns only the shipbuilding sector and not offshore business and therefore the Commission's reference to the possibility of other yards to penetrate into the offshore market is irrelevant. The application of provisions as regards the shipbuilding sector cannot be extended to other economic sectors only on the basis of assumed or factual behaviour of other participants on the market.

- (47) The fourth argument of Germany points out that as laid down in its letter of 23 December 1998 to the Commission, KWW was allocated an additional capacity of 22 000 cgt for year 1998, so that, taking into account the serial-effect, KWW will not exceed the total capacity of 107 000 cgt allocated to it for 1998. As a countermove, KWW was earlier demanded by *Bundesveranstalt für vereinigungsbedingte Sonderaufgaben* (hereinafter referred to as BvS) to repay part of the aid granted to it for fresh equity capital and investments in the context of the privatisation. Consequently, KWW paid on 23 December 1998, without recognising thereby any legal obligation, a partial amount of DEM 12 million to a blocked account until the final Commission decision.

V. Assessment

- (48) The Commission notes that the aid approved in compliance with the provisions of Council Directive 90/684/EEC on aid to shipbuilding and Directive 92/68/EEC amending Directive 90/684/EEC is considered as being compatible with the common market as it complied with Article 87(3)(e) of the EC Treaty. However, this applies only so long as the conditions laid down in the Commission decisions approving the aid in accordance with the above Directives are respected. Should the conditions for approving the aid not be complied with, the aid falls under the general prohibition of Article 87(1) of the EC Treaty and may therefore be considered incompatible with the common market, unless it can be declared compatible for other reasons.
- (49) Directive 92/68/EEC amending Directive 90/684/EEC contains a derogation from the rules on operating aid applicable to other Community yards for the shipyards in the former GDR in order to create the possibility for these yards to undergo urgent and comprehensive restructuring and to become competitive. According to Article 10a(2) of Directive 90/684/EEC as amended by Directive 92/68/EEC, until 31 December 1993, operating aid for the shipbuilding and ship conversion activities of the yards situated in the former GDR may be considered compatible with the common market under certain conditions relating to the amount of aid and an annual reporting obligation of the German Government. One of the conditions laid down in this provision is the agreement of the German Government to carry out before 31 December 1995 a genuine and irreversible reduction of 40 % of the shipbuilding capacity of 545 000 cgt existing on 1 July 1990.
- (50) Investment aid is regulated in Article 6 of Directive 90/684/EEC and closure aid in its Article 7. According to Article 6(1), investment aid may not be granted for investment in existing yards unless it is linked to a restructuring plan which does not involve any increase in the shipbuilding capacity of the yard or unless it is

directly linked to a corresponding irreversible reduction of capacity of other yards in the same Member State over the same period. Article 6(3) provides that investment aid may be deemed compatible with the common market provided that the amount and intensity of such aid is justified by the extent of the restructuring involved. According to Article 7, aid to defray the normal costs resulting from the partial or total closure of shipbuilding or ship-repair yards may be considered compatible with the common market provided that the capacity reduction resulting from such aid is of a genuine and irreversible nature.

- (51) In the Commission proposal for Council Directive 92/68/EEC providing changes to the Seventh Directive on aid to shipbuilding, it is stated that taking into account the impact of the restructuring on conditions of competition in the Community, balance has to be found between the restructuring of the former GDR shipbuilding industry, which is only possible with the support of a substantial amount of state aid and the possible negative influence on the competition conditions of other Community yards resulting from this aid. The possibility of giving extra aid above the current ceilings has to be met by accompanying restructuring and capacity reductions.
- (52) One of the conditions laid down in Article 10a(2) of Directive 90/684/EEC for the compatibility of the operating aid with the common market is the agreement of the German Government to carry out before 31 December 1995 a genuine and irreversible reduction of 40 % of the shipbuilding capacity of 545 000 cgt existing on 1 July 1990. The corresponding maximum overall capacity for the shipyards situated and operating in the territories of the former German Democratic Republic amount therefore to 327 000 cgt. Germany distributed this total capacity to the five remaining new building yards. In this context the capacity for KWW was set at 85 000 cgt⁽⁸⁾.
- (53) In its letter of 27 November 1992 to the Commission on the privatisation of Warnow Werft, Germany states that Kvaerner had contractually committed itself not to exceed the capacity of 85 000 cgt foreseen for KWW before 1 January 2006. It is noted that paragraph 27 of the privatisation contract of Warnow Werft, titled 'Limitation on Future Building Capacities', reads as follows: 'Kvaerner undertakes up until 31 December 2005 with regard to Warnow yard not to exceed its annual building capacity of 85 000 cgt unless the requirements based on the EEC Treaty are less restrictive from time to time.'
- (54) The Commission notes that the subsequently notified aid programme for the restructuring of the Warnow Werft yard was based on this annual capacity.

⁽⁸⁾ The Commission recalls that the Court of First Instance confirmed the importance of the allocation of capacities to the individual yards for the legality of the aid decision in case T-266/94 of 22 October 1996 (paragraphs 151 to 198).

- (55) The total amount of EUR 623,45 million (DEM 1 246,9 million) of restructuring aid was approved in four tranches in five separate Commission decisions. The first decision releasing the first tranche of aid was communicated to Germany by a letter of 3 March 1993 (N 692/D/91). In this decision it is stated that although the independent technical study mandated by the Commission had established that the new building capacity of Warnow Werft is unlikely to exceed the 85 000 cgt set by the German Government as the contribution of this yard to the maximum available East German capacity of 327 000 cgt, future monitoring is deemed necessary during the implementation of the investment programme in order to ensure that the reduction of the shipbuilding capacity is carried out.
- (56) The second decision was communicated to Germany in the letter dated 17 January 1994 (N 692/J/91). In this decision the same provision as the one mentioned above was laid down, with the difference that further monitoring was deemed necessary in order to ensure that the restriction of the shipbuilding capacity is respected. In addition, the German Government was reminded of the fact that non-compliance with the capacity limitation would oblige the Commission to request reimbursement of all aid.
- (57) In the third decision, communicated to Germany in the letter dated 20 February 1995 (N 1/95), it was again stated that further monitoring of the compliance with the capacity limitation is still needed. In addition, it was stated that the German Government had ensured that the yard would comply with its capacity limitation. The German Government was as well reminded of the fact that non-compliance with the capacity limitation would oblige the Commission to request reimbursement of all aid.
- (58) The fourth decision was communicated to Germany in the letter of 18 October 1995 (N 637/95) and the fifth in the letter of 11 December 1995 (N 797/95). In both decisions it was provided that further monitoring will be necessary to ensure that the actual and planned production respects the capacity limit. The same remarks as above on Germany's assurance that the capacity limitation will be complied with by the yard and on the possibility of reimbursement of all aid in case of non-compliance were repeated in the decisions.
- (59) The Commission notes that the annual capacity limitation of 85 000 cgt was one of the main conditions for the approval of the aid. The aid was approved on the basis of the restructuring notified to the Commission. This annual limitation was taken into the privatisation contract of Warnow Werft, which was approved by the Commission as part of the restructuring programme. In addition, the obligation to comply with the capacity limitation of 85 000 cgt was expressly mentioned in all other Commission decisions approving the aid except the first one, dated 3 March 1993. In these decisions it was also expressly stated that in case of non-compliance with this capacity limitation the Commission would be obliged to request for the reimbursement of all aid.
- (60) In the monitoring visit to the yard on 24 March 1999 it was confirmed that the production of KWW was 122 414 cgt in 1998. The production figures were discussed with the management of the yard in the presence of German authorities and these figures, as being based on the cgt-calculation method, were not contested by any of the parties. Consequently, the figures are considered as confirmed and incontestable. This means that KWW has exceeded its annual capacity limitation of 85 000 cgt by 37 414 cgt in 1998.
- (61) The Commission notes that the overall capacity limitation set by Article 10a of Directive 90/684/EEC for all former East German yards is 327 000 cgt. According to Article 10a(2)(c), the reduction of the overall capacity is to be 'genuine and irreversible'. The Court of First Instance has confirmed the Commission's interpretation of the notion of 'irreversibility' in its judgment of 22 October 1996⁽⁹⁾ as meaning that, with the Commission's agreement, capacity may be increased five years after the end of restructuring and in the absence of such agreement, it may be increased ten years thereafter. The Court stated that this notion shall be interpreted in the light of other provisions of Directive 90/684/EEC, such as its Article 7. Since the restructuring ended end 1995, the period of this capacity limitation is until end 2000 and 2005 respectively.
- (62) Germany allocated the overall capacity of 327 000 cgt between the five former East German yards as follows: KWW — 85 000 cgt; Volkswerft Stralsund — 85 000 cgt; MTW-Schiffswerft — 100 000 cgt; Peene-Werft 35 000 cgt and Elbwerft Boizenburg — 22 000 cgt. According to the monitoring report dated 22 February 1999 the production of Volkswerft was 84 805 cgt in 1998 and that of MTW-Schiffswerft 99 997 cgt. According to the results of the monitoring visit to Peene-Werft on 26 March 1999, the production of this yard was 34 037 cgt in 1998. As regards Elbwerft Boizenburg, the yard was closed end 1997. Germany informed the Commission with its letter of 17 November 1998 that they withdrew their notification as regards restructuring aid to the yard and closed it permanently. It is noted that Elbwerft Boizenburg produced 0 cgt in 1998. Consequently, the production of yards other than KWW in 1998 amounts to 218 839 cgt.
- (63) The Commission notes that the total unused capacity of other yards within their respective capacity limits was 23 161 cgt. Yet KWW has exceeded its annual capacity limitation of 85 000 cgt by 37 414 cgt in 1998. Consequently, due to the considerable exceeding by KWW of its capacity limitation in 1998, Germany has exceeded the overall capacity limitation of 327 000 cgt set for all former East German yards by 14 253 cgt in 1998.
- ⁽⁹⁾ Case T/266/94, Skibsværftsforeningen and others v. the Commission, ECR 1996 II, p. 1399.

- (64) According to the judgment of the Court of Justice of 18 May 1993 in joined cases C-356/90 and C-180/91 (Belgium/Commission)⁽¹⁰⁾, the compliance with the ceiling set pursuant to the provisions of the Council Directive setting the criteria for derogation from the prohibition of aid in Article 92 of the Treaty is the essential condition for aid to shipbuilding to be regarded as compatible with the common market and, where that ceiling is exceeded, the aid in question is automatically incompatible. In this context the Commission's role is limited to checking that that condition has been observed.
- (65) The Commission notes that an essential condition for the approval of aid, that is the compliance with the annual capacity limitation of 85 000 cgt as laid down in the Commission decisions approving the aid in accordance with Directive 90/684/EEC as amended by Directive 92/68/EEC, has not been respected in 1998. In addition, the Commission also notes that as regards 1998, Germany was in breach of Article 10a(2) of Council Directive 90/684/EEC laying down the overall capacity limitation for all former East German yards as a condition under which operating aid for the shipbuilding and ship conversion activities may be considered compatible with the common market.
- (66) The Commission notes that this decision addresses firstly, the breach of the individual capacity limitation of 85 000 cgt and secondly, the breach of overall capacity limitation of 327 000 cgt. The Commission stresses that the individual annual capacity limitation of 85 000 cgt was set in the five Commission decisions approving the aid as a condition for the compatibility of that aid with the common market. This annual limit was also acknowledged by Kvaerner as part of the privatisation contract and its compliance is both subject to monitoring by the Commission and to an annual reporting obligation by the yard. Moreover, the state aid concerned in this case is the lawfulness of the very aid approved by the Commission in its five decisions under the condition of the annual capacity limitation and the distortive effect of this aid on the shipbuilding sector.
- (67) For these reasons the Commission considers the considerable breach of the individual annual capacity limitation of 85 000 cgt as the main subject of this decision and therefore the consequences of exceeding the capacity limitation are decided on this basis. The exceeding of the overall capacity limit is a subsidiary consequence, even if a serious one, of the exceeding of the individual limit.
- (68) The objective of Council Directive 92/68/EEC was to allow the urgent and comprehensive restructuring of the shipbuilding industry in former GDR in order for it to become competitive. The Commission acknowledges that capacity limitations were introduced in this context in order to offset the distortive effect the state aid granted to the East German shipyards has on competition in this sector. It also stresses that when this capacity limitation, as a compensating factor and as an essential condition for approval of the aid and thereby for the compatibility of the aid with the common market, is not complied with, the aid is rendered incompatible with the common market.
- (69) The Commission notes that in its decision concerning aid to MTW-Schiffswerft and Volkswerft Stralsund⁽¹¹⁾ the Commission concluded that MTW had slightly exceeded its capacity limitation in 1996. The compensation for this excess was determined on the basis that MTW had to reduce its production correspondingly the following year and the amount of the operating aid to be granted to it the following year was reduced by an amount that corresponded to the excess. Consequently, the consequences of the excess were determined on the basis of the scale of the excess production in question, matching the financial consequences of this breach to the gravity of it, that is to the amount of the excess.
- (70) The Commission notes that the purpose of the notion on the recovery of aid in case of non-respect of the conditions set for the approval of aid in the Commission decision is to remind the recipient of the aid of its obligation to comply with these conditions and to make the consequences of the non-compliance clear. The aim and actual effect of recovery of aid is to seek to re-create the status quo *ex-ante* by annulling the negative effect on competition caused by the illegal aid, the illegality of which is caused by the non-compliance with the conditions set for the approval of the aid and thereby for its compatibility with the common market. In this case the condition breached is the capacity limitation. Consequently, and following the reasoning of the Commission decision concerning aid to MTW-Schiffswerft and Volkswerft Stralsund⁽¹²⁾, the scale of exceeding the capacity limitation indicates the scale of distortion of competition in question.
- (71) Since the scale of exceeding the capacity limitation indicates the scale of distortion of competition in question, the Commission considers that the amount of aid, which corresponds to the exceeding of the capacity limitation, is to be considered incompatible with the common market.
- (72) The Commission notes that aid which is incompatible with the common market shall be recovered.
- (73) The Commission notes that in its decisions communicated to Germany with letters of 17 January 1994, 20 February 1995, 18 October 1995 and 11 December 1995 it stated that the Commission will be obliged to demand the recovery of all aid if the restriction of capacity is not complied with.

⁽¹⁰⁾ ECR 1993 I, page 2323.

⁽¹¹⁾ OJ C 344, 14.11.1997, p. 2.

⁽¹²⁾ OJ C 344, 14.11.1997, p. 2.

- (74) Following the reasoning in the judgment of the Court of First Instance in case T-140/95 of 15 September 1998⁽¹³⁾ (Ryanair/Commission), it should be examined whether by declaring only the amount of aid, which corresponds to the exceeding of the capacity limitation, as incompatible with the common market and thereby subject to recovery, the Commission departs from the scope of its previous decisions on granting the aid in which it stated that the Commission will be obliged to demand the recovery of all aid if the restriction of capacity is not complied with.
- (75) The Commission notes that the aim and actual effect of recovery of aid is to seek to re-create the status quo *ex-ante* by annulling the negative effect on competition caused by the illegal aid. Following the reasoning of the Commission decision concerning aid to MTW-Schiffswerft and Volkswerft Stralsund⁽¹⁴⁾, the scale of exceeding the capacity limitation indicates the scale of distortion of competition in question.
- (76) Since the amount of aid which corresponds to the excess of the capacity limitation is declared incompatible it is subject to recovery. The recovery seeks to annul the negative effects of the exceeding of the capacity limitation on the competition, whereby the purpose and actual effect of the recovery are fulfilled.
- (77) Therefore the Commission considers that by declaring the amount of aid, which corresponds to the exceeding of the capacity limitation, as incompatible with the common market in this case it does not depart from the scope of the conditions of its previous decisions in a way that would have an effect on aim, purpose and effect of those conditions, the seeking to annul the negative effect on competition.
- (78) Therefore, the Commission concludes that the part of the aid of EUR 623,45 million (DEM 1 246,9 million) granted to Kvaerner Warnow Werft and approved by the Commission in four tranches with its decisions communicated to Germany with its letters of 3 March 1993 (N 692/D/91), 17 January 1994 (N 692/J/91), 20 February 1995 (N 1/95), 18 October 1995 (N 637/95) and 11 December 1995 (N 797/95), which corresponds to the exceeding of the annual capacity limitation of 85 000 cgt by 37 414 cgt, is no longer compatible with Article 87(3)(e) of the EC Treaty and therefore incompatible with the common market pursuant to Article 87(1) of the EC Treaty.
- (79) In their comments, both Germany and KWW contest the Commission's observation that an annual capacity limitation of 85 000 cgt was the main condition for approval of the aid. They claim that a condition for the approval was only that the approved and examined production facilities would be kept in accordance with the restructuring programme and investment plans.
- (80) The Commission notes that both the compliance with the investment programme and respecting the capacity limitation are conditions for approval of the aid. It is a constant practice of the Commission in all restructuring aid cases to approve the investment plan and monitor its compliance. Nevertheless, this does not change the fact that another essential condition for the approval of the aid was the compliance with the annual capacity limitation. The total amount of aid was approved in five separate Commission decisions, in four of which it is expressly mentioned that monitoring is necessary in order to ensure that the restriction of the shipbuilding capacity is respected. In addition, in four of these five decisions Germany is reminded of the fact that in case of non-compliance with the capacity limitation the Commission would be obliged to request reimbursement of the aid in question. In three of these decisions it is stated that the German Government had ensured that the yard would comply with its capacity limitation. Consequently, there is no doubt about the capacity limitation of 85 000 cgt being a condition for the approval of the aid and for the compatibility of the aid with the common market.
- (81) The second argument raised by KWW in its comments is that according to the wording of Article 10a(2)(c) of Directive 90/684/EEC and the Commission decisions approving the aid, the capacity gains due to productivity increase above the level foreseen by the Commission expert as until the end of the restructuring period, should be allowed to the yards. Capacity limitation and production limitation are different concepts and KWW did not understand the limitation as a production limitation.
- (82) The Commission notes that KWW had titled its production report of first half of 1995, submitted to the Commission by Germany with its letter of 16 August 1995, as 'Report on respecting the capacity limitation' (*Bericht über Einhaltung der Kapazitätsbeschränkungen*). It titled its report of 1996, submitted to the Commission by Germany with its letter of 17 February 1997, as 'Production limitation by EU-Commission' (*Produktionsbeschränkung durch EU-Kommission*). Moreover, the Commission had in its letters of 18 and 19 November 1996 to Germany requested it to inform the yards to strictly respect their capacity limitations in 1996 and in the following years.
- (83) In its letter of 3 March 1997 to Germany the Commission points out that KWW had exceeded its capacity limitation slightly in 1996 and that the planned production for 1997 is also very close to the limit. It asks Germany to take the necessary measures to correct the situation. In its letter of 14 April 1997 to Germany the Commission once again asks Germany to intervene to see that the yard changes its production plan in order not to exceed its capacity limit.
- (84) In its letter to the Commission of 1 April 1997, Germany states that BvS has demanded KWW to

⁽¹³⁾ ECR 1998 II, page 3327.

⁽¹⁴⁾ OJ C 344, 14.11.1997, p. 2.

respect its capacity limitation of 85 000 cgt when planning its production of 1997. As a result of this, KWW would submit a new plan for 1997 where the capacity limit is respected. Further, in its letter of 6 June 1997 to the Commission, Germany explains that the capacity of KWW in 1997 will be reduced by the amount of the slight excess of 1996, 92 cgt, so that in 1997 it would have a reduced capacity limit. Germany stressed that this was a non-recurring situation and in general division of capacity between different years to compensate excess was not possible. This was clearly explained to the yard as well. Germany also states that it had explained to the yard that even slight excesses of capacity limitation cannot be accepted in the future and that KWW had committed itself to deduct the 92 cgt exceeding of its capacity limitation in 1996 from its capacity of 1997.

(85) Considering the above, the Commission notes that there is no doubt about the fact that KWW has been very well aware of the nature and meaning of the capacity limitation of 85 000 cgt imposed on it.

(86) The fourth point raised by KWW is that the capacity limitation, if seen as a production limitation, should be considered as an average production of several years.

(87) The Commission notes that an annual capacity limitation was an essential condition for approval of the aid. This limit was set in order to offset the distortive effect of the aid on the shipbuilding industry and cannot be interpreted as an average annual target since this would deprive the limit of its purpose and effect. Moreover, the annual capacity limitation is clearly laid down in point 27 of the privatisation contract of the yard and accepted by KWW who is under the obligation to plan its production accordingly. The obligation to respect the annual capacity limit and the fact that dividing capacity between several years is not possible was clarified to KWW by Germany in 1997, according to Germany's letter on 6 June 1997 to the Commission.

(88) The last argument of KWW is that there is no legal basis for laying down the maximum capacity limit for individual yards.

(89) The Commission notes that it has in its decisions on the approval of restructuring aid to KWW laid down an annual capacity limitation of 85 000 cgt as a condition for the approval of the aid. It is normal practice for the Commission to attach to its decision on state aid conditions that would ensure the compatibility of that aid with the common market pursuant to Article 87 of the EC Treaty. By doing so the Commission acts in accordance with the Articles 87 and 88 of the EC Treaty, and in this present case the relevant specific rules on aid to shipbuilding.

(90) Germany argues in its comments that the cgt-calculation method is an inadequate method for measuring a capacity limitation of an individual yard.

(91) The Commission notes that the capacities of the East German yards before the restructuring were defined using cgt-calculation. In 1992 when the proposal for Directive 92/68/EEC⁽¹⁵⁾ was discussed at the Council and the whole restructuring of the East German shipyards and its modalities were examined in detail, the capacity reductions of these yards were defined using cgt-calculations as well. Consequently, the Council has in 1992 confirmed this calculation method as a basis of defining the capacities in the context of the restructuring of the East German yards.

(92) The Commission also notes that cgt-calculation was agreed between Germany and the Commission as a basis of the reporting in context of the monitoring of former GDR yards. Germany confirms this in its letters of 12 July 1994 and 3 April 1995 to the Commission. In the letter of 3 April 1995 Germany states that 'Germany and the Commission have reached agreement on the fact that the monitoring of production will be based on cgt-calculation based on coefficients in force before 1 January 1994'. This method has been used from the beginning of the restructuring and during the whole monitoring period and as regards all monitored yards. Germany has agreed on its application without ever contesting its application. The Commission sees no reason to speculate on the adequacy of this method on the basis of one yard breaching its capacity limitation.

(93) Both Germany and KWW argue in their comments that the exceeding by KWW of its capacity limitation has no negative effect on competition.

(94) The Commission notes that the very purpose of the capacity limitation is to offset the distortive effect the aid has on the European shipbuilding industry. Consequently, exceeding this limit already implies a distortion of competition.

(95) The Commission also notes that KWW operates in the market where other European yards operate. KWW itself confirms this in its comments by stating that due to building of the drilling rig it cannot compete in the European market and bid for contracts on products which other European yards build for a time period of two years. Consequently, by exceeding its capacity limitation set to offset the distortion of competition KWW has acted detrimentally to other yards in this market.

⁽¹⁵⁾ SEC (92) 991 final.

- (96) This position of the Commission is reinforced by the comments of interested parties. These indicate in their comments that the large container ships being built by KWW and partly causing the excess are the kind of ships also being built by other European yards. Consequently, the excess of KWW has a direct impact on the market where other European yards operate. They also stipulate that the capacity limitations of former East German yards are, among other factors, a basis for investment and production planning of other yards. Therefore the dispositions of other yards are affected if these limits are exceeded.
- (97) The last point raised by Germany in its comments is that KWW was allocated an additional capacity of 22 000 cgt for 1998, so that taking into account this factor and the serial-effect, KWW's capacity does not exceed 107 000 cgt allocated for it for 1998.
- (98) The Commission notes that any changes of allocation of capacity would need the consent of the Commission since the capacity limits are linked with the restructuring aid granted to the respective yards. In this case, the Commission has not approved an allocation of additional capacity of 22 000 cgt for KWW for 1998. In its letter of 4 December 1998 the Commission has communicated to Germany, that a capacity of 22 000 cgt of the Elbewerft yard cannot be reallocated as regards year 1998 since that capacity was not available for reallocation for the whole year but only from 17 November 1998 onwards when the notification for aid to the yard was withdrawn. In addition, it was the Commission's constant practice not to accept a retroactive reallocation of capacity. This was further confirmed by the Commission's letter of 8 January 1999 to Germany on the issue.
- (99) For these reasons, and because there is no legal basis for retroactive reallocations, the statement of Germany according to which the additional capacity of 22 000 cgt has been allocated to KWW for 1998 has no legal effect and is of no relevance for this procedure.
- (100) For the reasons explained above in points 48 to 77, the Commission concludes that since the part of the aid of EUR 623,45 million (DEM 1 246,9 million) granted to Kvaerner Warnow Werft and approved by the Commission in four tranches with its decisions communicated to Germany with the letters of 3 March 1993 (N 692/D/91), 17 January 1994 (N 692/J/91), 20 February 1995 (N 1/95), 18 October 1995 (N 637/95) and 11 December 1995 (N 797/95), which corresponds to the exceeding of the annual capacity limitation of 85 000 cgt by 37 414 cgt, is no longer compatible with Article 87(3)(e) of the EC Treaty. As no other basis of compatibility exists or has indeed been invoked by Germany or KWW, this part of the aid is incompatible with the common market pursuant to Article 87(1) of the EC Treaty.
- (101) The Commission has considered various options in determining the amount of the incompatible aid and has concluded the following.
- (102) The Commission notes that the duration of KWW's annual capacity limitation of 85 000 cgt is 10 years. Considering that the capacity limitation was exceeded in one year, in 1998, the Commission could have decided to determine the amount of unlawful aid solely on this basis. That would have led to the result that 1/10 of the aid would have been considered incompatible with the common market. On the other hand, it would also have been possible to calculate the proportion of the excess of 37 414 cgt to the total of the capacity limitation during the 10-year period (850 000 cgt) which would have given the proportion of 4,4 % as the amount of illegal aid.
- (103) The Commission has come to the conclusion that both the above methods are insufficient in order to determine the amount of unlawful aid, since they do not take into account the proportion in which the annual capacity limitation of 85 000 cgt is exceeded. In order to take this element into account the Commission has based its calculation on the combination of the pure proportional approach and a supplementary part which addresses the aggravated distortion of competition caused by the considerable amount of exceeding the annual capacity limitation in this case.
- (104) Since the duration of KWW's annual capacity limitation of 85 000 cgt is ten years, the proportion of the excess of 37 414 cgt to the total of the capacity limitation during this period (850 000 cgt) has been calculated, leading to the proportion of 4,4 %. In addition to this, the considerable exceeding of the capacity limitation in 1998 needs to be addressed since the Commission considers that the distortion of competition caused by the excess increases the greater the excess. Since the amount of excess of 37 414 cgt exceeds the yearly capacity limitation by more than 20 %, this additional element having impact on the level of distortion of competition has been taken into account in the calculation as well. This has been done by calculating the proportion of the amount of excess exceeding 20 % of the annual limitation (20 414 cgt) to the total of the capacity limitation (850 000 cgt), which gives the proportion of 2,4 %.
- (105) Consequently, the amount of the incompatible aid is the proportion of the total of the excess and the additional element linked to the greater distortion of competition caused by the excess of more than 20 % of the annual capacity limitation, to the total of the

capacity limitation calculated on the basis of all operating aid EUR 372,5 million (DEM 745 million) and investment aid EUR 237,45 million (DEM 474,9 million), altogether EUR 609,95 million (DEM 1 219,9 million) paid to KWW. Consequently, the amount of the aid which is considered incompatible with the common market on the basis of KWW's exceeding of its capacity limitation in 1998 is EUR 41,5 million (DEM 83,0 million). This aid shall be recovered.

(106) The Commission notes that in its decision to open the procedure⁽¹⁶⁾ in this case, it stated that the closure aid of EUR 13,5 million (DEM 27 million), approved by the Commission in its decision communicated to Germany with its letter of 3 March 1993, has been paid to finance the redundancy pay and other social measures in favour of former workers. As the yard had passed such monies to its former employees, the Commission would not seek the recovery of this amount. For this reason the closure aid is not included in the above calculation.

(107) The Commission stresses that the sums to be recovered shall bear interest from the date on which they were made available to the recipient until their actual recovery. The recovery shall be effected in accordance with the procedures of national law and the interest shall be calculated on the basis of the reference rate used for calculating the grant-equivalent of regional aids.

VI. Conclusions

(108) The Commission concludes that Kvaerner Warnow Werft GmbH has in 1998 exceeded its annual capacity limitation of 85 000 cgt by 37 414 cgt. This annual capacity limitation was set by the Commission in its decisions communicated to Germany with the letters of 3 March 1993, 17 January 1994, 20 February 1995, 18 October 1995 and 11 December 1995 as an essential condition for approval of a total of EUR 623,45 million (DEM 1 246,9 million) aid in accordance with Directive 90/684/EEC on aid to shipbuilding and 92/68/EEC amending Directive 90/684/EEC on aid to shipbuilding and thereby for the compatibility of the aid with the common market pursuant to Article 87(3)(e) of the EC Treaty.

(109) Since it is the opinion of the Commission that the scale of exceeding the capacity limitation indicates the scale of distortion of competition in question, the Commission considers that the amount of aid, which

corresponds to the exceeding of the capacity limitation of 85 000 cgt by 37 414 cgt in 1998, is no longer compatible with Article 87(3)(e) of the EC Treaty and thereby incompatible with the common market pursuant to Article 87(1) of the EC Treaty.

(110) Therefore, the aid of EUR 41,5 million (DEM 83,0 million) is incompatible with the common market and shall be recovered. The sums to be recovered shall bear interest from the date on which they were made available to the recipient until their actual recovery,

HAS ADOPTED THIS DECISION:

Article 1

The state aid, which Germany has implemented in favour of Kvaerner Warnow Werft GmbH in an amount of EUR 41,5 million (DEM 83,0 million), is incompatible with the common market pursuant to Article 87(1) of the EC Treaty.

Article 2

1. Germany shall take the necessary measures to recover from the recipient the aid of EUR 41,5 million (DEM 83,0 million).

2. Without prejudice to any order of the Court of Justice of the European Communities pursuant to Article 242 of the Treaty, recovery shall be effected without delay and in accordance with the procedures under German law, provided that it allows the immediate and effective execution of the Commission's decision. To this effect and in the event of a procedure before German courts, Germany shall take all necessary steps which are available in its legal system, including provisional measures, without prejudice to Community law⁽¹⁷⁾.

3. The sums to be recovered shall bear interest from the date on which they were made available to the recipient until their actual recovery. Interest shall be calculated on the basis of the reference rate used for calculating the grant-equivalent of regional aids.

⁽¹⁶⁾ OJ C 41, 16.2.1999, p. 23.

⁽¹⁷⁾ See Article 14(3) of Council Regulation (EC) 659/1999, OJ L 83, 27.3.1999, p. 1.

Article 3

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

Article 4

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 8 July 1999.

For the Commission

Karel VAN MIERT

Member of the Commission

COMMISSION DECISION
of 20 July 1999
concerning presumed aid allegedly granted by France to Sécuripost

[notified under document number C(1999) 2537]

(Only the French text is authentic)

(Text with EEA relevance)

(1999/676/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

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

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

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

Whereas:

I. Facts and procedure

- (1) The judgment of the Court of First Instance (CFI) of 28 September 1995 in Case T-95/94⁽¹⁾ annulled the Commission decision of 31 December 1993, by which it had declared that various measures affecting the French post office's subsidiary Sécuripost, a firm operating on the market for the secure transportation of moneys, and about which a complaint had been lodged by the *Chambre syndicale nationale des entreprises de transport de fonds et de valeurs* (Sytraval) and by Brink's France SARL (Brink's) did not constitute state aid within the meaning of Article 87 (formerly Article 92) of the Treaty. The Commission brought an appeal against this judgment but this was dismissed in its entirety by the Court of Justice on 2 April 1998 in Case C 367/95P⁽²⁾. The Court acknowledged that the pleas put forward by the Commission in support of its appeal were partly founded. However, it also held that the contested decision was marred by deficiencies in the reasons given which were in themselves sufficient to justify its annulment.
- (2) It should be noted that the original complainants (Sytraval and Brink's) did not take part in the appeal.
- (3) The file which is the subject of the present decision concerns the measures taken by the French State, either directly or through the post office, to assist Sécuripost prior to its transfer to the private sector, authorised by the French Government in 1993. On account of an

inadequate statement of reasons on a number of points, the Court of First Instance judgment annulled the Commission decision of 31 December 1993 finding that no state aid was involved. Consequently, the Commission initiated the procedure under Article 88(2) (formerly Article 93(2)) of the Treaty in respect of the measures concerned by those points, so as to examine them in the light of Articles 87 and 88 of the Treaty and to decide whether they were compatible with the common market.

- (4) The decision initiating the procedure was published on 22 October 1996 in the *Official Journal of the European Communities*⁽³⁾, giving notice to the other Member States and interested parties to submit their comments on the measures concerned to the Commission within one month of the date of publication.
- (5) In that decision, the Commission called on the French authorities to provide, *inter alia*, all the data on the aspects highlighted by the Court of First Instance and to send any other information and observations they considered relevant in the light of the Sytraval judgment in order that the Commission could assess the measures in question pursuant to Articles 87 and 88 of the Treaty.
- (6) The French authorities were informed of the Commission decision to initiate the procedure by letter of 26 June 1996. By letter of 12 September 1996, they sent the Commission a note providing a range of information on the points raised by it when it initiated the procedure. Additional information was provided, at the Commission's request, in a number of subsequent letters. The last of these letters reached the Commission on 28 October 1998.
- (7) The complainants did not intervene during the procedure and did not submit any comments. No other interested party or Member State besides France submitted comments.

⁽¹⁾ [1995] ECR II-2651.

⁽²⁾ [1998] ECR I-1719.

⁽³⁾ OJ C 311, 22.10.1996, p. 12.

II. The measures concerned

- (8) The points in the Commission decision of 31 December 1993 which were raised by the Court of First Instance related to the following measures.
- (a) *Secondment of officials to Sécupost*
- (9) The Court of First Instance held that the fact that the officials seconded to Sécupost by the post office may at any time be reassigned to the department originally employing them if staff reductions prove necessary in the undertaking to which they are seconded, without that undertaking having to pay in such circumstances any compensation for redundancy whatsoever, constitutes an objection to which the Commission did not respond, resulting in an inadequate statement of reasons.
- (b) *Absence of contributions by Sécupost to unemployment insurance funds*
- (10) The Court of First Instance concluded that, on this point, the reasons given in the contested decision were inadequate in so far as the Commission acknowledges that 'no contributions need to be made to unemployment insurance funds in respect of the employment of officials on secondment, since their employment is guaranteed by their status as officials'. Since it did not explain why this difference between the system applicable to Sécupost and that applicable to its competitors did not constitute aid, the Commission's statement of reasons was inadequate.
- (c) *Placing of premises at Sécupost's disposal*
- (11) The Court of First Instance held that 'Sécupost's premises are made available to it within the framework of the special system of precarious occupancy, and that, in its decision, the Commission provided no details regarding either the rents actually charged to Sécupost, or those which Sécupost's competitors have to pay for comparable premises'. The Commission did not therefore compare the rents actually charged to Sécupost and those payable by its competitors for comparable premises, which the Court of Justice considered to be a manifest error of assessment.
- (d) *Maintenance of Sécupost vehicles by SNAG*
- (12) The Court of First Instance held that the fact that SNAG (the post office's workshop and garage service) uses an invoicing system similar to that used by private garages was insufficient to rule out the presence of state aid under the Treaty.
- (13) It reproached the Commission for not having examined whether or not the rates charged disclose the existence of state aid. Its judgment calls for a comparison of the rates charged by SNAG and the rates charged by private garages for similar services. The Court of Justice confirmed the CFI's analysis, considering that the Commission had committed a manifest error of assessment.
- (e) *Loan of FRF 15 million granted to Sécupost for the financial year 1989*
- (14) The Court of First Instance considered inadequately reasoned the Commission's statement that the loan was granted within the framework of a global agreement between the companies in the Sofipost group and that the interest rate applied was half a percentage point higher than the bank base rate.
- (15) The Court of First Instance explained that 'the fact that the transaction was of a commercial nature is not in itself sufficient to show that it does not amount to state aid within the meaning of Article 92 of the Treaty, since such a transaction may none the less be effected at a rate which gives Sécupost a special advantage by comparison with its competitors'.
- (16) The Commission should therefore have examined whether the rate applied was in line with the market rate and, since it did not do so, the Court of Justice considered that it had committed a manifest error of assessment.
- (f) *Rates charged by Sécupost to the post office*
- (17) The Court of First Instance reproached the Commission because it had 'merely compared the prices charged with the provision of services to the post office and to Casino, (...) the comparison was based solely on the information relating to 1993, and (...) no attempt was made to justify or clarify it.... Furthermore, there was a steady fall in the rates charged by Sécupost to the post office between 1987 and 1993, in accordance, in particular, with the framework agreement between the post office and Sécupost of 30 September 1987, thus further magnifying the differences cited by the applicants'. In addition, 'In the absence of any details regarding the rates charged by Sécupost to the post office and to other customers in 1987, 1988, 1989, 1990, 1991 and 1992, the Court considers that it does not have at its disposal the requisite information enabling it to review the validity of the contested decision...'. The Court of Justice confirmed this analysis, considering that the Commission had committed a manifest error of assessment on this point.

III. The information provided by the French authorities

(a) *Secondment of officials to Sécupost*

(18) The French authorities maintain, first of all, that recruitment of officials gave rise to an overall additional cost, between 1988 and 1991, of some (...) compared with what would have been the situation if Sécupost had taken on employees on private-law contracts only. This was because of the much higher salaries paid to the seconded officials than would have been paid to staff employed on contracts subject to private law (for example, in 1990 the average monthly salary exclusive of social security contributions paid to an official working for Sécupost as a transporter of moneys was (...) as opposed to (...) paid to a Sécupost transporter of moneys employed under a private-law contract).

(19) As regards the cost of reassigning to their original department officials seconded by the post office to Sécupost, the French authorities explained that such reassignment gave rise to payment by Sécupost to the officials concerned of a reintegration indemnity following the breaking of the secondment contract. This indemnity was intended to compensate for the difference between the salary paid to the reassigned official during the period between the date of his actual reassignment and the date originally set for the end of the secondment, on the one hand, and the remuneration he would have been paid if he had remained on secondment at Sécupost until that original date, on the other. Officials seconded from the post office to Sécupost (secondment was due to last five years) were paid higher salaries during their secondment and the termination of their employment with Sécupost therefore gave rise to compensation for the early cessation of these more favourable conditions.

(20) The indemnity paid, on the basis of an agreement negotiated with the unions as part of the redundancy programme, was between (...) and (...) per reassigned official, depending on the date of reassignment. On average, it amounted to (...) per reassigned official.

(21) If Sécupost, instead of parting with the officials reassigned to the post office, had laid off private-sector employees, it would have had to make redundancy payments. The French authorities calculated the theoretical redundancy payment which Sécupost would have had to make. The calculation was based on the law applicable to Sécupost in this respect, i.e. the rules laid down in the collective agreement for the transport sector and the redundancy programme drawn up by Sécupost. On the basis of the average salary of an official employed by Sécupost and the rules deriving from the collective agreement, the redundancy payment for an employee on a private-law contract would have been (...). Sécupost paid a total of (...) to the 235 officials reassigned before 30 June 1991, whereas the total amount in redundancy compensation which would have had to be paid to

employees subject to private law but on the same salaries as the officials would have run to (...) × 235 or around (...). The cost to Sécupost of compensating the officials for their reassignment was therefore higher than the cost it would have incurred if it had made redundancy payments to employees subject to private law.

(22) Furthermore, the French authorities point out that the redundancy payments which Sécupost would have had to make to employees on private-law contracts were calculated on the basis of the salaries of the seconded officials and that the amounts would have been significantly lower if they had used a lower salary, in line with salaries actually paid to private-sector employees, given the reality of the labour market.

(b) *Absence of contributions to unemployment insurance funds*

(23) The French authorities confirmed that Sécupost did not have to pay into unemployment insurance funds for the seconded officials since their employment was guaranteed by their status as officials. However, they pointed out that seconded officials are generally subject to social security contributions at higher rates than those applicable to private-sector employees, with the disparity in the rates of employer's contributions in respect of officials and in respect of private-sector employees growing from 1,31 % in 1988 to 7,47 % in 1992. In particular, the rate for contributions to the civil servant's superannuation fund, which correspond to retirement contributions for employees, is considerably higher than the rate applied to private-sector employees.

(24) The French authorities calculated that the extra cost of employers' contributions linked to the employment of officials between 1988 and 1991 totalled (...).

(c) *Placing of premises at Sécupost's disposal*

(25) The French authorities gave various explanations regarding the circumstances in which Sécupost was able to rent all or part of its premises from the post office between 1988 and 1992.

(26) First of all, Sécupost's renting of premises from the post office was a temporary solution and it soon looked for other premises as alternatives to those it was renting from the post office. Of the premises Sécupost rented for its use, the proportion rented from the post office accounted for 93 % of total rented surface area in 1988, but this had fallen to only 7 % in 1992. The French authorities explained that Sécupost rapidly gave up the premises rented from the post office because they did not, generally speaking, correspond to its particular business requirements.

- (27) The French authorities note in particular that the average surface area of premises rented by Sécuripost from the post office was small (62 m² in 1988), while the premises which Sécuripost subsequently rented on the private market had a significantly larger surface area (324 m² on average in 1992). They also note that the premises were generally dilapidated and unsuitable for the use to which Sécuripost wished to put them. The French authorities gave several specific examples where Sécuripost had rented premises from the post office which were clearly unsuitable for its needs, whether owing to their size, location or fittings.
- (28) The French authorities also pointed out that the premises rented by Sécuripost from the post office were public property and had therefore been rented out in accordance with the specific rules governing public property. In particular this meant that Sécuripost was authorised to occupy the premises on a precarious and revocable basis only. The rent for occupying public property is set by the Ministry for Economics and Finance and is calculated using a fixed rate, determined by comparison with the rental value of comparable private property, and a variable rate, determined according to the specific advantage which the occupant gains by occupying the property.
- (29) As regards the premises rented by Sécuripost from the post office, the rental charge took the form of a rent set by agreement between the post office and Sécuripost. Since the file dates back such a long way, the French authorities were not able to find all the rental contracts drawn up between the post office and Sécuripost over the period under consideration. None the less, they were able to provide clarification of the rents charged for 43 premises throughout France.
- (30) Using this sample, the French authorities sought to compare the rents Sécuripost paid to the post office with those which it would have had to pay for comparable property on the private market. The comparison was based on the *Cote annuelle des valeurs vénales immobilières au 1^{er} janvier 1988*⁽⁴⁾ (annual rating of monetary values of property at 1 January 1988): this publication gives a band of rental values for new and old, renovated and non-renovated property for each French town. It also applies a weighting to assess the rental value of certain types of property (garage, car parks, etc.). The French authorities deducted 25 % from the rental value calculated using the Callon rating for the property that Sécuripost rented from the post office. They explained that a deduction of this size was common practice on the property market in the case of precarious occupancy contracts. According to the information provided by the French authorities, when the value of the property rented by Sécuripost is calculated using the Callon property rating and after reducing the rate by 25 % to take account of the precarious nature of the occupancy agreements, the market price of the 43 premises used in the sample is, on the whole, close to the rent paid by Sécuripost.
- (d) *Maintenance of Sécuripost vehicles by SNAG*
- (31) The French authorities confirmed that the invoices issued by SNAG for the repair and maintenance of Sécuripost's heavy goods vehicles were based on the rates charged by the dealer network of Renault Véhicules Industriels (RVI), both as regards the hourly rate and the time invoiced. As for the rates, the French authorities compared the reference rates for charging for labour in respect of the repair and maintenance of heavy goods vehicles used in 25 large garages in France (e.g. in Paris, Bordeaux and Orléans). The reference rates are used throughout the heavy goods vehicle maintenance and repair sector in France, including in the private sector. The data provided by the French authorities show that, for the period 1988 to 1992, the average rates that SNAG charged Sécuripost were not significantly different from the rates that RVI charged its own customers.
- (e) *Loan of FRF 15 million granted to Sécuripost for the financial year 1989*
- (32) The French authorities explained that Sofipost, a post office holding company, granted a loan of FRF 15 million to Sécuripost. It was a short-term loan granted for the period from 21 December 1989 to 23 October 1990. The interest rate applied was:
- 0,55 percentage point above the three-month PIBOR⁽⁵⁾ or 11,36 %, in 1989,
 - 0,60 percentage point above the three-month PIBOR, or 10,96 %, in 1990.
- (33) This rate is higher than the cost of borrowing outside the group borne by Sofipost (i.e. the refinancing rate granted to Sofipost by the banks, which means that Sofipost made a profit by lending on these terms to its subsidiary) and higher than the average intra-group lending rates used by some of the major French commercial and industrial groups. The French authorities explained that the special auditors' reports of various French groups for the year 1989 show that intra-group loans are common practice. These reports also reveal wide disparities in the rates used within different groups (e.g. 5 % for Eurocom as opposed to 15,34 % for BSN). In some groups, loans are granted interest-free or the rate is dependent on the performance of the subsidiary receiving the loan. The rate

(4) Editions Callon, 1988.

(5) The PIBOR (Paris Inter-Bank Offered Rate) is the money market rate, i.e. the annual rate at which banks are prepared to lend to one another for a period of three months. It is calculated on a daily basis by the French Banking Association as the arithmetic mean of the rates reported by 14 representative institutions on the Paris market.

granted to Sécupost is therefore at the top end of the range of the intra-group lending rates recorded in 1989.

This gives a rate of FRF 180,61 per delivery, compared with the standard national rate of FRF 163 offered by Sécupost to Casino. If we imagine the rates charged by Sécupost to the post office being applied to Casino, this would increase the charge per delivery by FRF 17,61.

(f) *Rates charged by Sécupost to the post office*

(34) The French authorities confirmed that Casino was the only Sécupost customer which could be compared with the post office in that both served a wide geographical area extending across France, and submitted a detailed comparison of the rates charged to the post office and to Casino. The comparison referred to 1993, because the Casino contract had been won in June 1992 as a result of a competitive bid.

(39) However, the French authorities consider that this difference of FRF 17,61 (or about 11 % of the rate charged to Casino) is largely justified by the extra costs arising from the specific constraints imposed on Sécupost by the post office.

(35) The French authorities also explained that, as opposed to what was stated by the Court of First Instance, the rates charged to the post office did not fall steadily but that, on the contrary, the rates charged in 1993, which had been in force since 1 January 1992, were higher than the previous rates, applicable since May 1989. Consequently, using the 1993 rates as a basis for comparison could not help but accentuate any difference between the rates charged by Sécupost to the post office and the market rates applicable during the period 1989 to 1993.

(40) There are four technical constraints affecting a contract for the transportation of moneys: journey time (dependent on the distance of the collection/delivery site from the central depot and on traffic density), security constraints (number and status of personnel, type of van), operating constraints (e.g. closing time of collection/delivery sites, need to pass by the Banque de France) and other constraints (e.g. national coverage).

(36) Before rising in 1989, the rates charged by Sécupost to the post office had fallen between 1987 and 1989. However, the French authorities pointed out that prior to 1989 Sécupost had no private customers, and that it was only from 1990 onwards that Sécupost recorded any significant turnover with its private customers. They also provided the Commission with the delivery rates charged by Sécupost to major customers other than the post office (and Casino) between 1990 and 1992. These customers were classified by geographical area (urban, suburban, rural) so as to enable a comparison to be made with the rates charged for the post office.

(41) The French authorities analysed and compared the contracts which Sécupost had with the post office and with Casino in the light of the above constraints.

(37) The pricing systems used for the post office and Casino are not identical. For the post office, Sécupost introduced a pricing system with rates differentiated according to geographical area (urban, suburban, rural). However, the contract with Casino was based on a standard national rate which in 1993 was FRF 163 per delivery.

(42) As regards journey time, the French authorities explained that the average distance between sites was 9,91 km for deliveries made on behalf of the post office and 5,08 km for those made on behalf of Casino. Taking account of the standard time spent at each site and of the average speed at which vans travel in urban, suburban and rural environments, the number of sites visited per hour is 3,4 for the post office, as compared with 4,9 for Casino.

(43) As regards security constraints, the post office imposed some which were not imposed under the contracts with Casino. The main requirements were: three security guards to accompany the consignment⁽⁶⁾ specific procedures for gaining access to post office premises, and approach and radio procedures. However, the French authorities were not in a position to quantify the effect of these constraints.

(38) In order to make a useful comparison between the rates charged to the two customers, the rates for the post office were applied to Casino's delivery structure.

(44) As regards operating constraints, the post office imposed a complex route, and waiting times at post offices could be long and were not necessarily always charged for. On the other hand, a standard contract such as that concluded with Casino stipulated an

⁽⁶⁾ The French authorities explained that a Decree of 13 July 1979 required the presence of three security guards for any transportation of moneys exceeding FRF 20 000. In its internal rules, the post office adopted a lower threshold: FRF 50 000 and then FRF 100 000.

automatic charge if the waiting time exceeded 10 minutes. In this connection, it should be remembered that unavailable periods added up to 130 minutes for the post office and 30 minutes for Casino. Thus, in a standard eight-hour day, a van on a post-office route has only five hours 50 minutes in which to complete invoiceable journeys, while a van on a standard route such as in the case of Casino will have seven hours 30 minutes.

- (45) Other constraints were the obligation to provide a service throughout France and the long payment periods, whereas private customers observed usual market practice. These constraints were not quantified by the French authorities.
- (46) It follows that, taking account only of the constraints on journey time and operation, the number of deliveries per day which could be carried out on average by Sécupost for the post office was (5 h 50 × 3,40), or 19,8 while for Casino it was (7h 30 × 4,9), or 36,75. The number of deliveries which could be made per day for Casino was thus 85 % higher than that for the post office. Furthermore, the average amount charged by Sécupost for a delivery on behalf of the post office, weighted for the geographical distribution of post establishments, was FRF 264, as opposed to the standard national rate of FRF 163 charged to Casino. By multiplying the number of deliveries per day by the rate charged per delivery, we can calculate the daily income generated by a van working on a post office route as (FRF 264 × 19,8), or FRF 5 227, while a van on a Casino route will bring in an average income of (FRF 163 × 36,75), or FRF 5 990. Consequently, Sécupost did not overcharge for its services to the post office relative to a comparable customer such as Casino, given the specific constraints imposed by the post office for transporting moneys on its behalf, even though only some of those constraints have been taken into account.

IV. Assessment

- (47) The Commission examined the information and data provided by the French authorities. It also conducted its own investigations into certain points. On this basis, it considers that the measures concerned do not constitute state aid within the meaning of Article 87 of the Treaty.
- (48) In particular, the Commission considers that employing seconded officials did not confer any advantage on Sécupost. The reassignment to the post office of seconded officials did not confer any advantage on Sécupost because the amount paid in compensation to the officials when they were reassigned earlier than planned was slightly higher than what would have been paid in compensation if these employees had been recruited by the company as private-sector employees, even without taking account of the fact that employees subject to private law would have earned lower salaries than the officials, these salaries forming the basis

for calculating redundancy payments. Moreover, the comparative study of employers' social security contributions for private-sector employees and for officials which the French Government carried out shows that, far from constituting state aid, employing officials entailed extra expense for Sécupost.

- (49) The information provided on the rents paid by Sécupost for the 43 premises throughout France shows that the rents were generally similar to and, on average, higher than the market rate, taking account of the deduction for the precarious nature of the occupancy contracts drawn up between the post office and Sécupost. The sample of 43 premises used by the French authorities represents a total surface area of 3 170 m²; or 35 % (in terms of surface area) of all the premises rented by Sécupost from the post office in 1988. From the sample we see that the average rent charged for the premises rented by Sécupost from the post office was (...) in 1988⁽⁷⁾. If we calculate the market value of this sample, and taking account of the deduction applicable on the basis of the precarious nature of the occupancy contracts signed by Sécupost and the post office, we obtain a market value of (...) in 1988, which is lower than the average rent paid by Sécupost for the same sample.
- (50) The Commission arranged for an expert report to be carried out in order to ascertain whether the deduction applied was really justified: the conclusions of this report show first of all that, since the premises rented by the post office to Sécupost were public property, they had to be rented on a precarious basis. The report also concludes that, while the precarious nature of a rental contract does not necessarily or automatically justify a deduction by comparison with the market value, the usual practice is to apply reduced rents to precarious private lettings.
- (51) Consequently, the French authorities correctly showed that the rents paid by Sécupost to the post office for 43 of the premises rented were in line with the market value for the rented property. Given that this sample of 43 premises is evenly spread throughout France and represents a significant share of all premises rented between 1988 and 1992 by Sécupost from the post office, the Commission considers that the French authorities have given sufficient justification to show that the rents paid by Sécupost to the post office were in line with the market values of the rented property and therefore that no state aid is involved.

⁽⁷⁾ This year was taken as the reference year: as explained above, Sécupost quickly found alternative premises to those rented from the post office after 1988.

(52) As regards vehicle maintenance, the Commission considers that the comparison with RVI rates is appropriate. The RVI network is a benchmark on the market in terms of the network size and market share⁽⁸⁾. The Commission made a statistical comparison of the rates charged by SNAG for vehicle maintenance and the rates charged by RVI. Overall, the rates are generally very similar throughout France: on average, at national level, the gap between the rates never exceeded 4 % over the reference period. On average, between 1988 and 1993, two of the reference rates used were very slightly lower for SNAG than for RVI, although the difference was not greater than 1,5 % and the third rate used was slightly higher for SNAG than for RVI (difference of 1,65 %). These differences in the rates are practically insignificant and lower than the statistical spread observed; the Commission therefore considers that SNAG invoiced Sécuripost for vehicle maintenance at the market rate and therefore that no state aid was involved.

(53) The Commission considers that the terms of the FRF 15 million loan are in line with the terms on which commercial relations between a parent and its subsidiary within a private group are normally conducted. The rate is higher than both the PIBOR and the cost of borrowing outside the group by Sofipost. Sécuripost therefore paid a mark-up to this financial holding company of the post office. In addition, the rate used is towards the top of the band of rates for intra-group loans established on the basis of the annual auditors' reports for 1989. Sofipost's behaviour can therefore be compared with that of a private holding company acting in accordance with market conditions.

(54) As regards prices charged, the Commission considers that the comparison with Casino is the only one which is wholly relevant. Before 1992 Sécuripost did not have any other customers comparable to the post office in terms of the geographical spread of deliveries. In addition, the application of the 1993 prices was cautious since they had been increased by comparison with the preceding period (1989 to 1992). Using the 1993 prices as a basis for comparison was bound, therefore, to accentuate any difference between the rates Sécuripost charged the post office and the market rates between 1990 and 1993. The Commission considers that the statistical comparison carried out by the French authorities, which takes into account only some of the constraints, shows that the rates Sécuripost charged its parent company between 1990 and 1993 were not excessive but were comparable to the rates charged to other customers, bearing in mind the constraints mentioned above. The constraints imposed by the post office and the corresponding charges give a daily income per van lower than that earned with Casino. An analysis of the rates Sécuripost charged customers other than Casino between 1990 and 1992 also confirm that the prices the post office was

charged were not excessive: applied to an equivalent geographical structure, the charges for the post office were, taking the average for the period 1990 to 1992, only 0,4 % higher than the charges for these other customers. Sécuripost therefore received no state aid in connection with the invoicing of deliveries for the post office between May 1990 and 1993.

(55) During the years 1987 to 1989 Sécuripost did not register any significant turnover from business with customers other than the post office, and the French authorities were not able to provide data for comparison between the market rates and the rates used by Sécuripost in its business with the post office. None the less, using the charges reported by the French authorities for customers other than the post office for the period 1990 to 1992 the Commission extrapolated the market rates for 1987 to 1989: this gives, for a geographical spread of deliveries equivalent to that of the post office, an estimated market rate of around FRF 248 per delivery. This estimated rate cannot be directly compared to the rate Sécuripost charged the post office because it is extrapolated from rates applied between 1990 and 1992 to customers spread over a smaller geographical area than that covered by the post office. Moreover, since this estimated rate was extrapolated to the period 1987 to 1989 from rates which Sécuripost charged customers other than the post office between 1990 and 1992, it is not appropriate to analyse the annual differences between the extrapolated rate and the rate applied to the post office: only an analysis of the average difference observed over the period 1987 to 1992 between the rate (extrapolated or real) applied by Sécuripost to customers other than the post office and the rates applied to the post office can produce a valid conclusion. That difference was around 5 %. Given the specific constraints imposed for deliveries on behalf of the post office, this difference is not excessive: the Commission therefore considers that the level of the rates Sécuripost charged the post office between 1987 and 1989 did not constitute state aid,

HAS ADOPTED THIS DECISION:

Article 1

The measures taken in respect of Sécuripost and covered in the Commission decision to initiate the procedure⁽⁹⁾ namely the secondment of post office officials to Sécuripost, the

⁽⁸⁾ 1992 statistics compiled by the French vehicle manufacturers union, the DAFSA study of April 1994 and the June 1996 edition of *Transport Magazine*.

⁽⁹⁾ OJ C 311, 22.10.1996, p. 12.

absence of contributions by Sécupost to unemployment insurance funds, the placing of post office premises at Sécupost's disposal, the maintenance of Sécupost vehicles by the Service National des Ateliers et Garages des PTT (SNAG), the granting of a loan of FRF 15 million by Sofipost (a post office holding company) to Sécupost for 1989 and the rates charged by Sécupost to the post office, do not constitute state aid within the meaning of Article 87(1) of the Treaty.

Article 2

This Decision is addressed to the French Republic.

Done at Brussels, 20 July 1999.

For the Commission
Monika WULF-MATHIES
Member of the Commission
