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COMMISSION

COMMISSION DECISION

of 29 September 1999

declaring a concentration to be compatible with the common market and the EEA Agreement

(Case IV/M.1532 — BP Amoco/Arco)

(notified under document number C(1999) 3059)

(Only the English text is authentic)

(Text with EEA relevance)

(2001/45/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) and Article 10(2) thereof,

Having regard to the Commission decision of 10 June 1999 to initiate proceedings in this case,

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

Whereas:

- (1) On 4 May 1999, the Commission received notification pursuant to Article 4 of Regulation (EEC) No 4064/89 (the Merger Regulation) of a proposed concentration by

which the undertaking BP Amoco plc (BPA) acquires control within the meaning of Article 3(1)(b) of the Merger Regulation of Atlantic Richfield Company (Arco).

- (2) By decision of 10 June 1999, the Commission found that the notified operation raised serious doubts as to its compatibility with the common market and initiated proceedings pursuant to Article 6(1)(c) of the Merger Regulation.

I. THE PARTIES AND THE OPERATION

- (3) BPA is the holding company of a multinational oil exploration, petroleum and petrochemical group comprising three core businesses, that is, BP Amoco Exploration (oil and gas exploration and production); BP Amoco Oil (refining, marketing, supply and transportation); and BP Amoco Chemicals (manufacturing and marketing of petrochemicals and related products). The BP Amoco Group was formed as a result of the merger between the British Petroleum Company plc and Amoco Corporation⁽⁴⁾. It has well-established operations in Europe, the United States of America, Australasia and parts of Africa, and is expanding its presence in Asia and South America.

⁽¹⁾ OJ L 395, 30.12.1989, p. 1; corrected version in OJ L 257, 21.9.1990, p. 13.

⁽²⁾ OJ L 180, 9.7.1997, p. 1.

⁽³⁾ OJ C ..., ..., p.

⁽⁴⁾ See Commission Decision of 11 December 1998 in Case IV/M.1293 — British Petroleum/Amoco Corporation.

- (4) Arco is involved in the exploration for, production, transportation and sale of crude oil and natural gas and in the refining of crude oil and the transportation and marketing of petroleum products. Although it has operations in a number of countries such as Venezuela, Algeria, Tunisia, the United Kingdom and Indonesia, the bulk of its activities take place in the USA (i.e., approximately 86 % of its total turnover in 1998).

decision-initiating proceedings the Commission had expressed serious doubts on these markets. However, there are, for the reasons indicated below, no competition concerns on these markets.

II. CONCENTRATION

- (5) The concentration being notified is an acquisition of sole control within the meaning of Article 3(1)(b) of the Merger Regulation. It will result in BPA acquiring sole control of Arco. The concentration will be effected by means of share sale. This will be achieved by Arco being merged into a newly established company incorporated in accordance with the laws of the State of Delaware, USA (Newco), which will itself be wholly owned by BPA. Following the merger of Arco with Newco, Arco will be the surviving legal entity and will, at that point, have become a wholly owned subsidiary company of BPA. Thus, as a result of these operations, BPA will have acquired ownership of the entire issued share capital of Arco.

Exploration, development and production process

- (8) Upstream activities comprise three types of commercial activity: the finding of new reserves, the development and the commercial exploitation of those reserves. The finding of new reserves is generally described as 'exploration'. Development concerns the setting up of adequate infrastructure for future production (oil platforms, pipelines, terminals, etc.). The exploitation of reserves is called 'production and sales'. Previous Commission decisions⁽⁶⁾ focused primarily on the impact of the then notified transactions on the production and sales segment.

III. COMMUNITY DIMENSION

- (6) Since the parties' combined aggregate worldwide turnover⁽⁵⁾ exceeds EUR 5 billion, they each have a Community-wide turnover of more than EUR 250 million, and they do not each achieve more than two thirds of their aggregate Community-wide turnover within one and the same Member State, the concentration has a Community dimension pursuant to Article 1(2) of the Merger Regulation.

- (9) Exploration and development is a time- and capital-intensive activity, which includes a number of successive steps. Firstly, countries which believe that hydrocarbon reserves could be discovered on their territory (such a country is called the 'host country') organise bids to grant exploration licences. The bidding processes vary from public auctions in the USA to situations where bidders are preselected by the host country. This preselection can be based to varying extents on technical capability, financial strength or other considerations (lobbying, cultural affinities, etc.).

IV. ASSESSMENT UNDER ARTICLE 2 OF THE MERGER REGULATION

A. EXPLORATION, DEVELOPMENT, PRODUCTION AND SALE OF CRUDE OIL AND NATURAL GAS

- (7) Both parties are active in the exploration, development and production of crude oil and natural gas and in the

- (10) Often, companies bid together in order to spread risks or to bring complementary skills. In some circumstances, host countries may require that some bidders join together in order to get the licence for exploration. Host countries may also require that their national oil companies be granted a share in any discovery made in the block under licence. In all cases when the licence is granted jointly to a number of companies, an operator for the block is named. The role of the operator is to manage technically and financially the exploration and possibly the development and production phases of the project. Most of the important decisions require unanimity from all the partners in the project.

⁽⁵⁾ Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Notice on the calculation of turnover (OJ C 66, 2.3.1998, p. 25). To the extent that figures include turnover for the period before 1 January 1999, they are calculated on the basis of average ECU exchange rates and translated into EUR on a one-for-one basis.

⁽⁶⁾ See Commission Decision in Case IV/M.1200 — Arco/Union Texas, OJ C 16, 21.1.1999, p. 8; Commission Decision in Case IV/M.88 — Elf Enterprise, OJ C 203, 2.8.1991; and Commission Decision in Case IV/M.85 — Elf Occidental, OJ C 160, 20.6.1991.

(11) The total time between the granting of a licence and actual production typically range from five years to 15 years. Costs of exploration and development projects can reach in the region of EUR 7 billion for projects in the 'frontier areas'. The split of expenditures between the exploration stage and the development stage is typically respectively 15 % and 85 %.

(12) It must also be mentioned that when production is started in a new area, infrastructure needs to be developed. This includes notably oil platforms, pipelines and terminals. Smaller fields, which would not be economical to develop on their own, can then be exploited through using the infrastructure already put in place for the bigger field. Such smaller fields are sometimes called 'satellite fields'. Exploration in the North Sea has typically followed that process.

Relevant product markets

(13) It is often argued that exploration, development and production and sale are too closely interlinked for more than one distinct product market to be defined. It may, however, be argued that exploration constitutes a separate product market. Indeed, it could be argued that a firm engaged in exploration has two categories of clients: the host country to which it has generally undertaken to provide a future flow of resources in case oil or gas is found; and the subsequent producers and sellers of oil and gas that may buy it out or join in the development and production. The transfer of rights over blocks is a widespread practice in the industry.

(14) Since the possible contents of the underground are not known at the time of exploration, the Commission considers that it is not justified to make a distinction between exploration for oil and exploration for natural gas. As regards the development, production and sales product markets, since gas and crude oil have differing applications and are subject to varying pricing behaviour as well as cost constraints, the Commission considered it appropriate at the stage of the decision-initiating proceedings to define one relevant product market for the development, production and sales of crude oil and another relevant product market for the development, production and sales of natural gas.

(15) The parties have contested the existence of an exploration market arguing that it is too closely linked to the subsequent steps of the production process to make it a possible product market. As will be explained in the section on effects of the merger on competition, it is not necessary for the appraisal of the effects on competition of the notified operation to define precisely

the relevant product markets according to the various stages of the exploration, development, production and sales of respectively crude oil and natural gas.

Relevant geographic markets

(16) The Commission considers that the exploration market is worldwide in scope and agrees with the parties that from a European-demand perspective the relevant geographic markets are worldwide in scope for development, production and sales of crude oil and probably include the EEA, Algeria and Russia for gas.

(17) The Commission examined whether smaller geographic areas could constitute relevant markets. Some purchasers of gas make, for security of supply reasons, a distinction in their purchasing policy as to the origin of the gas on the basis of the perceived political risks and their influence on the security of supply with regard to Russian and Algerian gas (Russia accounted for approximately 17 % of total western European supply and Algeria for 12 %). The most explicit example of this is the Spanish legislation ordering that not more than 60 % of the natural gas demand can come from the same country. It is, however, unlikely that a price increase of gas produced in the EEA would not be defeated by a small increase in the proportion of gas purchased from Russia and Algeria. In any case, the precise definition of the relevant geographic market can be left open, as this does not alter the conclusion of the competitive assessment.

Market players

(18) Traditionally, companies involved in the exploration, development and production and sales business were grouped in three categories with different profiles, strategic objectives and future exploration and development capabilities. The categories are: (i) the State-owned (mainly OPEC and some OECD-based companies such as Statoil) producers; (ii) the 'majors', that is, vertically integrated oil companies with international activities; and (iii) a multitude of substantially smaller oil companies, most of which are non-integrated upstream explorers and/or producers.

(19) The competition concerns identified by the Commission were raised mainly by the fact that as a result of the notified transaction, as well as of that notified by Exxon and Mobil, a distinct (fourth) tier of players might

prevail on the exploration and development activities. This group of 'super majors' would be composed of Exxon-Mobil, BP Amoco-Arco and Shell.

Position of the parties in the market

Exploration

- (20) There is no widely available or accepted indicator on the basis of which market shares can be calculated as a proxy to assess market power in the exploration market. Measurement of market shares could be carried out on the basis of the number of blocks where licences have been granted, the number of blocks where a given company is the operator, net acreage, total acreage under operatorship, capital expenditure in exploration, etc. There is wide agreement that proxies based on number of blocks or acreage would not be reliable as they cover widely varying situations.
- (21) On the basis of capital expenditures, Exxon-Mobil, BP Amoco-Arco and Shell would represent together, with roughly equivalent shares, between 30% and 40% of the total capital expenditures in exploration, development and production scheduled for 1999. The next largest player would represent one third of the average size of the three main players.
- (22) The parties have contested the adequacy of this measure of market power for the following reasons. First, capital expenditures vary according to the sites explored. This biases downwards the market share of national oil companies in low cost OPEC areas. Secondly, capital expenditures often do not reflect the correct share of ownership of the licence or of the output. This is because State companies often pay a share which is disproportionately lower than their licence interest or take of crude oil output. Thirdly, capital expenditures often include expenditure on investments such as gas liquefaction and infrastructure rather than sums invested purely in exploration.
- (23) Another possible way to measure market power would be to calculate the share of expected production of these companies (since current exploration and purchase of third-party rights will translate into future production). On the basis of the market investigation, the combined market share of the three super majors of the non-OPEC production, in some 10 years from now, would again be in the 30% to 40% range.

Production and sales

- (24) BPA and Arco would have together around [less than 15%] (*) of respectively the worldwide production of crude oil and the European production of natural gas in 1998. These numbers would be [less than 25%] for a combined Exxon-Mobil and less than 20% for Shell. These numbers have not materially changed over the years. Of the total natural gas production in the EEA, the three super majors account for almost 40%. However, of the natural gas consumed in the EEA, the three super majors account for less than 30%.
- (25) The industry often refers to proven reserves as a proxy for market power. On this basis, the parties would hold approximately [less than 3%] and [less than 5%] of respectively the worldwide proven reserves of crude oil and European-wide proven reserves of natural gas. However the parties argue that proven reserves are not a relevant indicator of future production. Proven reserves as stated by the oil companies have just a stock function and, as any other private company, private oil companies need to limit as much as possible their stocks. By means of their proven reserves, the company indicates that it is (or is not) able to replace the foreseeable depletion of existing oil fields and thereby to remain a viable player on the market. However, national oil companies do not need to justify further exploration and development investments to their shareholders since they benefit from the national reserves which usually largely exceed their needs. Therefore, such an indicator involves an upward bias in favour of national companies.
- (26) Currently and for the foreseeable future, the OPEC producers collectively enjoy substantial market power in crude oil production. They control a substantial amount of production and proven reserves (approximately 40% and 75%, respectively, whereas Saudi reserves account for more than one third of OPEC reserves). OPEC has been able in a number of instances in the past to influence⁽⁷⁾ crude oil prices up to a certain level.
- (27) Gazprom (17%) and Sonatrach (11%), the national Russian and Algerian suppliers, account for approximately 30% of EEA sales of natural gas and their reserves account for 88% (Gazprom 81,5%) of the combined proven reserves that can be sold in the EEA.

(*) Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets.

⁽⁷⁾ Prices in the crude oil trade markets may be significantly influenced by mere announcements following an OPEC meeting.

Effects of the merger on competition

- (28) The Commission raised the following serious doubts as to the effect on competition in the markets for exploration, development, production and sales of crude oil and natural gas. The notified acquisition together with the Exxon-Mobil merger could lead to the creation of a fourth tier of competitor in the industry composed of BP Amoco-Arco, Exxon-Mobil and Shell. Whatever the parameter retained (market capitalisation, oil and gas production, proven reserves etc.), there is now a material gap between these three super majors and the remaining majors.
- (29) It was considered whether it would be possible that the three super majors would in the future be in a privileged position to find and develop new important reserves compared to the other players in the market. This could come from their increased financial strength that would now enable them to hold a portfolio of risks of increased size. On the contrary the other competitors would have to pick and choose the areas where they intend to become active. Because of their less favourable access to capital and capacity to spread risks, smaller companies would, if they wanted to continue developing important fields, have to become smaller partners to the super majors to benefit from their combination of resources. Their only other alternative would be to become niche players focused on exploration. This may result in the super majors controlling the access by other explorers to the new frontier areas, first at the time of the granting of the first licences and then for further surrounding blocks since the super majors will have built the necessary infrastructure.
- (30) Since the typical time lapse between the first stages of exploration and the start of production varies between five and 15 years, under this scenario there would be a possibility that within some ten years, new non-OPEC reserves and production would be influenced to a significant extent by the super majors.
- (31) This could affect the production and sales markets in the following way. The competitive constraints limiting OPEC's ability to function as a cartel would be lessened. These three companies would have the same interests as OPEC and would be likely to align themselves on the OPEC decisions by limiting output to a certain level without fearing that others would take advantage of this. This would translate into the strengthening of OPEC's dominant position in the crude oil market through the creation of an oligopolistic structure combining both OPEC and the three super majors, thus creating incentives for alignment on OPEC's commercial strategies. OPEC would then be in a position to raise and sustain prices at the highest price threshold above which new exploration would be triggered.
- (32) On the basis of the foregoing, the Commission concluded that the operation raised serious doubts as to its compatibility with the common market and the functioning of the EEA agreement, which should be further explored in an in-depth investigation.
- (33) The parties contested the Commission's serious doubts on mainly two grounds. First, the super majors would still be facing competitive constraints from smaller oil companies. Secondly, host countries control oil and gas production and in any case would have no incentives to let oil companies restrict production.
- (34) The market investigation confirmed that small explorers do not seem to believe that the emergence of a new class of super majors would threaten their position. Because of size differences they would not compete for the same type of exploration rights and they would not be dependent on the bigger explorers to sell their oil. In addition, majors such as Chevron, Texaco, Elf or Total would all seem to have unchanged capacity to explore and develop fields anywhere in the world. The parties have provided numerous examples of the involvement of majors in current projects all over the world.
- (35) Second, the market investigation confirmed that typical concession contracts between governments and explorers-producers prohibit the latter from limiting their output (and leave such a decision to the discretion of the government).
- (36) As to natural gas, it is unlikely that the parties, together with the other super majors, could control the EEA production and therefore that competition would be affected. Even if such a market did exist (in view of the perceived political risk attached to the gas production in Russia and Algeria), no collective dominance between the super majors can be argued in view of the strong position of Norwegian gas delivered by competitors. In addition, producers of natural gas face very concentrated demand in the hands of the national wholesale gas transmission companies such as Gaz de France or Distrigaz.
- (37) Therefore, the Commission concludes that the concentration will not lead to the creation or

strengthening of a dominant position on the markets for the exploration, development, production and sale of crude oil and natural gas.

B. NATURAL GAS TRANSPORTATION AND PROCESSING

- (38) The concentration raises competition concerns in the markets for: (i) natural gas transportation through pipelines in the southern North Sea (SNS); and (ii) natural gas processing services in the SNS. These markets and the market for natural gas transportation through pipelines in the northern North Sea (NNS) will be dealt with further below.

Relevant product market

- (39) When natural gas emerges from the well-head of a production facility, the stream contains gaseous hydrocarbons and hydrocarbon liquids. This unprocessed gas often requires transportation by pipeline to a facility at which it is processed by separating the gaseous and liquid constituents. Thereafter, the gaseous stream undergoes further processing/purification in order to produce gaseous hydrocarbons meeting the technical specification necessary for carriage in the transmission system into which it will be introduced (pipeline quality gas). Producers of natural gas carry out this transportation and processing either through use of their own assets or, in some cases, by utilising pipelines and offshore/onshore gas processing facilities owned by other undertakings.
- (40) BPA is of the view that gas transportation and gas processing each fall in a separate product market. In the case of gas transportation, the relevant product market would be the market for the transportation by sub-sea pipeline of natural gas⁽⁸⁾. In the case of gas processing, BPA would regard the relevant product market as the market for processing natural gas.
- (41) Although the owners of a gas field require both transport and processing to be able to market their gas and will look for the cheapest overall combination, the Commission considers that it is appropriate to separate the transport and processing market since the competitive conditions differ between transport and processing. For instance, it is apparent from the market investigation, that all combinations are possible between own (newly constructed) pipelines and/or processing facilities and third-party access (TPA) to existing pipelines and/or processing facilities.

Relevant geographic market

- (42) Arco's interests in the Community in gas transportation and processing infrastructure arise in relation to

infrastructure located in only one Member State (the United Kingdom). These items of infrastructure are of two types: sub-sea gas pipelines and an interest in a gas-processing facility. All of these assets are located on the part of the UK continental shelf lying to the east of the UK mainland and on the eastern UK mainland itself.

- (43) The relevant geographic market consists, from a demand perspective, i.e. owners of gas fields requiring transport and/or processing, of the (existing or newly constructed) infrastructure that forms a viable economic alternative. In this respect, the eastern part of the UK continental shelf can be divided into two areas: the NNS, which is the area of the North Sea lying to the north of latitude 55° N, and the SNS, the area of the North Sea lying to the south of latitude 55° N.

- (44) BPA considers that, although gas fields in the NNS could, in theory, look to processing facilities in the SNS, in most instances a gas field located in the NNS is likely to seek transportation to and processing of its output at NNS processing facilities. In fact, there is only one pipeline under construction linking an NNS gas field with a SNS processing facility.

- (45) Gas fields in the SNS have looked in the past, and will continue to look in the future, to the terminal areas on the coastline adjacent to the SNS for the processing of their output (although to a minor extent, SNS gas fields have invited bids for transportation via pipelines landing in the Netherlands). It is apparent from the market investigation that, for the SNS, unlike the NNS, the construction of new infrastructure is not a realistic alternative to the use of existing facilities since the SNS is a 'mature gas province' where the new fields that might be discovered will be too small to support the construction of new infrastructure.

- (46) For these reasons, BPA considers that, as regards the market for the processing of gas and the market for sub-sea pipeline transportation of gas, the NNS and the SNS are separate geographic markets. Since Arco has no equity interests in the NNS gas processing market, this market is not further considered.

- (47) However, the geographic market is not smaller than that of the regions as defined above. There is ample evidence that the options for a new field are not limited to the different facilities at a single location (for example three gas processing facilities at Bacton) and/or a single location served with different pipelines (for example the three pipelines servicing the Bacton-Amoco processing plant).

⁽⁸⁾ Arco has no interests in on-shore production fields.

- (48) For these reasons, the Commission considers that, for both gas transportation and gas processing, the SNS and the NNS constitute distinct geographic markets.

Position of the parties in the market ⁽⁹⁾

(a) NNS pipelines

- (49) Table 1 gives an overview of the eight different pipelines linking NNS gas fields to the NNS gas processing plants, together with the parties' respective

equity ownership and the name of the operator. The Miller pipeline currently transports only minimal quantities of gas and will be expanded (see recital 59). In addition, there is one pipeline (SEAL) currently under construction that will link NNS gas fields with a SNS processing facility. Arco has a [...] % interest in this pipeline.

Overall, BPA has an equity ownership in three pipelines and Arco has an equity ownership in two pipelines. There is no overlap in the parties' ownership interests and in four of the nine pipelines, the parties have no interest.

Table 1: NNS pipelines

Gas processing facility	Pipelines	BPA/Arco equity ownership in pipeline	Operator
St Fergus (Shell/Esso)	FLAGS	0	Shell
	Fulmar	0	Shell
St Fergus (Total)	Frigg (two pipelines)	0	Total
	Miller	BPA [...] %	BPA
St Fergus (Mobil)	Britannia	Arco [...] %	Conoco/Chevron
	SAGE (Beryl)	0	Mobil
	SAGE (Brae)	BPA [...] %	Mobil
Teesside (BPA)	CATS	BPA [...] %	BPA
Bacton (Shell)	SEAL	Arco [...] %	Shell

Source: Parties' data.

- (50) These ownership interests give the parties an equity interest of around [15 % to 25 %] of the total nominal gas transportation capacity of the nine gas pipelines (assuming the expansion of the Miller pipeline) mentioned above. Of the total expected gas transportation throughput for 1999 of 5 058 mmscfd ⁽¹⁰⁾, the parties' equity interests in each pipeline multiplied by the expected actual throughput in each

pipeline, gives them a market share of around [10 % to 20 %].

(b) SNS pipelines

- (51) Table 2 gives an overview of the different pipelines linking the SNS gas fields to the SNS gas processing plants in Dimlington, Easington, Theddlethorpe and Bacton. It also sets out the equity ownership of each of the undertakings concerned and the name of the operator. It can be seen that BPA has an equity ownership in 10 pipelines and Arco has an equity ownership in seven pipelines. The parties' ownership overlaps in four of them. In four of the 17 pipelines, the parties have no interest.

⁽⁹⁾ In this section the references to capacity are based on actual capacity as indicated by the market players. Those references therefore constitute business secrets of the respective players that cannot be meaningfully summarised in a non-confidential manner. Although the nameplate capacity of the infrastructure is publicly available, this has proven not to be a reliable indicator in all markets.

⁽¹⁰⁾ Million metric standard cubic foot per day.

Table 2: SNS pipelines

Gas processing facility	Pipelines	BPA/Arco equity ownership in pipeline	Operator
Dimlington (BPA)	Cleeton	BPA 100 %	BPA
Easington (BPA and British Gas each have a processing facility)	West Sole (two lines)	BPA 100 %	BPA
	Rough (two lines)	0	BG
	Amethyst	BPA [...] % Arco [...] %	BPA
Theddlethorpe (Conoco)	Viking	BPA 50 %	Conoco
	LOGGS	BPA 50 %	Conoco
	Caister-Murdoch	Arco [...] %	Conoco
	Pickerill	Arco [...] % BPA [...] %	Conoco
	Sean	BPA [...] % Arco [...] %	Shell
Bacton (Shell)	Leman (two pipelines)	0	Shell
	Sole Pit	0	Shell
Bacton (BPA)	EAGLES	Arco [...] % BPA [...] %	Arco
	Leman	BPA [...] %	BP Amoco
	Inde	BPA [...] %	
Bacton (Phillips)	Thames	Arco [...] %	Arco
	Hewett (two pipelines)	Arco [...] %	Phillips
	Lancelot	0	Phillips

Source: Parties' data.

- (52) These ownership interests give the parties an equity interest of around [between 30 % and 50 %] of the total nominal gas transportation capacity of the gas pipelines in operation. Of the total expected gas transportation throughput for 1999 of 4 225 mmscfd, the parties' equity interests in each pipeline multiplied by the expected actual throughput in each pipeline, gives them a market share of [between 30 % and 40 %].
- (53) British Gas has a market share of around 15 %, and Conoco has around 10 %.

(c) SNS gas processing

- (54) Table 3 lists the seven SNS gas processing facilities with the parties' respective ownership interests and the name of the operator. It can be seen that the parties have an interest in five of these facilities (BPA 4 + Arco 1) and that there is no overlap. These ownership interests give the parties an equity interest of [between 40 % and 50 %] of the total nominal SNS gas processing capacity (Arco less than [...]). Of the total expected gas processing throughput for 1999, the parties' equity interests in each processing facility multiplied by the expected actual throughput in each facility gives them a market share of [between 30 % and 40 %].

Table 3: SNS gas processing

Gas processing facility	BPA/Arco equity ownership	Operator
Dimlington	BPA 100 %	BPA
Easington (BPA)	BPA 100 %	BPA
Easington (BG)	0	BG
Theddlethorpe	BPA 50 %	Conoco
Bacton (Shell)	0	Shell
Bacton (BPA)	BPA [...] %	BPA
Bacton (Phillips)	Arco [...] %	Phillips

Source: Parties' data.

- (55) Conoco and Exxon/Shell each have around 15 %.

Competitive assessment

- (56) A key element in the operation of UK pipelines and processing facilities is that unanimous agreement is

required amongst all the owners of the infrastructure with regard to major decisions, including the conditions of third party access to the infrastructure. As the main competition concern arising from an interest in such infrastructure is the possibility for the infrastructure owners to constrain the development of new, competing gas fields, the position of an individual company will depend not so much on its equity capacity share, but on the total capacity, and especially spare capacity⁽¹¹⁾, of the infrastructure in which it has an interest.

- (57) An increase in ownership resulting from the concentration in a particular infrastructure will, therefore, not endow BPA with any greater influence over this pipeline than exists prior to the concentration.

(a) NNS pipelines

- (58) Of the seven pipelines currently in operation (disregarding Miller and the SEAL pipeline under construction), BPA has an interest in two and Arco has an interest in one. These pipelines account for only half of the total capacity. Since there is currently, and for the coming two to three years, no spare capacity in the NNS pipelines, the competitive constraints for the owners of new gas fields do not depend on the equity interests of the owners of NNS pipelines and thus, in the context of this procedure, on the equity interests of BPA and Arco. There is therefore no dominant position on this market.

- (59) These competitive constraints are not fundamentally changed by the fact that in 2002, at least two other pipelines will become operational. They are the SEAL pipeline, where Arco has a [...] % interest, and the Miller pipeline, in which the owners (BPA [...] %, Conoco [...] % and Enterprise [...] %) plan to reach a capacity level of 1 200 mmscfd by 2002, accounting for less than [between 10 % and 25 %] of total capacity. The SEAL pipeline will accommodate transport of gas from own resources (newly developed gas fields), whereas the Miller capacity is targeted to accommodate transport of third party gas. Therefore, the transaction does not result in a change of market power of the merged entity vis-à-vis the owners of new gas fields since the SEAL pipeline in which Arco has an interest does not accommodate transport of gas from the owners of new gas fields. In other words, the notified operation does not lead to the creation or a strengthening of a dominant position.

⁽¹¹⁾ Defined as the unused capacity available in the infrastructure regardless of the origin of the actual gas throughput (equity gas of the owners of the infrastructure + gas for which a TPA agreement is concluded).

(b) SNS pipelines

- (60) As a result of the transaction, BPA will achieve an equity interest in 13 of the 17 existing pipelines. The total capacity of the pipelines in which the parties have an interest accounts for [greater than 60%] of total capacity and it is apparent from the market investigation that the four pipelines in which the parties do not have an equity interest have limited spare capacity. Therefore, BPA would be in a position to control the access to pipeline transport for new fields in the area since it controls the pipelines with free capacity in the area. Since the SNS is a 'mature gas province', it is not likely that further large fields will be discovered. It is, therefore, unlikely that new infrastructure will be built.
- (61) Therefore, the Commission concludes that the concentration will lead to the creation of a dominant position in the SNS pipeline transport market. BPA can use this position to the detriment of the owners of new (small) gas fields by asking high transport tariffs or offering a limited transport service.
- (62) BPA has argued that it would not have any market power in the SNS pipelines market as a consequence of the concentration because: (i) the SNS is a mature gas province with plenty of available capacity in the existing pipelines; (ii) new infrastructure can be built; and (iii) an industry custom exists that does not allow BPA to exercise its equity rights in more than one piece of competing pipeline infrastructure. The Commission does not accept these arguments for the following reasons.
- (63) The Commission recognises that there is overall capacity underutilisation in the SNS pipelines and, therefore, severe competition could be expected between the different pipelines whenever a new field (generally much smaller than the original fields) wants to negotiate third party access in order to attract the additional transport tariff income. However, it is apparent from the market investigation that the pipelines in which the parties do not have an interest have only limited spare capacity.
- (64) Second, even BPA recognises that no new major gas pipelines have been constructed in the SNS since 1992. This is not surprising since the fields that have developed recently in the SNS area are satellite fields of previously developed larger fields. Furthermore, it is not expected that new large fields will be discovered. No new pipelines are therefore expected to be constructed as the expected cashflow of satellite fields is too small to recover the investment needed for constructing a new, dedicated pipeline. In fact, such fields cannot, in general, be developed without guaranteed TPA to pipelines and processing facilities.
- (65) Thirdly, the parties refer to the 'step-out' custom in the UK oil and gas industry, under which, if two or more of the pipelines in which a company has an interest compete, that company abstains from exercising its right to vote in more than one of the pipeline consortia. BPA argues that it is thereby prevented from being able to exercise its right of veto so as to divert gas for example from the Bacton-Amoco line (where it has [...]%) to the Bacton-Leman line (where it has [...]%). The step-out custom is a general recognition of the fact that companies can at times find themselves in a position of conflicting interests when they hold ownership interests in infrastructure that is in competition to submit an offer for transportation and/or processing services to a potential user. Although it is rare for step-out obligations to be contained in the contract documentation relating to ownership of the various pieces of infrastructure, the custom is well established in the UK oil and gas industry. BPA believes that due observance of the step-out custom is an important factor in complying with the principle of non-discrimination (as contained in the Offshore Infrastructure Code of Practice) and hence avoiding sanctions under UK domestic law (i.e., Section 17 of the Petroleum Act 1998 and Section 12 of the Gas Act 1995).
- (66) The Offshore Infrastructure Code of Practice (issued by the UK Government's Department of Trade and Industry) is a code adopted by all owners of offshore oil and gas transportation infrastructure and aims to ensure objectivity and transparency in the processes of making infrastructure available to third-party users. Section 17 of the Petroleum Act 1998 provides the legal basis upon which the UK authorities can require the granting to third parties of access to oil and gas pipelines on reasonable terms following an initial refusal by the infrastructure owners to do so. Section 12 of the Gas Act 1995 provides the legal basis upon which the UK authorities can require the granting to third parties of access to gas processing facilities on reasonable terms following an initial refusal by the facility owners to do so.
- (67) The market investigation has confirmed the existence of such a step-out custom as described by the parties. However, the step-out custom is as such not a part of the voluntary Code of Practice. The respect of the custom, therefore, relies solely on the unilateral behaviour of all the companies concerned. The future

behaviour of BPA would therefore only be constrained by its voluntary commitment to a custom which is not necessarily enforceable.

(68) Even if it were accepted that the step-out custom is a reflection of the Code of Practice which in turn might be enforceable by the UK authorities, that would not be sufficient. The Commission cannot, in assessing concentrations pursuant to the stringent criteria of Article 2(3) of the Merger Regulation, accept that the presence of a regulator whose function is to monitor and sanction the behaviour of the companies in question justifies the conclusion that no dominant position is created.

(69) The Commission considers therefore that the concentration would create a dominant position on the SNS gas pipelines market.

(c) *SNS gas processing*

(70) The parties will have, as a consequence of the concentration, an interest in five of the seven gas processing facilities servicing the SNS sector. In addition, their share of the existing capacity and of the actual throughput is in excess of 40%. Furthermore, the two facilities in which the parties do not have an interest have a limited spare capacity at peak times. On the other hand, the facilities in which the parties have an interest have spare capacity in excess of 50% even at peak times. The merged entity might therefore be in a position to control the access for new fields in view of its sole ownership of two facilities and its shared ownership of three facilities where its control results from the unanimity requirements in two of these facilities. The available free capacity at peak times in the third terminal (Bacton-BPA), where each of the participants is free to offer its spare capacity to third parties, accounts for less than [between 10% and 20%] of the total capacity. However, BPA owns [more than 25%] of the total capacity in the terminal. The free capacity in this terminal available for the other owners only amounts to around 5% of the total capacity. In addition, it cannot be excluded that BPA could, in view of its operation of the terminal, further reduce the availability of this free capacity.

(71) The arguments made by BPA as described above with regard to SNS pipelines have also been made for the SNS processing market. For the same reasons as expressed above, they cannot be accepted.

(72) The concentration will therefore create a dominant position on the SNS gas processing market as well.

V. COMMITMENTS PROPOSED BY THE PARTIES

A. COMMITMENTS

(73) BPA has given a commitment to the Commission to divest the equity interests that Arco currently holds in [certain pieces of SNS gas transportation and processing infrastructure]. These equity interests will be divested to one or more purchasers approved by the Commission. In addition, BPA has given a commitment not to reacquire any of those assets without the Commission's prior approval.

(74) The full text of the undertakings is in the Annex.

B. ASSESSMENT

(75) The divestiture by BPA of the interests held by Arco in those pipelines and processing facilities where BPA currently has no interest means that the competitive situation of BPA will be the same before and after the concentration. That is because, as indicated above, in the SNS pipelines and processing facilities TPA is accorded on the basis of unanimous agreement between the owners. The competitive situation therefore depends on the number of pipelines in which a company has an interest and the total spare capacity of those pipelines. The divestiture of the equity interests in the 'additional' infrastructure therefore eliminates the overlap on the relevant markets between BPA and Arco. The Commission therefore concludes that, as a consequence of the commitments, there will be no creation of a dominant position on the relevant markets.

VI. CONCLUSION

(76) Having regard to Article 10(2) of the Merger Regulation, the Commission concludes that the commitments given by BPA are sufficient to remove its serious doubts, identified in its decision-initiating proceedings and in its subsequent investigation of the operation, in relation to Article 2(2) of the Merger Regulation.

- (77) The operation is, therefore, subject to the condition of full compliance with the commitments in the Annex, compatible with the common market and with the EEA Agreement,

Article 2

This Decision is addressed to:

BP Amoco plc
Britannic House
1, Finsbury Circus
London EC2M 7BA
United Kingdom

HAS ADOPTED THIS DECISION:

Article 1

Subject to the condition of full compliance with the commitments with regard to the divestiture of [certain pieces of SNS gas transportation and processing infrastructure] which are set out in the Annex, the concentration notified by BP Amoco plc on 4 May 1999 relating to the acquisition of control of Atlantic Richfield Company is declared compatible with the common market and with the EEA Agreement.

Done at Brussels, 29 September 1999.

For the Commission
Mario MONTI
Member of the Commission

ANNEX

Undertakings presented by BP Amoco plc pursuant to Article 8(2) of Regulation (EEC) No 4064/89 with a view to eliminating competition concerns

1. Definitions**1.1. In these undertakings:**

'ABL'	means Arco British Limited (a wholly owned subsidiary of Arco);
'approval date'	means the date of the Decision issued by the Commission pursuant to Article 8(2) of Regulation (EC) 4064/89 declaring the concentration between BPA and Arco compatible with the common market subject to BPA complying with the undertakings set out herein or, in the absence of any such Decision, the date upon which, pursuant to Article 10(6) of that Regulation, the said concentration is deemed to have been declared compatible with the common market;
'Arco'	means Atlantic Richfield Company;
'BPA'	means BP Amoco plc;
'BP Amoco affiliate'	means any company over which, or the purposes of Article 3(3) of Council Regulation (EC) 4064/89, BPA has the possibility of exercising decisive influence;
'Commission'	means the Commission of the European Communities;
[...]	
'Merger Agreement'	means the Agreement and Plan of Merger dated as of 31 March 1999, and made among BPA, Arco and Prairie Holdings, Inc.;
'nominee'	means the person appointed by BPA pursuant to paragraph 2.5, 2.6 or 2.7 (as the case may be);
'relevant assets'	means the following: [...]
[...]	

2. Divestment of relevant assets and related matters**2.1. BPA hereby undertakes to the Commission:**

- 2.1.1. to procure that ABL shall, no later than by [a specified time], have transferred legal title to the relevant assets to one or more purchasers approved by the Commission; and
 - 2.1.2. not without the Commission's prior approval to reacquire, and to procure that the BP Amoco affiliates shall not without the Commission's prior approval reacquire, any of the relevant assets, provided that if by the 14th day after the date upon which BPA sends a written request to the Commission seeking such approval, the Commission has not given written notice to BPA denying such approval, the Commission shall be deemed to have given such approval.
- 2.2. If at any time after the concentration completion date the Commission has reasonable grounds to suspect that BPA is failing to comply diligently with the undertaking given in paragraph 2.1.1 above, the Commission shall have the power to appoint a trustee.
 - 2.3. If by [a specified date], ABL has not transferred legal title to the relevant assets to one of more purchasers approved by the Commission, BPA shall appoint a trustee.
 - 2.4. The appointment of a trustee pursuant to paragraphs 2.2 and 2.3 shall be effected, and the mandate of any trustee so appointed, shall be as described in the Appendix hereto.

- 2.5. By [a specified date] after the approval date, BPA shall submit to the Commission the name of a person, independent of BPA, who BPA considers appropriate (in view of that person's knowledge and experience) to act as BPA's nominee (the nominee) for the purposes of participating after the concentration completion date in any discussions with the owners of equity interests in the relevant assets and exercising ABL's right to vote at meetings of the Operating Committees of the relevant assets in regard (in either case) to the transportation and/or processing in any of the relevant assets of gas owned by any party which does not own an equity interest in the relevant asset in question.
- 2.6. If the Commission rejects the name submitted to it by BPA pursuant to paragraph 2.5 above, BPA shall, within seven days of receiving written notice of such rejection, submit the name of an alternative person to act as nominee, provided that if by the 14th day after that date upon which BPA submits the name of a person to act as nominee (whether pursuant to paragraph 2.5 or pursuant to this paragraph 2.6), the Commission has failed to give BPA written notice of rejection of the person so named, that person shall be deemed to have been approved by the Commission to act as nominee.
- 2.7. In the event that the Commission, upon reasonable grounds, rejects two individuals proposed consecutively by BPA to act as nominee, the Commission shall name an alternative individual having the requisite degree of knowledge and experience to act as nominee, and within seven days of the Commission having done so, BPA shall appoint that person as nominee.
- 2.8. If upon reasonable grounds the Commission considers that the nominee is failing to carry out diligently his/her mandate, the Commission shall be entitled to give written notice thereof to BPA, in which event a new person shall be appointed (in accordance with the procedure described in paragraphs 2.5 to 2.7 above, *mutatis mutandis*) to act as nominee.
- 2.9. The nominee's mandate shall be to ensure that during the period commencing on the concentration completion date and ending on the date upon which legal title to a relevant asset is transferred to a purchaser approved by the Commission, ABL's rights under the Operating Agreement (or similar) in relation to the transportation and/or processing in that relevant asset of gas owned by parties who have no equity interest in that relevant asset, are exercised in the best interests of the relevant asset in question. In addition to the foregoing, the nominee shall from time to time (and no less frequently than every two months) provide a written report to the Commission on progress in the discharge of the nominee's mandate.

3. Notices and other communications

- 3.1. All notices and other written communications between the Commission and BPA required by or relating to the undertakings contained herein (including the Appendix hereto) shall be sent by facsimile or by overnight courier to the following number/address:

If to the Commission:

— if by facsimile: (32—2) 296 43 01,

— if by courier:

Commission of the European Communities (DGIV B)
150 Avenue de Cortenbergh/Kortenberglaan 150
Brussels
Belgium

marked for the attention of the Director in charge of merger control;

If to BPA:

— if by facsimile: (44—207) 496 45 71,

— if by courier:

BP Amoco Legal
BP Amoco plc
Britannic House
1 Finsbury Circus
London EC2M 7BA
United Kingdom

marked for the attention of Juan A. Rodriguez, solicitor.

- 3.2. Each notice and other communication sent by facsimile shall be deemed to have been received on the day and at the time indicated in the transmission report issued by the facsimile unit from which the said notice or other communication was sent unless such time is after 5 p.m. in the country of receipt or such day is not a working day in the country of receipt, in which event the said notice or other communication shall be deemed to have been received at 10 a.m. on the next working day in the country of receipt. Each notice and other communication sent by overnight courier shall be deemed to have been received on the day and at the time indicated in the acknowledgment of receipt given to the individual who effects such delivery unless such time is after 5 p.m. in the country of receipt or such day is not a working day in the country of receipt, in which event the said notice or other communication shall be deemed to have been received at 10 a.m. on the next working day in the country of receipt.

4. Reports and approval of purchaser(s) of relevant assets

4.1. BPA shall:

- 4.1.1. promptly inform the Commission of all material developments (including but without limitation the identity of any proposed purchaser of the relevant assets) that relate to the compliance by BPA with the undertakings set out herein; and
- 4.1.2. every two months during the period commencing on the approval date and ending at such time as legal title to the relevant assets has been transferred to one or more purchasers approved by the Commission, send to the Commission a written report describing the current status of the divestment process being followed in relation to the relevant assets.
- 4.2. At such time as BPA gives notice to the Commission of the identity of any proposed purchaser of any of the relevant assets, BPA shall include in such notice such information as BPA possesses in regard to the matters indicated in points (i) to (iv) of paragraph 4.3.
- 4.3. The Commission shall use its best endeavours to inform BPA within 14 days after receiving any notice sent pursuant to paragraph 4.2 above of the suitability of any proposed purchaser(s) of the relevant assets. The Commission, in determining whether any proposed purchaser is suitable, will take into account whether the prospective purchaser concerned: (i) appears to possess the status and resources necessary to own the relevant asset in question as a viable competitor to BPA; (ii) is independent of BPA; (iii) can be shown not to have significant and relevant commercial connections with BPA which may call into question its independence from BPA; and (iv) has, or reasonably can obtain, all necessary approvals from the relevant competition authorities and other regulatory authorities in the European Community and elsewhere (if necessary). If by the end of the 14th day after receiving any notice sent pursuant to paragraph 5.2 above, the Commission has not given BPA written notice of rejection of any proposed purchaser (specifying in reasonable detail the reasons for such rejection), the proposed purchaser(s) named in that notice shall be deemed to have been approved by the Commission as suitable to purchase the relevant asset in question.

5. Duration of undertakings

The undertakings given by BPA herein shall automatically lapse if and at such time as the Merger agreement is terminated pursuant to Article V thereof, or, if for any other reason, the proposed concentration between BPA and Arco does not proceed or is abandoned.

Appendix

1.
 - (a) If the Commission decides to exercise the powers referred to in paragraph 2.2, it shall request BPA to propose to the Commission, within seven days of BPA receiving notification of such request, the names of at least two experienced investment banks or similar such institutions, independent from BPA, whom BPA considers appropriate to be appointed as trustee.
 - (b) If by the later of the relevant date and the concentration completion date, ABL has not transferred legal title to the relevant assets to one or more purchasers approved by the Commission, BPA shall, by the seventh day after the later of the relevant date and the concentration completion date, propose to the Commission the names of at least two experienced investment banks or similar such institutions, independent from BPA, whom BPA considers appropriate to be appointed as trustee.
 - (c) The Commission shall have the discretion to approve or reject one or both of the names submitted by BPA pursuant to paragraphs 1(a) and/or 1(b) of this Appendix, save that if by the 14th day after the date upon which BPA submits such names, the Commission has not given BPA written notice that the Commission rejects the institutions so named by BPA, such institutions shall be deemed to have been approved by the Commission. If, pursuant to the foregoing, only one name is approved, BPA shall appoint the institution concerned as trustee. If more than one name is approved, BPA shall be free to choose the trustee to be appointed from among the names approved.
 - (d) If all the names submitted pursuant to paragraph 1(c) of this Appendix are rejected, BPA will submit the names of at least two further such institutions ('the further names') within seven days of being informed of the rejection. If only one further name is approved by the Commission (or deemed to have been so approved because the Commission has failed within 14 days of receiving the further names to have given BPA written notice that the Commission rejects such further name), BPA shall appoint the institution concerned as trustee. If more than one further name is approved, BPA shall be free to choose the trustee to be appointed from among the names approved.
 - (e) If all further names are rejected by the Commission, the Commission shall nominate a trustee to be appointed by BPA.
2. As soon as the Commission has given approval to one or more names submitted, or nominated a trustee, BPA shall appoint the trustee concerned within seven days thereafter.
3. The trustee's mandate shall comprise the following functions:
 - (a) to monitor BPA's maintenance of the viability and market value of the relevant assets, and that each of the relevant assets is being operated in the normal course of business and consistent with its status;
 - (b) to monitor the satisfactory discharge by BPA of its obligations under the undertaking given in paragraph 2.1.1 (save that any trustee appointed pursuant to paragraph 2.3 shall, in addition to the other duties forming part of his/her mandate, be required by [...] after his/her appointment to transfer legal title to the relevant assets to one or more purchasers approved by the Commission [...]). In particular, the trustee shall:
 - (i) monitor and advise the Commission as to the adequacy of the procedure for selecting purchasers to purchase the relevant assets and as to the conduct of the negotiations with each such purchaser;
 - (ii) monitor and advise the Commission as to whether the agreements to be entered into with each purchaser of one or more of the relevant assets will properly provide for the divestiture of the relevant asset(s), as provided for in the undertaking given in paragraph 2.1.1; and
 - (c) to provide written reports ('the trustee's reports') to the Commission on progress in the discharge of the trustee's mandate, identifying any respects in which he/she has been unable to discharge his/her mandate. Such reports shall be provided at regular monthly intervals commencing one month after the date of his or her appointment, or at such other time(s) or time periods as the Commission may specify.

4. At any time during the term of the trustee's appointment, the Commission may, if on reasonable grounds, it believes that the undertaking given in paragraph 2.1.1 is not being properly complied with, request the trustee to carry out the following additional functions ('the request'), and the trustee's mandate shall be deemed to be extended accordingly (save that in the event of conflict with the initial functions (as specified in paragraph 3 of this Appendix), the trustee shall give priority to the discharge of these additional functions):
 - (a) to ensure that the relevant assets are not being operated other than in the normal course of business consistent with their status;
 - (b) to ensure the proper divestment of the relevant assets;
 - (c) in the trustee's reports, or in any event within no later than one month of being notified of the request, to submit to the Commission a proposal for the method and timescale proposed by the trustee for the divestiture in accordance with the undertaking given in paragraph 2.1.1 of the relevant assets (in which event the Commission will, as soon as reasonably practicable, approve the proposal or indicate any changes that it may require);
 - (d) in the trustee's reports, or as soon as negotiations are entered into with prospective purchasers, to provide to the Commission sufficient information to enable the Commission to decide on the suitability of the purchaser(s) in question;
 - (e) to break off negotiations with any prospective purchasers, or to instruct BPA to break off such negotiations, if it appears to the Commission that the negotiations concerned are being conducted with an unsuitable purchaser; and
 - (f) to submit to the Commission for approval an agreement for sale and purchase of the relevant assets (or any of them); such agreement to be unconditional on both purchaser and seller and irrevocable except for the approval(s) required from the Commission, and any approvals required from any other authority or person.
 5. BPA undertakes to provide the trustee with all such assistance and information, including copies of all relevant documents, as he or she may reasonably require in carrying out his or her mandate, and to pay reasonable remuneration for his/her services.
 6. If BPA should announce that the proposed concentration between BPA and Arco has been irrevocably abandoned, the trustee's mandate(s) shall be deemed to be discharged, and his/her appointment shall forthwith be terminated.
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COMMISSION DECISION
of 26 July 2000
on the measure and State aid
implemented by Germany for the SICAN group and its project partners
(notified under document number C(2000) 2466)
(Only the German version is authentic)
(Text with EEA relevance)
(2001/46/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular 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 Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty⁽¹⁾, and in particular Article 7 thereof,

Having regard to the Commission Decision of 11 March 1998⁽²⁾ to initiate the procedure laid down in Article 88(2) in respect of State aid C 20/98,

Having called on interested parties to submit their comments pursuant to those provisions⁽³⁾,

Whereas:

- (4) By letter dated 26 May 1998 the Commission informed Germany that it had decided to initiate the procedure laid down in Article 88(2) of the EC Treaty in respect of the aid.
- (5) The Commission 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 aid, but received no such comments.
- (6) Following the letter informing it of the initiation of the procedure, Germany sent the Commission additional information on the following dates: 21 July 1998, 14 September 1998, 24 November 1998, 11 January 1999, 17 February 1999, 3 March 1999, 27 April 1999, 15 June 1999 and 16 June 1999.
- (7) Representatives of Germany and of the Commission held meetings on 30 September 1998 and 20 May 1999.
- (8) On 2 February 2000 the Commission requested further information, which Germany provided by letter dated 15 March 2000.

I. PROCEDURE

- (1) By letter dated 30 September 1996 a complaint was lodged with the Commission concerning a presumed EUR 150 million of State aid to SICAN, a firm located in Hannover, Lower Saxony.
- (2) By letter dated 4 November 1996 the Commission asked Germany for information, which the Federal Government provided by letter dated 20 March 1997. In addition to this information, the Federal Government sent three separate messages informing the Commission that aid had been granted.
- (3) The Federal Government provided additional information at a meeting on 2 December 1997 between representatives of Germany and of the Commission.

II. DETAILED DESCRIPTION OF THE MEASURES AND OF THE PRESUMED AID

- (9) On the basis of the information which the Commission had in its possession at the time of initiation of the procedure, the facts were as follows⁽⁵⁾.

A. THE GROUP

- (10) In 1989 the Government of the *Land* of Lower Saxony decided, within the framework of the European project 'JESSI', to set up, together with the Federal Government, SICAN as a strategic centre of competence for the key

⁽¹⁾ OJ L 83, 27.3.1999, p. 1.

⁽²⁾ OJ C 307, 7.10.1998, p. 13.

⁽³⁾ See footnote 2.

⁽⁴⁾ See footnote 2.

⁽⁵⁾ Detailed information is to be found in the Commission notice to the other Member States (initiation of the procedure in the SICAN case), see footnote 3.

technology of microelectronics and their utilisation in areas of industry and services in order to support and provide Lower Saxony enterprises with the necessary skills in the fields of telecommunications, consumer electronics, data technology, mechanical engineering and electrical engineering in applying microelectronics, by carrying out research projects together with or for them. Subsequently, the group was reorganised and acquired the structure that was to be its until 1998. While the enterprises of the SICAN group were organised as private limited companies (GmbHs), they were, according to the German authorities, set up to fulfil the public service task described above, and State influence is said to have been exercised through the supervisory organs of the parent company.

(11) The SICAN group was composed of a management holding company SICAN Beteiligungs-GmbH (hereinafter 'SIBEG'), two operating subsidiaries SICAN GmbH (hereinafter 'SICAN') and SICAN F&E-Betriebs-GmbH (hereinafter 'SIBET') and a company owning the assets of the group SICAN Anlagen Verwaltungs GmbH (hereinafter 'SIAG'). SIBEG was primarily owned by German and American companies. SICAN was a wholly owned subsidiary of SIBEG. The shares in SIBET were held by SIBEG (51 %) and Nord/LB and some German *Länder* (49 %). The only shareholder in SIAG was Nord/LB, as a result of which SIAG was indirectly state-owned.

(12) SICAN carried out more than 500 precompetitive development projects under contract to private customers between 1990 and 1998. SIBET is said to have been primarily non-profit oriented and not active in the market. It also carried out R & D projects but mostly at the stage of industrial research, in collaboration with partners from industry and research institutes. SIAG was non-profit oriented and owner of the assets of all SICAN companies (buildings, plant, software and other equipment). It placed these assets at the disposal of SICAN and SIBET and rendered services to these companies through its staff.

B. THE PRESUMED AID

(a) Amounts granted

(13) The procedure was initiated on the basis that more than EUR 100 million of public funding had been granted to the SICAN group between 1990 and 1998, the bulk of which was given to SIAG to finance the assets of the group and to cover operating costs.

(14) From 1990, the group received more than EUR 100 million of public funding from federal and *Land* sources. The lion's share went to SIAG to finance the assets of the group (EUR 57,5 million (DEM 113,74 million)) and

for operating costs (EUR 5,92 million (DEM 11,71 million)). SIBET received EUR 31,76 million (DEM 62,79 million) for investment and R & D projects. SICAN received EUR 13,64 million (DEM 26,97 million) as start-up funding in 1990/1991 and has been self-supporting ever since.

(b) Aid to project partners of SIBET and SICAN

(15) As far as direct aid is concerned, EUR 5,11 million (DEM 10,11 million) was given to SIBET to be passed on as project funding to its collaboration partners (research institutes and industry). The maximum intensity for industrial partners was 50 %. The projects were claimed to qualify as industrial research. No direct project funding was given to partners of SICAN.

(16) As far as any indirect benefits to the partners of SIBET and SICAN are concerned, the German authorities claimed that SIBET and SICAN rendered their services, if not at market prices, then at least at full cost and hence did not pass on any indirect benefits to other enterprises.

(c) Aid to SICAN and SIBET as such

(17) As far as aid to SICAN and SIBET is concerned, beyond the direct funding mentioned in recital 15, advantages were transferred from SIAG to SICAN and SIBET through the billing of services rendered by SIAG. While SIAG billed SICAN and SIBET for the full cost of personnel services, the German authorities declared that the fees paid for the use of the assets owned by SIAG did not include depreciation costs or the EUR 5,92 million (DEM 11,71 million) that SIAG had received to cover operating costs.

(d) Position of Germany

(18) In Germany's view the aid granted for projects of SICAN and SIBET was in keeping with the Community framework for State aid for research and development⁽⁶⁾ (R & D framework) since the average intensity never exceeded the intensities permissible under the framework.

(19) In addition, Germany had submitted three 'NN notifications' by letter dated 20 March 1997, which were described in greater detail in the notice on the initiation of the procedure.

⁽⁶⁾ OJ C 45, 17.2.1996, p. 5.

- (20) Finally, at the meeting on 4 December 1997, Germany's representatives asserted that aid to the project partners of the SICAN group could fall under a research and development scheme approved by the Commission, without specifying which aid scheme.

III. DECISION OF THE COMMISSION TO INITIATE THE PROCEDURE

- (21) The Commission initiated the formal investigation procedure⁽⁷⁾ because, on the basis of the information in its possession, it doubted whether the conditions of the R & D framework were fulfilled. In order to assess this, it would, *inter alia*, have been necessary to attribute the aid involved to specific research projects and then to determine the research stage and quantify the total amount of aid granted, so as to allow for a calculation and evaluation of the aid intensity involved and to demonstrate the necessity and the incentive effect of the aid. The German authorities had not provided the information that was needed in order to make such an assessment. In particular, they had not been able to demonstrate that the SICAN group applied a cost-accounting system which would have made it possible to guarantee that all services were rendered by the company to third parties at the market price or at full cost.

IV. COMMENTS FROM INTERESTED PARTIES

- (22) The Commission received no comments from interested parties.

V. COMMENTS FROM GERMANY

- (23) In response to the Commission's decision to initiate the Article 88(2) procedure, the German authorities provided extensive information which may be summarised as follows.

A. DIRECT AID TO PROJECT PARTNERS OF SIBET

- (24) With regard to direct aid to project partners of SIBET, Germany emphasised that it was the aim of the industrial research projects carried out with collaboration partners to provide an incentive to apply microelectronics and thereby increase the level of skill of the collaboration partners through concrete research projects. Germany submitted lists showing that SIBET carried out 17 projects at the stage of industrial research. For these projects, collaboration partners

received a total of DEM 9,73 million (EUR 4,97 million), of which DEM 2,7 million (EUR 1,38 million) went to public research institutes and DEM 7 million (EUR 3,58 million) to 15 industrial partners. Germany submitted project descriptions of those 15 projects as requested by the Commission and claimed that all projects had rightly been classified as industrial research. The listed individual amounts of aid granted to these 15 companies and the list of project costs incurred by them showed that the ceiling of 50% of project costs was not exceeded.

- (25) Five project partners were not covered by the definition of small and medium-sized enterprise (SME) in accordance with the Community guidelines on State aid for small and medium-sized enterprises⁽⁸⁾. In one case, the aid amount (below DEM 36 000 or EUR 18 406) was beneath the *de minimis* threshold as laid down in the Commission notice on the *de minimis* rule for State aid⁽⁹⁾. For the other four companies, Germany provided information which was supposed to explain why the aid served as an incentive within the meaning of point 6 of the R & D framework for the company to carry out the research.

- (26) The 15 projects are described below. Unless the name of the company is given, the recipient was an SME as defined by the Community.

- (27) Project 1005:

A module for processing sensor data was developed which can perform a variety of functions and has very small physical dimensions. As a result, new technical functions can be carried out which considerably improve performance in mechanical engineering. This is therefore an industrial research project in which, through systematic exploration of the technologically innovative functions, the knowledge obtained can be used to improve existing mechanical engineering techniques considerably: for instance, in the machine tool industry, the module can be used to determine the degree of abrasion of diamond grinding discs and hence improve their utilisation (the discs are very expensive). In addition, unlike traditional methods, the electronics developed mean that various machine components and controls can be directly linked through the CAN bus.

Aid amounting to DEM 166 000 (EUR 84 874) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

⁽⁷⁾ See footnote 2.

⁽⁸⁾ OJ C 213, 23.7.1996, p. 4.

⁽⁹⁾ OJ C 68, 6.3.1996, p. 9.

(28) Project 1006:

A new type of control system for CO₂ laser welding was developed which, by regulating the laser power, radically improves weld quality. This makes the whole welding process more efficient. Hitherto, optimum processing parameters had to be determined empirically through lengthy trials. The results of the project help directly to improve both the production process and the product quality. This is therefore an industrial research project in which the knowledge obtained by systematic exploration can be used to improve existing methods of CO₂ laser beam welding considerably. As a rule, a visual inspection of the processed work used to be necessary, but this can now be substantially reduced.

Aid amounting to DEM 117 000 (EUR 60 076) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(29) Project 1008:

Radio microphones are used for the wireless transmission of high-grade audio signals in TV studios, televised theatre and concert halls. The transmission quality of existing analogue FM systems is of VHF-FM sound broadcasting standard, enhanced by a companding system. However, this will no longer be sufficient for future sound recording requirements (CD quality). In this industrial research project, a working model of a pioneering, completely digitised radio microphone system was developed, which provided the basis for the series production of a technically innovative product and hence meant that the knowledge acquired could be used to improve existing products considerably.

The developed transmission system has not been further developed to the stage of industrial use; rather, systematic knowledge and comprehensive, detailed knowledge has been accumulated by the partners, which are the basis for further developments.

Aid amounting to DEM 362 691 (EUR 185 440) was granted to Sennheiser, the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

With regard to the incentive effect, Germany stated that the project was technically pioneering at that time. Sennheiser's development department could not have carried out such a project to such a high technical

standard without the financial support and the collaboration with a highly qualified project partner. Since the cooperation with a young company with little experience in the market segments presented a risk for Sennheiser which was difficult to assess (the project was one of the first ones of the SIBET group), it would certainly not have been carried out without the aid. The risk can also be seen from the fact that the development took considerably longer than originally envisaged.

(30) Project 1009:

The aim here was to develop a sensor system for registering excessive ozone concentrations, which can be caused by air-disinfection or odour-control equipment. The system was derived from a semiconductor gas sensor unit consisting of a new, microstructured semiconductor gas sensor, a microcontroller circuit and a voltage control for an air-disinfection unit. Similar systems are not available on the market at present. The system for regulating the ozone concentration is currently used for long-term measurements in air-conditioning systems. It represents a substantial improvement on commercially available systems. Thus the knowledge obtained from this industrial research project can be used to improve measuring methods and systems considerably.

Aid amounting to DEM 142 500 (EUR 72 859) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(31) Project 1010:

In the field of broadband communications technology, synchronous digital hierarchy (SDH) has become the worldwide communications standard. In particular, SDH technology makes visual communication (e.g. videoconferences) and the linking of local computer networks possible. The ATM process utilised means that a broadband ISDN can be introduced which all existing and future services will make available to network customers via optical fibre. Among the other things developed in this project were key components for an ATM system. The results of the research make considerable improvements in ATM applications and systems possible. For instance, the hardware and software components developed form the basis for innovative products in multimedia applications.

Aid amounting to DEM 1 822 398,92 (EUR 931 777) was granted to Ericsson Eurolab, the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

With regard to the incentive effect Germany stated that, when the project started and the aid was approved, Ericsson Telekom GmbH had roughly 185 employees. The company had been set up as a joint venture between Ericsson and FUBA, which holds 49% of the shares.

Through the broadly planned research project, both SIBET and the project partner got involved in an area of microelectronics which was new to them (deep submicron). Within the project, the partners primarily gained expertise which indirectly influenced the further development activities of the project partners, while the developed products did not allow for direct industrial use, but only served to prove, in principle, the feasibility of the envisaged objectives.

The industrial partner would not have carried out the project to the stated technological standard and with a cost share of roughly DEM 3,6 million, had not the aid amounting to DEM 1,8 million served as a financial incentive. The project was too remote from the general day-to-day business of Ericsson Eurolab.

The project resulted in the creation of additional jobs for qualified engineers in the R & D field, in particular in order to develop further the knowledge gained through the project.

(32) Project 1013:

Companies wishing to establish themselves on the world weighing-technology market are forced to offer a wide range of products in order to provide optimum solutions for their many different customers. The aim of the project was, by modularising the electronics, to shorten development times and reduce logistical expenditure. By using multichip module technology and ASIC developments, it was possible to develop a new generation of weighing and measuring products. The knowledge acquired helps to improve existing systems and methods considerably and can be utilised for the development of new products in this market segment.

Aid amounting to DEM 679 677,01 (EUR 347 513) was granted to Sartorius, the industrial cooperation partner. The aid intensity corresponded to less than 50% of the project costs incurred by the partner (DEM 1,4 million).

With regard to the incentive effect Germany stated that, within the project, basic knowledge for new techniques (modularisation of electronics, use of multichip modules and ASIC-developments) for use in electronic scaling was developed. The objective of this project went

beyond the competence of Sartorius in R & D and therefore did not form part of the normal day-to-day business of the R & D department. Without aid, the industrial partner would not have envisaged such a far-reaching R & D project in this field, since the effort and the risk would have been too high.

For the project, scientists at Sartorius put in roughly 10 000 hours, corresponding to seven man years.

(33) Project 1014:

The brisk spread of mobile radio is leading to rapid generational change in terminal equipment and network hardware (base stations, aerials and repeaters) and, at the same time, to greater coverage. Repeaters bridge areas in which no direct radio contact between base and receiver is possible. The aim of the project was to develop a low-cost repeater system using new set-up and linking techniques. As well as flexible design, opportunities to reduce the costs of the entire system in the development stage and the later production stage were to be investigated at all operational units. By using new technologies and development methods, it was possible to improve current levels of performance in these areas substantially. Knowledge of new methods of developing the necessary components was acquired from this industrial research project, and the results can be used for designing new systems.

Aid amounting to DEM 701 664,50 (EUR 358 755) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(34) Project 1015:

Under this project, a low-cost, low-maintenance measuring and control system was developed for continuously recording water quality in canals. By using new, smart signal-processing algorithms (fuzzy logic and artificial neuron networks), the problem of determining water quality was reduced to magnitudes which were simple to measure. With this approach, an innovative method of controlling reservoirs was devised, making possible substantial savings in building costs and avoiding the need for extensions. This means that the knowledge acquired from this industrial research project can be used to make considerable improvements in both existing reservoirs and those still under construction.

Aid amounting to DEM 411 615,10 (EUR 210 455) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(35) Project 1016:

In the automobile components supply industry, sensor systems with very specific qualities are needed which are not freely available on the market, or not at suitable prices. The trend today is clearly towards integrated sensor and system solutions which can be manufactured using semiconductor mass production technology. Suitable signal transmission techniques and control of sensor balancing are critical if the sensors are to be usable. In the project, a sensor signal amplifier for use in motor vehicles was developed which could be adapted to sensor components; its design was miniaturised to save space. With the module that was developed, any sensor component can be balanced quickly, reliably and cheaply using a resistance bridge. Sensors have previously been balanced using individual resistances with a narrow tolerance range, which are subsequently soldered manually into the electronics. By using the modules and processes developed in this project, a clear improvement in costs and quality could be achieved compared with traditional sensor-balancing methods. The knowledge acquired in this industrial research project is extremely useful for the optimisation of existing, and the development of new, procedures.

Aid amounting to DEM 666 739 (EUR 340 898) was granted to Wabco, the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

With regard to the incentive effect, Germany stated that the project served to develop a method which avoids the expensive calibration of sensors through use of intelligent circuits. The results of the research were to be converted into a functional ASIC model.

The technological standard of the project went far beyond the capabilities of Wabco's R & D department. It was the first time SIBET had entered into such a technically demanding commitment in the area of the development of integrated circuits for use in vehicles, for which a particularly high degree of reliability is expected due to the additional difficulties resulting from in-vehicle operation. The high technical risk is evident from the fact that the ASIC developed on the basis of the knowledge gained in this project has never been ready to go into production and has never been used in a modified or more highly developed form in any of the company's products and hence has not been put to any direct commercial use.

Against this background it is clear that, had not a considerable amount of aid been granted to the industrial project partner, the project would have been less ambitious and probably would never have been finished owing to the difficulties which kept arising during the course of the project. It follows directly from this that the knowledge and know-how gained during the project, important as it is to future developments, would not have become available until later, if at all.

The project absorbed considerable capacity within the electronics development department of the industrial partner, as is to be expected with skilling measures.

(36) Project 1019:

The testing of integrated circuits during development and before incorporation into the final product is becoming increasingly important as far as quality and costs are concerned. Rapid advances in microelectronics require the continual improvement and extension of tester hardware. The development of test heads which have to be continually adapted to the increasing frequencies of the components to be tested is an essential task if competitive microelectronic components are to be developed and tested in this field. In this project, a high-performance test head was developed using modern assembly technology and bonding methods. Also developed was an integrated circuit which can quadruple the performance of testers currently available on the market. The principal users of the test head can work with optimised testing procedures and so improve the efficiency of their development and production divisions. Development times can be shortened and reject rates reduced. Thus the knowledge acquired from the research process can be used to go some way towards optimising existing methods and systems. At the same time, the requirements associated with an industrial research project are fully satisfied.

Aid amounting to DEM 423 950 (EUR 216 762) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(37) Project 1023:

A module which ensures anti-trapping was developed for motor vehicle window-opening mechanisms, especially for windows which close automatically. In addition to the anti-trapping function, the control module developed makes it possible to determine the window position by measuring the motor power supply without an additional sensor system. This results in

lower unit cost and cheaper installation. Current designs cannot easily be fitted with an anti-trapping device that meets all requirements, because their controls (using relays and mechanical limit switches) are too simple or because they need an additional sensor system. Consequently, the product developed in this project is a substantial improvement on existing solutions. As befits an industrial research project, the experience and results acquired can be used to improve existing methods considerably and, at the same time, as a basis for a completely new technology in the field of motor vehicle window-operating mechanisms.

Aid amounting to DEM 549 495,82 (EUR 280 952) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(38) Project 1024:

Monitoring intracranial pressure in hydrocephalus patients is an essential aspect of neurosurgery, as regards both post-operative care and the treatment of accident victims. A pressure sensor with signal processing was developed to measure the intracranial pressure between the cerebral membrane and the skull bone. An implantable telemetric data and energy transmission device supplements the sensor system. In addition, at a further stage, the telemetric pressure measuring unit will be fitted with an actively adjustable valve to allow controlled run-off of the cerebral fluid into the abdominal cavity. The medical engineering product resulting from this project substantially improves and simplifies existing monitoring and measuring techniques as far as both doctor and patient are concerned. The knowledge acquired can be used to improve existing methods of measuring intracranial pressure considerably and, at the same time, to develop new medical engineering products; it justifies the classification as an industrial research project.

Aid amounting to DEM 477 003 (EUR 243 887) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(39) Project 1025:

With the progressive integration of microelectronic circuits and systems, multichip modules (MCMs) are

becoming increasingly important. Multichip modules contain various electronic components (chips and sensors), very densely packed on a substrate. The comparatively high value of an MCM requires not only function control but also fault diagnosis so that a defect can be repaired. It is currently possible to test MCMs only with special solutions. The aim of the project is to make it possible to test MCMs using available testing systems and to develop special test methods so as to reduce testing costs. The availability of the software and mechanical components developed opens up a completely new product field. The industrial research project has resulted in hardware and software components which can supplement commercial testing systems and which make it economically viable to change to testing mixed analogue/digital systems. These can be used to improve existing processes considerably and, at the same time, as a basis for developing new processes and systems in this field. Accordingly, the requirements of an industrial research project are satisfied.

Aid amounting to DEM 236 683,26 (EUR 121 014) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(40) Project 1026:

An electronic unit was developed for controlling filling processes which use high-speed force flow packers. The fuzzy control technology makes it possible to regulate difficult processes. Where force flow packers are installed, the optimum adjustment of the filling process is particularly difficult using current technology. The solution devised in the project made it possible to fill sacks more quickly, even using different fillers. Quicker, automatic set-up is also possible when the force flow packer is initially installed, with the advantage that a sudden change in the characteristics of the filler can be recognised, the prescribed weight for filled sacks can be achieved more successfully and burst sacks can be avoided. The results will substantially improve the production process and existing automatic filling machines; among other things, this justifies the project's classification as an industrial research project.

Aid amounting to DEM 258 050 (EUR 131 938) was granted to the industrial cooperation partner. The aid intensity corresponded to 50% of the project costs incurred by the partner.

(41) Project 1027:

The processing of materials by laser will become increasingly important in many areas of manufacturing industry. Lasers allow very high processing quality and speeds. In this project an on-line error-detection system was developed for cutting and welding metal sheet. It speeds up processing time considerably and makes a decisive contribution to quality assurance. The error-detection system developed can be used to improve existing laser systems considerably and as an effective basis for the development of new processes in this field.

Aid amounting to DEM 35 261,31 (EUR 18 028) was granted to VW AG, the industrial cooperation partner. The aid intensity corresponded to 25% of the project costs incurred by the partner. The aid falls under the *de minimis* rule⁽¹⁰⁾.

- (42) Finally, Germany made clear that the aid to the partners had not, as asserted at the meeting on 4 December 1997, been granted on the basis of an approved R & D scheme of the *Land* of Lower Saxony.

B. INDIRECT AID TO CUSTOMERS OF SICAN AND SIBET

- (43) One reason for the initiation of the procedure was that Germany had not substantiated its claim that, in so far as SICAN and SIBET pursued market activities, they charged their customers the full cost of their services, taking into account all aid granted to the group. In particular, Germany could not demonstrate that SICAN had a cost-accounting system enabling it to determine the relevant costs for each individual project. Doubts therefore remained as to whether indirect advantages, which could also be considered State aid, had been passed on to customers.
- (44) Following the initiation of the procedure Germany confirmed that, apart from performing a public service task, SICAN and SIBET at the same time pursued market activities. SICAN carried out 793 precompetitive development projects under contract to companies, while SIBET carried out 233 such projects.
- (45) On the basis of the attribution of costs to different categories, the study presented by Germany calculates the costs per productive hour for SICAN employees. When establishing the costs incurred by SICAN and SIBET, the depreciation for use of the equipment owned by SIAG is taken into account as an advantage received

by SICAN and SIBET and is divided between the public service task and the market activities as well. On the basis of the examination of contracts with third parties, the study concludes that third parties were billed at least at full-cost prices.

C. CONSULTANCY SERVICES TO COMPANIES

- (46) Consultancy services to companies were provided free of charge but in accordance with the *de minimis* rule.

D. AID TO THE SICAN GROUP⁽¹¹⁾

- (47) Germany stated that the total amount of aid granted was DEM 206 million (EUR 105 million), of which SIBET received DEM 74,5 million (EUR 38 million), SIAG DEM 104 million (EUR 53 million) and SICAN, as already indicated, DEM 26,9 million (EUR 14 million).
- (48) With regard to the SICAN group, Germany stated that the public funding of SICAN would not constitute State aid since the group, while partly carrying out market-oriented activities, would for the most part fulfil a task of general public interest.
- (49) The task of general public interest can be described more specifically as follows: while the overall objective was to provide companies in the region with the skills needed in order to participate in the JESSI programme, it was proposed to train university graduates in microelectronics in order to enable them to participate in JESSI and similar programmes. Such training was provided as of 1993. It was directed primarily at postgraduate students, PhD students and students in microelectronics. During the training, trainees were employed by the SICAN group on a short-term basis, but were not under contract to a future employer. Trainees received practical project training, which was provided by the regular staff members of the SICAN group, mostly SICAN and SIBET.
- (50) NIGAN e. V. was founded in 1993 specifically to recruit and train trainees (PhD students, students about to take their diplomas, student trainees) and to support the further education of engineers and scientists in microelectronics. While it was NIGAN that designed and organised the training programmes for postgraduate trainees, most of the training, which was done on the project, was carried out by SICAN and SIBET.

⁽¹⁰⁾ See footnote 9.

⁽¹¹⁾ Including potential aid to SIBEG shareholders through the training of future employees of those shareholders.

- (51) The overall number of trainees in the SICAN group was as follows:

	1993	1994	1995	1996	1997	1998	Total
No of trainees	209	185	215	360	314	156	1 439
Average period in months	5	5,5	6,3	5,3	5,2	6,3	
No of regular staff (posts)	114	103	152	247	205	312	

From 1993 until 1998, the total number of trainees in SICAN was 831, while 435 trainees received training in SIBET. For SICAN and SIBET alone, this gives a total number of 1 266 trainees. In addition, a smaller number of trainees (173) was allocated to other entities in the group.

SICAN and SIBET and was divided between the public service task and the market activities.

- (52) Since the cost-calculation system of SICAN at that time did not distinguish between costs incurred in the fulfilment of the public service task and costs incurred for market activities, Germany engaged a consultancy firm to carry out such a distinction retrospectively based on the documentation provided by the SICAN group. The costs of the respective activities were separately determined and compared with the public funding received. The years 1993, 1995 and 1998 were subjected to particularly close scrutiny. In April 1999 Germany submitted a study on the allocation of costs and the corresponding allocation of the State funding received.
- (53) On the basis of the study's findings, Germany asserts that it can now state positively that all the public funding received by the SICAN group was employed in its entirety for funding the task of general common interest and thus did not constitute State aid within the meaning of Article 87(1) of the EC Treaty.
- (54) For the staff members involved in the training activity, a certain percentage of their working hours was attributed to providing training. The working hours of trainees were regarded partly as productive work for the SICAN group and partly as training.
- (55) When establishing the costs incurred by SICAN and SIBET, the depreciation for use of the equipment owned by SIAG was taken into account as a benefit received by
- (56) Germany confirmed that, while fulfilling a task of general common interest, SICAN and SIBET pursued at the same time market activities. While for SIBET this market activity was less significant, for SICAN it soon accounted for the major part of its activities.
- (57) In Germany's view, inasmuch as the SICAN group carried out a task of general interest, it has to be regarded as a public non-profit research and training establishment. In the case of the industrial research carried out by SIBET, the results were published and made available to companies on non-discriminatory terms, as can be seen from the publication lists and examples of publications submitted by Germany.
- (58) Germany concludes that the SICAN group has, for its non-market activities, to be considered a public research institute and the public funding received cannot be classed as State aid within the meaning of Article 87(1) of the EC Treaty.
- (59) At the Commission's request Germany provided information on any profits made by SIBET. The detailed calculations show that SIBET did not make any profits. The results of the group as a whole were balanced or slightly positive, except for 1995 and 1997 when the group made a loss.
- (60) Germany submitted lists showing that SIBET carried out 17 projects at the industrial research stage at a total cost of DEM 43,2 million (EUR 22,09 million). In addition, it carried out 233 projects at the precompetitive development stage with a total contract value of DEM 13,3 million (EUR 6,80 million).

- (61) Germany also submitted a list with titles and contract values of the 793 precompetitive development projects carried out by SICAN under contract to companies, the total contract value being DEM 147 million (EUR 75,16 million).
- (62) With regard to the professional future of persons who had previously received training within the SICAN group, Germany presented the following information at the Commission's request.
- (63) Of the 510 engineers newly employed by the SICAN group between 1991 and 1997, 195 had previously benefited from skilling measures under the supervision of NIGAN. In such cases, the initial salary of the employee reflected the professional experience which the former trainee had acquired during the training process. Employment did not always directly follow the training measure. Only in a few cases did the employee continue to work on the same project as that on which he had previously been trained.
- (64) There has never been a contractual obligation for NIGAN trainees to work within the SICAN group for a certain period of time once the training was finished. Former trainees sought employment according to the options which the market offered. Therefore, the vast majority of them joined other companies without any regional limitation. As far as could be established by Germany, seven former trainees have joined shareholders of SIBEG.

E. PRIVATISATION OF THE GROUP

- (65) In 1998 the public service task was ended and the group was completely privatised. Four private companies became the shareholders of the SIBEG holding company.

VI. ASSESSMENT

- (66) As already indicated, the procedure was initiated because there was insufficient information on which to base a proper assessment as to whether the aid in question was compatible with the applicable State aid rules. The additional information obtained from Germany following the initiation of the procedure now leads to the following assessment.

A. DIRECT AID TO PROJECT PARTNERS OF SIBET

- (67) With regard to aid which was channelled through the SICAN group to project partners of SIBET, the Commission concluded that the SICAN group was managing a scheme on behalf of the State which consisted in financing industrial research projects. The aid granted to the project partners of SIBET constitutes State aid in that it strengthens the position of the recipients in comparison with competitors. The aid thereby has a potential effect on trade between Member States. It falls under Article 87(1) of the EC Treaty.
- (68) It is obvious that no derogation provided for in Article 87(2) and (3) other than Article 87(3)(c) under research and development can be applicable in the present case. The aid does not fall under Article 87(2). It is neither regional State aid, nor aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State or to facilitate the development of certain economic activities (except research and development) or to promote culture and heritage conservation. In any case, the German Government never invoked these derogations.
- (69) The aid might therefore qualify for exemption under Article 87(3)(c) of the EC Treaty if all the conditions of the Community framework for State aid for research and development⁽¹²⁾ are met. On the basis of the information provided by Germany following the initiation of the procedure, the Commission concludes, however, that this is not the case for all the projects in question. With regard to the eligible costs of the projects, the Commission has no doubts that the conditions of the R & D framework are met. With regard to the research stage, the resulting maximum permissible aid intensity and the incentive effect, the following may be said about each individual project.

- (70) Project 1005:

With regard to project 1005, the Commission concludes that a part of the project included the development of a data-treatment module which can be used industrially for mechanical engineering applications. The project therefore goes beyond precompetitive development⁽¹³⁾.

⁽¹²⁾ See footnote 6.

⁽¹³⁾ See Annex I, third indent, of the abovementioned framework.

Consequently, the project does not fall within the stage of industrial research⁽¹⁴⁾ and cannot even be regarded as precompetitive development. The granting of the aid was thus incompatible with the common market.

(71) Project 1006:

The German authorities have failed to demonstrate that the project is effectively industrial research. Indeed, in the project description it is stated that the results of the project contributed directly to the improvement of industrial processes and in particular of 'existing methods of CO₂ laser-beam welding'. The project therefore goes up to the point where it can be used industrially. The Commission finds therefore that the project goes beyond the stage of precompetitive development⁽¹⁵⁾.

Consequently, the project does not fall within the stage of industrial research⁽¹⁶⁾ and cannot even be regarded as precompetitive development. The granting of the aid was thus incompatible with the common market.

(72) Project 1008:

This project went up to the point where, according to the German authorities, 'a working model of a pioneering, completely digitised radio microphone system was developed, which provided the basis for the series production of a technologically innovative product'. It thus appears that the results of the project can be almost directly used for industrial production. The Commission regards the project as falling within the stage of precompetitive development. Accordingly, the aid intensity of 50 % was not justified⁽¹⁷⁾.

Sennheiser is a leading producer of high-quality microphones. It started developing and marketing wireless microphones for TV and radio studios back in the 1950s⁽¹⁸⁾. In a context of continuing changeover from analogue technologies to digital technologies⁽¹⁹⁾, it

is highly probable that Sennheiser would have embarked on a research project involving digitised radio microphone systems even without State aid. Against this background the Commission takes the view that the aid was not necessary as an incentive to the recipient to carry out the project⁽²⁰⁾. Nor can the partnership between Sennheiser and SIBET justify Sennheiser's not carrying out the research project unaided. Pursuant to point 6.5 of the R & D framework the Commission attributes particular importance to proof of an incentive effect when assessing aid for individual, close-to-the-market research projects undertaken by large firms, as is the case here.

The Commission therefore concludes that the incentive effect of the aid has not been suitably proven and the granting of the aid was accordingly incompatible with the common market.

(73) Project 1009:

The Commission concludes that the project falls within the definition of industrial research⁽²¹⁾. Since the aid was granted to an SME, the Commission assumes, as it may pursuant to point 6.4 of the framework, that the aid provided a necessary incentive for the firm to undertake the research.

The granting of the aid was thus compatible with the common market.

(74) Project 1010:

The Commission concludes that the project falls within the definition of industrial research⁽²²⁾. The results of the project have been suitably published, and the incentive effect has been reasonably justified. The granting of the aid was thus compatible with the common market.

(75) Project 1013:

The Commission concludes that the project included the development of new scaling and weighing devices and therefore went beyond the stage of precompetitive development⁽²³⁾. The aid is thus incompatible with the common market.

⁽¹⁴⁾ See Annex I, second indent, of the abovementioned framework.

⁽¹⁵⁾ See Annex I, third indent, of the abovementioned framework.

⁽¹⁶⁾ See Annex I, second indent, of the abovementioned framework.

⁽¹⁷⁾ See point 5.5, second paragraph, of the abovementioned framework.

⁽¹⁸⁾ See <http://www.sennheiser.com/Image/im1bX001.htm>.

⁽¹⁹⁾ See www.infowin.org/ACTS/ANALYSIS/PRODUCTS/THEMATIC/MMB/02/digital.htm: 'Digital broadcasting is set to displace analogue broadcasting, for both radio and TV, in the coming years' (copyright 'ACTS Information Window' — 1997; published on the website of the Advanced Communications Technology and Services programme, known simply as ACTS, one of the specific programmes of the 'Fourth Framework Programme of European Community activities in the field of research and technology development and demonstration (1994 to 1998)').

⁽²⁰⁾ See point 6.3 of the abovementioned framework.

⁽²¹⁾ See Annex I, second indent, of the abovementioned framework.

⁽²²⁾ See Annex I, second indent, of the abovementioned framework.

⁽²³⁾ See Annex I, third indent, of the abovementioned framework.

(76) Project 1014:

The Commission concludes that the project was not effectively industrial research. In its view, it included the development of a commercial product ('a low-cost repeater system') and therefore went beyond the stage of precompetitive development⁽²⁴⁾. The aid is thus incompatible with the common market.

effect has been reasonably justified⁽³⁰⁾. The aid can therefore be considered compatible with the common market.

(77) Project 1015:

The Commission concludes that the project was not effectively industrial research. In particular, it does not appear that new knowledge that could meaningfully be used for the development of new products, processes or services was acquired during the project. The aid intensity of 50 % was therefore not justified⁽²⁵⁾.

However, the project encompasses the development of an innovative control system based on new and relatively complex signal-processing techniques. The Commission therefore concludes that the aid qualifies as precompetitive development⁽²⁶⁾.

Since the recipient was an SME, it would have been permissible to grant aid amounting to 35 % of project costs (25 % basic aid intensity⁽²⁷⁾ plus a 10 percentage points bonus for SMEs⁽²⁸⁾). Since the aid was granted to an SME, the Commission assumes, as it may pursuant to point 6.4 of the framework, that the aid provided a necessary incentive for the firm to undertake the research.

The aid amount exceeding an aid intensity of 35 % is incompatible with the common market.

(78) Project 1016:

The Commission concludes that the project falls within the definition of industrial research⁽²⁹⁾. The incentive

(79) Project 1019:

The Commission concludes that the project falls within the definition of industrial research⁽³¹⁾. Since the aid was granted to an SME, the Commission assumes, as it may pursuant to point 6.4 of the framework, that the aid provided a necessary incentive for the firm to undertake the research. The granting of the aid can thus be considered compatible with the common market.

(80) Project 1023:

The Commission concludes that the project was not effectively industrial research: on the contrary, an anti-trapping module for motor vehicle window-opening mechanisms has been developed up to a stage which appears to be very close to market introduction. Consequently, the activity carried on under the project does not fall within the definition of R & D. The granting of the aid to the recipient was therefore incompatible with the common market.

(81) Project 1024:

The Commission concludes that the project falls within the definition of industrial research⁽³²⁾. Since the aid was granted to an SME, the Commission assumes, as it may pursuant to point 6.4 of the framework, that the aid provided a necessary incentive for the firm to undertake the research. The aid can thus be considered compatible with the common market.

(82) Project 1025:

The Commission concludes that the project falls within the definition of industrial research. Since the aid was granted to an SME, the Commission assumes, as it may pursuant to point 6.4 of the framework, that the aid provided a necessary incentive for the firm to undertake the research. The granting of the aid was thus compatible with the common market.

⁽²⁴⁾ See Annex I, third indent, of the abovementioned framework.

⁽²⁵⁾ See point 5.5 of the abovementioned framework.

⁽²⁶⁾ See annex I, third indent, of the abovementioned framework.

⁽²⁷⁾ See point 5.5 of the abovementioned framework.

⁽²⁸⁾ See point 5.10.1 of the abovementioned framework.

⁽²⁹⁾ See Annex I, second indent, of the abovementioned framework

⁽³⁰⁾ See point 6 of the abovementioned framework.

⁽³¹⁾ See Annex I, second indent, of the abovementioned framework.

⁽³²⁾ See Annex I, second indent, of the abovementioned framework.

(83) Project 1026:

The Commission concludes that the project was not effectively industrial research. In particular, it does not appear that new knowledge that could be useful for the development of new products, processes or services was acquired during the project. The aid intensity of 50 % was therefore not justified⁽³³⁾.

However, the project encompasses the design of an innovative control system based on new and relatively complex techniques, such as 'fuzzy logic'. The Commission therefore concludes that the aid qualifies as precompetitive development⁽³⁴⁾.

Since the recipient was an SME, it would have been permissible to grant aid amounting to 35 % of project costs (25 % basic aid intensity⁽³⁵⁾ plus a 10 percentage points bonus for SMEs⁽³⁶⁾). Since the aid was granted to an SME, the Commission assumes, as it may pursuant to point 6.4 of the framework, that the aid provided a necessary incentive for the firm to undertake the research.

The aid amount exceeding 35 % is incompatible with the common market.

(84) Project 1027:

The aid was granted in accordance with the *de minimis* rule and was therefore not subject to notification⁽³⁷⁾.

B. INDIRECT AID TO CUSTOMERS OF SICAN AND SIBET

- (85) On the basis of the new information in its possession, the Commission concludes that no indirect aid was transferred to customers of SICAN or SIBET, but that these customers were billed at least at full-cost prices, whereby not only the direct funding but also all indirect advantages received through SIAG were taken into account in the underlying retrospective cost calculation.

C. CONSULTANCY SERVICES TO COMPANIES

- (86) These services, provided in accordance with the *de minimis* rule, did not have to be notified.

D. AID TO THE SICAN GROUP⁽³⁸⁾

- (87) While Germany had, from the outset, claimed that SICAN had been set up to fulfil a task of general public interest, this task was originally described as that of supporting and providing with skills Lower Saxony enterprises by carrying out research projects together with or for them. No information describing in concrete terms this task of general public interest was provided which would have explained more precisely which additional activities, apart from the cooperation as a research partner, had been triggered by that task and had been carried out with a view to fulfilling that task.
- (88) On the basis of the detailed information subsequently provided, the Commission concludes that the activities of the SICAN group did in fact comprise what may be regarded in part as a task carried out in the general public interest.
- (89) In particular as regards the training provided to a large number of short-term employees, the Commission considers that it would not have been in the commercial interest of a firm to train so many university graduates who stayed with the company for an average period of some six months only. Following the training period, it was intended that the trainees should leave SICAN again. Germany indicated that a number of former trainees, 195, worked within the SICAN group after finishing their training. While this may represent a considerable proportion of engineers newly employed by the SICAN group, the Commission maintains that the number of trainees was, in any case, far too high in comparison with the permanent SICAN personnel for the training to be considered a useful selection mechanism for future employees which would have provided an indirect advantage for the SICAN group⁽³⁹⁾.
- (90) In any case, the starting salary of the employee reflected the professional experience which the former trainee had acquired in the training process and in most cases

⁽³³⁾ See point 5.5 of the abovementioned framework.

⁽³⁴⁾ See Annex I, third indent, of the abovementioned framework.

⁽³⁵⁾ See point 5.5 of the abovementioned framework.

⁽³⁶⁾ See point 5.10.1 of the abovementioned framework.

⁽³⁷⁾ See Commission notice on the *de minimis* rule (footnote 10).

⁽³⁸⁾ Including potential aid to SIBEG shareholders through the training of future employees of those shareholders.

⁽³⁹⁾ See paragraph 51.

the employee did not continue to work on the project on which he had been trained. Since at the time of the training trainees were not yet under contract to microelectronics firms, the Commission furthermore concludes that the training programme was not carried out with the ultimate aim of finding suitable employees for specific firms, in particular those holding shares in SIBEG. This conclusion is borne out by the fact that it could only be established that seven former trainees joined shareholders of SIBEG at a later stage. From the fact that the vast majority of trainees joined employers without any regional limitation it can furthermore be concluded that the option to employ former trainees did not result in a particular benefit for companies in Lower Saxony.

(91) It can therefore be concluded that in principle the training and the organisational and administrative activities connected with it were carried out in the general public interest and did not form part of the economic activities of SICAN. As far as this activity is concerned, the SICAN group functioned like a training centre and did not pursue a market activity. It follows that, as far as public funding was used to finance the carrying-out of the task of general public interest, it does not constitute State aid.

(92) Since the SICAN group did not have a cost-accounting system distinguishing between costs incurred in fulfilling this task of general public interest and costs incurred for market activities, the additional question arises whether the necessary classification of tasks as falling into one or other category can now be done retrospectively. In the Commission's view, this cannot be ruled out per se. The method applied by the consultancy firm to make such a distinction retrospectively is acceptable. The detailed figures presented show that the costs incurred in carrying out the public service task did not exceed the funding received. The Commission therefore concludes that the funding of the activity carried out in the public interest does not constitute State aid and that the market activities of the SICAN group were not financed through State aid.

VII. CONCLUSIONS

(93) The Commission finds that Germany has implemented the aid in question in infringement of Article 88(3) of the Treaty,

HAS ADOPTED THIS DECISION:

Article 1

1. The aid granted to industrial project partners of SIBET constitutes State aid. This aid was granted unlawfully.

2. The aid which Germany granted to industrial project partners of SIBET is compatible with the common market as far as projects 1009, 1010, 1016, 1019, 1024 and 1025 are concerned.

3. For the following projects, the aid which Germany granted to industrial project partners of SIBET is incompatible with the common market:

Project 1005: aid amounting to DEM 166 000

Project 1006: aid amounting to DEM 117 500

Project 1008: aid amounting to DEM 362 691

Project 1013: aid amounting to DEM 679 677,01

Project 1014: aid amounting to DEM 701 664,50

Project 1023: aid amounting to DEM 549 495,82

For project 1015 the aid amount exceeding an aid intensity of 35 % (DEM 123 484,53) is incompatible with the common market.

For project 1026 the aid amount exceeding an aid intensity of 35 % (DEM 85 515) is incompatible with the common market.

Article 2

The measure which Germany implemented in favour of the SICAN group does not constitute State aid within the meaning of Article 87(1) of the EC Treaty.

Article 3

1. Germany shall take all necessary measures to recover from the recipients the aid referred to in Article 1(3) and unlawfully made available to them.

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

Article 4

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

Article 5

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 26 July 2000.

For the Commission
Pedro SOLBES MIRA
Member of the Commission