

II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 11 November 2003

on the State aid which the United Kingdom is planning to provide under the WRAP environmental grant funding and WRAP lease guarantee fund

(notified under document number C(2003) 4087)

(Only the English text is authentic)

(Text with EEA relevance)

(2004/317/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

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

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

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

Whereas:

1. PROCEDURE

(1) By letter dated 9 July 2002, registered on 16 July 2002, the United Kingdom notified the Commission, pursuant to Article 88(3) of the Treaty, of the Waste and resources action programme (WRAP). By letter dated 2 August 2002, the Commission asked for further information, which was provided by the United Kingdom authorities by letter dated 28 August 2002. Following a meeting between the Commission and the United Kingdom authorities that was held on 29 August 2002, the United Kingdom authorities provided further information by letter dated 13 September 2002, registered on 18 September 2002. The Commission sent another request for information by letter dated 23 October 2002, to which the United Kingdom authorities replied by letter dated 3 December 2002, registered on 6 December 2002. By letter dated 15 January 2003, regis-

tered on 23 January 2003, the United Kingdom authorities requested a new meeting with the Commission, which was held on 21 January 2003. Following that meeting, the United Kingdom authorities provided supplementary information by a series of letters dated between 24 January 2003 and 7 February 2003.

(2) On 19 March 2003, the Commission decided partly to approve the WRAP programme and to initiate the procedure laid down in Article 88(2) of the Treaty with respect to the WRAP environmental grant funding and part of the WRAP lease guarantee fund that had been notified on the basis of the Community guidelines on State aid for environmental protection⁽²⁾ (the environmental aid guidelines). By letter dated 21 March 2003, the Commission informed the United Kingdom of this decision. The case was registered under number C 21/2003.

(3) By e-mail dated 8 April 2003, registered on the same day under number A/32568, the United Kingdom authorities requested the removal of certain elements of confidential information from the Commission decision. The Commission replied by letter dated 22 April 2003. The United Kingdom authorities responded by e-mail dated 2 May 2003, registered under number A/33144. The Commission sent further comments on the question of confidentiality by letter dated 7 May 2003. The United Kingdom authorities agreed to these comments by letter dated 12 May 2003, registered on 19 May 2003 under number A/33512.

⁽¹⁾ OJ C 129, 3.6.2003, p. 6.

⁽²⁾ OJ C 37, 3.2.2001, p. 3.

- (4) By letter dated 25 April 2003, and registered on the same day under number A/32958, the United Kingdom responded to the opening of the procedure.
- (5) The Commission decision to initiate the procedure was published in the *Official Journal of the European Union* ⁽³⁾. The Commission invited interested parties to submit their comments on the aid.
- (6) The Commission received 29 comments from interested parties. It forwarded them to the United Kingdom by letter dated 17 July 2003. The United Kingdom's comments were received by e-mail dated 26 August 2003, and registered the same day, under number A/35866.
- (7) In its decision of 23 July 2003 in case C 61/2002, the Commission decided partially to approve the aid granted to Shotton Newsprint. That case was an individual application of the WRAP Environmental Grant Funding.
- (8) By letter dated 1 August 2003, the Commission requested further information, which was provided by the United Kingdom authorities by letter dated 3 September 2003, registered on 4 September 2003, under number A/36039.
- (9) A meeting was held on 12 September 2003 between the Commission and representatives of the United Kingdom government and of the WRAP programme. In the course of this meeting, the Commission asked further questions of the United Kingdom authorities, to which they replied by e-mail dated 26 September 2003 and registered on 29 September 2003 under number A/36643, and e-mail dated 30 October 2003 and registered on 31 October 2003 under number A/37458.
- (11) The legal basis for the programme is Section 153 of the Environmental Protection Act 1990 and the Financial Assistance for Environmental Purposes (No 2) Order 2000.
- (12) The objective of WRAP is to promote sustainable waste management and efficient markets for waste management and recycling. In particular, the aim of the United Kingdom authorities is to fulfil the Community targets for waste recycling set by Council Directive 1999/31/EC of 26 April 1999 on the landfill of waste ⁽⁴⁾, (the landfill Directive) which requires Member States to reduce the disposal of municipal waste to landfill and by Council Directive 94/62/EC of 20 December 1994 on packaging and packaging waste ⁽⁵⁾ (the packaging Directive) which requires significant increases in packaging waste recycling by at least 2006.
- (13) In order to increase waste recycling in the United Kingdom, WRAP has put into place different schemes, notified on 16 July 2003. The Commission gave a positive decision on the following ones: the WRAP grant funding regional scheme, notified on the basis of the guidelines on national regional aid, the WRAP SME grant funding scheme, notified on the basis of the Commission Regulation (EC) No 70/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to State aid to small and medium-sized enterprises ⁽⁶⁾, the WRAP pilot fund, and the part of the WRAP lease guarantee fund that had been notified on the basis of the Guidelines on national regional aid ⁽⁷⁾ and Regulation (EC) No 70/2001. On two remaining schemes, the WRAP environmental grant funding and the part of the WRAP lease guarantee fund that had been notified on the basis of the Community guidelines on State aid for environmental protection, the Commission decided to open the formal investigation procedure laid down in Article 88(2) of the EC Treaty.

2. DESCRIPTION OF THE MEASURE

2.1. Presentation of WRAP and its objectives

- (10) The aid is given within the framework of the Waste and resources action programme. According to the information submitted by the United Kingdom, WRAP is an entity established to promote efficient markets for recycled materials and products, by stimulating demand for recycled materials and products. WRAP's members comprise the charity Wastewatch, the Environmental Services Association and the Secretary of State for Environment, Food and Rural Affairs. It is responsible for administering the aid, and is funded by the government for the period 2001 to 2004. WRAP functions as an adjunct to the government, and implements government policies, although it has a private corporate form.

⁽³⁾ See footnote 1.

2.2. The WRAP environmental grant funding

2.2.1. Aim and mechanisms of the scheme

- (14) The purpose of this grant funding programme is to subsidise investments by private companies in recycling facilities in order to increase the recycling of waste in the United Kingdom. According to the United Kingdom authorities, the necessity of such investment aid stems from the uncertainty of returns on this type of investments, due to the risks and costs associated with obtaining and using appropriate waste materials and the difficulty in motivating the purchase of products made from recycled materials. The selected firms will commit

⁽⁴⁾ OJ L 182, 16.7.1999, p. 1.

⁽⁵⁾ OJ L 365, 31.12.1994, p. 10.

⁽⁶⁾ OJ L 10, 13.1.2001, p. 33.

⁽⁷⁾ OJ C 74, 10.3.1998, p. 9.

themselves to recycle a certain amount of waste per year. These firms will then conclude supply contracts with local authorities. As a result, local authorities will have the incentives to set up systems of selective collection of waste since they will have the guarantee of selling their selected waste. Through the creation of these reprocessing units, it is therefore expected that markets for waste products will be created.

- (15) The waste products concerned by this scheme are wood, glass, plastics, aggregates and compost. In order to select the recipients of support, and to determine the proportional level of aid funding, WRAP uses open and competitive tenders for each type of products. These tenders are advertised in the specialised press throughout the Community. Projects are selected on the basis of a certain number of criteria: most economically advantageous offer, magnitude and relevance of deliverables in relation to the environmental objectives of the competition and organisational feasibility.

2.2.2. *Types of projects to be subsidised*

- (16) Under the WRAP environmental grant funding, WRAP intends to fund projects in various sectors.
- (17) In the wood sector, WRAP will finance three or more projects, involving the creation of new reprocessing capacity that will produce different types of end products: animal bedding, horticultural and landscaping mulches, or activated carbon (a specific type of filter to be used in industrial chemical engineering applications). According to the United Kingdom authorities, waste wood is not normally used for the manufacture of end products. Animal bedding, for example, has traditionally been manufactured from virgin wood. In 2001, only about 5 % of all bedding in the United Kingdom was manufactured from waste wood. According to the United Kingdom authorities, this is due to the fact that the cost of waste wood processed for recycling is normally higher than the cost of virgin wood processed for equivalent application. This is why support to stimulate investment in new recycling infrastructure (for example, advanced decontamination equipment) is necessary.
- (18) In the glass sector, WRAP wants to subsidise one new facility that would process up to 80 000 tonnes of waste glass per annum (from domestic and commercial waste stream) by grinding it to very small particle size, below 90 microns. This will allow for and facilitate new end uses, in particular for waste green glass, which currently has very limited end uses. One possible use of this fine glass powder is as a fluxing agent in bricks and sanitary ware products. This is a relatively innovative technology. According to the United Kingdom authorities, the only comparable facility in the Community that they are aware of is in Sweden, where the ground glass is used as a cement additive. A potential recipient has already been selected. It is a joint venture project between Cleanaway Ltd and Glass Group Ltd. The United Kingdom authori-

ties also stress that this project has further environmental benefits, other than the diversion of 80 000 tonnes of glass from landfills. For instance, the use of glass in sanitary ware will reduce the need for primary mineral extraction.

- (19) In the plastic sector, WRAP's proposed intervention involves the creation of a new automated plastic bottle sorting and reprocessing capacity, which would divide the materials by polymer type and by colour. The sorted material would then be converted into plastic feedstock, which could be used for the production of new plastic bottles. Currently, waste plastic sorting is normally done by hand in the United Kingdom, and the state of the art manufacture of plastic bottles uses virgin polymer. In 2001, 460 000 tonnes of plastic bottles were consumed in the United Kingdom, of which less than 500 tonnes (0,1 %) contained any recycled material.
- (20) With respect to aggregates, the United Kingdom authorities have already implemented a levy on aggregates extraction from the ground to provide an incentive for the reuse of waste aggregates (for example, from construction and excavation activity). Due to the already low costs of virgin aggregates and high costs of aggregates recycling equipment, the levy in itself is insufficient incentive for the market to invest in such capacity. As a result, WRAP intends to subsidise up to 20 projects across the United Kingdom that would involve the creation of sorting and reprocessing capacity for waste aggregate. These projects would focus on waste aggregates that are currently hardly recycled at all, in particular waste aggregates with a high level of contamination from soil, clays and other contaminants. It is expected that this intervention will increase recycling of waste aggregates by two million tonnes by 2004.
- (21) With respect to the compost sector, WRAP considers that this is an immature sector, with a lack of comprehensive infrastructure for collection, processing and composting of organic waste (mainly garden and public park waste). This is due to the relatively high capital cost of establishing infrastructure and the low value of compost products. WRAP intends to support up to 20 projects that will involve the processing of organic waste into basic compost products, and the manufacturing of more sophisticated horticultural products by blending these basic compost products with other inputs to create more sophisticated horticultural products. These end products will mostly be used in horticulture, landscaping and organic horticulture. It is expected that this intervention will increase the recycling of organic waste by 500 000 tonnes, and the share of composted products in these sectors. For instance, in 2002, in the United Kingdom, composted products represented less than 3 % of the three million cubic metres of raw materials used in horticulture. The product normally used for this end application is peat. Its replacement by composted products will also have the environmental benefit of conserving peat bogs.

2.2.3. Eligible costs

(22) The United Kingdom authorities have included in the calculation of the eligible costs the entirety of the investments linked to the recycling activity.

(23) For example, for the wood projects, the eligible investments include the segregation, chipping and shredding equipment capable of producing different grades of reprocessed wood, the equipment for contaminant removal, and the equipment for end product processing (for example, dyeing equipment and baling and bagging equipment). For the glass project, the eligible investments include the grinding equipment capable of processing glass to produce finely ground glass. For the plastics project, the eligible investment costs include the equipment to sort and reprocess waste plastics. In the case of compost, they include the equipment to shred, aerate, turn and mix the organic waste material. Finally, in the case of aggregates, they include the equipment to sort, screen, wash, crush and grind aggregate materials so that they meet specific requirements required for end applications.

(24) From these eligible investment costs, the United Kingdom authorities will deduct the costs of investments necessary to comply with any mandatory compliance standards. They will also deduct the net benefit to the recipient over five years, taking account of the savings over five years of life of the investment, any increase in production during that five year period, and any increased revenue or other benefits to the recipient during that period. For example, in the aggregate project involving Huntsmans Quarries Ltd, the calculation of the benefits includes an estimate of the profit after tax including the operational costs, cost of capital and aggregate levy contribution, using costing presented by the company. To those profits, valued at GBP 110 000 the United Kingdom authorities have also added an estimate of Huntsmans's saved reserve,⁽⁸⁾ valued at GBP 26 532. From those benefits, they have deducted various additional extra costs, such as management overhead, which result in a valuation of the net benefits over the first five years of GBP 109 632. In some cases, like the glass project, no net benefit is expected. However, WRAP will require that the relevant portion of the aid be repaid, should a net benefit occur.

2.2.4. Aid intensity

(25) The aid intensity of the grants will not exceed 30 %, plus the extra percentage points allowed under point 34 of the environmental aid guidelines for projects involving small and medium-sized enterprises and/or located in assisted areas.

(26) The United Kingdom authorities will ensure that no project receives aid for the same eligible costs from other sources if the cumulated aid exceeds the aid intensities applicable under the environmental aid guidelines. In order to ensure compliance with this principle, recipients will be asked to provide a declaration concerning any other aid applied for.

2.2.5. Budget

(27) The total budget for the WRAP environmental grant fund is EUR 20,3 million. The total budget for the three wood projects is EUR 0,75 million. The budget is EUR 1 million for the glass project, and EUR 3,3 million for the plastics project. The budget for the 20 aggregates projects is EUR 8,55 million, and EUR 5,7 million for the 20 compost projects.

2.2.6. Reporting

The United Kingdom authorities will report annually to the Commission on the activity of the scheme.

2.3. The WRAP lease guarantee fund

(28) Like the WRAP environmental grant funding, the WRAP lease guarantee fund supports investments in reprocessing activities and aims, in this way, to contribute to an increase in the waste recycling capacity in the United Kingdom.

(29) The fund will provide guarantees that will cover leases of machinery and equipment for the purpose of reprocessing waste material and manufacturing products from those materials. Only leases that have a duration of at least five years will be eligible. The maximum value for an individual asset to be supported under this measure will be GBP 5 million. As regards the part of the WRAP lease guarantee fund notified on the basis of the environmental aid guidelines, which the object of this Decision, the United Kingdom authorities made the commitment that projects involving 'state of the art' processes will not be eligible for lease guarantee support. By 'state of the art', is meant a process in which the use of a waste product to manufacture an end product is economically profitable and normal practice (for example, the use of waste paper for the production of newsprint).

⁽⁸⁾ Thanks to the production of recycled aggregate, Huntmans Quarries Ltd will be able to spare its quarry of virgin aggregate, the life of which will therefore be extended.

- (30) According to the United Kingdom authorities, leasing companies are very reluctant to provide leases for waste recycling equipment. This is due to the perceived low resale value of the specialist equipment used in the recycling sector. As a result, leasing contracts for such equipment are regarded by leasing companies as very high-risk and are therefore disproportionately expensive.
- (31) In order to remedy this situation, the guarantees provided by the fund will cover the residual value of the equipment, which, under an operating lease, will remain the lessor's asset, and which the lessor will sell at the end of the lease-period or earlier, in the case of bankruptcy of the lessee. Before the lease contract is signed, the management agent will set a residual value for the asset concerned in negotiation with a panel of lessors. The Fund will be obliged to acquire this asset for the agreed residual value in two circumstances: either if the lessee becomes bankrupt, or if the residual value of the assets falls short of the guaranteed value at the end of the lease period.
- (32) In order to calculate the net grant equivalent of these guarantees, the United Kingdom authorities have used the method laid down in the Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees⁽⁹⁾, which states that the grant equivalent is equal to (guaranteed sum x risk) — premium. In the case of a GBP 100 000 investment, the guaranteed residual value would typically be GBP 20 000. According to the United Kingdom, a normal commercial asset finance portfolio has a risk basis of 10 to 20 % default rate. Given the higher risk profile of the waste recycling activities covered by the fund, the United Kingdom authorities estimate that it would be appropriate to apply a higher default rate, namely 30 %. The grant equivalent for a GBP 100 000 investment would therefore be GBP 20 000 x 30 % = GBP 6 000. There are unlikely to be premiums paid to WRAP. This means that the aid intensity for this aid will be 6 000/100 000 = 6 %. The calculation of this aid intensity is based on the assumption that the guaranteed residual value is set at 20 % of the value of the investment. In some cases, this guaranteed residual value could exceed 20 %. In such cases, the calculation of the aid element will vary accordingly. In any case, the United Kingdom authorities confirmed that the aid intensity should normally not be higher than 15 %.
- (33) The section of the WRAP lease guarantee fund to which this decision relates concerns the application of the fund to investments carried out by large firms in non-assisted areas, and is notified under the environmental aid guidelines⁽¹⁰⁾. As in the WRAP environmental grant funding scheme, the United Kingdom authorities have included in the calculation of the eligible costs all of the investments linked to the recycling activity, that is to say, in that case, the investments that are the object of the guaranteed lease. From these eligible costs, the United Kingdom authorities will deduct the benefits from the investment over a five-year period.
- (34) The size of the lease guarantee fund is approximately EUR 3,6 million, which will enable it to guarantee a maximum of EUR 12 million in residual values over a five-year period (the fund will operate until 31 December 2006). Since this fund is mainly directed at small and medium-sized enterprises, it is likely that few large firms located in non-assisted areas will, in any case, benefit from the application of this fund.
- (35) The United Kingdom authorities will report annually to the Commission on the activity of the scheme.

3. REASONS TO INITIATE THE FORMAL INVESTIGATION PROCEDURE

- (36) The Commission doubted that the WRAP environmental grant funding and the WRAP lease guarantee fund would qualify for an assessment under the environmental aid guidelines.
- (37) In particular, under point 29 of the environmental aid guidelines, investment aid may be authorised on the basis of the guidelines when firms undertake investment in the absence of mandatory Community standards or where they have to undertake investment in order to comply with national standards that are more stringent than Community ones. The Commission considered that investment aid granted under the WRAP environmental grant funding and the WRAP lease guarantee fund does not fulfil such an aim and is actually meant to enable the United Kingdom to fulfil the targets set by the landfill Directive. The Commission noted that investment aid approved under the environmental aid guidelines aims at reducing the emissions and pollution caused by the beneficiary in the course of its production process. The aim of these schemes is different: it is the whole activity of the beneficiaries (the recycling of waste) that is supposed to have environmental benefits. The Commission doubted that the aim of the environmental aid guidelines was to apply to such situations.

⁽⁹⁾ OJ C 71, 11.3.2000, p. 14.

⁽¹⁰⁾ As for the guarantees given to investments carried out by large firms in assisted areas or by SMEs, the Commission, in its decision of 19 March 2003, found that they were compatible with the guidelines on national regional aid and with Regulation (EC) No 70/2001 respectively.

- (38) Furthermore, supposing the environmental aid guidelines were applicable to these schemes, the Commission doubted whether the calculation of the eligible costs was in conformity with the guidelines. This is because the United Kingdom authorities included the entirety of the investments linked to the recycling activity, and because they did not provide sufficient information on how they intended to calculate the benefits accruing to the recipients of the aid over a five-year period.
- (39) Finally, the Commission expressed doubts as to whether these two schemes could be exempted directly on the basis of Article 87(3) of the Treaty, since the United Kingdom authorities had not sufficiently shown why State aid was necessary in this area, and why it did not adversely affect trading conditions to an extent contrary to the common interest.
- (42) Comments from the other interested parties are very similar to one another in content and form. They underline the existence of a market failure in the recycling of various waste products, and the unsatisfactory level of selected waste collection in the United Kingdom. Some comments acknowledged that raising tax on landfills is part of the solution, but this cannot be done until cheap alternatives to landfills have been developed. In their views, WRAP's intervention will help to create these alternatives and to establish markets for recyclable products.
- (43) Most comments underline the relative smallness of the support provided by WRAP, and the lack of significant impact on competition of the measures involved. At the same time, they underline the positive effects of the measures on the environment, with a reduction of waste going to landfills. Some third parties mention more specific benefits. For instance, the Royal Society for the Protection of Birds underlines the problems raised by the use of peat bog and its impact on birds' habitat. The replacement of the use of peat by compost will help to protect this natural habitat.

4. COMMENTS FROM INTERESTED PARTIES

- (40) The Commission received comments from 29 third parties. These comments were introduced by the German and the Irish governments, by the Community Recycling Network, the Local Authority Recycling Advisory Committee, Friends of the Earth, the Consumers' Association, the Soft Drinks Association, Coca Cola Enterprises Ltd, the Composting Association, the Soil Association Producer Services, the Royal Society for the Protection of Birds, Recycling of Used Plastics Ltd, Nampak Plastics, Dryden Aqua, the Glass Recycling Group Ltd, Knauf Insulation, Dr Andrew Smith and Dr Philip Jackson from CERAM Research Ltd, the Aggregate Industries United Kingdom Ltd, Hanson Aggregates Ltd, the British Aggregates Association, the Wood Recyclers Association, the Wood Panel Industries Federation, Kronospan Ltd, the Environmental, Food and Rural Affairs Committee, Mr. Colin Pickthall MP, Mr. David Kidney MP, Mrs Helen Clarke MP and Mrs Julia Drown MP. All these comments, apart from those of the British Aggregates Association, were in favour of the WRAP schemes.
- (41) The British Aggregates Association claims that the proposed aid to the aggregate sector would discriminate between different types of waste aggregates. According to the Association, aid will be granted to recyclers of industrial mineral processing waste and to recyclers of slate and shale quarry processing waste. Therefore, the scheme cannot deliver any environmental benefits since the subsidised recycled material would simply replace other material that is currently recycled without subsidy.
- (44) Therefore, all third parties, with the exception of the British Aggregates Association, consider that this is a clear case of environmental aid, which should be exempted on the basis of the environmental aid guidelines.

5. COMMENTS FROM THE UNITED KINGDOM

- (45) On the question of the applicability of the environmental aid guidelines, the United Kingdom authorities state that there is no reason to limit the application of these guidelines to the pollution caused by the beneficiary, as stated in the Commission decision to open the formal investigation procedure. They note that under point 42 of the environmental aid guidelines, aid can be approved for the management of waste. They also recall that the guidelines refer to the Community strategy for waste management, which makes waste management a 'priority objective for the Community in order to reduce the risks to the environment' ⁽¹⁾. Therefore, it is, in their view, wrong that schemes designed to increase waste recycling should be excluded from the environmental aid guidelines on an a priori basis.

⁽¹⁾ COM(96) 399 final of 30.7.1996.

(46) Concerning point 29 of the environmental aid guidelines, the United Kingdom authorities interpret this point as simply meaning that a firm cannot receive aid if the aid is merely designed to help it comply with a legal obligation imposed on that firm as the result of Community law. If there is no relevant law with which the firm must comply, as is the case here, then the aid may have the desired incentive effect and a company is in no way precluded from receiving State aid under the environmental aid guidelines. The United Kingdom authorities further add that there is no per se prohibition on a Member State supporting companies which assist that Member State in complying with its obligations deriving from Community law. For these reasons, the United Kingdom authorities consider that these two aid measures can fall within the scope of the environmental aid guidelines.

(47) On the question of the eligible costs, the United Kingdom authorities quote point 37 of the guidelines which states that 'eligible costs must be confined strictly to the extra investment costs necessary to meet the environmental objectives'. Since the environmental objective of the schemes is to increase waste recycling, the United Kingdom authorities claim that all the extra investment costs necessary to increase waste recycling, that is to say, all the investments linked to the recycling activity, are to be included in the eligible costs. As to the calculation of the benefits accruing to the recipient of the aid over the first five years, the United Kingdom authorities have provided a detailed description of how they are calculated in a number of concrete examples.

(48) If the Commission concludes that the environmental aid guidelines are not applicable to the case in question, the United Kingdom authorities submit that the two aid measures can be exempted directly on the basis of Article 87(3)(c) of the Treaty. On the question of the necessity of the aid, the United Kingdom authorities first underline that measures taken to increase waste recycling and based on the principle of the internalisation of costs have been taken. They include an increase of the tax on landfill. However, given that the pre-tax cost of landfill is so low in the United Kingdom, the post-tax cost of landfill in the United Kingdom remains well below European averages and will not be sufficient in itself to deter excessive landfill. Furthermore, the fact that landfill does not happen does not necessarily ensure that recycling does happen. That is why the United Kingdom authorities have concluded that it is necessary to target recycling directly under the WRAP programme. Under the terms of Article 87(3)(c) of the Treaty, aid

may be considered to be compatible with the common market when it facilitates the development of certain economic activities and certain economic areas and where it does not adversely affect trading conditions to an extent contrary to the common interest. In the present case, the United Kingdom authorities put forward that the two aid schemes at stake aim at supporting waste recycling, which is fully in line with Community environmental policy. Furthermore, the aid is proportional and does not adversely distort competition. The aid amounts are relatively small, the aid is targeted at sectors where there is a market failure and the use of competitive tenders ensures that only the minimum support necessary to stimulate market forces is provided.

(49) On the specific objection of the British Aggregate Association, the United Kingdom authorities replied that the waste aggregates that are allegedly discriminated against are in fact the by-products of virgin aggregate extraction. The United Kingdom authorities do not consider that these products are real waste, whose recycling needs to be supported, since such support would also encourage increased extraction of virgin aggregate and would defeat the objective of encouraging the use and recycling of aggregates. Under the WRAP environmental grant funding, the United Kingdom authorities will limit their support to the recycling of waste aggregate, that is to say, aggregate that has been used once, and aggregates that are by-products of industrial processes other than extraction of virgin aggregates, such as mineral wastes arising from the production of china, clay, coal and slate.

6. ASSESSMENT OF THE AID

6.1. The WRAP environmental grant funding

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

(50) Under Article 87(1) of the Treaty, 'any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the common market.'

(51) In this case, the measure is funded by resources granted by the State under the WRAP programme. It gives a selective economic advantage to certain firms, operating in specific sectors, in the form of a grant. The use of a public tender procedure can ensure that the amount of

the subsidy is limited to the minimum necessary but does not remove the aid character of the measure. Furthermore, the waste products that are recycled can be internationally traded. For instance, it is estimated that up to 25 % of United Kingdom waste plastics was exported in 2001, while 10 000 tonnes of waste glass was imported, mainly from Ireland. Similarly, the end products that are made from the recycled waste (for example, animal bedding or activated carbon made from waste wood or sanitary ware incorporating waste glass) can also be internationally traded. For these reasons, the WRAP environmental grant funding constitutes aid within the meaning of Article 87(1) of the Treaty.

6.1.2. *Assessment of the compatibility with Article 87 of the Treaty*

- (52) The Commission has assessed whether the exemptions set out in Article 87(2) and (3) of the Treaty apply. The exemptions in paragraph 2 of Article 87 of the Treaty could serve as a basis to consider aid compatible with the common market. However, the aid does not have a social character and is not granted to individual consumers, it does not make good the damages caused by natural disasters or exceptional occurrences and it is not required in order to compensate for the economic disadvantages caused by the division of Germany. The exemptions in Article 87(3)(a), (b) and (d) of the Treaty, which refer to promotion of the economic development of areas where the standard of living is abnormally low or where there is serious underemployment, to projects of common European interest and to the promotion of culture and conservation cannot apply either. In any case, the United Kingdom did not attempt to justify the aid on those grounds.
- (53) As far as the first part of the exemption in Article 87(3)(c) of the Treaty is concerned, namely aid to facilitate the development of certain economic activities, the Commission notes that the aid did not have purposes such as research and development. Nor can it be found to be compatible with the guidelines on national regional aid or Regulation (EC) No 70/2000. All the projects of the WRAP environmental grant funding that were compatible with those two texts, were the object of a positive decision of the Commission on 19 March 2003. Therefore, by definition, the WRAP environmental grant funding exclusively comprises projects that are not compatible with Community rules on regional aid or aid to small and medium-sized enterprises.
- (54) It should therefore be examined whether this scheme qualifies for an exemption under Article 87(3)(c) of the Treaty on other grounds than those referred to in recitals 52 and 53. The Commission will assess in the following recitals whether the WRAP environmental grant funding scheme is compatible with the environmental aid guidelines, and whether it is directly compatible with Article 87(3)(c) of the Treaty.
- #### 6.1.2.1. *Assessment under the environmental aid guidelines*
- (55) In its decision of 19 March 2003, the Commission acknowledged that the WRAP environmental grant funding scheme has environmental benefits. The recycling of waste is more environmentally friendly than putting it into landfill. However, in its decision of 17 July 2003, in case C 61/2002 Shotton paper — newspaper reprocessing case, which concerned investment aid for waste paper recycling, the Commission concluded that the environmental aid guidelines were not applicable to this type of aid. Since that case is an individual application of the WRAP environmental grant funding to the specific sector of waste paper, the same conclusion must be drawn with respect to the scheme itself.
- (56) The reasons why the environmental aid guidelines are not applicable are the following. According to point 29 of the environmental aid guidelines, investment aid may be granted 'to enable firms to improve on Community standards applicable, or when the firms undertake investment in the absence of Community standards applicable (...)'.
(57) The first possibility expressed in point 29 of the environmental aid guidelines, which allows aid to be granted in order to enable firms to improve on Community standards applicable, does not apply in this case. The aid is granted in order to improve the United Kingdom's environment in general, and to help the United Kingdom to achieve its obligations under the landfill and packaging Directives. It is not granted to enable the beneficiaries to improve on the standards applicable to them directly.
(58) As regards the second possibility in point 29 of the environmental aid guidelines, which concerns aid for firms to undertake investments in the absence of Community standards applicable, the United Kingdom argued that the relevant standards applied to the Member State itself, rather than to the firm, and that investment aid under the environmental aid guidelines could therefore be allowed. In its decision in case C 61/2002, the Commission has already rejected that argument. This exception should be interpreted in the light of point 18 (b) of the environmental aid guidelines, which states that

aid 'may act as an incentive to firms to improve on standards or to undertake further investment designed to reduce pollution from their plants'. On this basis, the Commission considers that point 29 of the environmental aid guidelines concerns cases of investment aid where an undertaking invests to improve its own environmental record, and to reduce its own pollution. This is not the case under the present scheme.

(59) The Commission also considers that no other provisions of the environmental aid guidelines apply to the case at stake. The Commission recalls, in this context, that operating aid to promote waste management may be authorised, under the conditions set out in points 42 to 46 of the Guidelines, for waste management. However, the measures in question, which constitute investment aid, do not fulfil these conditions.

(60) The United Kingdom authorities tried to draw a distinction between case C 61/2002 Shotton Paper and the present case, and argued that there were sufficient differences between the two cases to reach different conclusions concerning the applicability of the environmental aid guidelines in this case. In particular, they noted that the Shotton paper case involved a much higher amount of aid than the individual amounts provided under the WRAP environmental grant funding, that it concerned a mature market while the scheme is targeted at immature markets with a clear market failure, and that the aid measure subsidised a 'state of the art' process while the technologies which the WRAP environmental grant funding seeks to develop are untested in the market place. The Commission considers that these arguments are of a factual nature, which are relevant in the context of the discussion of the direct applicability of Article 87(3)(c) of the Treaty. They are not, however, such as to alter the Commission's legal interpretation of point 29 of the environmental aid guidelines which leads it to conclude that the guidelines are not applicable in the present case.

(61) It must therefore be concluded that the environmental aid guidelines are not applicable to the WRAP environmental grant funding.

6.1.2.2. Direct Application of Article 87(3)(c) of the Treaty

(62) The granting of investment aid in favour of waste recycling is not foreseen in the environmental aid guidelines, despite its environmental benefits. It is therefore appropriate to consider whether this type of aid fulfills the criteria to be directly compatible with Article 87(3)(c) of the Treaty.

(63) Article 87(3)(c) of the Treaty states that 'aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest' may be considered to be compatible with the common market.

(64) The Commission first notes that the objective of this aid measure is to encourage waste recycling. Waste recycling is an essential element of waste management, which the Commission considers to be 'a priority objective for the Community in order to reduce the risks to the environment' ⁽¹²⁾. The importance of this objective was underlined by the landfill Directive, which requires Member States to reduce the disposal of municipal waste to landfill and by the packaging Directive, which requires significant increases in packaging waste recycling. Waste recycling is therefore an economic activity, the development of which should be encouraged, because of its environmental benefits, both at national and Community levels.

(65) In order to be compatible with Article 87(3)(c) of the Treaty, the aid measure must also be proportionate to the objective, and must not distort competition to an extent contrary to the common interest. Some elements of appreciation of the proportionality of this type of aid measure were set out by the Commission in its decision in case C 61/2002. In that case, the Commission concluded that the aid given to increase waste paper recycling capacity of Shotton was not proportionate, nor necessary, and led to an undue distortion of competition. The Commission first noted that producing newsprint paper on the basis of waste paper is the normal state of the art technique, which is economically profitable and widely spread. Therefore, providing aid for the development of such equipment appeared to be disproportionate and not necessary. Furthermore, given the high amount of aid involved (EUR 35 million), granted to one single undertaking, which is a major player in the market of newsprint, the Commission concluded that the aid would cause an undue distortion of competition.

(66) The Commission considers that a different conclusion can be reached as regards this aid measure. The United Kingdom authorities have convincingly argued that the projects to be subsidised under the WRAP environmental grant funding do not involve 'state of the art' processes, which can be defined as processes in which the use of a waste product to manufacture an end product is economically profitable and therefore normal practice. Some of the WRAP projects involve techniques that are little tested in the market place. This appears to

⁽¹²⁾ Community strategy for waste management, COM(96) 399 final of 30.7.1996.

be the case of the glass project, which involved the fine grinding of glass for its subsequent incorporation into sanitary ware or bricks, or the plastics project, which involves automated plastic bottle sorting equipment (a process normally done by hand in the United Kingdom). Other projects, like the wood, compost or aggregates projects, involve activities in which the use of waste product as raw material is not the normal practice. In the case of wood, for instance, the cost of waste wood processed for recycling is normally higher than the cost of virgin wood processed for equivalent application, which normally makes its use unprofitable. Since this aid scheme does not subsidise 'state of the art' processes, the aid can be considered to be necessary.

(67) As to the impact of the measure on competition and on trade between Member States, the Commission first notes that the amounts of aid are significantly lower than that granted in the Shotton paper case. The largest amount of individual aid to be granted under this scheme is EUR 3,3 million, compared to EUR 35 million in the Shotton case. Furthermore, for most waste products, the aid is spread over several projects (up to 20 in the case of compost and aggregates). All but one of the comments from third parties were in favour of the project. Only one comment, from the British Aggregates Association underlined the potential negative impact on competition of the measure, in the specific sector of aggregates, since it would discriminate between different types of recycled materials. However, it appears that the waste aggregates that are allegedly discriminated against are by-products of virgin aggregate extraction. The United Kingdom authorities have argued that these products cannot be considered as real waste. However, according to the definition of waste contained in Council Directive 75/442/EEC of 15 July 1975 on waste⁽¹³⁾, such by-products are to be generally considered as waste. Additionally, the Court of Justice of the European Communities has recently defined criteria for case-by-case determination of whether by-products may be considered as waste⁽¹⁴⁾. This jurisprudence does not alter the general conclusion that by-products of virgin aggregate extraction are to be considered as waste. Nevertheless, the Commission considers that it is legitimate not to support the reprocessing of by-products of virgin aggregate extraction. Supporting the latter would have the unwanted effect of encouraging extraction of virgin aggregate and would defeat the objective of encouraging the recycling of materials that have already been used. In addition, the relevant projects would focus on waste aggregates which are currently hardly recycled at all, in particular waste aggregates with a high level of contamination from soil, clays and other contaminants. The situation of such aggregates clearly differs from that of by-products of virgin aggregate extraction. The Commission therefore considers that there is no undue discrimination in the area of aggregates.

⁽¹³⁾ OJ L 194, 25.7.1975, p. 39. Directive as last amended by Directive 96/350/EC (OJ L 135, 6.6.1996, p. 32.)

⁽¹⁴⁾ See judgment of 11 September 2003, in Case C-114/2001 *Avesta-Polarit Chrome Oy*, not yet reported.

(68) Furthermore, in order to determine whether the aid does cause an undue distortion of competition, regard must be paid to the aid intensities granted to the various projects. The United Kingdom authorities have based their calculation of the eligible costs and the relevant aid intensities on the principles laid down in the environmental aid guidelines. The Commission has already concluded that the guidelines are not applicable to the aid measure in question. However, given the environmental objective of the WRAP environmental grant funding, it is appropriate to find guidance in the environmental aid guidelines on the way the eligible costs should be calculated and aid intensities determined in this case.

(69) On the question of the eligible costs, point 37 of the environmental aid guidelines states that 'eligible costs must be confined strictly to the extra investments costs necessary to meet the environmental objectives', which is normally done by deducting, from the eligible investment costs, 'the cost of a technically comparable investment that does not provide the same degree of environmental protection'. Under the WRAP environmental grant funding scheme, the United Kingdom authorities have not deducted the cost of any such comparable investment from the eligible investment costs. This approach appears to be justifiable given the specificity of the measure. As explained in point 6.1.2.1, the environmental aid guidelines are applicable to aid measures intended to make a certain production process more environmentally friendly, by reducing its polluting emissions. This is why point 37 recommends the deduction from the eligible investment costs of a comparable, less environmentally friendly investment. In the present case, however, the situation is different. It is the whole economic activity of the aid beneficiary (waste recycling) that is environmentally friendly. It is therefore appropriate to consider that the whole cost of investment is eligible. Furthermore, as recommended by point 37 of the guidelines, the United Kingdom authorities have deducted from the costs of these investments the benefits over a five-year period. They have provided the Commission with descriptions showing how these benefits had been calculated. These calculations appear to be correct. The aid intensities calculated on the basis of these eligible costs will not exceed the thresholds laid down in points 34 and 35 of the environmental aid guidelines.

(70) Finally, the Commission notes that an open tender procedure is used to select the beneficiaries and determine the amount of the aid. This system helps to guarantee that the aid is limited to the minimum and is proportionate.

- (71) Given that the aid amounts granted are relatively small, that they are calculated in accordance with the principle laid down in the environmental aid guidelines and set at the end of a open tender procedure, and that no comment convincingly demonstrated that the measure in question was creating an undue distortion of competition, it may be concluded that the WRAP Environmental Grant Funding does not adversely affect trading conditions to an extent contrary to the common interest.
- (72) In the light of the above, it is concluded that the WRAP environmental grant funding is compatible with Article 87(3)(c) of the Treaty.
- (73) The Commission intends to amend the environmental aid guidelines in order to expressly provide for the possibility to approve State aid which has environmental benefits at the global level of the Member State or the Community, and not at the individual level of the beneficiary. Given the lack of experience in this field of environmental aid, such cases will be assessed on their own merits. Pending the amendment of the guidelines, the Commission will apply the same criteria as in the present decision to any similar case

6.2. The WRAP lease guarantee fund

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

- (74) The WRAP lease guarantee fund is funded by resources granted by the State under the WRAP programme. The Commission notes that the fund provides guarantees that cover leases of machinery used to recycle waste. It enables firms that want to acquire this equipment to obtain a lease on conditions that are more favourable than normally available on the market. Since the lessees do not pay any premium for the guarantee, they clearly get an economic advantage from this measure. This economic advantage is specific, since only firms operating in the sectors of waste recycling can benefit from the application of this fund. Furthermore, the products manufactured by those companies may be internationally traded, so this aid measure may have an effect on competition and trade between Member States. For these reasons, it may be concluded that the WRAP lease guarantee fund constitutes aid to the lessees within the meaning of Article 87(1).

6.2.2. Assessment of the compatibility with Article 87 of the Treaty

- (75) In its decision of 19 March 2003, the Commission made a detailed analysis of the WRAP guarantee fund, in the

light of the Commission Notice on State aid in the form of guarantees. It concluded that the guarantee fund was in line with the Notice, and in particular that the calculation of the grant equivalent was correct and the aid intensity was estimated to be around 6 % on average⁽¹³⁾. Since the mechanisms of this fund have not changed and will apply in exactly the same way to large firms in non-assisted areas, the same conclusions are applicable to the present analysis.

- (76) Secondly, this aid measure is very similar to the WRAP environmental grant funding. The only significant difference between the two measures is the form of the aid: grant in the case of the WRAP environmental grant funding, and guarantee in the case of the WRAP lease guarantee fund. Like the WRAP environmental grant funding, this scheme aims at supporting investment aid in the field of waste recycling. Consequently, the conclusions concerning the compatibility of the WRAP environmental grant funding with Article 87(2) and Article 87(3) of the Treaty can be applied to the WRAP lease guarantee fund. For the same reasons, it can be concluded that Article 87(2), the guidelines on national regional aid, Regulation (EC) No 70/2001⁽¹⁶⁾ and the environmental aid guidelines do not apply.

- (77) On the question of whether the WRAP lease guarantee fund is directly compatible with Article 87(3)(c) of the Treaty, the United Kingdom authorities have committed themselves not to grant guarantees to leases of equipment involved in 'state of the art' processes.

- (78) Secondly, the calculation of the eligible costs is comparable to the situation under the WRAP environmental grant funding, and the principles laid down in point 37 of the environmental aid guidelines. It notes in particular that the United Kingdom authorities will deduct from the eligible investment costs, the benefits from the investment over a five year period.

- (79) The Commission also notes that the maximum value of an individual asset to be supported under this fund is GBP 5 million, that the aid intensity will not exceed 15 %, and that, therefore, the maximum possible grant equivalent of a guarantee is GBP 750 000. In the large majority of cases, this amount is likely to be significantly smaller, because the value of the asset will be lower, and the aid intensity will generally be around 6 %.

⁽¹³⁾ See point 83 and 84 of the decision.

⁽¹⁶⁾ The part of the Lease Guarantee Fund that was compatible with the regional aid guidelines and Commission regulation (EC) No 70/2001 was the object of a positive decision of the Commission on 19 March 2003.

(80) Therefore, given that no 'state of the art' process will be eligible for guarantees, given that the grant equivalent of the guarantees will not be, on average, of a high level, and that the aid intensities will be significantly lower than the thresholds imposed in the environmental aid guidelines, it can be concluded that guarantees granted by the WRAP lease guarantee fund will 'not affect trading conditions to an extent contrary to the common interest.' Since its aim is to encourage the recycling of waste, which is a priority objective of the Community, the WRAP lease guarantee fund fulfills the criteria to be considered compatible with Article 87(3)(c) of the Treaty,

HAS ADOPTED THIS DECISION:

Article 1

The WRAP environmental grant funding and the WRAP lease guarantee fund are compatible with the common market within the meaning of Article 87(3)(c) of the EC Treaty.

Implementation of the aid is accordingly authorised.

Article 2

This Decision is addressed to the United Kingdom of Great Britain and Northern Ireland.

Done at Brussels, 11 November 2003.

For the Commission

Mario MONTI

Member of the Commission