

II

(Non-legislative acts)

DECISIONS

COMMISSION DECISION

of 23 February 2011

on State aid granted by Italy to Portovesme Srl, ILA SpA, Eurallumina SpA and Syndial SpA (State aid measures C 38/B/04 (ex NN 58/04) and C 13/06 (ex N 587/05))*(notified under document C(2011) 956)***(Only the Italian text is authentic)****(Text with EEA relevance)**

(2011/746/EU)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular the first subparagraph of Article 108(2) thereof,

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

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

Whereas:

(3) By letters dated 22 January 2004 and 19 March 2004, the Commission requested further information on these measures. The Italian authorities replied by letters dated 9 February 2004 and 9 June 2004. By letter of 20 September 2004, Italy submitted further information.

(4) By letter dated 16 November 2004, the Commission informed Italy that it had decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union (TFEU) in respect of the measure.

(5) The Commission's decision to initiate the procedure was published in the *Official Journal of the European Union* ⁽²⁾. The Commission invited interested parties to submit their comments on the measures.

1. PROCEDURE

1.1. Case C 38/B/04

(1) By letter dated 4 December 2003, a law firm representing a complainant brought to the Commission's attention a series of articles published in the Italian press concerning the Italian Government's intention to introduce preferential electricity tariffs for certain undertakings located in Sardinia.

(2) The tariffs were introduced by Article 1 of the Prime Ministerial Decree of 6 February 2004 ('the 2004 Decree'). The Decree had two distinct effects: a) it introduced new preferential electricity tariffs for the companies Portovesme Srl, ILA SpA and Eurallumina SpA, and b) it prolonged an existing preferential tariff in favour of Alcoa Trasformazioni, a producer of primary aluminium ('Alcoa').

(6) Italy submitted observations by letters dated 4 February 2005 and 11 February 2005.

(7) The Commission also received observations from other interested parties, including three of the undertakings benefiting under the measures and a competitor of Portovesme. By letter dated 22 March 2005 the Commission forwarded those observations to Italy, which was given the opportunity to comment. Italy's comments were received by letter dated 20 September 2005.

(8) On 29 October 2008 the case C 38/04 was split into part A, concerning Alcoa, and part B, concerning Portovesme, ILA and Eurallumina.

⁽¹⁾ OJ C 30, 5.2.2005, p. 7, and OJ C 145, 21.6.2006, p. 8.

⁽²⁾ OJ C 30, 5.2.2005, p. 7.

- (9) On 19 November 2009 the Commission adopted a final negative decision with respect to Alcoa, ordering recovery of the aid ⁽³⁾.

1.2. Case C 13/06

- (10) By Article 11(12) of Decree-Law No 35 of 14 March 2005, converted into statute by Law No 80/2005 of 14 May 2005 laying down urgent provisions under the Action Plan for Economic, Social and Territorial Development ('Law No 80/9005'), the Italian authorities prolonged until 2010 the preferential electricity tariff for Portovesme, ILA and Eurallumina, and extended the benefit of the tariff to Syndial SpA, a chlorine producer also based in Sardinia.

- (11) The Commission received a complaint from a company competing with Syndial by letter dated 22 July 2005, followed by further submissions from the same company dated 7 October 2005 and 7 December 2005.

- (12) Italy notified the measure to the Commission by letter dated 23 November 2005. By letter dated 28 November 2005, Italy provided additional information.

- (13) By letter dated 22 December 2005 the Commission asked for further information, which Italy provided by letter dated 3 March 2006.

- (14) In the meantime, by letter dated 20 January 2006, the same competitor of Portovesme which had submitted observations in case C 38/B/04 complained about the new measure.

- (15) By letter dated 26 April 2006, the Commission informed Italy that it had decided to initiate the procedure laid down in Article 108(2) TFEU in respect of the changes and the extension of the special tariff scheme introduced by Law No 80/2005.

- (16) The Commission asked Italy for further clarification by letter dated 22 August 2006; Italy replied by letter dated 28 September 2006.

- (17) The Commission's decision to initiate the procedure was published in the *Official Journal of the European Union* ⁽⁴⁾. The Commission invited interested parties to submit their comments on the measures.

- (18) The Commission received observations from interested parties, including the beneficiaries, the two competitors of Portovesme and Syndial, and a producer of renewable energy. By letter dated 5 October 2006 the Commission forwarded those observations to Italy, which was given the opportunity to comment. Italy's comments were received by letter dated 1 December 2006.

- (19) Italy provided additional information by letters of 16 April 2007, 10 May 2007, 14 May 2007 and 22 June 2010.

1.3. Scope of the present Decision

- (20) The present decision covers both the tariffs introduced by Article 1 of the 2004 Decree for beneficiaries other than Alcoa ('the 2004 tariffs') and those introduced by Article 11(12) of Law No 80/2005 and subsequently spelt out in decisions taken by the Electricity and Gas Authority (*Autorità per l'Energia Elettrica e il Gas* — 'AEEG') ('the 2005 tariffs').

2. DETAILED DESCRIPTION OF THE MEASURE

2.1. The disputed 2004 tariffs

- (21) Article 1 of the 2004 Decree extended 'the [tariff] treatment laid down in Article 2 of the Decree of the Ministry for Industry, Trade and Crafts of 19 December 1995 ("the Alcoa Decree") to energy supplies for the production and processing of aluminium, lead, silver and zinc, but only in respect of plants already in existence at the date of entry into force of the present Decree and located on islands with insufficient or no interconnection to the national electricity and gas grids'.

- (22) This tariff treatment was to be transitory; it was to end 'upon the completion or upgrade of the connections with the national electricity and gas grids' and no later than 30 June 2007.

- (23) In practice, the 2004 Decree extended the preferential tariff already enjoyed by aluminium producer Alcoa to three energy-intensive companies located in Sardinia: Portovesme, a producer of zinc, silver and lead ⁽⁵⁾; ILA, a producer of processed aluminium products; and Eurallumina, a producer of alumina ⁽⁶⁾.

- (24) At the regulatory level, the tariff was implemented through decisions (*delibere*) of the AEEG.

⁽³⁾ Commission Decision 2010/460/EU of 19 November 2009 on State aid measures C 38/A/04 (ex NN 58/04) and C 36/B/06 (ex NN 38/06) implemented by Italy for Alcoa Trasformazioni (OJ L 227, 28.8.2010, p. 62).

⁽⁴⁾ OJ C 145, 21.6.2006, p. 8.

⁽⁵⁾ For its plants in Portoscuso and San Gavino.

⁽⁶⁾ Alumina is an intermediate raw material, obtained from bauxite, which is used for aluminium smelting. A large part of Eurallumina's output serves Alcoa's nearby smelting facilities.

(25) AEEG decision No 110/04 stipulated that the preferential tariffs would be applied only if the notification procedure had a positive outcome. However, following instructions from the Prime Minister's Office specifying that the 2004 Decree had not been formally notified under the State aid rules but only 'presented' to the Commission in the framework of a 'preliminary inquiry' (*indagine conoscitiva preliminare*), the AEEG implemented the 2004 Decree through decision No 148/04 ⁽⁷⁾.

(26) The system allowed the beneficiaries to be given compensatory payments on the terms laid down in the Alcoa Decree. For a given plant covered by the scheme, the compensatory payment was equal to the difference between the price paid to the company supplying the plant with electricity and a preferential price set by the State, multiplied by the electricity consumption of the plant. The method used to calculate the preferential price (or 'preferential tariff') was laid down in decision CIP No 15/1993. The price was subject to an indexation mechanism based on the variation of Italian power generation costs (the 'Ct component'). In 2004 the preferential price applied to the Sardinian beneficiaries ranged between EUR 26 and EUR 35 per MWh.

(27) The administrative management of the scheme was entrusted to the Electricity Industry Equalisation Fund (*Cassa Conguaglio per il Settore Elettrico*) ⁽⁸⁾. In practice, the tariff system worked as follows. The beneficiaries sent the Equalisation Fund detailed monthly data on the quantities of electricity they had consumed and the prices they had paid to their power suppliers. They then received from the Equalisation Fund cash payments calculated as indicated above ⁽⁹⁾.

(28) The resources required to finance the compensatory payments were raised through a parafiscal charge

⁽⁷⁾ The tariff mechanism is described in Article 73 of the consolidated rules for the provision of the services of transmission, distribution, measurement and sale of electricity for the regulatory period 2004–2007 (*Testo integrato delle disposizioni per l'erogazione dei servizi di trasmissione, distribuzione, misura e vendita dell'energia elettrica per il periodo di regolazione 2004-2007*). This document is drawn up and regularly updated by the AEEG.

⁽⁸⁾ The Equalisation Fund is a public body established by Legislative Decree No 98 of 26 January 1948; it acts on instruction from the AEEG, and among other things handles the financial flows related to preferential electricity tariffs (collection of levies and payment to final recipients).

⁽⁹⁾ The beneficiaries could also terminate their existing supply contracts and turn directly to the Single Buyer (*Acquirente unico*), a State-owned body responsible for pooling demand from consumers who wish to be supplied by it and procuring electricity on their behalf on the wholesale electricity market at the best possible price. If a beneficiary of the compensatory payments had decided to opt for this system, the State would have taken the Single Buyer price as the reference for the calculation of the compensatory payments. This arrangement was designed to minimise the costs of the scheme to the general public, as it discouraged beneficiaries from concluding unfavourable supply contracts with their own power suppliers (which would have resulted in higher compensatory payments). However, it was optional: the beneficiaries were not required to address themselves to the Single Buyer in order to receive the compensatory payments.

imposed on all Italian electricity consumers via component A4 of the standard electricity tariff ⁽¹⁰⁾.

(29) The scheme was to have ended on 30 June 2007. However, its implementation was discontinued on instructions from the AEEG soon after the Commission opened the formal investigation in November 2004 ⁽¹¹⁾.

(30) The data provided by Italy shows that Portovesme and Eurallumina received subsidies for electricity consumed between April and October 2004, and ILA received subsidies for electricity consumed between April and September 2004. The total payments made by the Equalisation Fund to these three undertakings under the scheme are set out below (in euro).

Portovesme Srl	12 845 892,82
Eurallumina SpA	5 208 152,05
ILA SpA	291 120,27

2.2. The disputed 2005 tariffs

(31) By Article 11(12) of Law No 80/2005, the Italian authorities extended 'the tariff treatment laid down in the Decree of the Ministry for Industry, Trade and Crafts of 19 December 1995 to energy supplies for the production and processing of aluminium, lead, silver and zinc and for the chlorine-soda cycle, by reference to prices applied to similar supplies on the European markets, but only in respect of plants already in existence at the date of entry into force of the present Decree, located in Sardinia and connected to the high-voltage network. This tariff treatment shall be subject to long-term commitments to be agreed between the beneficiaries, the Sardinian local authorities and the responsible Ministries.'

(32) Thus Law No 80/2005 in substance reintroduced the tariff scheme implemented in 2004, which extended the Alcoa treatment to other energy-intensive beneficiaries based in Sardinia. In practice, the Law applied only to Portovesme, ILA and Eurallumina, and to Syndial, a chlorine-soda producer which had not benefited from preferential prices before.

⁽¹⁰⁾ The standard Italian electricity tariff, which reflects the mechanism for imputing electricity costs to end-users, is divided into tariff components. Each component is designed to finance specific costs. Component A2, for example, finances the costs of dismantling old nuclear plants, while component A3 finances renewable energy installations. Component A4 financed preferential electricity tariff schemes. All end-users' bills share this structure.

⁽¹¹⁾ Letter from the AEEG to the Ministry for Production Activities dated 17 December 2004. According to the information available, however, the 2004 Decree has not been formally repealed by the Italian authorities.

(33) It should be noted that from 2005 onwards the preferential price was no longer pegged to the historical tariff originally laid down in the 1995 Alcoa Decree, but was now to be set independently by the AEEG so as to match the average electricity prices paid by the beneficiaries' competitors on the European market ⁽¹²⁾. The price was subject to annual updates: according to Article 11(13) of the Law, 'the tariff terms referred to in Articles 11 ⁽¹³⁾ and 12 shall apply from 1 January 2005 and shall be updated by the AEEG, which shall each year increase the nominal values of the tariffs by 4 %, or, if this latter value be higher, by the percentage increase in the average wholesale price of electrical energy recorded on the main European electrical energy exchanges, principally Frankfurt and Amsterdam.' In decision No 217/05, the AEEG gave an interpretation of this update mechanism which was more favourable to the beneficiaries, as it laid down that the annual increase in the tariff could not exceed 4 %.

(34) In the same decision, the AEEG set the preferential prices applicable to the various industries for the year 2005 as follows:

Industries qualifying for preferential tariffs	Preferential price EUR/MWh
Aluminium processing	50
Lead and zinc	23
Aluminium production	27
Chlorine cycle	27

(35) Like the 2004 tariffs, the 2005 tariffs were to be financed by means of a parafiscal levy charged to all electricity end-users via component A4 of the standard electricity tariff. The management of the financial flows of the system was again entrusted to the Equalisation Fund.

(36) Entitlement to the tariff was conditional upon a commitment by which the beneficiaries undertook to carry out productive investment in Sardinia on the basis of industrial plans to be submitted to the regional authorities. For example, Portovesme undertook to invest in the self-generation of electricity or to participate in the construction of new power plants.

(37) Italy notified Article 11(12) of Law No 80/2005 in accordance with Article 108(3) TFEU. Payment of the

2005 tariffs was subject to the authorisation of the scheme by the Commission. The 2005 tariffs have consequently not been implemented.

2.3. Proceedings before national courts

(38) Solvay Chimica Italia and Solvay Chimica Bussi SpA, which operate in the chlorine-soda cycle and are located outside Sardinia, brought legal proceedings before the Regional Administrative Court of Lombardy ⁽¹⁴⁾ challenging the decisions taken by the AEEG in implementation of Article 11(12) of Law No 80/2005, on the grounds that they involved the granting of unlawful State aid and that they breached other provisions of Italian law ⁽¹⁵⁾. On 27 November 2006 the Court stayed the proceedings before it, pending the conclusion of the State aid investigation initiated by the Commission in Case C 13/06.

2.4. Combination with previous incompatible aid — Deggendorf

(39) After the opening of proceedings, Italy indicated that Eurallumina had not reimbursed the incompatible aid which had been the subject of Case C 80/01 (aid for alumina production) ⁽¹⁶⁾, but that, according to the company, the Sardinian regional authorities had issued a recovery order in respect of this measure on 8 May 2006.

3. DECISION TO INITIATE PROCEEDINGS UNDER ARTICLE 108(2) TFEU

(40) The Commission decided to initiate the formal investigation on the following grounds.

3.1. Case C 38/B/04

(41) In its decision to open the formal investigation ⁽¹⁷⁾, the Commission considered whether it might be that the 2004 tariffs for Portovesme, ILA and Eurallumina did not constitute State aid, on the ground that they were similar to the preferential tariff granted to Alcoa in 1996, which the Commission had held not to constitute State aid in its decision of 4 December 1996 ('the Alumix decision') ⁽¹⁸⁾.

⁽¹⁴⁾ Case reference R.G. n. 2317/2005.

⁽¹⁵⁾ In particular Legislative Decree No 79/1999, which implemented Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity (OJ L 27, 30.1.1997, p. 20).

⁽¹⁶⁾ Commission Decisions C/2005/4436/06 of 7 December 2005 and C/2007/286/3 of 7 February 2007.

⁽¹⁷⁾ Commission Decision C(2004) 4329 of 16 November 2004 (OJ C 30, 5.2.2005, p. 7).

⁽¹⁸⁾ OJ C 288, 1.10.1996, p. 4.

⁽¹²⁾ This term is in all likelihood be understood as referring to the EU/JEEA market.

⁽¹³⁾ This Article extended the Alcoa and Terni tariffs to 2010.

(42) The Commission observed that the new tariff seemed different from the *Alumix* tariff, as the *Alumix* tariff was granted directly by ENEL, the Italian monopolist electricity operator, while the new tariff involved the selective intervention of the State to compensate the difference between the market price agreed by the beneficiaries with their power suppliers and the preferential price fixed in 1996. The Commission concluded that the 2004 Decree did not merely extend to new beneficiaries the scope of an existing measure that did not constitute State aid, but rather introduced a new scheme for the benefit of the three undertakings concerned, with a financial mechanism that was very different from the *Alumix* tariff.

(43) The opening decision classified the tariffs introduced by the 2004 Decree as operating aid, and assessed whether that aid could be authorised on the basis of the Guidelines on National Regional Aid ('the Regional Aid Guidelines')⁽¹⁹⁾, since Sardinia was an assisted region within the scope of Article 107(3)(a) until the end of 2006. The Commission doubted whether the aid could be authorised on that basis, since ad hoc aid of that kind, granted to a limited number of undertakings, did not seem to promote regional development.

(44) The Commission also expressed concern that the measure might have the effect of reducing the level of taxation applicable to electricity. Any such reduction would have to have a legal basis in Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity⁽²⁰⁾.

3.2. Case C 13/06

(45) In its decision of 27 April 2006 opening the formal investigation, the Commission classified the 2005 tariff scheme as new operating aid.

(46) The Commission considered whether the preferential tariff could be authorised as regional operating aid on the basis of the Regional Aid Guidelines, since Sardinia was to be an assisted region within the scope of Article 107(3)(a) TFEU until the end of 2006.

(47) Despite Italy's insistence that high electricity prices in Sardinia handicapped the development of the island, the Commission took the view that Italy had not

shown that prices were significantly higher in Sardinia, either on average or specifically for energy-intensive users⁽²¹⁾. The Commission pointed out that the over-capacity that existed in electricity generation in Sardinia could only have the effect of encouraging power generators to sell electricity at the lowest possible price, until such time as the completion of the interconnection projects, which was scheduled for 2010, enabled them to export power from Sardinia.

(48) Besides, Italy had not explained why higher prices should be regarded as a regional handicap, or how the tariff would contribute to regional development. The Commission accordingly doubted whether the aid was necessary.

(49) The Commission also doubted whether ad hoc aid of this kind was proportional to the regional disadvantages, in particular in view of the method used to calculate the preferential price, which bore no relation to the prices charged in the rest of Italy but was based on the average prices charged in Europe to energy-intensive users.

(50) The Commission noted that the duration of the measure exceeded five years, which was usually the maximum period for which regional operating aid would be authorised, and that the aid was not degressive in real terms, in view of the 4 % cap imposed on increases in the tariff.

(51) As regards the period covered by the Guidelines on National Regional Aid 2007–2013⁽²²⁾, the Commission noted that Sardinia would cease to qualify for aid under Article 107(3)(a) TFEU, and in particular for operating aid. The Guidelines would allow a two-year transitional period for the linear phasing-out of existing operating aid schemes, but it did not seem appropriate to allow new operating aid to be introduced for a few months and then phased out, especially given the doubts expressed and the distortive nature of the aid.

(52) In conclusion, the Commission doubted whether the preferential tariff for Portovesme, ILA, Eurallumina and Syndial could be authorised either as regional aid or on any other grounds, which Italy had in any event failed to identify.

⁽¹⁹⁾ OJ C 74, 10.3.1998, p. 9, points 4.15 to 4.17, as amended (OJ C 258, 9.9.2000, p. 5).

⁽²⁰⁾ OJ L 283, 31.10.2003, p. 51.

⁽²¹⁾ In particular, the Italian authorities argued that prices for energy-intensive users were negotiated bilaterally and were therefore not in the public domain. This meant that they were unable to quote electricity prices paid by the beneficiaries and by their competitors in other Italian regions.

⁽²²⁾ OJ C 54, 4.3.2006, p. 13.

- (53) As regards Eurallumina, the Commission observed that the company had not yet reimbursed unlawful and incompatible State aid it had received⁽²³⁾, and that under the rule in *Deggendorf*⁽²⁴⁾ it consequently could not receive aid under any new measure.

4. OBSERVATIONS SUBMITTED BY INTERESTED PARTIES

4.1. Case C 38/B/04

- (54) In response to the Commission's invitation to submit comments on the 2004 decision to open the in-depth investigation, observations were received from the original complainant, several of the beneficiaries (Portovesme, Eurallumina and Alcoa), and other interested parties. Only the observations relevant to the preferential tariff for Portovesme, ILA and Eurallumina are summarised here. The observations made by Alcoa are not included, as they are comprehensively addressed in the final decision specifically concerning that company⁽²⁵⁾.

4.1.1. Observations submitted by Portovesme

- (55) Portovesme argued that the preferential tariff addressed a market failure, namely the failure of the recently liberalised Sardinian electricity market to deliver competitive prices owing to the market power of the incumbent operators. Portovesme claimed that ENEL and Endesa (whose power generation assets in Sardinia were subsequently sold to E.ON) formed a duopoly, and artificially kept electricity prices in Sardinia in line with average Italian prices, whereas in fact Sardinian prices should be much lower, especially for large electricity consumers, given the overcapacity in electricity generation, which ought to encourage generators to sell at competitive prices.
- (56) Portovesme contended that the preferential price enjoyed corresponded to the price the company would have obtained under normal market conditions, i.e. if the electricity market functioned correctly.
- (57) According to Portovesme, the compensatory payments received from the Equalisation Fund (amounting to EUR 37 per MWh) brought the price paid by Portovesme into line with power prices paid by its competitors, and did not distort competition, since all EU zinc producers

paid equivalent prices, and the measure merely offset the competitive disadvantage suffered by the company as a result of Sardinia's structural problems (which included the absence of natural gas).

- (58) Metals like zinc, aluminium and lead were commodities for which there was one world price, arrived at on the London Metal Exchange. Variations in local production costs did not translate into differences in world prices. In particular, Portovesme's zinc production was so small (at less than 1 % of world production) that it could not affect the world price.

- (59) Without the tariff Portovesme would have to close its plant, but the closure would not benefit other EU zinc producers, who would not be in a position to increase output, and the gap would be filled by imports from third countries. Portovesme concluded that the preferential tariff did not affect competition or trade in the EU.

- (60) Moreover, according to Portovesme, the compensatory payments from the Equalisation Fund did not involve State resources, since the Equalisation Fund merely redistributed private funds which came from electricity end-users.

- (61) Portovesme noted that power off-take by energy-intensive industries was important to ensure security and continuity of supply in Sardinia, and to avoid inefficiencies in power generation which would lead to higher electricity costs for end-users.

- (62) Finally, the company points out that, if it was obliged to close down its plant, the consequences for Sardinia's production base would be very serious, as 790 direct jobs and 500 indirect jobs would be lost.

4.1.2. Observations submitted by Eurallumina

- (63) Eurallumina argued that alumina production costs in Europe were higher than in other regions of the world, owing mainly to higher electricity and fuel prices and to the cost of transporting bauxite⁽²⁶⁾. The higher costs could not be passed on in the form of higher prices, since the price of alumina was set on the London Metal Exchange and individual producers had no influence over it. European alumina production therefore suffered from a competitive disadvantage compared with the rest of the world.

⁽²³⁾ Case C 80/01 (alumina case, Commission Decision 2006/323/EC). The case concerned exemptions from excise duties on heavy oil used for the production of alumina in Sardinia, in Gardanne (France), and in Shannon (Ireland).

⁽²⁴⁾ Judgment of the Court of Justice in Case C-355/95 *Textilwerke Deggendorf v Commission* [1997] ECR I-2549.

⁽²⁵⁾ See recital 9 of the present Decision.

⁽²⁶⁾ Aluminium ore, the raw material for the production of alumina.

(64) In addition to the general problems affecting European alumina refineries, Eurallumina also pointed to specific Sardinian problems that prevented local industries from reaping the benefits of electricity market liberalisation, notably the market power of incumbent electricity operators (see Portovesme's observations in recital 55 above). Eurallumina also contended that the absence of natural gas was a specific handicap for the production of alumina in Sardinia, as the large quantities of steam required for the process had to be obtained using more expensive heavy oil.

(65) According to Eurallumina, after liberalisation the market power of electricity generators in Sardinia led to an increase in electricity prices: without the tariff, Eurallumina would have had to pay EUR 65,95 per MWh for its electricity supplies, as against the EUR 44 per MWh it used to pay before liberalisation. The 2004 tariff brought the price down to EUR 35 per MWh.

(66) Like Portovesme, Eurallumina contended that, if it was forced to go out of business, other EU alumina producers would not be able to step in, as they already worked at maximum capacity, and the gap would be filled by imports from third countries. Closure would lead to the loss of 400 direct jobs and 250 indirect jobs⁽²⁷⁾. Given that it was the sole supplier of alumina for Alcoa's smelter, Eurallumina considered that the closure of its alumina plant might also jeopardise Alcoa's viability in Sardinia.

(67) Eurallumina concluded that the tariff introduced by the 2004 Decree was necessary pending the development of the new infrastructure that would remove the main factors of competitive disadvantage affecting Sardinian industry.

4.1.3. Observations submitted by other interested parties

(68) A competitor of Portovesme — the same company that had originally brought the case to the Commission's attention — wrote to the Commission again after the opening of the formal investigation. It submitted an analysis of the 2004 preferential tariff in which it concluded that the tariff constituted unlawful State aid. The disputed tariff scheme was fundamentally different from the *Alumix* tariff granted to Alcoa: it was impossible to take the view that it did not constitute State aid. The aid must be held incompatible with the common market, as it could not be approved either as regional operating aid or as restructuring aid.

⁽²⁷⁾ At the time of the drafting of this decision, Eurallumina has been out of production for more than a year, with workers receiving *cassa integrazione* layoff benefit.

(69) Solvay Chimica Italia and Solvay Chimica Bussi, who operate in the chlorine-soda industry, sent observations on the 2004 tariffs in July 2005, after the expiry of the one-month deadline for submitting comments in response to the decision to open the formal investigation. Despite the delay, these companies asked to be considered interested parties. In their observations they submitted that both the 2004 and the 2005 tariffs constituted unlawful and incompatible State aid.

4.1.4. Observations submitted by Italy

The tariff addresses a market failure

(70) Italy argued that the electricity market in the EU was not yet fully competitive, as the Commission had itself acknowledged in its fourth Annual Report on the Implementation of the Gas and Electricity Internal Market⁽²⁸⁾. Undertakings, in particular energy-intensive ones, were unable to choose their suppliers freely and to procure electricity on comparable terms in the various Member States. These difficulties were not related to the undertakings' own entrepreneurship, but were the result of the structural deficiencies of energy markets. The current situation in the EU energy market had negative effects on free competition in the product markets of energy-intensive users.

(71) In Italy, despite the liberalisation of the sector, there were particular structural deficiencies, such as insufficient interconnection between the different parts of the national grids and a concentrated market structure. In these circumstances, liberalisation had not translated into better prices for energy-intensive users. The problems were particularly acute in Sardinia, where interconnection was limited.

(72) Italy submitted, therefore, that a special tariff system reflecting demand profiles should be considered justified, as a regulatory measure that simulated the mechanisms that would be at play in a fully competitive market. The measure restored the level playing field between energy-intensive undertakings operating in different Member States, eliminating the geographical disadvantages which affect undertakings located in Sardinia. The scheme anticipated the expected effects of the liberalisation process. According to Italy, similar measures were implemented in other Member States, where energy-intensive users benefited as a result of regulated electricity tariffs.

(73) According to Italy, the 2004 decree pursued two further objectives: to support employment in Sardinia, which was concentrated in the metals sector, and to maintain a sufficient level of demand for power generation in Sardinia, which suffered from overcapacity.

⁽²⁸⁾ Document COM(2004) 863 final.

The tariff is not State aid

- (74) Italy contended that the new tariff scheme was equivalent, de facto, to the *Alumix* tariff, which the Commission had found did not constitute State aid. The differences between the old and the new scheme were due solely to the new 'tariff structure' required by the launch of the liberalised energy market.
- (75) Italy submitted that the tariff scheme did not constitute State aid. As regards the use of State resources, the tariff system was comparable to the arrangement in the *PreussenElektra* case, which the Court of Justice had held did not involve State resources⁽²⁹⁾. The Equalisation Fund was a technical body that kept the accounts of the system, and could not dispose freely of the financial resources it handled. The fact that the AEEG and the Ministry of Finance exercised a measure of control over the Equalisation Fund's activities did not mean that the State could freely dispose of those resources. According to Italy, therefore, the resources used to finance the tariff mechanism were entirely private.
- (76) Italy further submitted that the tariff did not have an impact on trade within the Union, and could not distort competition, for reasons linked to the existence of a world price for the products, which were commodities (see observations submitted by Portovesme, recital 55 above). Moreover, both EU and Italian production had failed to keep pace with rising demand for the metals concerned. In 2005 domestic production covered only 12 % of Italian demand for aluminium, 55 % of Italian demand for zinc, and 80 % of Italian demand for lead. There was a worsening production deficit for these metals in the EU and in Italy, and demand was increasingly being met by imports from third countries. If the metals industry in Italy disappeared, no new EU entrant would replace the capacity shut down in Italy, as EU plants were already working at full capacity, and no existing producer or new entrant would have an incentive to increase capacity, since the long-term prospects for the availability of affordable power were uncertain. The maintenance in Italy of these production capabilities consequently could not damage competitors. Since the preferential tariff was not lower than the electricity prices paid on average by the companies' competitors, it did not encourage exports from Sardinia towards other Member States.

If the tariff did constitute aid, it would be regional operating aid and would be compatible

- (77) Italy argued that, even if the Commission were to conclude that the measure was indeed State aid, the tariff could be considered compatible with the internal market on the ground that it was regional operating aid, which was admissible in Sardinia on the basis of the exemption in Article 107(3)(a) TFEU.

- (78) According to Italy, the imperfections of the Sardinian electricity market (market concentration, poor interconnection, and overcapacity in electricity generation) and the lack of access to gas infrastructure constituted a regional handicap, and the tariff sought to alleviate that handicap.
- (79) Electricity prices in Italy were 38 % higher than the EU average for energy-intensive users. This created a competitiveness problem which was exacerbated, in Sardinia, by the shortcomings of the local electricity market and the absence of access to the natural gas grid.
- (80) Italy contended that the measure contributed to regional development because the metals industry made a major contribution to the economy and to employment in Sardinia: the metals industry accounted for 12 % of the employed workforce and for 12,2 % of regional GNP in manufacturing. The tariff had positive repercussions on employment and the maintenance of the social and economic fabric of the island.
- (81) According to Italy, the tariff was proportional to the disadvantages faced by the beneficiaries, because it merely aligned the electricity prices paid by Sardinian producers on the average prices paid by their EU competitors.
- (82) The tariff was also short-term and transitional, since it was expected to end upon the completion of infrastructure projects aimed at improving interconnection with the electricity and gas grids (the new SAPEI interconnection cable and the GALSI gas pipeline)⁽³⁰⁾.
- (83) According to Italy, the measure was also degressive, because the preferential price was indexed on the basis of variations in fuel prices, and could only increase or remain unchanged.

4.2. Case C 13/06

4.2.1. Observations submitted by Portovesme

- (84) Portovesme considered that the 2005 tariffs did not distort competition, that they were necessary to ensure the survival of the industries concerned, and that they could be considered compatible as regional aid. The company's arguments are similar to those put forward by Italy, to which reference may be made (see recitals 87 to 104).

⁽³⁰⁾ Italy had estimated that these infrastructures would be completed in 2007. In the context of Cases C 13/2006 and C 36b/2006 Italy put back the expected date to 2010. At the time of the adoption of this decision, the GALSI pipeline has not been built (it is expected to be commissioned in 2014), and the SAPEI cable is only partly operational.

⁽²⁹⁾ Case C-379/98 [2001] ECR I-2099.

4.2.2. Observations submitted by Eurallumina

- (85) Eurallumina likewise considered that the 2005 tariffs did not distort competition, were necessary to ensure the survival of the industries concerned, and could be considered compatible as regional aid. The company's arguments are similar to those put forward by Italy, to which reference may be made.

4.2.3. Observations submitted by other interested parties

- (86) The two competitors of Portovesme and Syndial that had submitted observations in Case C 38/B/04 submitted observations in this case too. Both of them contended that the disputed measure constituted operating aid which should be considered incompatible with the internal market.

4.2.4. Observations submitted by Italy

The tariffs are part of a regional support strategy

- (87) Italy contended that the 2005 tariffs were very different from the tariffs implemented in 2004, since they were now in line with the requirements of the Regional Aid Guidelines.
- (88) According to Italy, the tariffs might, on the basis of a superficial assessment, be classified as operating aid, but in reality they were part of an array of measures designed to favour regional development in Sardinia. Italy drew attention, in particular, to the close link between the tariffs and the commitment to carry out long-term investments that beneficiaries were requested to give. The suspensive clause making the implementation of the measure subject to authorisation by the Commission testified, according to Italy, to its regional aid character.
- (89) The memorandum of understanding (*protocollo d'intesa*) signed by the Region and the beneficiaries was the lynchpin of this strategy. It comprised the following:
- (a) the productive investments described in the industrial plans submitted by the beneficiaries;
 - (b) the speedy authorisation of energy interconnection infrastructure enabling the beneficiaries to source energy at competitive prices (the GALSI gas pipeline and the SAPEI interconnection cable);
 - (c) the award of an integrated concession for the exploitation of the Sulcis coalmine and the construction/operation of a new coal-fuelled power plant intended to supply power to the beneficiaries; and
 - (d) the preferential tariffs.

- (90) Italy took the view that the tariffs should be seen as a policy instrument aimed at safeguarding sectors threatened by high energy prices, which would otherwise relocate outside Italy and Europe, owing to aggressive competition from non-EU companies with lower production costs. The tariffs were to be applied until the completion of the planned infrastructure and the achievement of a competitive internal market for energy. The measure was in line with the spirit of regional aid, because it promoted economic growth and employment on an island where energy-intensive production suffered from a competitive disadvantage owing not only to the imperfect state of liberalisation of the electricity market but also to exceptional infrastructural deficiencies in Sardinia as regards interconnection to the national electricity and gas grids.

- (91) In support of this integrated approach, Italy cited the First Report of the High Level Group on Competitiveness, Energy and Environment ⁽³¹⁾, which found that the liberalisation process in the energy sector had not produced satisfactory results, that better interconnection was necessary, and that long-term supply contracts with predictable prices or partnerships between customers and energy suppliers were desirable. Italy argued that the measures planned for Sardinia moved in this direction, but that short-term measures such as the tariffs were also needed in order to safeguard the competitiveness of Sardinian industry and ensure its survival until the planned investments were carried out and the structural problems were resolved.

The aid offsets a regional disadvantage

- (92) Italy contended that it was not possible to compare power prices paid by the Sardinian beneficiaries and average power prices paid by comparable undertakings on the Italian mainland, since energy-intensive undertakings purchased electricity via bilateral contracts which were not in the public domain. According to Italy, the Commission erred in carrying out a comparison based on prices recorded on power exchanges, since only a marginal part of these undertakings' energy supplies was procured on exchanges.
- (93) According to Italy, prices negotiated via bilateral contracts would be favourable to consumers only if the consumers could freely choose their suppliers and source electricity which was produced using competitive technologies. This was not possible in Sardinia, where power generation plants could not produce cheap electricity since they had no access to natural gas. Besides, new investments in modern power generation were discouraged by the limited electrical interconnection which made it impossible to export electricity. Another factor was market concentration and the role played by incumbent operators.

⁽³¹⁾ First Report of the High Level Group on Competitiveness, Energy and the Environment, 'Contributing to an integrated approach on competitiveness, energy and environment policies', http://ec.europa.eu/enterprise/policies/sustainable-business/policy-integration/high-level-group/reference-material/index_en.htm. The High Level Group was a forum in which representatives of the Commission and business leaders took part.

- (94) In these circumstances, according to Italy, there was justification for applying tariffs which stabilised electricity prices until more effective competition was achieved on the electricity market. Italy once again argued that the preferential tariffs simulated the mechanism of a fully competitive market.
- (95) As regards the overcapacity in electricity generation which led the Commission to doubt that power prices in Sardinia were higher than on mainland Italy (since overcapacity should rather encourage generators to sell at competitive prices to large consumers — see recital 47), Italy put forward the following arguments. Sardinian overcapacity in electricity generation could not lead to lower prices for consumers, because in this specific case overcapacity was the result of limited interconnection, which made it necessary to establish a very high power reserve in order to safeguard the continuity of electricity supplies on the island ⁽³²⁾. Since this reserve was in any event remunerated via charges imposed on all electricity end-users, power suppliers had no interest in selling the electricity produced using this idle capacity at more competitive prices.

The aid is proportional

- (96) According to Italy the measure was proportional, because the price fixed by the AEEG for 2005 (see recital 34 above) corresponded to the average price paid in the EU by the beneficiaries' competitors, which was calculated objectively by the regulator. Italy also pointed out that in Member States with regulated tariffs large industrial consumers paid prices as low as EUR 25 per MWh for their electricity supplies in 2005.
- (97) Italy therefore contested the data submitted by the complainants, which in its view were methodologically flawed, in that they overestimated the average electricity prices paid by the beneficiaries' competitors in the EU.

The aid is temporary and degressive

- (98) According to Italy, the duration of the scheme, at six years rather than five, was justified by the need to wait for the completion of the energy infrastructure.
- (99) Italy also contended that the degressivity requirement was met: the tariffs were degressive because they were adjusted on the basis of the weighted average of variations on the Amsterdam and Frankfurt power exchanges and could only increase but not decrease.
- (100) The tariffs were pegged to price variations on the power exchanges because, according to Italy, this was an objective benchmark which was broadly representative of trends in energy prices. However, Italy maintained that actual price increases for EU energy-intensive users were generally considerably lower than the increases

recorded on exchanges, as such users paid prices agreed through bilateral contracts, or set by the State where there were regulated tariffs, and these prices were less prone to variation.

- (101) Italy concluded that that the annual 4 % increase applied to the Sardinian tariffs was in line with the increases in energy prices applied to their direct EU competitors.
- (102) Italy drew attention to the existence in the EU of measures which had effects equivalent to the disputed preferential tariffs, and argued that all of them should be assessed in the same way, regardless of their form, since their common objective was to ensure the survival of energy-intensive industries in the EU and prevent their relocation outside the national territory.

Eligibility of Sardinia for regional aid after 2007

- (103) Although from 2007 onwards Sardinia could no longer benefit from regional operating aid, Italy argued that the Regional Aid Guidelines made provision for a phasing-out of schemes which were ongoing at the time a region ceased to be eligible for the exemption in Article 107(3)(a) TFEU. Thus the Commission was still in a position to authorise the measure under the 2007 Regional Aid Guidelines. In any event, Italy contended that the disputed measure should not be viewed as ordinary operating aid.

No impact on trade within the Union

- (104) Italy contended once again that the tariffs did not affect trade between Member States, on the basis of the arguments already set out with respect to aluminium, zinc and lead in recital 76. The same reasoning, Italy maintained, applied to the chemical industry. Italy pointed out that in 2003 imports of chemical products into Italy had exceeded exports, and that EU and Italian production had slumped since 2001. With specific reference to the production of PVC, which was the main application of chlorine, Italy pointed to a production deficit in the country: in 2002, only 470 000 tonnes of PVC had been produced in Italy, while consumption had been 970 000 tonnes.

5. ASSESSMENT OF THE MEASURE

5.1. Existence of State aid pursuant to Article 107(1) TFEU

- (105) A measure constitutes State aid within the meaning of Article 107(1) TFEU if the following conditions are all fulfilled: the measure (a) confers an economic advantage on the beneficiary; (b) is granted by the State or through State resources; (c) is selective; and (d) affects trade between Member States and is liable to distort competition within the EU.

⁽³²⁾ This high reserve level (80 % of maximum power absorbed by the network) was fixed by Ministerial Decree of 7 August 2000.

5.1.1. Existence of an advantage

- (106) Under the 2004 and 2005 tariff arrangements, the State intervened to subsidise the electricity price negotiated by the beneficiaries with their suppliers. In 2004, for example, on the basis of the bilateral supply contracts in force at the time and in the absence of the compensatory payments, Portovesme would have paid EUR 63 per MWh⁽³³⁾ and Eurallumina EUR 65,95. These figures were provided by Italy and the beneficiaries themselves, and are therefore not in dispute.
- (107) In 2005, according to the data provided by Italy, the electricity price negotiated by Syndial with its supplier exceeded EUR 60 per MWh, whereas the tariff would bring it down to EUR 27 per MWh. The rationale of the two measures was that the State would reimburse to the beneficiaries the extra costs they had sustained in order to purchase electricity in Sardinia compared to average prices paid by their EU competitors.
- (108) Portovesme contends that the preferential price corresponds to the price which would prevail in a fully competitive market, and therefore does not provide an advantage. The Commission has already rejected this line of reasoning in the *Alcoa* case, which concerned virtually identical tariffs. When assessing the presence of an advantage, neither the Union lawcourts nor the Commission have ever taken into account the conditions that would prevail in a hypothetical market that functioned better. The framework of reference has always been the conditions prevailing on the actual markets concerned⁽³⁴⁾.
- (109) This argument also supposes that where a market was not functioning properly a Member State would be justified in setting prices that simulated conditions of effective competition (see Italy's comment in recital 72 above).
- (110) This reasoning cannot be accepted, as it runs counter to the settled principle of EU case-law according to which 'the fact that a Member State seeks to approximate, by unilateral measures, conditions of competition in a particular sector of the economy to those prevailing in other Member States cannot deprive the measures in question of their character as aid'⁽³⁵⁾. The Commission considers that the same principle applies to situations

where a Member State seeks to approximate conditions of competition to those that would prevail in a fully competitive market.

- (111) Further, if this submission were to be accepted, there would be no State aid where a Member State granted a subsidy to bridge the gap between a price freely negotiated between two market operators and the theoretical price at which agreement might have been arrived at in conditions of full competition. This would defeat the fundamental purpose of State aid control.
- (112) Italy contends that these tariffs are identical to the *Alumix* tariff, which the Commission considered not to constitute aid (see recital 74 above), and should likewise be considered free of aid.
- (113) The Commission points out that the situation on which the Commission took a position in the *Alumix* case was very different. In *Alumix*, the tariff was granted by ENEL, which at the time was a public body supplying electricity on a monopoly basis in an electricity market which had yet to be liberalised⁽³⁶⁾. In that situation, the Commission had to ascertain whether ENEL was selling at an artificially low price or behaving like a rational market economy operator. Given the monopoly over electricity generation and supply held by ENEL, there was no competitive market price to which the Commission could refer to assess the existence of an advantage. Therefore, the Commission devised a method to identify the lowest theoretical market price at which a rational supplier would be prepared to sell to its 'best customer'.
- (114) However, this method cannot be applied in a situation where prices are negotiated by end-users with power suppliers on a liberalised market and are subsidised by compensatory payments ex post. Thus the analysis in the *Alumix* decision, and the Commission's findings in that case, are manifestly devoid of relevance here. This was borne out by the judgment of the Court of First Instance which upheld the decision to open the formal investigation in *Alcoa*⁽³⁷⁾ (paragraph 132 of the judgment).
- (115) In the present case, the market operator principle does not apply. The position would have to be assessed in the light of the market operator test if the State sold electricity to the companies concerned, either directly or through a State-owned company, as it did in *Alumix*. But here the electricity is supplied by private companies. There is therefore no need, as there was in *Alumix*, to examine whether the State's behaviour has been comparable to that of a rational market operator.

⁽³³⁾ This figure was obtained by adding to the preferential price of approximately EUR 26 per MWh a compensatory payment of EUR 37 per MWh.

⁽³⁴⁾ See, for example, the Dutch glasshouse growers case, Commission Decision 85/215/EEC of 13 February 1985 on the preferential tariff charged to glasshouse growers for natural gas in the Netherlands (OJ L 97, 4.4.1985, p. 49). In order to assess the presence of an advantage in certain gas prices in that case, the Commission considered actual market conditions and applied the market economy operator test.

⁽³⁵⁾ See, for example, the judgment of the Court of Justice in Case C-372/97 *Italy v Commission* [2004] ECR I-3679, paragraph 67.

⁽³⁶⁾ The first liberalisation directive, Directive 96/92/EC, was implemented in Italy by Decree No 79/1999 (see footnote 15).

⁽³⁷⁾ Case T-332/06 *Alcoa Trasformazioni* [2009] ECR II-29 (appeal pending).

- (116) It must be concluded that the 2004 and 2005 compensatory payment systems mitigate the charges payable under the supply contracts concluded by the beneficiaries, which would normally have to be included in the companies' budgets. In line with well-established case-law, therefore, the disputed measures confer an economic advantage on the recipients ⁽³⁸⁾.

5.1.2. Selectivity

- (117) Since the preferential electricity tariffs in Italy are granted exclusively to undertakings operating existing facilities located in Sardinia and belonging to a closed list of industries identified in the legislative and regulatory instruments that form the legal basis of the measures, the advantage they confer is a selective one.

5.1.3. State resources and imputability to the State

- (118) It is settled case-law that an advantage constitutes State aid within the scope of Article 87(1) TFEU only if it is granted directly or indirectly through State resources ⁽³⁹⁾ and is imputable to the State ⁽⁴⁰⁾.
- (119) As explained in recital 28, the compensatory payments at issue here are financed by means of a parafiscal charge collected by the Equalisation Fund via the A4 component of the electricity tariff. This charge is obligatory, being imposed by means of decisions of the AEEG that implement national legislation. The Equalisation Fund is a public body established by law which carries out its functions on the basis of precise instructions laid down in the decisions of the AEEG.
- (120) It is also settled case-law that the yield of a levy which is obligatory under national law and is paid to a body established by law constitutes a State resource within the meaning of Article 87(1) of the Treaty when it is earmarked for the funding of a measure which fulfils the other criteria of that Article ⁽⁴¹⁾.
- (121) Italy relies on the judgment of the Court of Justice in *PreussenElektra* ⁽⁴²⁾ to substantiate the thesis that the measure at hand is not financed through State resources. Italy argues that the funds required to finance the tariff are transferred by private parties (electricity consumers) to private parties (the beneficiaries); the role of the State is confined to the enactment of a law requiring payment of the required sums, with no discretion to dispose of the funds other than in the implementation of the statutory scheme. In particular, according to Italy and several of

the beneficiaries, the Equalisation Fund cannot exercise any control over the funds, and is merely an accounting intermediary.

- (122) In the *PreussenElektra* case, the Court held that an obligation imposed on private electricity supply undertakings to purchase electricity produced from renewable energy sources at minimum prices higher than the real economic value of that type of electricity did not constitute State aid, because the measure did not involve any direct or indirect transfer of State resources.
- (123) The Commission points out that in *PreussenElektra* the resources required to finance the measure were provided by the electricity suppliers directly to the producers of renewable energies, without transiting through any public body. In that system, the sums to be transferred could never be at the disposal of the Member State's authorities. In the case at hand, however, the monies transit through a public body, the Equalisation Fund, before being channelled to the final beneficiary. Thus *PreussenElektra* addresses different factual circumstances, and is not relevant to the present case.
- (124) The judgment in *Pearle* ⁽⁴³⁾ cannot assist Italy or the beneficiaries either. In *Pearle*, the Court found that, under certain specific conditions, the yield of a levy which transited through a public body did not constitute State resources. In *Pearle*, the measures were financed entirely by a particular trade at the sole initiative of the trade itself. The monies were collected via a parafiscal levy transiting through a public body which could not at any time dispose of the funds freely. In addition, there was a correspondence between the entities which paid the levy and those which received the benefits of the measure.
- (125) Italy contends that the Equalisation Fund does not have any discretion in the disbursement of the funds, which are earmarked for the financing of the tariffs and never come within 'the perimeter of public finance'. Thus the State cannot freely dispose of the funds, and consequently the funds do not constitute State resources.
- (126) As a preliminary remark, it should be pointed out that, while some of the *Pearle* criteria may subjectively be viewed as more central than others, there is no such thing as a 'key criterion' in *Pearle*. The tests enumerated in the judgment are cumulative. This is also the interpretation given by the Court of First Instance in *Earl Salvat*, where it examined a parafiscal levy challenged in that case in the light of each and every one of the *Pearle* criteria ⁽⁴⁴⁾.

⁽³⁸⁾ Judgment of the Court of Justice in Case C-241/94 *France v Commission* [1996] ECR I-4551, paragraph 34.

⁽³⁹⁾ See for example *PreussenElektra*, cited above, paragraph 58.

⁽⁴⁰⁾ See for example the judgment of the Court of Justice in Case C-482/99 *France v Commission (Stardust Marine)* [2002] ECR I-4397, paragraph 24.

⁽⁴¹⁾ See the judgments of the Court of Justice in Case 78/76 *Steinike & Weinlig* [1977] ECR 595 and Case 47/69 *French textiles* [1970] ECR 487.

⁽⁴²⁾ See footnote 29.

⁽⁴³⁾ Judgment of the Court of Justice in Case C-345/02 *Pearle and Others* [2004] ECR I-7139.

⁽⁴⁴⁾ Judgment of the Court of First Instance in Case T-136/05 *Earl Salvat v Commission* [2007] ECR II-4063, paragraphs 137–165.

- (127) Before considering the role played by the Equalisation Fund, the Commission has ascertained whether any of the other tests enumerated in *Pearle* are satisfied. It is clear that here, by contrast with the *Pearle* case, the disputed tariffs were established at the initiative of the State, not at the initiative of an economic sector. In *Pearle*, moreover, the beneficiaries of the measure were also the sole contributors of the resources used, so that the intervention of the public body did not tend to create an advantage which would constitute an additional burden on the State. In the case at hand, the beneficiaries do not bear the financial burden of the levy, which rests solely on electricity consumers. Thus the *Pearle* judgment cannot validly be relied upon irrespective of whether merit can be found in the argument that the Equalisation Fund is a mere accounting intermediary.
- (128) Turning now to the Equalisation Fund itself, the Commission points out that, according to settled case-law, no distinction should be made between cases where the aid is granted directly by the State and cases where it is granted by a public or private body designated or established by the State⁽⁴⁵⁾. Thus the public or private status of the Equalisation Fund is not a determining factor for the purpose of applying the State aid rules. The fact that the Equalisation Fund is a public body does not automatically mean that Article 107 TFEU is applicable⁽⁴⁶⁾; similarly, the intervention of a private body would not in itself preclude application of that Article.
- (129) However, the analysis cannot be limited to the powers of the Equalisation Fund in its capacity as a public body. What has to be ascertained, rather, is the more general question whether the State, either directly or through any other body designated by it, can exercise control over the funds used to finance the tariff. The same test would have to be applied if the Equalisation Fund were a private body.
- (130) The recent judgment of the Court of Justice in the *Essent*⁽⁴⁷⁾ case provides definitive guidance on this point. In *Essent*, the Netherlands had introduced by law a surcharge on electricity prices. The surcharge was paid by electricity consumers to network operators, which in turn transferred the monies to a designated company, SEP. SEP had no discretion in the management of the funds and operated under close control by the authorities. The Court came to the conclusion that the proceeds of the surcharge constituted State resources, because the surcharge on the price of electricity was imposed by national law, and therefore constituted a charge, and SEP was not entitled to use the proceeds from the charge for purposes other than those provided by the law, so that the monies remained under public control and were thus available to the national authorities. The Court considered that this was sufficient for such monies to be characterised as State resources.
- (131) The similarities with the case at hand are evident. The surcharge on the electricity price used to finance the tariffs at issue here is imposed, as in *Essent*, by law. The Equalisation Fund plays the same role as SEP, as it centralises and manages the proceeds of the parafiscal charge, and is subject to the same constraints, as it cannot use the proceeds from the charge for purposes other than those provided by law (the financing of preferential tariffs). The State is in a position to control and orient the use of the resources: the Equalisation Fund discharges its accounting functions on precise instructions from the AEEG, which acts within its statutory regulatory powers and/or in implementation of national legislation. Thus the resources handled by the Equalisation Fund remain under public control at all times.
- (132) This analysis is consistent with the Commission's decision in the Italian stranded costs case, in which it classified as State resources the monies administered by the Equalisation Fund in the A6 account⁽⁴⁸⁾.
- (133) The classification as State resources of the monies administered by the Equalisation Fund was borne out in the judgment of the Court of First Instance in the *Iride* case⁽⁴⁹⁾.
- (134) Italy's Supreme Court of Cassation had already ruled that the legal personality of the Equalisation Fund was not separate from that of the Italian State, and that the monies transferred to the Equalisation Fund should be considered State property, even if they derived from private entities and were intended for private undertakings (judgment No 11632/03 of 3 April 2003). In the *Iride* case, the applicants, Iride SpA and Iride Energia SpA, brought an action in the Court of First Instance challenging a decision whereby the Commission had categorised as State resources the sums administered by the Equalisation Fund in the A6 account. The arguments put forward by the applicants were very similar. They disputed the substance of the Court of Cassation's ruling, contending that the role of the Equalisation Fund was merely that of an accounting intermediary between private citizens subject to a financial obligation and the beneficiaries of the sums concerned, a role which did not allow the Equalisation Fund to make use of the monies deposited even for a short period of time. The applicants also claimed that the case-law developed in *PreussenElektra* was applicable.
- ⁽⁴⁵⁾ Judgment of the Court of Justice in Case 57/86 *Greece v Commission* [1988] ECR 2855, paragraph 12; *PreussenElektra*, cited above; judgment of the Court of Justice in Case C-126/01 *Gemo* [2003] ECR I-13769, paragraph 23.
- ⁽⁴⁶⁾ Judgments in *Stardust Marine*, cited above; *Pearle*, cited above; and *Earl Salvat*, cited above.
- ⁽⁴⁷⁾ Judgment of the Court of Justice in Case C-206/06 *Essent Netwerk Noord v Aluminium Delfzijl* [2008] ECR I-5497, paragraphs 69 and 70.
- ⁽⁴⁸⁾ Commission Decision C(2004) 4333 of 1 December 2004, Case No N 490/2000 *Italy — stranded costs of the electricity sector*.
- ⁽⁴⁹⁾ Judgment in Case T-25/07 *Iride* [2009] ECR II-245, paragraph 39.

- (135) The Court of First Instance, after pointing out that it had no jurisdiction to review the interpretation of Italian legislation by the Court of Cassation, confirmed that the monies held in the Equalisation Fund's A6 account were to be classified as State resources, because, in addition to being State property, they were under constant State control ⁽⁵⁰⁾.
- (136) That conclusion concerned the Equalisation Fund's A6 account, used to finance the stranded costs of Italy's electricity sector. It can, however, logically be extended to the A4 component, which finances the disputed tariffs. The judgment of the Court of Cassation was based on an analysis of the legal personality of the Equalisation Fund, and its finding with respect to State property therefore applies to all of the monies deposited with the Equalisation Fund. The same is true of the finding by the Court of First Instance that the State can control the resources administered by the Equalisation Fund. There is no difference between the A6 account and the A4 component other than the purpose to which the resources are put (covering stranded costs in the case of the A6 account, and financing preferential tariffs in the case of the A4 component). The sums transferred to the Sardinian beneficiaries from the A4 component must therefore also be categorised as State resources.
- (137) In addition to being financed by State resources, the disputed tariffs are imputable to the State, since the legal basis for the measures is laid down in national legislation and decrees and in the decisions taken by the AEEG, which is a public body, in the exercise of its public authority functions ⁽⁵¹⁾.
- 5.1.4. *Effect on trade and distortion of competition*
- (138) As regards the effect of the measures on trade between Member States and the ensuing distortion of competition, it is undisputed that the markets concerned (lead, zinc, silver, aluminium and chlorine/soda) are fully open to competition. This by itself is enough to establish that the tariffs have an effect on intra-Union trade.
- (139) Nevertheless, the Commission has considered the argument advanced by the beneficiaries and by Italy that in the metals industry (the argument has not been put forward expressly in respect of chlorine) the tariffs have no effect on trade and do not distort competition because there are no actual trade flows between Member States; no such trade flows are likely to develop, and in view of the particular features of the industry the tariffs do not damage the beneficiaries' competitors in the Union.
- (140) In the Commission's decisions and the judgments of the Court of Justice it has never been accepted that an absence of actual trade flows shows that an aid measure has no effect on intra-Union trade. The Court has in fact consistently ruled that aid to an undertaking may be such as to affect trade between the Member States and distort competition even if the beneficiary undertaking does not participate in intra-Union trade itself. Where a Member State grants aid to an undertaking, domestic production may for that reason be maintained or increased, with the result that undertakings established in other Member States have less chance of exporting their products to the market in that Member State ⁽⁵²⁾.
- (141) Moreover, the pattern of decreasing EU production, increasing imports from non-Union countries, and limited or no trade flows between Member States is not unusual: indeed it is typical of industries which are experiencing structural difficulties or which are subject to high competitive pressure. Such industries are particularly sensitive to measures taken by Member States to improve the competitive position of their domestic industries.
- (142) The fact that production of zinc, lead and silver in Italy is too modest to affect the reference price is irrelevant. The fact that there is a reference price for these metals which is not easily influenced by conditions of production in a single Member State does not mean that there cannot be competition between undertakings based in the EEA and selling on the worldwide metal markets. It is conceivable that aid to the Sardinian beneficiaries will not enable them to reduce the world price for their products and squeeze competitors out of the market, and that other European producers may remain in business as long as they can sell profitably at the world price. But the profits obtained in Italy thanks to the subsidised electricity tariffs strengthen the companies' competitive position in a general sense. For example, accumulated capital reserves can be used to take over competitors and to increase market share. This reasoning is all the more relevant considering that some of the beneficiaries belong to multinational companies ⁽⁵³⁾.

⁽⁵⁰⁾ *Iride*, cited above, paragraph 28.

⁽⁵¹⁾ See the judgments of the Court of Justice in Case 303/88 *Italy v Commission* [1988] ECR 1433 and Case 47/69 *France v Commission* [1970] ECR 4393; see also the judgment of the Court of First Instance in Case T-351/02 *Deutsche Bahn v Commission* [2006] ECR II-1047.

⁽⁵²⁾ Judgments of the Court of Justice in Case 102/87 *France v Commission* [1988] ECR 4067, paragraph 19, and Case C-305/89 *Italy v Commission* [1991] ECR I-1603, paragraph 26.

⁽⁵³⁾ Portovesme is owned by the multinational Glencore. Eurallumina is owned by the Russian company Rusal.

(143) Contrary to what the beneficiaries claim, the fact that the price paid in Italy in the sectors concerned is comparable to the average electricity price paid in Europe by competing producers cannot be taken as evidence that the interests of other European producers are not threatened by the Italian tariff. It was clearly established in Case C-372/97 *Italy v Commission* that unilateral measures aimed at approximating conditions of competition in a Member State to those prevailing in other Member States do affect trade (and therefore cannot escape classification as aid). Moreover, some of the power supply agreements in place in other Member States may involve State aid, and the Commission has opened in-depth investigations into several measures of this kind⁽⁵⁴⁾. Even though this defence has not been put forward expressly by Italy or Alcoa, the Commission considers it useful to draw attention to the well-established principle that the existence of unlawful aid in some Member States cannot justify the adoption of similar measures by another Member State.

(144) In any event, the complaints received from the beneficiaries' competitors provide an indication that the disputed tariffs do raise competition problems and affect trade within the Union.

(145) Moreover, Italy did not notify the 2004 tariffs. According to settled case-law, where aid has not been notified, the Commission is not obliged to demonstrate the actual consequences of the measure on competition and trade between Member States: 'If the Commission were required in its decision to demonstrate the real effect of aid which had already been granted, that would immediately favour those Member States which grant aid in breach of the duty to notify laid down in Article 93(3) of the [EC] Treaty, to the detriment of those which do notify aid at the planning stage'⁽⁵⁵⁾.

(146) The conclusion must be drawn that the disputed preferential electricity tariffs are liable to improve their beneficiaries' competitive position vis-à-vis competing undertakings in the EU. It is settled case-law that in such circumstances it must be held that trade between Member States is affected and competition distorted⁽⁵⁶⁾.

⁽⁵⁴⁾ See, for example, the Commission decisions to open proceedings in respect of regulated electricity tariffs in France (Case C 17/07, Commission decision C/2007/2392 of 13 June 2007, OJ C 164, 18.7.2007, p. 9) and in Spain (Case C 3/07, Commission decision C/2007/123/3 of 24 January 2007, OJ C 43, 27.2.2007, p. 9).

⁽⁵⁵⁾ Judgment of the Court of Justice in Case C-301/87 *France v Commission* [1990] ECR I-307, paragraphs 32 and 33; judgments of the Court of First Instance in Case T-214/95 *Vlaams Gewest v Commission* [1998] ECR II-717, paragraph 67; and Joined Cases T-298/97, T-312/97, T-313/97, T-315/97, T-600/97 to 607/97, T-1/98, T-3/98 to T-6/98 and T-23/98 *Alzetta and Others v Commission* [2000] ECR II-2319, paragraph 79.

⁽⁵⁶⁾ See, for example, the judgments of the Court of Justice in Case 730/79 *Philip Morris v Commission* [1980] ECR 2671, paragraph 11, and in Joined Cases C-393/04 and C-41/05 *Air Liquide Industries v Ville de Seraing and Province de Liège* [2006] ECR I-5293.

5.1.5. Conclusions on the presence of aid

(147) The Commission concludes that the disputed 2004 and 2005 tariffs constitute State aid within the meaning of Article 87(1) TFEU and can be authorised only if they qualify for one of the exemptions provided for in the Treaty. This conclusion is consistent with that arrived at in the *Alcoa* case, which concerned virtually identical tariffs.

5.2. New aid or existing aid

(148) The situations in which a measure constitutes existing aid are exhaustively enumerated in Article 1 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty⁽⁵⁷⁾.

(149) It is undisputed that the measures at issue were not put into effect before Italy's accession to the Union (Article 1(b)(i) of the Regulation), are not deemed to have been authorised owing to the Commission's failure to take a decision within the prescribed procedural deadlines (Article 1(b)(iii)), and cannot be deemed to be existing aid owing to the expiry of the limitation period (Article 1(b)(iv)). They did not become aid as a result of the evolution of the common market and without having been altered by the Member State (first sentence of Article 1(b)(v)).

(150) In the light of the above, the Commission considers that the disputed tariffs constitute new aid.

5.3. Lawfulness of the aid

(151) Pursuant to Article 108(3) TFEU, Member States must notify any plans to grant or alter aid, and may not put the proposed measures into effect until the notification procedure has resulted in a final decision.

(152) Since Italy failed to notify Article 1 of the 2004 Decree, the 2004 tariffs constitute unlawful aid.

⁽⁵⁷⁾ OJ L 83, 27.3.1999, p. 1. The second sentence of Article 1(b)(v) of the Regulation reads: 'Where certain measures become aid following the liberalisation of an activity by Community law, such measures shall not be considered as existing aid after the date fixed for liberalisation'.

- (153) But Italy did notify Article 11(12) of Law No 80/2005, and refrained from implementing that measure. It has therefore complied with its obligations under Article 108(3) TFEU.

6. COMPATIBILITY OF THE AID

- (154) In derogation from the general prohibition on State aid laid down in Article 107(1) TFEU, aid may be declared compatible if it qualifies for one of the exceptions enumerated in the Treaty.
- (155) The 2004 and 2005 tariffs constitute operating aid. Italy's claim that the 2005 tariffs should not be considered operating aid because they are part of a regional support strategy and are conditional upon productive investment should be dismissed. Even though the memorandum of understanding provides that the beneficiaries must carry out certain investments, the aid component in the 2005 preferential tariffs is not a proportion of the eligible expenditure, and is not subject to a maximum aid intensity. There are no indications that the measure complies with the criteria for investment aid, or that the aid is proportional. Instead, the measure is clearly pegged to electricity consumption and aimed at mitigating electricity procurement costs, which are operating costs incurred by the companies concerned. Thus it cannot be construed as investment aid.
- (156) Operating aid is, in principle, incompatible with the internal market. In Case C-86/89 *Italy v Commission*, the Court of Justice found 'that the aid in question, which was granted without any specific conditions and solely according to the quantities used, should be regarded as an operating aid to the undertakings concerned and that, as such, it affected trading conditions to an extent contrary to the common interest' ⁽⁵⁸⁾.
- (157) In Case T-459/93 *Siemens v Commission* the Court of First Instance recalled the principle that 'operating aid, that is to say, aid intended to relieve an undertaking of the expenses which it would itself normally have had to bear in its day-to-day management or its usual activities, does not in principle fall within the scope of Article 92(3) aforesaid [now Article 107(3) TFEU] ... According to the relevant case-law, the effect of such aid is in principle to distort competition in the sectors in which it is granted, whilst nevertheless being incapable, by its very nature, of achieving any of the objectives of the aforesaid exceptions'.
- (158) Nevertheless, there are clearly defined situations in which operating aid may be granted. In particular, operating aid

may be granted for environmental purposes on the basis of the Community guidelines on State aid for environmental protection ⁽⁵⁹⁾. In assisted areas operating aid can also be authorised on an exceptional basis as regional aid. The Commission has assessed whether the disputed tariffs might fall into one of these categories.

- (159) The Commission observes that the tariffs do not pursue any environmental purpose, and consequently cannot be authorised as environmental aid.

6.1. Compatibility with the 1998 Regional Aid Guidelines

- (160) Exceptionally, operating aid may be granted in assisted areas eligible for aid under the exemption in Article 107(3)(a) TFEU. The Region of Sardinia was eligible for such aid until the end of 2006. The Commission has therefore examined whether, during that period, the 2004 and the 2005 tariffs could be authorised under the 1998 Regional Aid Guidelines.
- (161) According to point 4.15 of the Guidelines, operating aid can be granted exceptionally, provided that (i) it is justified in terms of its contribution to regional development and its nature and (ii) its level is proportional to the handicaps it seeks to alleviate. It is for the Member State to demonstrate the existence of any handicaps and gauge their importance. Under point 4.17 of the Guidelines, operating aid must be both limited in time and progressively reduced.
- (162) According to point 2 of the Guidelines, 'An individual *ad hoc* payment made to a single firm, or aid confined to one area of activity, may have a major impact on competition in the relevant market, and its effects on regional development are likely to be too limited ... Consequently, the derogations in question [from the general prohibition of aid] will normally be granted only for multisectoral aid schemes open, in a given region, to all firms in the sectors concerned'. An electricity tariff which is granted selectively to a few individual undertakings in certain sectors is clearly not in line with the spirit of regional aid, which expected to be multisectoral. However, since there is no absolute prohibition of *ad hoc* regional aid, the Commission has considered whether there are any exceptional circumstances that would warrant the granting of the tariff.
- (163) The Commission has considered, in particular, the deficiencies of the Sardinian electricity market, as documented by Italy and the beneficiaries, to assess whether they might constitute a regional handicap.

⁽⁵⁸⁾ [1990] ECR I-3891; see also Case C-301/87 *France v Commission* [1990] ECR I-307, paragraph 50.

⁽⁵⁹⁾ OJ C 37, 3.2.2001, p. 3 and OJ C 82, 1.4.2008, p. 1.

6.1.1. *The Sardinian electricity market in the Italian context*

(164) The Italian electricity market is generally highly concentrated, although less so in the north of the country. The dominant operator in all zones is the former monopolist ENEL, except in Sardinia, where it holds a duopoly with E.ON. ENEL has considerable market power and has been found by the Italian competition authority to have abused this power in several instances. Electricity prices in Italy are generally high, owing to a generation mix based largely on fossil fuels (essentially gas), the absence of nuclear capacity, and congestion on the interconnectors with the rest of Europe.

(165) In Sardinia, which accounts for 4,1 % of net installed power in Italy⁽⁶⁰⁾, electricity is produced mainly in thermoelectric power plants using fossil fuels (coal, fuel oil, and refinery tar). The island has no natural gas distribution infrastructure.

(166) Sardinia suffers from excess generation capacity, especially in the high-cost segment (oil-fired plants), owing to the Government's plans to concentrate Italy's heavy industry on the island, which have never come to fruition, and which led ENEL to overinvest in generation plants. Apart from being structurally more expensive, the plants are quickly becoming technically obsolete. During the period under consideration, the export of Sardinian electricity to the Italian mainland was limited by the modest capacity of the interconnector, which was prone to congestion⁽⁶¹⁾.

(167) Two power companies, ENEL and E.ON, together hold a 95 % market share of electricity supply in Sardinia (roughly 58 % E.ON and 42 % ENEL). According to the Energy Sector Inquiry⁽⁶²⁾, Sardinia can be classified in competition terms as a duopoly with collective dominance. Market concentration is high, though not the highest in Italy⁽⁶³⁾. Owing to their control of virtually all mid-merit to peak plants, E.ON and ENEL set the price at most times of the day. However, the situation in Sardinia appears less critical than in the south of Italy, where ENEL alone sets the price at all times of day⁽⁶⁴⁾.

⁽⁶⁰⁾ Source: *Indagine conoscitiva sullo stato della liberalizzazione dei settori dell'energia elettrica e del gas naturale*, May 2005.

⁽⁶¹⁾ Sardinia was connected to mainland Italy via an obsolete 270 MWh interconnector known as SACOI. In 2009 the first section of a new interconnection cable, SAPEI, became operational.

⁽⁶²⁾ Communication from the Commission — Inquiry pursuant to Article 17 of Regulation (EC) No 1/2003 into the European gas and electricity sectors (Final Report), SEC(2006) 1724, COM(2006) 851 final.

⁽⁶³⁾ The HHI index in Sardinia varies between 3 000 and 3 500. In the South zone, however, the HHI is higher.

⁽⁶⁴⁾ In Sardinia, E.ON can set the price for 67 % of the hours, and ENEL for 29 % of the hours. If adjacent zones are also considered, ENEL is price-setting in the macrozone Macrosud-Sardegna for 63 % of the hours. In the MacroSud region, ENEL is price-setting for 100 % of the hours.

(168) Wholesale electricity prices in Italy are among the highest in Europe⁽⁶⁵⁾, and prices in Sardinia are among the highest in Italy. In 2007, the national average price (PUN) was EUR 70,99 per MWh, whereas the average Sardinian zonal price was EUR 75,00 per MWh, down from EUR 80,00 per MWh in 2006⁽⁶⁶⁾. In 2008 and 2009, average regional prices in Sardinia continued on an upward trend. In the first half of 2009, prices in Sardinia remained constantly above the national average (with an average price of EUR 106,60 per MWh compared with a PUN of EUR 60,50 per MWh).

(169) Prices paid in Sardinia by the beneficiaries of the tariffs in 2004/2005, on the basis of bilateral contracts, ranged from EUR 60 to EUR 65 per MWh. It has not been possible to compare these prices to those recorded on the Italian mainland, as the Commission does not possess the relevant data (which Italy has claimed it is unable to provide — see recital 92 above). However, based on the above analysis of general price trends, which may be broadly representative of price trends in bilateral contracts, it seems possible to presume that, in the period under consideration, energy-intensive undertakings in Sardinia paid a higher price than on the Italian mainland.

(170) In conclusion, the electricity market in Sardinia exhibits a combination of problems, including high prices, a high degree of market concentration, dominant operators' market power, excess generation capacity in the high-cost segment, relative inefficiency of obsolete generating plants, lack of access to natural gas infrastructure, and insufficient interconnection. These problems are likely to translate into higher electricity prices for end-users, including the most energy-intensive ones.

6.1.2. *Existence of a regional handicap*

(171) The first issue to be addressed is whether such problems constitute a regional handicap, i.e. whether they have a severe impact on the economic development of Sardinia. In case C 34/02, the Commission did not accept that the lack of energy interconnection constituted a handicap⁽⁶⁷⁾. While it is true that SMEs suffer less from high electricity prices than do large, energy-intensive industries, nevertheless the welfare of an individual industry cannot be automatically equated to the welfare of a region. The Commission considers that Italy has not sufficiently substantiated the alleged regional handicap arising from the state of the Sardinian electricity market.

⁽⁶⁵⁾ For example, in 2007 the average wholesale price in Italy (for baseload power on the day-ahead market) on IPEX (Italy's electricity exchange) was EUR 70,99 per MWh, compared with EUR 37,97 on Germany's EEX exchange and EUR 40,78 on France's Powernext exchange.

⁽⁶⁶⁾ 2008 Report of the AEEG, based on data from the exchange manager, GME.

⁽⁶⁷⁾ Commission Decision C(2002) 3715 of 16 October 2002, *Region of Sardinia: measures to reduce the energy costs of small and medium-sized enterprises* (OJ C 132, 4.6.2002, p. 6).

- (172) But even if one were to suppose that there was indeed a regional handicap, the criteria laid down by the Regional Aid Guidelines would still have to be fulfilled. The Commission has accordingly assessed whether these tests are satisfied.

6.1.3. Contribution to regional development

- (173) Aid must sustainably contribute to regional development and be proportional to the handicaps it seeks to alleviate. Operating aid in an assisted region cannot be authorised by reason of difficulties experienced by one industry, but must be shown to make a lasting contribution to regional development. In the case at hand, this is unlikely. Even if one were to accept that the maintenance on the island of some industrial production facilities would contribute to employment and to the maintenance of a manufacturing base on the island, the effects would not be lasting. If high electricity prices are a structural problem in Sardinia, as Italy claims, the difficulties experienced by energy-intensive industries will resurface as soon as the tariffs are removed.

- (174) The Italian authorities present the tariffs as a temporary measure, designed to last only until the completion, in 2010, of the infrastructure projects currently under way in connection with energy generation and interconnection (the GALSI pipeline and the SAPEI marine cable)⁽⁶⁸⁾. Italy's argument is that better interconnection will bring the prices charged to these companies down. The Commission considers that, while the new infrastructure may reduce or level out price disparities between Sardinia and the mainland, it seems highly unlikely that such projects could halve electricity prices, so as to bring them to the levels allegedly required to make these industrial activities profitable in the long term.

- (175) The Commission also points out that the existence of a State subsidy aimed at reducing electricity costs for large users does not encourage electricity suppliers to bring prices down in order to avoid losing their largest customers, nor does it prevent a worsening of their cost structures. Instead, the subsidy tends to heighten the incentive for suppliers to exploit their market power. Therefore, even if were true, given the situation of overcapacity, that energy-intensive companies would normally be able to obtain a competitive price were it not for the market power of the electricity suppliers (who, according to Italy and the beneficiaries, have an interest in keeping prices high), the Commission considers that the preferential tariff is not the appropriate instrument to curtail such market power.

⁽⁶⁸⁾ At the time of writing (December 2010), the SAPEI cable is partly operational, whereas the GALSI pipeline is not expected to come on stream before 2014.

6.1.4. Proportionality

- (176) The subsidy granted to the beneficiaries of the tariffs is not calculated in such a way as to offset the regional disparity (i.e. the differential between electricity prices in mainland Italy and prices in Sardinia for the same category of customer), but rather aims to align Sardinian prices on those paid by the beneficiaries' competitors in the EU. The prices set for the Sardinian beneficiaries are particularly low, and certainly below prices on mainland Italy, which are among the highest in the EU. Therefore, the tariffs are not proportional to the regional handicap they allegedly seek to alleviate.
- (177) The very method chosen to calculate the amount of the subsidy suggests that the measure pursues an industrial policy objective rather than a regional objective. Indeed, the industrial policy dimension of the tariffs has been underlined repeatedly by Italy in its submissions.

6.1.5. Degressivity

- (178) Regional operating aid must be progressively reduced (point 4.17 of the Regional Aid Guidelines). Since the updating mechanisms for the 2004 and the 2005 tariffs are different, they have been assessed separately.
- (179) The 2004 tariffs are indexed on the basis of variations in fuel prices and can only increase or remain unchanged. According to Italy, this ensures that the aid is progressively reduced. The Commission considers that the requirement of degressivity can be considered fulfilled only if the compensatory payments — which are equal to the effective amount of the aid — are guaranteed to decrease over time. It is not sufficient that the tariff should increase over time, since a higher tariff may nevertheless represent a higher volume of aid if, in the meantime, the prices charged to end users in the market concerned have increased faster than the tariff. The Italian method does not provide any guarantee in this respect⁽⁶⁹⁾.
- (180) As regards the 2005 tariffs, The Commission has assessed the indexation mechanism introduced by Article 11(13) of Law No 80/2005, as interpreted by the AEEG in decision 217/05 (see recital 33). According to the implementing rules laid down by the AEEG, the tariff is to be increased yearly by a percentage reflecting trends in electricity prices in the EU, but the increase cannot exceed 4 %. According to Italy, this mechanism ensures progressive reduction.

⁽⁶⁹⁾ It should be noted that variations in market prices are not correlated only with variations in fuel prices. Other factors are liable to push up market prices: in the specific context of Sardinia, these may include the market power of incumbent operators, imbalances between supply and demand, or interconnection problems. The Italian method does not ensure that over time the actual amount of aid will decrease, or even remain stable.

(181) The Commission takes the view, however, that the fact that the nominal tariff is subject to a rather limited annual increase does not mean that the net amount of aid — as measured by the compensatory payments — will decrease over time.

(182) If it is accepted that price trends on power exchanges can be considered broadly representative of changes in bilateral contract prices, as Italy has suggested, the 2005 tariffs would be degressive only in the event of a drop in average EU prices (since the tariffs cannot decrease, but only increase). In all other cases the tariffs would confer a growing advantage⁽⁷⁰⁾. Since, from 2004 until at least 2007, EU average electricity prices were on a sharp upward trend (rising faster than 4 % a year) the element of aid contained in the 2005 tariffs would have increased over time.

(183) Italy further contends that, in reality, bilateral contracts are less prone to price increases than prices on power exchanges, and that therefore the 2005 tariffs are de facto degressive. The Commission points out that the indexation method submitted for assessment is based on variations in prices on power exchanges, and that Italy has not submitted data on the evolution of bilateral contract prices. Thus Italy's statement is not sufficiently substantiated.

(184) In fact, the limited information at the Commission's disposal suggests the opposite, i.e. that bilateral contract prices increased sharply in Sardinia (see, for example, Eurallumina's statement that in 2005/2006 it paid a price of EUR 80 per MWh on the free market, up from EUR 65 per MWh in 2004). In these circumstances, had the tariffs been implemented, the compensatory payments would have increased over time.

(185) Thus neither the 2004 tariffs nor the 2005 tariffs fulfil the degressivity requirement.

6.1.6. *Conclusions on the compatibility of the measure as regional aid*

(186) The Commission concludes that the tariffs at issue cannot be considered compatible as regional aid under

the 1998 Regional Aid Guidelines. Since Sardinia ceased to be assisted pursuant to Article 107(3)(a) after December 2006, it is not necessary to examine the compatibility of the aid in the light of the Regional Aid Guidelines for 2007–2013.

(187) The Commission took a similar negative position in 2005 in respect of a measure designed to reduce Eurallumina's energy costs in Sardinia. The Commission considered that the disputed measure, which took the form of an exemption from excise duties on heavy oils, could not be authorised on the basis of the Regional Aid Guidelines⁽⁷¹⁾.

6.2. **Other considerations relevant to compatibility**

(188) It has been submitted by Italy and the undertakings concerned that the schemes serve the purpose of remedying the shortcomings of the electricity markets, which have not yet delivered competitive prices. They argue that energy prices are threatening the competitiveness of energy-intensive industries. The aid has an incentive effect, they contend, since without it the companies would close down.

(189) The Commission does not consider it possible to accept that operating aid for a few industrial companies is an appropriate response to the lack of competition on the local electricity market, which affects all electricity users.

(190) It is also questionable whether the aid is an appropriate and proportional means of preventing relocation outside the EU. There is no precedent in the Commission's decisions or in the judgments of the Union's lawcourts for accepting this argument as a justification for the granting of State aid. Decisions to relocate production, in whole or in part, are part of a company's business strategy, and the Commission has never held that they constitute a market failure. In the *Terni*⁽⁷²⁾ and *Alcoa*⁽⁷³⁾ cases the Commission expressed doubts about similar arguments linking aid measures to the goal of preventing the relocation of industry outside the EU.

⁽⁷⁰⁾ In particular, even in the event of an increase in average EU prices smaller than 4 %, the tariff advantage would still increase in absolute terms. For example, if the preferential price was EUR 30 per MWh and the average electricity price in Europe was EUR 60 per MWh (compensatory payment: EUR 30), a 3 % increase in the average EU price (bringing it to EUR 61,8) would lead to an updated tariff of EUR 30,90. The new compensatory payment per MWh would be EUR 61,80 – EUR 30,90 = EUR 30,90, which is a higher amount of aid.

⁽⁷¹⁾ The *Alumina* case, Decision 2006/323/CE of 7 December 2005.

⁽⁷²⁾ Commission Decision of 20 November 2007 on the State aid C 36/A/06 implemented by Italy in favour of ThyssenKrupp, Cementir and Nuova Terni Industrie Chimiche, paragraphs 144 and 145. That decision was upheld by the General Court in Cases T-53/08, 62/08, 63/08 and 64/08; an appeal is pending.

⁽⁷³⁾ Decision referenced in footnote 3, at paragraph 244.

- (191) It should also be pointed out that the conclusions of specialised bodies such as the High Level Group on Competitiveness, Energy and the Environment ⁽⁷⁴⁾, which have been cited in the course of the proceedings, do not suggest that special State aid should be granted to address the competitiveness issues raised by high energy prices, but instead defend the need for full compliance with the applicable State aid rules ⁽⁷⁵⁾.
- (192) In the light of the above, the Commission considers that the disputed 2004 and 2005 tariffs do not qualify for any of the exemptions in Article 107 TFEU. The exemptions in Article 107(2) TFEU are not applicable, since the aid is not of a social character, is not designed to make good the damage caused by natural disasters or exceptional occurrences, and was not granted to compensate for the economic disadvantages caused by the division of Germany. The exemptions in Article 107(3)(b) and (d) TFEU are also inapplicable, since the measure is not aimed at promoting the execution of an important project of common European interest, or remedying a serious disturbance in the economy of a Member State, or promoting culture and heritage conservation. Turning to the exemption in Article 107(3)(a) TFEU, the analysis carried out above in recitals 160 to 187 demonstrates that the tariff cannot be approved as aid aimed at promoting the economic development of an area where the standard of living is abnormally low or where there is serious unemployment. With respect to Article 107(3)(c) TFEU, operating aid does not qualify for this exemption in principle, as indicated in recitals 155 to 158, and the Commission has not been able to identify any specific circumstances which might justify the granting of such aid in this case.
- (193) The Commission therefore considers that both the 2004 and the 2005 tariffs are incompatible with the internal market.
- (194) Having drawn this conclusion, the Commission does not need to examine the possible cumulative effect of the new aid and the old incompatible aid referred to in recital 31 in the light of the *Deggendorf* judgment.

⁽⁷⁴⁾ See footnote 31.

⁽⁷⁵⁾ For example, in its Third Report, in February 2007, the High Level Group states 'Against this background, the use of incentives, including general purpose subsidies and state aids can be justified as a policy instrument. They may promote responsible social and environmental behaviour, regional cohesion, sustainable development and cultural diversity. However, they should only be used where there is a clear market failure, where subsidies prove to be the appropriate instrument for meeting a well defined common interest objective, and when they do not distort competition or harm the environment ... Action is justified when such subsidies undermine other policy objectives such as fighting climate change, the Lisbon Strategy for Jobs and Growth, proper functioning of energy markets, or access to raw materials, without meeting their initial objective' (http://ec.europa.eu/enterprise/policies/sustainable-business/policy-integration/high-level-group/reference-material/index_en.htm).

7. RECOVERY

- (195) Article 14(1) of Regulation (EC) No 659/1999 states that in cases of unlawful aid which is not compatible with the internal market effective competition must be restored, unless recovery would be contrary to a general principle of Community law.
- (196) In the present case, only the 2004 tariffs (Case C 38/A/04) are subject to recovery, since the 2005 tariffs (Case C 13/06) have not been implemented.

7.1. Legitimate expectations and other general principles of Community law which might prevent recovery

- (197) According to settled case-law, when aid has been granted without prior notification under Article 108(3) TFEU the recipient of the aid cannot have a legitimate expectation that its grant is lawful ⁽⁷⁶⁾. A diligent undertaking should be able to establish whether the notification procedure has been followed and whether the aid is lawful.
- (198) However, a recipient of illegally granted aid is not precluded from relying on exceptional circumstances on the basis of which it had legitimately assumed the aid to be lawful, and thus declining to refund that aid ⁽⁷⁷⁾.
- (199) The beneficiaries of the 2004 tariffs have not made any submissions in this respect, nor has the Commission identified any exceptional circumstances which might have led the beneficiaries to entertain any legitimate expectation. In particular, no expectation that the tariffs would not constitute State aid could have arisen as a result of the 1996 *Alumix* decision. As indicated in the 2004 opening decision (see recital 37) the tariff that served as a blueprint for the disputed 2004 tariffs was not the original *Alumix* arrangement, which the Commission found did not constitute aid in 1996, but an entirely new measure, which had been substantially modified (in particular as regards its financing mechanism) ⁽⁷⁸⁾ and extended in time by the Italian authorities. In this situation, a prudent recipient should have verified that the new measure was lawful.

⁽⁷⁶⁾ Judgments of the Court of Justice in Case C-24/95 *Alcan Deutschland* [1997] ECR I-1591, paragraphs 25, 30 and 31, and in Joined Cases C-183/02 P and C-187/02 *Demesa and Territorio Histórico de Álava v Commission* [2004] ECR I-10609, paragraph 45.

⁽⁷⁷⁾ Judgment of the Court of Justice in Case C-5/89 *Germany v Commission* [1990] ECR I-3437, paragraph 16.

⁽⁷⁸⁾ Whereas the original *Alumix* tariff was granted directly by State-owned power supplier ENEL, which was held to be acting as a rational market operator in selling electricity at the *Alumix* price, the 2004 tariff was subsidised by the State from the proceeds of a parafiscal levy.

- (200) The Commission further considers that recovery would not breach any other general principle of Community law.

7.2. Quantification of the amounts to be recovered

- (201) All incompatible aid received by Portovesme, ILA and Eurallumina under Article 1 of the 2004 Decree must be recovered, with interest, in accordance with Chapter V of Commission Regulation (EC) No 794/2004 of 21 April 2004 implementing Council Regulation (EC) No 659/1999 laying down detailed rules for the application of Article 93 of the EC Treaty⁽⁷⁹⁾.
- (202) The purpose of recovery is to restore the recipients to the competitive position they occupied before the grant of the incompatible aid by eliminating the undue advantage conferred by it. In the case at hand, the advantage conferred is equal to the difference between the preferential tariff and the electricity price the beneficiaries would have paid on the market in the absence of the disputed tariffs.
- (203) All the companies concerned were purchasing electricity on the basis of bilateral contracts at the time the tariffs were introduced. The State intervened to subsidise the contractually agreed price by making compensatory payments. The amounts to be recovered are therefore equal to the compensatory payments received by the recipients over the period concerned (see recital 30).

8. CONCLUSION

The Commission finds that both the 2004 and the 2005 tariffs constitute operating aid which is not eligible for any exemption from the general prohibition of State aid under the EC Treaty, and is therefore incompatible with the internal market.

In the case of the 2004 tariffs, which were unlawfully implemented in breach of Article 108(3) TFEU, all payments of outstanding aid must be cancelled, while the aid already paid must be recovered. The amount to be recovered corresponds to the sum of all compensatory payments made by the Equalisation Fund to Portovesme, ILA and Eurallumina.

The 2005 tariffs, which were duly notified by Italy as required by Article 108(3) TFEU, must not be applied,

HAS ADOPTED THIS DECISION:

Article 1

1. The State aid which Italy plans to grant to Portovesme Srl, Eurallumina SpA, ILA SpA and Syndial SpA under

Article 11(12) of Decree-Law No 35 of 14 March 2005, converted into statute by Law No 80/2005 of 14 May 2005, is incompatible with the internal market.

2. The aid may accordingly not be granted.

Article 2

The State aid unlawfully granted by Italy in breach of Article 108(3) TFEU, on the basis of Article 1 of the Prime Ministerial Decree of 6 February 2004, amounting to EUR 12 845 892,82 for Portovesme Srl, EUR 5 208 152,05 for Eurallumina SpA, and EUR 291 120,27 for ILA SpA, is incompatible with the internal market.

Article 3

1. Italy shall recover the aid referred to in Article 2 from the beneficiaries.
2. The sums to be recovered shall bear interest from the date on which they were put at the disposal of the beneficiary until their actual recovery.
3. The interest shall be calculated on a compound basis in accordance with Chapter V of Regulation (EC) No 794/2004.
4. Italy shall cancel all future payments of the aid referred to in Article 2 with effect from the date of adoption of this Decision.

Article 4

1. Recovery of the aid referred to in Article 2 shall be immediate and effective.
2. Italy shall ensure that this Decision is implemented within 4 months following the date of notification of this Decision.

Article 5

1. Within two months following notification of this Decision, Italy shall submit the following information to the Commission:
 - (a) the total amount (principal and recovery interest) to be recovered from the beneficiary;
 - (b) a detailed description of the measures already taken and planned to comply with this Decision;
 - (c) documents demonstrating that the beneficiary has been ordered to repay the aid.

⁽⁷⁹⁾ OJ L 140, 30.4.2004, p. 1.

2. Italy shall keep the Commission informed of the progress of the national measures taken to implement this Decision until recovery of the aid referred to in Article 2 has been completed. At the Commission's request, it shall immediately submit information on the measures already taken and planned to comply with this Decision. It shall also provide detailed information concerning the amounts of aid and recovery interest already recovered from the beneficiary.

Article 6

This Decision is addressed to the Italian Republic.

Done at Brussels, 23 February 2011.

For the Commission
Joaquín ALMUNIA
Vice-President
