

COMMISSION DECISION (EU) 2015/507**of 16 September 2014****on the measure SA.23129 — (12/C) (ex 12/NN) (ex CP 141/2007) implemented by Germany***(notified under document C(2014) 6411)***(Only the German text is authentic)****(Text with EEA relevance)**

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

Whereas:

1. PROCEDURE

- (1) On 30 March 2007, Neubrandenburger Wohnungsgesellschaft mbH (hereinafter: 'NEUWOGES') lodged a complaint with the Commission, on the basis of Article 20(2) of Council Regulation (EC) No 659/1999 ⁽²⁾, alleging that illegal state aid had been granted to Bavaria Immobilien Trading GmbH & Co, Immobilien Leasing Objekt Neubrandenburg KG and Bavaria Immobilien Beteiligungsgesellschaft mbH & Co. Objekte Neubrandenburg KG (hereinafter: 'BAVARIA 1' and 'BAVARIA 2'; together: 'BAVARIA') by means of a land-lease and sale contract (*Erbbaurechtsvertrag*) and a general management contract (*Generalverwaltervertrag*). NEUWOGES requested the initiation of a formal investigation procedure pursuant to Article 108(2) TFEU.
- (2) On 6 August 2007, 14 May 2008, 6 April 2009 and 3 February 2012, the Commission called for further information from the German authorities. The German authorities responded on 4 September 2007, 12 October 2007, 17 October 2007, 11 July 2008, 14 July 2008, 12 December 2008, 30 June 2009 and 28 February 2012. NEUWOGES submitted comments on 30 May 2007, 5 November 2007, 26 February 2008, 15 July 2008, 30 September 2008, 18 December 2008, 6 March 2009, 4 June 2009, 15 July 2009, 26 August 2009, 22 September 2009 and 19 January 2012. BAVARIA commented on 13 May 2008.
- (3) On 28 November 2008, Rostock Regional Court (*Landgericht Rostock*) handed down its judgment with regard to the court proceedings between BAVARIA and NEUWOGES. BAVARIA had sued NEUWOGES for failure to comply with the contract concluded between the two parties, in response to which NEUWOGES had claimed that the contract involved unlawful and incompatible state aid and was therefore void. Rostock Regional Court concluded that no advantage was conferred on BAVARIA and there was therefore no state aid within the meaning of Article 107(1) TFEU. NEUWOGES appealed against the judgment, and the proceedings before Rostock Higher Regional Court (*Oberlandesgericht Rostock*) are pending. Additionally, BAVARIA initiated proceedings before Greifswald Administrative Court (*Verwaltungsgericht Greifswald*), seeking to obtain a ruling granting it access to all the files held by NEUWOGES or the City of Neubrandenburg in relation to the contracts in question. The case is still pending.
- (4) By letter of 4 June 2009, NEUWOGES asked the Commission, in accordance with Article 265(2) TFEU, to initiate the formal investigation procedure within two months.
- (5) By letter of 29 July 2009, the Commission communicated its preliminary assessment to NEUWOGES to the effect that neither the land-lease and sale contract nor the general management contract constituted state aid within the meaning of Article 107(1) TFEU.
- (6) By letter of 26 August 2009, NEUWOGES contested the Commission's assessment of the facts and called on the Commission to initiate the formal investigation procedure within two weeks.
- (7) The Commission informed NEUWOGES by letter of 15 September 2009 that it would send a further letter containing an assessment of NEUWOGES' latest comments. By letter of 22 September 2009, NEUWOGES informed the Commission that it did not agree with the Commission's proposal.

⁽¹⁾ OJ C 141, 17.5.2012, p. 28.

⁽²⁾ Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union (OJ L 83, 27.3.1999, p. 1).

- (8) On 9 October 2009, NEUWOGES brought an action before the General Court of the European Union and requested that it annul the decision allegedly contained in the Commission's letter of 29 July 2009 or, in the alternative, declare that the Commission had failed to act by refusing to initiate the formal investigation procedure under Article 108(2) TFEU. On 9 January 2012, the General Court dismissed the annulment action as inadmissible and the action for failure to act as unfounded ⁽³⁾.
- (9) By letter of 19 January 2012, NEUWOGES again called on the Commission to initiate the formal investigation procedure provided for in Article 108(2) TFEU.
- (10) By letter of 21 March 2012, the Commission informed the German authorities of its decision to open the formal investigation. The Commission's decision to initiate the procedure (hereinafter: the 'Opening Decision') was published in the *Official Journal of the European Union* ⁽⁴⁾. The Commission invited interested parties to submit their comments on the measure. On 22 March 2012, NEUWOGES brought an appeal against the General Court's decision of 9 January 2012. On 15 November 2012, the Court dismissed the appeal as being devoid of purpose ⁽⁵⁾.
- (11) The Commission received comments from NEUWOGES on 17 July 2012, 2 October 2012, 4 April 2013 and 15 April 2014, and from BAVARIA on 18 June 2012 and 22 April 2013. The submissions were forwarded to the German authorities on 7 August 2012 and 16 September 2013. On behalf of the German Government, the City of Neubrandenburg commented on 23 July 2012 and 28 September 2012, and Berlin *Land* on 16 May 2012, 28 September 2012 and 30 September 2013.

2. DESCRIPTION OF THE MEASURES

- (12) NEUWOGES is a limited liability company incorporated under German law. The City of Neubrandenburg holds 100 % of its shares. NEUWOGES pursues the objective of providing affordable housing to large parts of the population in Neubrandenburg and the surrounding areas. NEUWOGES today owns 33 % of all housing in the City of Neubrandenburg. BAVARIA 1 and BAVARIA 2 are property companies that were specifically founded for transactions with NEUWOGES and are majority-owned by closed real-estate funds. BAVARIA 1 is owned by BAVARIA Immobilien Beteiligungsgesellschaft mbH & Co. Erste Leasing Fonds KG (94 %) and BAVARIA Immobilien Management GmbH i.l (6 %), while BAVARIA 2 is wholly owned by Perseus Immobilien Verwaltungs GmbH & Co. KG — LBB Fonds Dreizehn. The shares of both BAVARIA Immobilien Beteiligungsgesellschaft mbH & Co. Erste Leasing Fonds KG and Perseus Immobilien Verwaltungs GmbH & Co. KG — LBB Fonds Dreizehn are held by private investors. Both funds were initiated and marketed by Berliner Immobilien Holding GmbH, which belonged to the Bankgesellschaft Berlin until 1 January 2006 and has since been owned directly and wholly by Berlin *Land*.
- (13) NEUWOGES is the owner of, *inter alia*, a number of plots of land in Neubrandenburg, on which twelve housing blocks with an aggregate total of 557 individual flats and some commercial units are situated. On 21 January 1998, NEUWOGES and BAVARIA concluded the land-lease and sale contract and the general management contract (hereinafter: 'contracts at issue' or, together, 'sale-and-lease-back transaction').

2.1. LAND-LEASE AND SALE CONTRACT

- (14) On 21 January 1998, NEUWOGES and BAVARIA concluded a land-lease and buildings sale contract for 12 buildings with a total of 557 individual flats. Under that contract, BAVARIA obtained a lease on the land for 75 years and bought the buildings.
- (15) The land-lease and sale contract is divided into two main components:
- (a) First, BAVARIA committed itself to paying a total of EUR [...] ^(*) ⁽⁶⁾ to NEUWOGES, of which EUR [...] constituted capitalised rent on the land for the period up to 31 December 2028 and EUR [...] constituted the purchase price for the buildings.
- (b) From 1 January 2029, BAVARIA will also have to pay an annual rent for the land of [...] % of the current land value, which has been calculated at EUR [...] per m² or EUR [...] per year, for a period of 10 years. For the subsequent remaining duration of the land-lease and sale contract, an adjustment of the rent in line with the development of the total cost-of-living index is foreseen, provided the latter fluctuates by more than [...] %.

⁽³⁾ Case T-407/09 *Neubrandenburger Wohnungsgesellschaft v Commission*, not yet reported.

⁽⁴⁾ See footnote 1.

⁽⁵⁾ Case C-145/12 P *Neubrandenburger Wohnungsgesellschaft v Commission* EU, not yet reported.

^(*) Parts of the text have been amended to ensure that confidential information is not published. These parts are hereinafter replaced by square brackets.

⁽⁶⁾ Throughout this Decision, the Commission has converted all original DM amounts into EUR amounts, using the official conversion rate of EUR 1 = DM 1,95583. Small rounding errors may have occurred. All digits after the decimal point have been omitted from this Decision.

- (16) In 1997, before concluding the land-lease and sale contract with BAVARIA, NEUWOGES had in-house experts value the property (buildings and land). According to this valuation, the value of the property was EUR [...]. In 2007, NEUWOGES additionally instructed an external expert to retrospectively calculate the 1997 market value of the property. The 2007 valuation estimated the property's 1997 value at EUR [...].

Inherited Debt Support Law (*Altschuldenhilfegesetz*)

- (17) The land-lease and sale contract was concluded in the context of the Inherited Debt Support Law⁽⁷⁾. After the reunification of Germany in 1990, the former 'people's housing companies' in East Germany were incorporated as legally separate communal housing companies. The old entities' assets and liabilities were transferred to these new companies, which were thus placed under a heavy burden. To enable the housing companies to be viable in the long term, the federal legislator passed the Inherited Debt Support Law, which entered into force on 27 June 1993.
- (18) Under the Inherited Debt Support Law, communal housing companies in East Germany could obtain debt relief upon application. Under Section 4(1)-(2) of the Law, the debt exceeding EUR 76,69 per m² could be written off up to a maximum of EUR 434,60 per m². In return, the housing company had to accept certain obligations, in particular to make all reasonable efforts to privatise 15 % of its apartments (Section 4(5)(1) in conjunction with Section 5), to have a business plan envisaging speedy privatisation, modernisation and renovation of its apartments (Section 4(5)(2)) and to report on its investment programme and the privatisation (Section 4(5)-(7)). In the version of the law that was in force at the relevant time (1997/98), the housing companies had until 31 December 2003 to fulfil their privatisation obligation. Where a housing company had failed to fulfil its privatisation obligation (i.e., by not making all reasonable efforts to do so), the debt relief already granted had to be repaid.
- (19) A certain percentage of the revenue exceeding EUR 76,69 per m² obtained by the housing company through privatisation had to be transferred to the 'inherited debt relief fund' (*Erblastentilgungsfonds*). At the relevant time (1997/98), Section 5(2) of the Inherited Debt Support Law provided that, for all privatisations up to 31 December 1998, 45 % of the qualifying revenue had to be transferred. For privatisations up to 31 December 2000 or 31 December 2003, the transfer quotas were set at 50 % and 55 % respectively. Where privatisation took the form of selling only the buildings and granting a lease for the land (rather than selling the buildings and land outright), the revenue on the basis of which the transfer obligations were calculated was the sale price of the buildings and the cash value of the agreed land rent (Section 5(2) of the Inherited Debt Support Law).
- (20) In the course of 1995, it emerged that the originally envisaged form of privatisation — i.e. sale to the tenants — was unlikely to lead to a privatisation quota of 15 %. Accordingly, the Bank for Reconstruction (*Kreditanstalt für Wiederaufbau*), charged with administering the debt relief programme, started accepting what was known as 'mediated privatisation'⁽⁸⁾. Under this model, which was supposed to be applied only where the 15 % quota could foreseeably not be reached via direct privatisation, a housing company could sell apartment buildings *en bloc* to a commercial buyer. In order for the sale to be counted towards the housing company's 15 % privatisation obligation, the commercial buyer had to accept an obligation both to modernise the buildings and to attempt to sell as many apartments as possible (and a minimum of one third of them) to the tenants⁽⁹⁾. Where, after firm offers of sale had been made, significantly less than one third of the tenants were interested in buying, the commercial buyer could exempt 60 % of the apartments from the privatisation obligation, thereby limiting its obligations to the privatisation of one third of the remaining 40 % of the apartments⁽¹⁰⁾.

NEUWOGES and the Inherited Debt Support Law

- (21) The land-lease and sale contract was eventually recognised by the Bank for Reconstruction as constituting a relevant 'mediated privatisation' under the Inherited Debt Support Law. Entering into the sale-and-lease-back

⁽⁷⁾ Inherited Debt Support Law (*Altschuldenhilfegesetz*) of 23 June 1993 (Federal Law Gazette I p. 944, 986), as last amended on 31 October 2006 (Federal Law Gazette I p. 2407).

⁽⁸⁾ See the Federal Ministry of Regional Planning's letter 'Anerkennung mieternaher Privatisierungsformen' dated 18 May 1995, and the Bank for Reconstruction's Merkblatt zu Mieterprivatisierung, mieternahen Privatisierungsformen und subsidiärem Drittverkauf dated 22 December 1995.

⁽⁹⁾ Letter from the Federal Ministry of Regional Planning, 'Anerkennung mieternaher Privatisierungsformen' dated 18 May 1995, p. 183.

⁽¹⁰⁾ The Bank for Reconstruction's 'Merkblatt zu Mieterprivatisierung, mieternahen Privatisierungsformen und subsidiärem Drittverkauf' dated 22 December 1995, pp. 5-6.

transaction therefore helped NEUWOGES fulfil its privatisation obligation under the Inherited Debt Support Law. However, it is unclear and a matter of dispute to what extent this law influenced the commercial considerations underlying NEUWOGES' decision to conclude the contracts, and whether the debt relief obtained by NEUWOGES pursuant to the law must be taken into account in analysing whether the sale-and-lease-back transaction constituted aid to BAVARIA.

- (22) By its own account, NEUWOGES received total debt relief of EUR [...] ⁽¹¹⁾. NEUWOGES submitted that it was difficult to apportion a part of the total debt relief it received to the sale-and-lease-back transaction, since the Inherited Debt Support Law granted debt relief only if the housing company had entirely fulfilled its privatisation obligation. However, if a portion of the total debt relief received were to be apportioned to an individual privatisation on the basis of the share of these privatisations in NEUWOGES' total privatisation obligation, then total gross debt relief of EUR [...] could be mathematically apportioned to the sale-and-lease-back transaction. Of the revenue generated by the BAVARIA sale, EUR [...] had to be transferred to the inherited debt relief fund, leaving NEUWOGES with mathematical net relief of EUR [...] ⁽¹²⁾.

2.2. GENERAL MANAGEMENT CONTRACT

- (23) On 21 January 1998, BAVARIA and NEUWOGES also signed the general management contract, which effectively leased the buildings back to NEUWOGES. Under this contract, NEUWOGES remains responsible for administering and commercially exploiting the buildings in question for 30 years. All the income from renting the buildings remains with NEUWOGES. In exchange for these rights of use, NEUWOGES committed itself to paying a fixed monthly leasing payment of EUR [...] (EUR [...] per year) until the modernisation was complete, and EUR [...] (EUR [...] per year) thereafter. From 1 January 2000, this leasing payment increased by [...] % annually.

2.3. GLOBAL LUMP-SUM CONTRACT

- (24) BAVARIA committed itself to modernising the buildings in question, for which purpose it concluded a global lump-sum contract with BRG Bau-Regie GmbH (hereinafter: 'BRG'), a 100 % subsidiary of NEUWOGES. Under this contract, BAVARIA paid BRG a lump sum of EUR [...] for the agreed modernisation works.

3. OBSERVATIONS BY GERMANY

- (25) In replying to the Opening Decision, Germany confines itself to explaining that it is not making any submissions in response to the Opening Decision in this case. Instead, it is leaving it to the territorial units concerned — the city of Neubrandenburg and Berlin *Land* — to do so.

4. COMMENTS BY INTERESTED PARTIES

4.1. NEUWOGES

- (26) NEUWOGES submits that, in concluding the contracts at issue, it did not behave like a market economy operator (hereinafter: 'MEO') and thus granted BAVARIA an economic advantage that constitutes state aid within the meaning of Article 107(1) TFEU. NEUWOGES estimates that the contracts at issue resulted in losses amounting to EUR [...] in nominal terms and EUR [...] after discounting. These losses are viewed by NEUWOGES as constituting incompatible state aid to BAVARIA.
- (27) For the purpose of assessing the market conformity of the contracts at issue, NEUWOGES argues that the land-lease and sale contract and the general management contract must be examined separately from each other (section 4.1.1). With respect to the individual contracts, NEUWOGES asserts that neither the land-lease and sale contract (section 4.1.2) nor the general management contract (section 4.1.3) would have been concluded by a MEO. NEUWOGES submits further that a MEO would have chosen an alternative approach (section 4.1.4). Finally, NEUWOGES asserts that the advantage conferred on BAVARIA constitutes a transfer of state resources that was imputable to the city of Neubrandenburg (section 4.1.5).

⁽¹¹⁾ NEUWOGES first submitted that the total debt relief amounted to EUR [...] and the attributable share to EUR [...]. However, it later corrected the attributable share to EUR [...]. Assuming that this correction stemmed from a correction of the total debt relief, the latter amount was corrected accordingly.

⁽¹²⁾ See Rostock Regional Court, judgment of 28 November 2008 (hereinafter: 'Rostock Regional Court judgment', p. 24).

4.1.1. Joint versus separate assessment of the contracts at issue

- (28) NEUWOGES submits that, with respect to whether or not the contracts at issue were concluded under market conditions, the land-lease and sale contract and the general management contract must be assessed strictly independently of one another. According to NEUWOGES, the two contracts are each legally independent and were each intended to exist separately. NEUWOGES maintains that if the two contracts had in actual fact been intended to form a single unit, they would have both had to be notarised; however, only the land-lease and sale contract was notarised.
- (29) On the basis of these arguments, NEUWOGES proceeds to assess the market conformity of each contract separately.

4.1.2. Land-lease and sale contract

- (30) NEUWOGES is of the opinion that, in the light of the 1997 and 2007 valuations of the property (buildings and land) in question, no MEO would have concluded the land-lease and sale contract with BAVARIA at the agreed price. Neither the payment of rent for the land, nor the debt write-off pursuant to the Inherited Debt Support Law and resulting from the land-lease and sale contract, nor the obligation to modernise, nor the limited bidding process could cause this conclusion to be changed in any respect.

4.1.2.1. Purchase price

- (31) NEUWOGES points out that BAVARIA paid a cash amount of EUR [...] for the buildings plus EUR [...] as capitalised rent for the land. It further recalls that the two valuations, carried out in 1997 and 2007, estimated the value of the property as a whole (value of land and buildings combined) at EUR [...] and EUR [...] respectively. Finally, NEUWOGES recalls that each valuation estimated not only the total value of the property, but also the separate values of the land (1997 valuation: EUR [...]; 2007 valuation: EUR [...]) and of the buildings (1997 valuation: EUR [...]; 2007 valuation: EUR [...]).
- (32) Asserting that the 1997 valuation represents a realistic estimate of the property's value at the relevant time (1997/98), NEUWOGES argues that only the price actually paid by BAVARIA for the buildings (rather than the price for the buildings plus the capitalised land rent) should be taken into account for comparison purposes. Accordingly, NEUWOGES asserts that it received EUR [...] less than the market price at the relevant time (1997/98). It further argues that, even if, for the sake of argument, the debt write-off pursuant to the Inherited Debt-Support Law is added to the sales price, the price paid by BAVARIA would still remain 16 % lower than even the lower 2007 valuation. According to NEUWOGES, the price paid by BAVARIA was far below the market price, so that no MEO would have agreed to sell at this price.
- (33) In this context, NEUWOGES points out that, according to the 'Commission Communication on state aid elements in sales of land and buildings by public authorities' ⁽¹³⁾, a sale price that is up to 5 % lower than that calculated in an independent valuation can, under certain circumstances, be accepted as the market price. NEUWOGES argues that, *a contrario*, a price that, viewed in even the most positive light, is at least 16 % lower than the lowest valuation cannot be accepted as the market price.

4.1.2.2. Capitalised rent for the land

- (34) NEUWOGES submits that, for the purpose of comparing the price paid by BAVARIA with the prices calculated in the two valuations of 1997 and 2007 (which estimated the value of full ownership of the buildings and land), the capitalised rent for the first 30 years should not be taken into account. As this rent is paid for the right to use the land for 75 years, rather than for the ownership of the land, it cannot be relied on for the purpose of comparing the price paid for the buildings by BAVARIA and one or other of those estimated in the two valuations.

4.1.2.3. Debt write-off pursuant to the Inherited Debt Support Law

- (35) NEUWOGES argues further that, for the purpose of comparing the price paid by BAVARIA with the prices determined in the two valuations, the debt write-off, pursuant to the Inherited Debt Support Law, that resulted from the contracts at issue — amounting to EUR [...] — cannot be taken into consideration. The reasons are as follows:

— The debt write-off pursuant to the Inherited Debt Support Law is a benefit conferred on NEUWOGES by a third party (the Bank for Reconstruction), which has no connection with the buyer. There is no reason why a vendor should accept a price below the market price simply because the transaction will result in some additional benefits granted by a third party.

⁽¹³⁾ OJ C 209, 10.7.1997, p. 3.

- BAVARIA did not assume any responsibilities under the Inherited Debt Support Law that were previously incumbent on NEUWOGES and that would merit remuneration in the form of a lower sale price. While BAVARIA did formally assume the obligation to attempt to sell a number of apartments to the tenants, it charged NEUWOGES with actually carrying out the privatisation at NEUWOGES' own expense, and hence did not assume any real responsibility. Nor was BAVARIA at risk of being held liable if the privatisation efforts were to fail.
- Because the debt write-off was linked to NEUWOGES' fulfilling its obligation to privatise 15 % of its apartments and the BAVARIA deal satisfied only 20 % of the total privatisation obligation, a proportional allocation of the debt write-off facilitated by the deal is not realistically (as opposed to mathematically) possible. In other words: if NEUWOGES had not fulfilled its total privatisation obligation, it would not have received any benefit under the Inherited Debt Support Law from the BAVARIA deal.
- At most, the sale-and-lease-back transaction meant that NEUWOGES had to transfer only a comparatively low percentage (45 %, rather than 50 % or 55 %) of the revenue to the inherited debt relief fund, whereas not concluding the contract and searching for an alternative buyer would have involved the risk of having to divert a larger share of the sales revenue into the fund.
- In any event, NEUWOGES claims to have eventually fulfilled its privatisation obligation at a rate of 165 %, meaning that even without the BAVARIA deal the debt write-off would have been confirmed.

4.1.2.4. Modernisation

- (36) NEUWOGES further submits that it did not benefit from the modernisation carried out by BAVARIA, as BAVARIA was the owner of the buildings and thus the only beneficiary of the modernisation.

4.1.2.5. Bidding Process

- (37) NEUWOGES asserts that the limited bidding process carried out in 1997 cannot be invoked as an indication that the price paid by BAVARIA was in actual fact the market price. It submits that the bidding process was not open, transparent, unconditional and non-discriminatory, and is therefore insufficient for establishing the market value.

4.1.3. General Management Contract

- (38) NEUWOGES asserts that no MEO of similar size and in a similar situation would have concluded the general management contract, as it was clear from the outset that the contract would result in substantial losses. Specifically, NEUWOGES argues that losses were foreseeable from the start, as the calculations underlying the contract were based on assumptions about the future development of the rental market in Neubrandenburg that were clearly too optimistic. NEUWOGES also maintains that various allegedly similar contracts provided by BAVARIA for the purpose of comparison cannot prove the market conformity of the general management contract; NEUWOGES accepted this clearly disadvantageous contract only for political reasons, which are irrelevant in applying the MEO test.

4.1.3.1. The General Management Contract in the light of market expectations

- (39) NEUWOGES submits that the central provisions of the General Management Contract — a fixed monthly leasing payment that is increased annually by [...], a non-indexed cost deduction of initially approximately [...], and a duration of 30 years — do not correspond to conditions that a MEO would have agreed to. More specifically, NEUWOGES asserts that:
- the low calculated risk of loss of rent of only [...] of the net rent income imposes on NEUWOGES the financial risk of not being able to achieve an occupancy rate of at least [...];
 - the indexation of the fixed leasing payment by [...] per year means that NEUWOGES bears the financial risk of not being able to impose annual rent increases corresponding to at least this rate;
 - since the costs are not independently indexed, NEUWOGES bears the financial risk of any increase in administration and maintenance costs, and only a rent increase of over [...] per year could conceivably offset an increase in costs;
 - these financial risks are significant in the light of the long, 30-year, duration.
- (40) NEUWOGES argues that it was clear from the outset that these risks would materialise, leading to heavy losses, and that accordingly no MEO would have concluded the contract. According to NEUWOGES, a MEO would conclude only a contract that was profitable or that at least did not result in losses. NEUWOGES asserts that the general management contract could have been expected to result in a profit only if it had been reasonable to

expect that the high occupancy rate, annual rent increases of [...] % and stable costs could actually be achieved. According to NEUWOGES it was, however, already clear when the contract was concluded that an average occupancy rate of [...] % would not be achievable, that a rent increase of at least [...] % per year would be impossible, and that the administration and maintenance costs would inevitably increase over the duration of the contract. To support these assertions, NEUWOGES points to both the projected population decline and the real-estate market in Neubrandenburg, maintaining that, in the light of these factors, the contract was bound to result in a loss. Since Neubrandenburg's population was in decline even before the contracts at issue were concluded, there was a significant oversupply of apartments from at least 1995 onwards, with the unattractive prefabricated apartment blocks, which are the subject of the contract, being most affected by vacancies and low rents.

- (41) NEUWOGES alleges that a MEO would have based its calculations on more pessimistic expectations, such as projected annual rent increases of between [...] % and [...] %, a risk of loss of rent of [...] % and an indexation of the costs of [...] %. NEUWOGES presents an *ex post* cash-flow analysis prepared in 2012 demonstrating that, on the basis of these assumptions, the cash flow that would have been expected to result from the general management contract was EUR [...] in nominal terms and EUR [...] after discounting⁽¹⁴⁾. It is NEUWOGES' submission that this amount constitutes the state aid received by BAVARIA. A number of variations of this cash-flow analysis are also provided, showing that, even if more optimistic assumptions had been justified (such as an average vacancy rate of [...] %, annual rent increases of [...] % and an increase in costs of [...] %), the overall predicted cash flow would also have been negative. The general management contract would have been expected to result in a profit only if allegedly quite unrealistic assumptions had been accepted ([...] % vacancy rate, [...] % annual rent increase and [...] % increase in costs).

4.1.3.2. Comparison contracts

- (42) NEUWOGES disputes that certain contracts from similar transactions (the [...] ⁽¹⁵⁾, [...] ⁽¹⁶⁾ and [...] ⁽¹⁷⁾ contracts) can prove the market conformity of the general management contract. Rejecting suggestions that these contracts are comparable, NEUWOGES argues that they differ from the general administration contract in the following material respects:
- Since no evidence was presented that the economic situation and outlook of these cities (in which the properties to which the comparison contracts relate are located) were sufficiently similar to those of Neubrandenburg, it cannot be assumed that the contracts as a whole are comparable.
 - The indexation of the leasing payment in the comparison contracts differs significantly from that in the general management contract (i.e. 1,0-1,5 %).
 - None of the individual comparison contracts is suitable for comparison because the circumstances are different in each case ([...]: less onerous maintenance obligations; [...]: commercial properties rather than apartments, which had a vacancy rate of 0 % at the conclusion of the contract; [...]: the properties were located in a growth region).
- (43) Rather than proving the market-conformity of the general management contract, NEUWOGES submits that the comparison contracts demonstrate precisely its non-conformity, since they include less onerous provisions despite relating to property with a better economic outlook.

4.1.3.3. Political motivation

- (44) NEUWOGES submits that the general management contract, despite clearly being economically disadvantageous, was concluded for political reasons. After pointing out that the reasons for which a public authority grants state aid are not relevant to the legal assessment, NEUWOGES argues that the political motivation proves precisely that economic considerations were not the deciding factor. More specifically, NEUWOGES asserts that the general management contract was concluded for the following reasons:
- There was intense political pressure to promote both the modernisation and privatisation of apartments owned by local housing companies in the former East Germany.
 - By modernising and privatising apartments, the city of Neubrandenburg hoped to counteract the ongoing decrease in population numbers.

⁽¹⁴⁾ NEUWOGES based its calculations on a discount rate of 5 %.

⁽¹⁵⁾ General management contract with [...] dated 19 December 1997.

⁽¹⁶⁾ General management and rent guarantee contract with [...] dated 13 August 1998.

⁽¹⁷⁾ General management and rent guarantee contract with [...] property development company, dated 1 December 1999.

— Concluding the general management contract, in combination with the global lump-sum contract, maintained a high level of investment in Neubrandenburg, a fall in which would have had significant consequences for the local unemployment rate.

4.1.4. *Alternatives*

- (45) NEUWOGES finally submits that a MEO would have preferred alternatives to the contracts at issue.
- (46) First, NEUWOGES submits that an outright sale would have been preferable, since it would have generated a profit, whereas the general management contract could from the start have been expected to result in losses. It claims that the property (buildings and land) could have been sold at or above the price determined in the valuations. It is further claimed that even if a buyer had simply bought the land and demolished the buildings, such a sale would have been more profitable. This assessment would remain the same even if the debt write-off pursuant to the Inherited Debt Support Law were taken into account, since NEUWOGES could have attempted to fulfil its obligations by privatising other buildings and, even without the debt-write off, a sale would have been more profitable than the sale-and-lease-back transaction. NEUWOGES claims that the reasons for not choosing any of these alternatives are to be found in NEUWOGES' political commitments.
- (47) Second, NEUWOGES further argues that a MEO would also have preferred financing a more limited modernisation itself, continuing to rent without any modernisation, or demolishing the buildings. Again, the reasons for not choosing these alternatives lie in NEUWOGES' political commitments.
- (48) Finally, NEUWOGES maintains that, if a decision to modernise had been taken, it would have been more profitable for NEUWOGES to finance these works by other means. For instance, a loan could have been taken up for which a guarantee from the City of Neubrandenburg could have been secured, rendering the loan conditions more favourable than those of the BAVARIA deal.

4.1.5. *State resources and imputability*

- (49) NEUWOGES is of the opinion that the alleged advantage was granted through state resources and is imputable to the State.
- (50) First, NEUWOGES submits that the City of Neubrandenburg, which was its sole shareholder and dominated its supervisory board, had a dominating influence on NEUWOGES. Based on this control, the losses allegedly resulting from the sale-and-lease-back transaction constitute foregone state resources.
- (51) Second, NEUWOGES argues that, in this case, virtually all the indicators of imputability are present. It points out that the City of Neubrandenburg has far-reaching control over NEUWOGES, that serving the city's interests is of the utmost importance for NEUWOGES, that the transaction in question was concluded for political reasons, and that the evidence indicates that the City of Neubrandenburg had the final say on the sale-and-lease-back transaction.

4.2. BAVARIA

- (52) BAVARIA rejects NEUWOGES' submissions, arguing instead that the contracts at issue were normal market transactions not conferring an advantage and accordingly not constituting state aid. BAVARIA first asserts that the contracts at issue have to be seen as an economic unit (section 4.2.1); second, that the contracts as a whole were not such that no MEO would have agreed to them (section 4.2.2); third, BAVARIA asserts that the alternatives put forward by NEUWOGES would not have been more advantageous to NEUWOGES (section 4.2.3); finally, BAVARIA submits that no imputable transfer of state resources was involved (section 4.2.4).

4.2.1. *Joint versus separate assessment of the contracts at issue*

- (53) BAVARIA argues that the contracts at issue have to be seen as a unit and cannot be assessed in isolation from each other. The sale and subsequent lease-back of the buildings constitute two interdependent parts of one transaction. BAVARIA stresses that the transaction was advertised as a package and perceived as such by NEUWOGES, as evidenced by the internal minutes documenting its decision-making process.
- (54) In consequence — according to BAVARIA — the MEO test has to be applied to the transaction as a whole, not to each individual contract.

4.2.2. *The transaction did not confer an advantage upon NEUWOGES*

- (55) According to BAVARIA, the possible existence of an advantage is already excluded by the fact that NEUWOGES undertook a bidding process (albeit a limited one) in order to survey the market. It is asserted that there is no reason to doubt that NEUWOGES chose the economically most advantageous offer available.

- (56) BAVARIA considers that, in order to determine whether, regardless of the bidding process, a MEO would have engaged in the transaction, the particular situation of NEUWOGES has to be taken into account. This included the need to take up capital as well as to modernise the apartments in order to privatise them (while maintaining moderate rents) and obtain the debt write-off pursuant to the Inherited Debt Support Law. In the light of these factors, BAVARIA asserts that a MEO finding itself in the same circumstance would also have engaged in the transaction.
- (57) Regarding the provisions in the general management contract and the risks associated with a worse-than-expected development of the real-estate market in Neubrandenburg (such as a higher-than-expected vacancy rate, etc.), BAVARIA argues that the risk of not being able to achieve the desired rent and occupancy rate was not imposed on NEUWOGES, but rather remained with NEUWOGES. If NEUWOGES had not undertaken the transaction with BAVARIA, it would also have had to bear the consequences of a worse-than-expected development of the market.
- (58) With respect to the individual provisions of the general management contract, BAVARIA submits that the average rent per m² underlying the calculation of the leasing payment was actually slightly lower than what could have been expected in the light of the relevant rent table for Neubrandenburg. BAVARIA further stresses that the same rent table assumed increasing rents for the period after 1 January 2000, with the result that expecting a rent increase of [...] % per year was not unrealistic.
- (59) Moving on to the land-lease and sale contract, BAVARIA stresses that no direct comparison can be made with the 1997 and 2007 valuations, since these valuations concerned an outright sale, whereas the land-lease and sale contract, while constituting a sale of the buildings, involved only the creation of a ground lease on the land. As the ownership of the land remained with NEUWOGES, the value of the land as stated in the valuations could not be considered. BAVARIA further maintains that, in any event, the valuations have no continuing significance since they determined only the theoretical value of the property, not the actual market value.
- (60) BAVARIA further submits that the debt write-off obtained through the transaction has to be considered. It submits that securing this write-off pursuant to the Inherited Debt Support Law was one of NEUWOGES' goals in entering into the transaction at issue.
- (61) BAVARIA also submits that, apart from the precise conditions of the land-lease and sale contract and the general management contract, the advantages obtained by NEUWOGES through the global lump-sum contract must be considered. BAVARIA maintains that NEUWOGES insisted on charging its subsidiary BRG with the modernisation of the properties, bearing in mind that NEUWOGES would receive all profits made by BRG (but was also liable to cover any losses). In this light, the profits generated from the contract with BRG, EUR [...], have to be considered a relevant benefit for NEUWOGES.
- (62) As regards the overall logic of the sale-and-lease-back model, BAVARIA submits, finally, that it is only natural that NEUWOGES has to repay BAVARIA's initial investment plus interest. Indeed, BAVARIA refers to the minutes of NEUWOGES' internal decision-making process to show that the latter was perfectly aware that the purpose of the leasing payment was to pay back BAVARIA's initial investment.

4.2.3. Alternatives

- (63) With respect to the alternatives that NEUWOGES puts forward and believes would have been economically more advantageous, BAVARIA submits that these alternatives were either not actually available or not more advantageous. First, with respect to the alleged option of selling directly to the tenants, BAVARIA argues that it is very unlikely that NEUWOGES would have succeeded in selling unmodernised flats, but that it was at the same time lacking the funds to finance the necessary modernisation. Second, as regards financing the modernisation with a loan, BAVARIA claims that NEUWOGES would have had all the same risks and costs it had under the BAVARIA deal. Additionally, selling modernised apartments, either directly to the tenants or to a commercial buyer, would not have been attractive, since NEUWOGES would have had to pass on a significant percentage of the higher price to the inherited debt relief fund.

4.2.4. State resources and imputability

- (64) BAVARIA finally submits that the transaction does not involve state resources and is not imputable to the State. In particular, it argues that NEUWOGES is a normal company governed by private law that does not receive any state funds, directly or indirectly. The general control exercised by the supervisory board, which is dominated by representatives of the City of Neubrandenburg, is insufficient to impute the transaction to the State. NEUWOGES' argument, according to which the City of Neubrandenburg urged NEUWOGES to conclude this transaction for political reasons, is not plausible.

4.3. CITY OF NEUBRANDENBURG

- (65) The City of Neubrandenburg, the owner of NEUWOGES, submits that the contracts at issue involve state aid. While the city endorses the arguments put forward by NEUWOGES, it presents its own reasoning with regard to a number of points.

4.3.1. *Advantage*

- (66) First, Neubrandenburg maintains that the land-lease and sale contract and the general management contract must be assessed separately, since the contracting parties carefully kept them apart, both in a legal and an economic sense. Second, Neubrandenburg refers to NEUWOGES' arguments regarding the forecast decrease in its population which, it maintains, a MEO would have taken into account. Neubrandenburg also stresses that high vacancy rates would have been clearly foreseeable by a MEO. Third, Neubrandenburg asserts that the modernisation commissioned by BAVARIA was of such a basic nature that it did not justify the expectation of high occupancy rates and large rent increases.
- (67) Moreover, Neubrandenburg rebuts the additional arguments put forward by BAVARIA. Most relevantly, it argues that the bidding process cannot be taken as an indicator that BAVARIA's offer was the best available on the market. In any event, it submits that a MEO would not have accepted BAVARIA's offer even if it had indeed been the best offer available on the market. As regards alleged alternatives, Neubrandenburg essentially seizes on the arguments put forward by NEUWOGES. With regard to the valuations and BAVARIA's argument that the estimated prices could not have been achieved, Neubrandenburg asserts that, since it is no longer possible to ascertain what price NEUWOGES could actually have obtained on the market in 1998, the valuation has to be used as an indication of the market price at the relevant time.

4.3.2. *State resources and imputability*

- (68) The City of Neubrandenburg argues that the transaction is imputable to it, since it exercised a sufficient degree of control over NEUWOGES in general and over the sale-and-lease-back transaction in particular.
- (69) As its sole shareholder, the City of Neubrandenburg claims to have had full control over NEUWOGES. In particular, NEUWOGES' management was duty-bound to follow the City's directives. Furthermore, eight of the ten members of NEUWOGES' supervisory board are representatives of the City, giving the latter another mechanism through which it can exert its control. In fact, the City of Neubrandenburg was under a legal duty under regional law to ensure that it could exercise appropriate influence over NEUWOGES.
- (70) As regards the transaction in question, the City of Neubrandenburg claims that not only did it have the ability to exert control, but that it actually did so in this transaction. Neubrandenburg is of the view that, inter alia, the minutes of the supervisory board demonstrate the close involvement of city representatives, and that a decision of that board was necessary before the transaction could be concluded. With regard to the terms of the transaction, Neubrandenburg submits that the City demanded that local political interests had to be satisfied.
- (71) In conclusion, the City of Neubrandenburg submits that the City's control over the sale-and-lease-back transaction, and its responsibility for this, is borne out by the facts, so that the transaction must be imputed to it.

4.4. BERLIN LAND

- (72) Berlin Land, which is closely connected to BAVARIA⁽¹⁸⁾, submits that the contracts at issue do not contain any state aid component as no advantage was conferred upon BAVARIA.

4.4.1. *Advantage*

- (73) Berlin first argues that the contracts at issue have to be viewed as one transaction, as they formed mutually complementary parts of a sale-and-lease-back transaction. Berlin asserts that they were also treated as such by NEUWOGES itself.
- (74) Regarding the MEO test, Berlin submits that, considering NEUWOGES' economic position at the relevant time (1997/98) and the type of transaction it sought (privatisation in compliance with the conditions under the Inherited Debt Support Law in order to secure the debt write-off, modernisation and continued administration of the apartments, and the maintenance of moderate rents), BAVARIA offered a balanced solution.

⁽¹⁸⁾ See recital 12.

- (75) More particularly with regard to the land-lease and sale contract, Berlin first argues that the bidding process undertaken by NEUWOGES demonstrates that NEUWOGES considered BAVARIA's offer to be the best financing offer available on the market at the relevant time (1997/98). Second, it submits that the debt write-off pursuant to the Inherited Debt Support Law must be considered, since compliance with the privatisation obligation under that law was a central motivation of NEUWOGES. Third, Berlin underlines that it was in NEUWOGES' economic interest to sell at a relatively low price (by selling unmodernised buildings with the obligation to modernise, rather than undertake the modernisation itself and then sell), since a lower price meant that less money had to be passed on to the inherited debt relief fund.
- (76) With respect to the general management contract, Berlin first argues that the comparison contracts demonstrate that neither the duration nor the indexation of the leasing payment by [...] % per year were uncommon. Second, the indexation is justified in the light of the average inflation rate at the relevant time (1997/98). Third, the rent per m² was within the applicable rent table rates for Neubrandenburg.

4.4.2. State resources and imputability

- (77) Like BAVARIA, Berlin *Land* argues that the City of Neubrandenburg did not fund NEUWOGES. Rather, it argues, only revenue generated from its own activities was available to NEUWOGES, over which the local authorities had no direct control.
- (78) As regards imputability, Berlin asserts that it is not plausible to maintain that the City of Neubrandenburg decided to grant aid to a real-estate fund from Berlin, to the detriment of its own local housing company. Further, it alleges that there are no sufficient indications that the City of Neubrandenburg intended the conclusion of the contracts to be imputed to it.

5. REASONS FOR INITIATING THE FORMAL INVESTIGATION PROCEDURE

- (79) In its decision opening the formal investigation procedure, the Commission took a preliminary position on a range of issues and called on interested parties to submit information with respect to three issues in particular.
- (80) First, the Commission provisionally accepted that the land-lease and sale contract and the general management contract have to be assessed as a unit, not in isolation from each other, as both were integral parts of a real estate sale-and-lease-back transaction⁽¹⁹⁾. It concluded that the assessment of a potential economic advantage was therefore based on an analysis of the returns that NEUWOGES could have expected in 1998 from the joint conclusion of the land-lease and sale contract and the general management contract⁽²⁰⁾.
- (81) As regards the land-lease and sale contract in particular, the Commission expressed two doubts:
- First, clarification was required as to whether the debt write-off pursuant to the Inherited Debt Support Law could be taken into account in the assessment⁽²¹⁾.
 - Second, the Commission sought further information on the differences between the 1997 and 2007 valuations, asserting that without further clarification it was impossible to determine which, if any, represented the actual market value of the property in 1997/98⁽²²⁾.
- (82) With respect to the general management contract, the Commission reasoned first that the comparison contracts indicated that the conditions agreed between NEUWOGES and BAVARIA were not unusual on the market at the relevant time (1997/98)⁽²³⁾. The Commission asserted, second, that the — albeit limited — bidding process carried out by NEUWOGES demonstrates that NEUWOGES had the ability to inform itself in the market and take an economically rational decision⁽²⁴⁾. Third, the Commission referred to the fact that the contractually agreed rent level for 2008 actually corresponded to the average rent in the relevant neighbourhood in 2008 or was only slightly below this⁽²⁵⁾.
- (83) Despite the fact that all these factors pointed towards the conclusion that the general management contract did conform to normal market conditions, the Commission solicited further information about the actual expectations of participants in the real estate market in 1998 in order to analyse the respective arguments in more depth⁽²⁶⁾.

⁽¹⁹⁾ Opening Decision, recital 46.

⁽²⁰⁾ Opening Decision, recital 47.

⁽²¹⁾ Opening Decision, recital 55.

⁽²²⁾ Opening Decision, recital 56.

⁽²³⁾ Opening Decision, recital 60 et seq.

⁽²⁴⁾ Opening Decision, recital 62.

⁽²⁵⁾ Opening Decision, recital 64.

⁽²⁶⁾ Opening Decision, recital 66.

- (84) The Commission finally examined the cash-flow analysis submitted by NEUWOGES, ultimately coming to the conclusion that, due to methodological deficiencies, the analysis could not prove an economic advantage in favour of BAVARIA ⁽²⁷⁾.
- (85) In conclusion, the Commission decided that, on the basis of the submitted information, it could not prove that BAVARIA had been granted an economic advantage ⁽²⁸⁾. However, it indicated its intention to analyse the participants' arguments in more depth and called upon all interested parties to provide additional useful information ⁽²⁹⁾.

6. NATIONAL COURT PROCEEDINGS

- (86) On 28 November 2008, Rostock Regional Court issued its judgment in first-instance proceedings between BAVARIA and NEUWOGES. BAVARIA had initiated the proceedings as, from October 2006 onwards, NEUWOGES had refused to pay the monthly leasing payment agreed in the general management contract, arguing that the contract was void because it contained illegal state aid.
- (87) In its judgment, Rostock Regional Court reasoned that the land-lease and sale contract and the general management contract had to be viewed as a unit and not in isolation, as they both formed part of one and the same sale-and-lease-back transaction ⁽³⁰⁾.
- (88) With respect to the land-lease and sale contract, Rostock Regional Court first calculated the annual rent for the land over the first 30 years of the contract, arriving at a figure of [...] % per year. The court expressed the view that this did not constitute inappropriately low remuneration since NEUWOGES received the ground rent for the first 30 years upfront and could invest it, which would not have been the case if the rent had been paid on a yearly basis ⁽³¹⁾.
- (89) Rostock Regional Court further affirmed that the debt write-off obtained by NEUWOGES under the sale-and-lease-back transaction had to be taken fully into account, as the transaction created the conditions allowing for the debt write-off to be secured ⁽³²⁾. When the debt write-off is added to the purchase price for the buildings, the resulting figure is only 16 % lower than that determined for the buildings in the 2007 valuation and is thus not disproportionate to the buildings' value ⁽³³⁾. The court finally reasoned that NEUWOGES had an interest in a low purchase price, as a lower purchase price reduced BAVARIA's overall investment volume and the corresponding leasing payment ⁽³⁴⁾. Additionally, it held that a lower purchase price was also beneficial since NEUWOGES' payment obligations towards the inherited debt relief fund depended on the price obtained in the sale ⁽³⁵⁾.
- (90) As regards the general management contract in particular, Rostock Regional Court began by expressing the view that a duration of 30 years was not uncommon in real-estate leasing transactions ⁽³⁶⁾. Second, it considered that the contractually agreed leasing payment of initially EUR [...] per m² was not disproportionate to the average rents for comparable buildings at the relevant time (1997/98) ⁽³⁷⁾. Rostock Regional Court further considered that the yearly increase in the leasing payment by [...] % was justified, having regard to average inflation between 1970 and 1998 (i.e. 3,52 % per year) ⁽³⁸⁾. In addition, the court remarked that the actual development of rents in the relevant neighbourhoods over the first 10 years of the contract roughly corresponded to the contractually agreed increase. Third, the court maintained that the costs of administration and maintenance had been calculated according to the applicable legislation and did not indicate an advantage for BAVARIA ⁽³⁹⁾.
- (91) With respect to the risk of loss of rent of [...] %, Rostock Regional Court was of the opinion that, under any lease, the lessee has to bear the risk of whether the leased object can be used as intended ⁽⁴⁰⁾. The court supported this conclusion by arguing that no credit institution would accept responsibility for whether or not the property for which a loan was taken out could be used as intended.

⁽²⁷⁾ Opening Decision, recital 68.

⁽²⁸⁾ Opening Decision, recital 69.

⁽²⁹⁾ Opening Decision, recital 70.

⁽³⁰⁾ Rostock Regional Court, p. 18.

⁽³¹⁾ Rostock Regional Court, pp. 23-24.

⁽³²⁾ Rostock Regional Court, pp. 24-25.

⁽³³⁾ Rostock Regional Court, p. 26.

⁽³⁴⁾ Rostock Regional Court, p. 26.

⁽³⁵⁾ Rostock Regional Court, p. 26.

⁽³⁶⁾ Rostock Regional Court, p. 19.

⁽³⁷⁾ Rostock Regional Court, pp. 19-20.

⁽³⁸⁾ Rostock Regional Court, p. 20.

⁽³⁹⁾ Rostock Regional Court, pp. 20-21.

⁽⁴⁰⁾ Rostock Regional Court, p. 21.

- (92) Rostock Regional Court finally compared the average leasing rate resulting from the sale-and-lease-back transaction with the interest rates on traditional loans. Arguing that the average yearly leasing interest rate was at [...] % per year, Rostock Regional Court held that this could not be said to have been disproportionate to the likely development of interest rates for building loans, which could be as high as 10 % per year ⁽⁴¹⁾.
- (93) In conclusion, Rostock Regional Court found that BAVARIA had not been granted an advantage, as a MEO would also have concluded the contracts in question ⁽⁴²⁾.
- (94) NEUWOGES appealed against this judgment, and proceedings before the Rostock Higher Regional Court are pending.
- (95) Additionally, BAVARIA initiated proceedings before Greifswald Administrative Court, seeking to obtain a ruling granting it access to all files held by NEUWOGES or the City of Neubrandenburg in relation to the contracts in question. BAVARIA claimed to have previously attempted to obtain such access by means of a freedom of information application, which was, however, rejected by Neubrandenburg on the basis of the argument that BAVARIA already had access to all relevant documents in the context of the proceedings before the Rostock Regional Court and Higher Regional Court and the European Commission ⁽⁴³⁾. The case before the Greifswald Administrative Court is also still pending.

7. ASSESSMENT OF THE MEASURE

7.1. EXISTENCE OF AID UNDER ARTICLE 107(1) TFEU

- (96) Article 107(1) TFEU provides that 'aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market'. Accordingly, a measure constitutes state aid if the following four cumulative conditions are met:
- (a) The measure confers a selective economic advantage upon an undertaking.
- (b) The measure is imputable to the State and financed through state resources.
- (c) The measure distorts or threatens to distort competition.
- (d) The measure has the potential to affect trade between Member States.

7.1.1. *Selective advantage conferred upon an undertaking: general principles*

- (97) According to the settled case-law of the Court of Justice, the conditions that a measure must meet in order to be regarded as 'aid' within the meaning of Article 107 TFEU are not met if the recipient undertaking, in circumstances corresponding to normal market conditions, could have obtained the same advantage as that made available to it through state resources. In order to assess whether the same measure would have been adopted in normal market conditions by a MEO in a situation as close as possible to that of the State, only the benefits and obligations linked to the capacity of the State as shareholder — to the exclusion of those linked to its capacity as a public authority — are to be taken into account ⁽⁴⁴⁾.
- (98) The applicability of the MEO test ultimately depends on the Member State concerned having conferred, in its capacity as an economic operator and not in its capacity as public authority, an economic advantage on an undertaking. It follows that, if a Member State relies on that principle during the administrative procedure, it must, where there is doubt, establish unequivocally and on the basis of objective and verifiable evidence that it took the measure in its capacity as an economic operator. That evidence must show clearly that, before or at the same time as conferring the economic advantage, the Member State concerned took the decision to carry out a commercial operation in respect of the undertaking by means of the measure actually implemented. In that regard, it may be necessary to produce evidence showing that the decision was based on economic evaluations comparable to those that a rational private operator in a situation as close as possible to that of the Member State would have had carried out before making the investment, in order to determine the future profitability of that investment.
- (99) By contrast, for the purposes of showing that, before or at the same time as conferring the advantage, the Member State took that decision as a MEO, it is not enough to rely on economic evaluations made after the advantage was conferred, or on a retrospective finding that the investment made by the Member State concerned was actually profitable, or on subsequent justifications of the course of action actually chosen ⁽⁴⁵⁾.

⁽⁴¹⁾ Rostock Regional Court, pp. 22-23.

⁽⁴²⁾ Rostock Regional Court, p. 26.

⁽⁴³⁾ BAVARIA submission of 18 June 2012, pp. 4-5.

⁽⁴⁴⁾ Case C-124/10 P *Commission v EDF*, not yet reported, paragraphs 78 and 79.

⁽⁴⁵⁾ Case C-124/10 P, paragraphs 81 to 85.

- (100) It follows from the foregoing, first, that the documents presented by the parties that post-date the adoption of the measure cannot be taken into account as such for the application of the MEO test in this case.
- (101) It follows from the above, second, that the effect of the Inherited Debt Support Law on the financial situation of NEUWOGES cannot be taken into account either for the application of the MEO test in this case. Indeed, the Inherited Debt Support Law pursued a public policy purpose, and only a limited category of companies (Section 2 of the Inherited Debt Support Law) was eligible for the benefits awarded by it. This law would not have been applicable to a MEO in a situation as close as possible to NEUWOGES.

7.1.2. Structure of the assessment in the present case

- (102) In order to determine whether the contracts at issue have granted an advantage to BAVARIA, it must be determined whether those contracts fell within the range of transactions a MEO in a situation as close as possible to NEUWOGES' would have engaged in.
- (103) The Commission's assessment comprises three steps. First, as a preliminary step, the financial implications of the transaction for NEUWOGES are analysed to determine what profits it could expect to obtain from the transaction (section 7.2). Second, in order to determine whether any available alternative would have been economically more attractive, the sale-and-lease-back transaction is compared to other options, such as a direct sale (section 7.3). Third, a benchmarking exercise is carried out by comparing the transaction in question with similar sale-and-lease-back transactions concluded around the same time, by analysing the results of a limited bidding process carried out by NEUWOGES, and by comparing the terms of the transaction with the standard interest rates of other financing transactions available at the relevant time (late 1997/early 1998) (section 7.4). Taken together, these three levels of analysis enable a conclusion to be drawn concerning whether NEUWOGES behaved like a MEO.

7.2. THE FINANCIAL IMPLICATIONS OF THE TRANSACTION FOR NEUWOGES

- (104) The first step in the analysis of the financial implications of the transaction under scrutiny is to determine the nature of the transaction. In this case, the question revolves mainly around whether the two contracts concluded between NEUWOGES and BAVARIA constitute two parts of an integrated, single transaction or whether they must be assessed as separate transactions (section 7.2.1). Second, in order to facilitate a proper assessment of the financial impact of the transaction on NEUWOGES, the particular nature of a sale-and-lease-back operation is examined (section 7.2.2). After the financial impact of the land-lease and sale contract (section 7.2.3) and the general management contract (section 7.2.4) has been separately analysed in depth, a global assessment of the profitability to be expected from the transaction for NEUWOGES is undertaken (section 7.2.5).

7.2.1. Joint versus separate assessment of the contracts in question

- (105) It should first be pointed out that both the Commission's Opening Decision and Rostock Regional Court's judgment concluded that the two contracts in question had to be analysed in conjunction with one another⁽⁴⁶⁾. The formal investigation confirmed that finding, for the following reasons:
- (a) The two contracts constitute mutually complementary parts of a single sale-and-lease-back transaction. The leaflet produced by BAVARIA, advertising its particular sale-and-lease-back model, indicated that the transaction would be implemented via two contracts, one regulating the sale and one the lease-back⁽⁴⁷⁾. The two contracts were then always referred to as one package transaction.
- (b) The contracts were concluded on the same day (21 January 1998) and refer to one another⁽⁴⁸⁾, indicating their close connection and the fact that neither of the contracts would have been concluded without the other.
- (c) The terms of the contracts are inseparably linked to one another, as is evidenced by BAVARIA's original price calculation, submitted by NEUWOGES⁽⁴⁹⁾. The amount of the upfront cash payment depended on the leasing payment to be paid on a monthly basis by NEUWOGES and BAVARIA's investment in the modernisation of the buildings. Indeed, in a sale-and-lease-back transaction, the leasing payment serves to repay the lessor's

⁽⁴⁶⁾ See recitals 80 and 87 above.

⁽⁴⁷⁾ BAVARIA leaflet, 'Leasingmodell Immobilien', p. 4.

⁽⁴⁸⁾ See, for example, Part I (3) of land-lease and sale contract; Preamble to the general management contract.

⁽⁴⁹⁾ NEUWOGES' submission of 17 July 2012, Annex 1.

original investment. This means that, if the provisions of the general management contract had been different, the figures in the land-lease and sale contract would have changed as well, and *vice versa* ⁽⁵⁰⁾.

- (d) The minutes of NEUWOGES' supervisory board meetings show that the two contracts were always considered by NEUWOGES as forming part of one single transaction ⁽⁵¹⁾. For instance, the submissions to the supervisory board meetings of 30 October 1997 and 16 December 1997 state that the financing of the purchase price by the buyer is based on a leasing model, showing that NEUWOGES was well aware of the connection between the land-lease and sale contract and the general management contract. Similarly, during the meeting on 16 December 1997, the management of NEUWOGES explained to the supervisory board that the payment negotiated with BAVARIA was the price that could be achieved for this 'package' and that the 'package' entailed some risks for the company, which were, however, bearable. The reference to the 'package' and the risk involved again demonstrates that both contracts were perceived as a single transaction.
- (106) NEUWOGES' arguments relating to the failure to have one of the contracts in question notarised are unpersuasive. NEUWOGES' main argument is that this failure to notarise demonstrates the intention of the parties to conclude two separate, mutually independent contracts. The Commission points out that, as state interventions take various forms and must be assessed in relation to their effects, it cannot be excluded that several consecutive measures of state intervention must, for the purposes of Article 107(1) TFEU, be regarded as a single intervention. That could be the case in particular where consecutive interventions, especially having regard to their chronology, their purpose and the circumstances of the undertaking at the time of those interventions, are so closely linked to each other that they are inseparable from one another ⁽⁵²⁾. The notion of a single transaction for the purpose of EU state aid law is therefore broader than the notion of a single transaction under German contract law. The considerations listed in recital 105 show that, based on the chronology, the purpose, and the circumstances of the undertaking at the time the contracts in question were concluded, those contracts have to be regarded as a single transaction for the purpose of EU state aid law.

7.2.2. Background: how the sale-and-lease-back transaction works

- (107) The transaction between BAVARIA and NEUWOGES is based on BAVARIA's real-estate leasing model (*Leasingmodell Immobilien*). The basic formula underlying this model is that the buyer (BAVARIA) finances its original investment by leasing the purchased buildings back to the seller (NEUWOGES). To determine the investment volume and the corresponding leasing payments, the leasing model uses a simple formula, by which the investment volume is calculated by dividing the nominal yearly leasing payment by the leasing rate (expressed as a %):

$$\text{Investment Volume} = \text{Monthly Leasing Payment} \times 1200 / \text{Leasing Rate}$$

$$\text{Monthly Leasing Payment} = \text{Investment Volume} \times \text{Leasing Rate} / 1200$$

The leasing rate, in turn, results from a combination of the duration of the contract, the indexation of the leasing payment, and the residual value of the buildings:

Leasing Rate (%):

Duration: 25 years

Indexation	Residual Value (%)							
	0	1	1,5	2	2,5	3	3,5	
10	8,385	7,687	7,35	7,02	6,701	6,39	6,068	
50	7,80	7,149	6,836	6,53	6,232	5,943	5,661	
100	7,066	6,478	6,194	5,917	5,647	5,384	5,129	

⁽⁵⁰⁾ See also BAVARIA Leaflet 'Leasingmodell Immobilien', pp. 8, 10.

⁽⁵¹⁾ Submission 110/97 to the meeting of NEUWOGES' supervisory board on 30 October 1997; minutes of the meeting of NEUWOGES' supervisory board on 30 October 1997; submission 114/97 to the meeting of NEUWOGES' supervisory board on 12 December 1997; minutes of the meeting of NEUWOGES' supervisory board on 16 December 1997.

⁽⁵²⁾ Case 399/10 P — *Bouygues and Bouygues Télécom v Commission and Others*, not yet reported, paragraphs 103 and 104.

Duration: 30 years

Indexation	Residual Value (%)						
	0	1	1,5	2	2,5	3	3,5
10	7,94	7,196	6,83	6,488	6,148	5,81	5,498
50	7,552	6,844	6,503	6,177	5,847	5,53	5,229
100	7,069	6,464	6,08	5,774	5,47	5,17	4,893

- (108) It is, then, clear that the investment volume depends on the leasing rate as well as on the monthly leasing payments and *vice versa*. Once the participants in the transaction have chosen the basic parameters (duration, yearly indexation, residual value) and either the target overall investment volume or the intended monthly leasing payments, the missing parameters can be calculated. The formula is such that a shorter duration, a lower residual value, a lower indexation or lower nominal monthly leasing payments will all lead to a lower total investment volume.
- (109) Once the overall investment volume has been determined, the costs for modernisation, taxes and other potential costs are deducted. The remaining amount represents the purchase price. In the NEUWOGES/BAVARIA sale-and-lease-back transaction, this purchase price (upfront cash payment) does not differentiate between the price paid for the ownership of the buildings and the rent for the land.

Calculation underlying the BAVARIA — NEUWOGES transaction

Total Investment Volume	EUR [...]
Modernisation	EUR [...]
Taxes and Fees	EUR [...]
Privatisation Remuneration	EUR [...]
Purchase Price	EUR [...]

- (110) The sale-and-lease-back transaction in question consists of two elements, the land-lease and sale contract and the general management contract, which are in turn related to the global lump-sum contract. The financial implications of the land-lease and sale contract, the general management contract, and the global lump-sum contract for NEUWOGES have to be evaluated in this light.

7.2.3. *Determining the likely financial impact of the land-lease and sale contract on NEUWOGES*

- (111) The central components of the land-lease and sale contract are the sale of the buildings and the creation of a 75-year ground lease on the land on which they stand. BAVARIA committed itself to paying a total of EUR [...] to NEUWOGES, of which EUR [...] constituted capitalised rent on the land for the period up to 31 December 2028 and EUR [...] constituted the purchase price for the buildings⁽⁵³⁾. From 1 January 2029, for a period of 10 years, BAVARIA will also have to pay an annual rent of [...]% of the current land value, which has been calculated at EUR [...] per m² or EUR [...] per year⁽⁵⁴⁾. From 2039 onward, and until the land-lease and sale contract expires at the end of 2073, an adaptation of the rent to the total cost-of-living index is provided for, insofar as the latter fluctuates by more than [...]%⁽⁵⁵⁾.
- (112) In addition to purchasing the buildings and acquiring a ground lease on the underlying land, BAVARIA accepted the obligation to modernise the buildings, agreeing to enter into a contract with NEUWOGES' subsidiary, BRG, for the construction works.
- (113) To determine the purchase price to be paid by BAVARIA to NEUWOGES under the land-lease and sale contract, the parties assumed a monthly leasing payment of EUR [...] per m², an indexation of [...]% per year, a residual

⁽⁵³⁾ Part IV, Section 1 of the land-lease and sale contract.

⁽⁵⁴⁾ Part III, Section 10(2) of the land-lease and sale contract.

⁽⁵⁵⁾ Part III, Section 10(3) of the land-lease and sale contract.

value of the buildings of [...] % (to be paid by NEUWOGES after the expiration of the 75-years ground lease contract and based on an expert evaluation at that time), and a duration of 30 years for the lease-back⁽⁵⁶⁾ The total investment volume resulting from these assumptions was EUR [...] ⁽⁵⁷⁾. After the deduction of modernisation costs of EUR [...], privatisation costs of EUR [...] and taxes/fees of EUR [...], the resulting sale price was set at EUR [...] ⁽⁵⁸⁾.

Monthly Leasing Payment × 1 200/Leasing Rate = Investment Volume

EUR [...] × 1 200/[...] = EUR [...]

- (114) This final price was then separated into the price of the buildings ([...] % = EUR [...]) and the capitalised rent for the land ([...] % = EUR [...]) ⁽⁵⁹⁾. The amounts allocated to the land and the buildings were not calculated separately, but rather set as portions of the overall sale price.
- (115) The first benefits that NEUWOGES derived from the transaction were therefore the cash payment of EUR [...] and, starting after 30 years, the income from the rent on the land to be paid by BAVARIA.

7.2.3.1. Other factors

Privatisation remuneration

- (116) Before proceeding, it must be observed that the cash payments of EUR [...] made by BAVARIA to NEUWOGES as privatisation remuneration must in any case be taken into account.
- (117) As the buyer of the buildings and lessee of the land, BAVARIA had to undertake clearly prescribed efforts to sell a portion of the apartments to the tenants pursuant to the contracts at issue. That condition had been included in the contract so that a sale could be accepted as 'mediated privatisation' for the purposes of the Inherited Debt Support Law. Under that law, a commercial buyer had to attempt to sell as large as possible a portion — at least one third — of the apartments acquired in the transaction to the tenants ⁽⁶⁰⁾. This obligation involved making efforts to inform the tenants of their options and gauge their interest in buying apartments. The task of making such efforts was effectively transferred back to NEUWOGES through the land-lease and sale contract (Part V Sections 1-3), and a remuneration for NEUWOGES of EUR [...] per m² was agreed, resulting in a total remuneration for the privatisation effort of EUR [...].
- (118) Initially, it was not intended that NEUWOGES would receive any remuneration for the privatisation efforts, and the amounts later paid as a separate remuneration for the privatisation efforts were simply part of the originally envisaged sale price ⁽⁶¹⁾. Indeed, it did not make sense for BAVARIA to remunerate NEUWOGES for performing activities in which BAVARIA had no commercial interest. Obtaining the debt relief pursuant to the Inherited Debt Support Law, for which engaging in the privatisation efforts was necessary, was solely in NEUWOGES' economic interest.
- (119) However, the remuneration for the privatisation efforts was later deducted from the sale price and paid separately, presumably because maintaining it as part of the sale price would have meant its having to be transferred to the inherited debt relief fund. The sale price paid by BAVARIA to NEUWOGES was reduced by the corresponding amount. From BAVARIA's perspective, this change made no economic difference. NEUWOGES received exactly the same amount of funds from BAVARIA as it would have received if no separate privatisation remuneration had been agreed. Indeed, NEUWOGES itself included the privatisation payments in the revenue to be derived from the sale-and-lease-back transaction ⁽⁶²⁾.
- (120) The handling of these payments as a separate fee rather than as part of sale price was relevant for NEUWOGES only against the background of the Inherited Debt Support Law. However, as explained above (in recital 101), a MEO would not have taken the Inherited Debt Support Law into account. The fact that NEUWOGES engaged in the privatisation efforts and expended resources on them is not relevant in this context. A MEO not acting against the backdrop of the Inherited Debt Support Law would not have engaged in privatisation efforts, which is why they cannot be taken into account in applying the MEO test.

⁽⁵⁶⁾ Sections 2-4 of the general management contract.

⁽⁵⁷⁾ NEUWOGES' submission of 17 July 2012, Annex 1.

⁽⁵⁸⁾ NEUWOGES' submission of 17 July 2012, Annex 1.

⁽⁵⁹⁾ See letter from NEUWOGES to BAVARIA of 24 November 1997, p. 2.

⁽⁶⁰⁾ See Part IV Section 3 of the land-lease and sale contract in connection with Part V Sections 3, 4 EBV.

⁽⁶¹⁾ See BAVARIA's submission of 22 April 2013, Annex 12.

⁽⁶²⁾ See submission 114/97 to the meeting of NEUWOGES' supervisory board on 12 December 1997.

- (121) Accordingly, the remuneration for privatisation efforts paid by BAVARIA to NEUWOGES has to be considered a relevant benefit for NEUWOGES and one that has to be added to the sale price in order to determine the total financial impact of the sale-and-lease-back transaction on NEUWOGES.

Modernisation

- (122) The modernisation carried out in the context of the sale-and-lease-back transaction had further financial implications for NEUWOGES. It must be pointed out that the modernisation costs were directly related to the payment by BAVARIA to NEUWOGES under the land-lease and sale contract. This payment resulted from a calculation of the total investment volume minus the costs, including modernisation costs (see recital 109 above). In other words: the higher the modernisation costs, the lower the purchase price. It is for this reason that in an alternative calculation of the transaction, in which lower rent levels, a lower indexation and thus significantly lower leasing payments were assumed, the purchase price was still above that of the actual land-lease and sale contract, mostly because the modernisation costs in this alternative calculation were assumed to be much lower than eventually agreed between BAVARIA and BRG ⁽⁶³⁾.
- (123) Against this background, it should be noted that the lump-sum modernisation payment made by BAVARIA to NEUWOGES' wholly owned subsidiary BRG under the global lump-sum contract was much higher than the modernisation costs originally estimated by NEUWOGES ⁽⁶⁴⁾. While NEUWOGES' original estimate assumed total costs of EUR [...] or EUR [...] per m², the lump-sum modernisation costs finally agreed between BAVARIA and NEUWOGES' subsidiary BRG amounted to EUR [...] or EUR [...] per m². In other words, the agreed costs exceeded the originally estimated costs by EUR [...] or [...].%. The significantly higher agreed lump-sum costs significantly reduced the payment by BAVARIA to NEUWOGES under the land-lease and sale contract.
- (124) No explanation was provided for this divergence between the originally estimated costs and the agreed lump-sum payment. This is particularly surprising in view of NEUWOGES' original assertion that the estimated modernisation costs averaging EUR [...] per m² were 'common' or 'usual' costs[...] ⁽⁶⁵⁾. The study 'Between Modernisation and Demolition: Prefabricated Apartment Blocks in East Germany' (hereinafter: the 'Pestel study'), submitted by NEUWOGES, also estimated the costs of a modernisation similar to that carried out by BRG at between EUR [...] per m² and EUR [...] per m² ⁽⁶⁶⁾. As the owner and administrator of the buildings, NEUWOGES had intimate knowledge of the modernisation needs, and it is hard to see why it would have originally underestimated these so drastically.
- (125) The modernisation costs must be taken into account in determining the financial impact of the land-lease and sale contract. First of all, it is clear that it was irrelevant to BAVARIA itself what modernisation costs NEUWOGES' subsidiary, BRG, would charge it, simply because all additional modernisation costs would simply be set off against the purchase price. NEUWOGES, on the other hand, had a manifest economic interest both in having BAVARIA contract with BRG to undertake the modernisation works and in shifting part of the sale price onto the modernisation costs. The reason for the latter consideration is that profits made from the modernisation by NEUWOGES' subsidiary were not subject to the transfer obligations under the Inherited Debt Support Law. According to its own estimates, the profits earned by BRG (and hence NEUWOGES) from the BAVARIA modernisations amounted to EUR [...] ⁽⁶⁷⁾. These profits constitute a direct benefit for NEUWOGES that must be taken into account. In justifying the sale price, NEUWOGES' management too stressed that BRG was contracted to carry out the modernisation works ⁽⁶⁸⁾.

Ground rent

- (126) Moving on to the ground rent, it is important to address NEUWOGES' argument that BAVARIA did not effectively have to pay any rent for the first 30 years, since the capitalised rent for the land was included in the sale price. However, whether the ground rent is paid on a yearly basis or upfront as capitalised rent is hardly decisive for this assessment. There is no indication that such an arrangement was irrational; it merely expressed a preference for upfront liquidity on the part of NEUWOGES.
- (127) Finally, it must not be forgotten that BAVARIA is under the obligation to pay the ground rent even after the general management contract expires. From 1 January 2029, for a period of 10 years, BAVARIA will have to pay an annual rent of [...] % of the current land value, which has been set at EUR [...] per m². For the subsequent remaining term, an adaptation of the ground rent to the total cost-of-living index is provided for, as

⁽⁶³⁾ BAVARIA's submission of 18 June 2012, Annex 11.

⁽⁶⁴⁾ See letter from NEUWOGES to BAVARIA of 7 March 1997 and BAVARIA's first offer in response thereto (BAVARIA's submission of 18 June 2012, Annexes 9 and 10).

⁽⁶⁵⁾ See letter from NEUWOGES to BAVARIA of 7 March 1997 (BAVARIA's submission of 18 June 2012, Annex 9).

⁽⁶⁶⁾ Pestel-Study (NEUWOGES' submission of 17 July 2012, Annex 2), p. 68 ('Sanierungsstufe 2').

⁽⁶⁷⁾ NEUWOGES' submission of 27 September 2012, Annex.

⁽⁶⁸⁾ Submission 114/97 to the meeting of NEUWOGES' supervisory board on 12 December 1997, p. 3.

long as the latter fluctuates by more than [...]%. Assuming for the sake of simplicity that the cost-of-living index will not fluctuate, these future payments will have a nominal value of EUR [...]. For an overall evaluation, the discounted value in 1998 of these future payments must also be considered as part of the benefit received by NEUWOGES.

7.2.3.2. Conclusions

(128) It must be pointed out that it was the purpose of the foregoing analysis to determine the financial impact of the land-lease and sale contract on NEUWOGES as accurately as possible. This analysis leads to the conclusion that the relevant benefits received by NEUWOGES include:

- (a) the cash price paid by BAVARIA (EUR [...]);
- (b) the fee paid for the privatisation efforts (EUR [...]);
- (c) the profits earned from the modernisation (EUR [...]);
- (d) the cash value of the ground rent after 2029 (EUR [...], after discounting).

7.2.4. Determining the likely financial impact of the general management contract on NEUWOGES

(129) Under the general management contract, NEUWOGES is responsible for managing the buildings in question. In return for the right to keep all income generated from renting the apartments and commercial space, NEUWOGES has to pay the owner (BAVARIA) a fixed monthly leasing payment, set at EUR [...] until the completion of the modernisation works, and EUR [...] thereafter (Section 3 of the general management contract). The contract has a duration of 30 years from the completion of the modernisation works (Section 2.1). The monthly leasing payment is indexed at [...]% per year (Section 4.2). The purpose of the following analysis is to determine the financial impact of the general management contract on NEUWOGES.

7.2.4.1. Background (Calculations)

(130) The monthly leasing payment is the result of multiplying the likely net rent per m² and per month — reduced by the costs of administration and maintenance and taking account of the risk of loss of rent — by the number of m² available ⁽⁶⁹⁾. The central assumptions are, then, the likely net rent per m² and per month, and the likely costs. In the general management contract, the parties assumed net rent levels of EUR [...] per m² after modernisation and costs of EUR [...] per m², leading to the monthly leasing payment being set at EUR [...] per m² ⁽⁷⁰⁾.

$(\text{Average rent/m}^2 - \text{Administration Costs} - \text{Maintenance Costs} - \text{Risk of loss of Rent}) \times \text{Total m}^2 = \text{Monthly Leasing Payment}$

$(\text{EUR [...] - EUR [...] - EUR [...] - EUR [...]}) \times \text{EUR [...] = EUR [...]}$

(131) In setting the particular parameters that were eventually included in the general management contract, NEUWOGES had a choice ⁽⁷¹⁾. By setting a different rent level or a higher indexation, it could precisely determine its monthly payments over the duration of the contract and the price it would obtain from the sale ⁽⁷²⁾. There was, then, a direct correlation between assuming a higher or lower risk in setting a particular leasing payment (e.g. by setting different rent levels, indexation, and costs) and the liquidity received in the form of the sale price. For example, in an alternative calculation provided by BAVARIA, which assumes an indexation of 2,0 %, rent levels of EUR [...] and hence a leasing payment of EUR [...], the monthly leasing payment would have amounted to EUR [...] instead of EUR [...] ⁽⁷³⁾. Of course, the sale price would have been lower as well.

⁽⁶⁹⁾ Cf. NEUWOGES' submission of 17 July 2012, Annex 1.

⁽⁷⁰⁾ Ibid.

⁽⁷¹⁾ BAVARIA submits that NEUWOGES freely chose the relevant parameters. See BAVARIA's submission of 22 April 2013, para. 23. See, in addition, the letter from NEUWOGES to BAVARIA of 6 May 1997 (BAVARIA's submission of 18 June 2012, Annex 1a), where NEUWOGES asks BAVARIA to prepare the contracts with a 30-year duration, [...] % indexation of the leasing payment and [...] % residual value.

⁽⁷²⁾ It is important to note in this context that the monthly leasing payment, together with the yearly indexation (here, [...] % per year), the duration of the contract (here, 30 years), and the residual value of the buildings (here, [...] %), result in the overall investment volume. This means that, where lower rent levels, higher costs, or a lower indexation are chosen, the overall investment level is reduced. Considering, further, that the sale price is a direct consequence of the total investment volume minus the modernisation costs, privatisation costs and taxes/fees, the sale price is directly dependent on the rent level, costs, indexation, etc.

⁽⁷³⁾ BAVARIA's submission of 18 June 2012, Annex 11.

7.2.4.2. Financial impact analysis

General considerations

- (132) In determining the financial impact of the general management contract on NEUWOGES, it is important to note two considerations. First, the leasing payment is calculated on a per m² basis. Since a number of apartments were sold by BAVARIA after the conclusion of the contract, the relevant amount changed from, initially, [...] m² to [...] m² in 1999, [...] m² in 2000, and [...] m² in 2001. After 2001, the relevant amount remained stable at [...] m². In its submissions, NEUWOGES used these progressively decreasing amounts of m² to calculate projected financial flows. As only the *ex-ante* perspective is important, NEUWOGES should not have reduced the overall amount of m² underlying its calculations by the amount actually sold thereafter, but by the amount it expected, in early 1998, to be sold thereafter. Accordingly, the following analysis will not be based on the numbers used in NEUWOGES' submissions; rather, it will use the numbers that NEUWOGES included in its original profit projection, which assumed a progressive reduction from [...] m² to [...] m² until 2003. Second, to determine the financial impact of the contract for NEUWOGES, expected when the transaction was concluded, future income and costs must be discounted, requiring a discount rate to be set. In line with its original letter and the cash-flow analyses provided by NEUWOGES, the Commission assumes the discount rate to be 5 % per year⁽⁷⁴⁾.

Reliability of NEUWOGES' cash-flow analyses

- (133) Before proceeding to provide an independent economic analysis of the general management contract, it is first necessary to comment on the *ex post* cash-flow analyses provided by NEUWOGES, which are supposed to demonstrate the cash-flow that a prudent MEO would have expected the general management contract to generate *ex ante*. NEUWOGES argues that under realistic *ex ante* assumptions — claimed by NEUWOGES to be an increase of rent of [...] % per year, an indexation of costs of [...] % per year and a vacancy rate of [...] % — the general management contract would, *ex ante*, have been expected to lead to a total negative cash-flow of EUR [...] in nominal terms and of EUR [...], discounted⁽⁷⁵⁾. NEUWOGES also submits that only where allegedly unrealistic *ex ante* assumptions are made — rent increase of [...] % per year, vacancy rate of [...] %, and stable costs — could the general management contract have been expected to result in a positive value of EUR [...] in nominal terms and EUR [...], after discounting⁽⁷⁶⁾. On this basis, NEUWOGES submits that it was clear, *ex ante*, that rent increases of [...] % would have to be enforced every year simply to cover the leasing payment, leaving no room for increases in costs.
- (134) It must be observed in this respect that NEUWOGES makes assumptions about the cost levels that are un-persuasive (and the initial cost levels are the same in all the analyses provided by NEUWOGES). The calculations underlying the general management contract, as concluded, assume total costs (administration, maintenance, risk of loss of rent) amounting to some [...] % of the rent. In contrast, NEUWOGES' cash-flow analyses assume an initial cost level (after modernisation) of not less than [...] % ([...] % risk of loss of rent, [...] % administration and maintenance). Even if the dramatic increase in loss of rent (from [...] % to [...] %) is ignored, there is an increase in other costs from [...] % to [...] % of the rent. NEUWOGES' submissions do not adequately explain why this increase would be necessary. On the contrary, NEUWOGES states that the level of [...] % (EUR [...] per m²) was plausible for the period directly after the modernisation, but would then increase every year by [...] %⁽⁷⁷⁾. Similarly, the valuation commissioned by NEUWOGES before the sale assumed total cost levels (including risk of loss of rent⁽⁷⁸⁾) of between [...] % and [...] % (1997 valuation). As the valuation does not specify what percentage is allocated to loss of rent, it is not possible to determine how its basic assumptions regarding other costs depart from those of NEUWOGES. In any event, even if one were to assume that the 1997 valuation was based on an estimate of risk of loss of rent of [...] %, the other costs assumed by NEUWOGES are higher. In the light of this, NEUWOGES' cash-flow analyses cannot be accepted and must be corrected on the basis of an initial cost level of [...] % excluding risk of loss of rent⁽⁷⁹⁾.

⁽⁷⁴⁾ The Commission's own reference discount rate for the relevant period is 5,94 % (http://ec.europa.eu/competition/state_aid/legislation/reference_rates_eu15_en.pdf). However, since the Opening Decision assumed a discount rate of 5 %, and given that NEUWOGES adopted this rate in its own calculations, the Commission has decided to continue assuming a discount rate of 5 %.

⁽⁷⁵⁾ NEUWOGES' submission of 17 July 2012, Annex 7.

⁽⁷⁶⁾ NEUWOGES' submission of 17 July 2012, Annex 8(e).

⁽⁷⁷⁾ NEUWOGES' submission of 17 July 2012, p. 60.

⁽⁷⁸⁾ See Section 18 of the Land Valuation Order (*Wertermittlungsverordnung*) of 6 December 1988, BGBl. I, p. 2209.

⁽⁷⁹⁾ The Commission notes that NEUWOGES, in its cash-flow analyses, already indexed the costs for 1999. The Commission, however, only started indexing the costs from 2000 onwards. The reason is that cost calculations were done with the post-modernisation period in view, and this period started in 1999. Likewise, NEUWOGES argued in its submission that the cost level was reasonable immediately after the modernisation, i.e. in 1999. In the light of this, it is more appropriate to start increasing the costs only from 2000 onwards.

- (135) In the light of this, it must further be remarked that NEUWOGES' submission that rent increases of [...] % would need to be enforced to cover the increase in the leasing payment alone is erroneous. Since the leasing payment is calculated as a percentage of the original overall rent (here [...] %), a rent increase of [...] % would allow *both* the increase in the leasing payment *and* an increase in the costs by [...] % to be covered. Where the costs are stable, a smaller rent increase would already suffice to offset the increase in the leasing payment. In fact, assuming a risk of loss of rent of [...] % and otherwise stable costs, a yearly rent increase of [...] % would suffice to cover the increase in the leasing payment. Any increase over and above that would be available for NEUWOGES to offset rising costs or make a profit.

Financial impact analysis

- (136) When entering into the contract, NEUWOGES itself undertook a nominal cash-flow analysis⁽⁸⁰⁾. In this analysis, it assumed that its own costs (administration, maintenance) would rise by [...] % p.a., that it could increase the rent by [...] % every three years, that it could maintain a vacancy rate of [...] % and that [...] % of the apartments would be sold on to the tenants. On this basis, NEUWOGES expected a nominal cash-flow of EUR [...] to be generated by the general management contract over its duration of 30 years.
- (137) The formal investigation procedure has revealed no reason to believe that these calculations were made on the basis of expectations *known* to be too optimistic. No evidence has been submitted that the NEUWOGES representatives who presented these figures to NEUWOGES' board did so believing they were inaccurate. In fact, it appears that NEUWOGES does not allege that its managers were consciously entering into a disadvantageous transaction for political reasons, but rather that an erroneous assessment was made of the economic implications (which, in NEUWOGES' submission, a MEO would have avoided)⁽⁸¹⁾.
- (138) Nevertheless, it is necessary to enquire whether these expectations were such that a MEO would not have based its decision on them. In this context, it is noted that NEUWOGES submits that a MEO would have expected a rent increase of merely [...] % p.a., a risk of loss of rent of [...] % and an increase in administration and maintenance costs of [...] %⁽⁸²⁾. On the basis of these assumptions, NEUWOGES claims that the total cash flow would be EUR – [...] in nominal terms and EUR – [...] after discounting, with the more than sevenfold increase in the loss of rent having the most significant impact.

7.2.4.3. Market expectations

- (139) As a first step, reference is made to the documents providing information as to the actual expectations of the two parties to the transaction. First, the minutes of the supervisory board meeting of 16 December 1997 demonstrate that NEUWOGES' managers considered the risks involved in the transaction as 'bearable'⁽⁸³⁾. On the basis of these minutes, it is, furthermore, clear that NEUWOGES acted on the basis of calculations that assumed a rent increase of [...] % every three years, an increase in costs (without reference to the risk of loss of rent) of [...] %, and a risk of loss of rent of [...] %⁽⁸⁴⁾.
- (140) NEUWOGES consulted the auditor Nordrevision before signing the contracts, which estimated that a rent increase of [...] % corresponded to the general inflation rate, but would probably not be achievable⁽⁸⁵⁾. It also took the view that, while the initial costs were reasonable under the assumption of no vacancies (the calculations were based on an estimate of costs of [...] % of the rent), an indexation of those costs in line with that of the indexation of the leasing payment was necessary⁽⁸⁶⁾.
- (141) BAVARIA, for its part, assumed that, on the basis of an expectation that the population of Neubrandenburg would remain stable (due to the establishment of various big service providers)⁽⁸⁷⁾ and the good location of the buildings, a very low vacancy rate could be expected⁽⁸⁸⁾. It further assumed that rent increases in line with the indexation of the leasing payments would be achievable⁽⁸⁹⁾.

⁽⁸⁰⁾ See Submission 114/97 to the meeting of NEUWOGES' supervisory board on 12 December 1997, Annex 6.

⁽⁸¹⁾ See, for example, NEUWOGES' submission of 5 November 2007, p. 4.

⁽⁸²⁾ NEUWOGES' submission of 17 July 2012, p. 61.

⁽⁸³⁾ Minutes of NEUWOGES' supervisory board meeting of 16 December 1997, p. 5.

⁽⁸⁴⁾ See submission 114/97 to the meeting of NEUWOGES supervisory board on 12 December 1997, Annex 6.

⁽⁸⁵⁾ Letter from Nordrevision to NEUWOGES of 20 November 1997 (NEUWOGES' submission of 25 April 2007, Annex 13), p. 3.

⁽⁸⁶⁾ *Ibid.*

⁽⁸⁷⁾ It should be noted that in 1997/1998, the City of Neubrandenburg and Mecklenburg-Vorpommern *Land* assumed that the population numbers would remain stable. See Germany's submission of 4 September 2007, p. 6.

⁽⁸⁸⁾ Proposed Decision for BAVARIA's Product Committee meeting of 13 September 1997 (BAVARIA's submission of 22 April 2013, Annex 15), p. 2.

⁽⁸⁹⁾ *Ibid.*, p. 3.

- (142) Finally, it should be pointed out that the valuation of the property commissioned by NEUWOGES before the sale contains information about relevant expected developments. The 1997 valuation assumed cost levels of between [...] % and [...] %, but did not specify what percentage is allocated to the risk of loss of rent ⁽⁹⁰⁾.

7.2.4.4. Assessment

Administration costs

- (143) First, the expectations regarding the costs of administration and maintenance, both as regards their initial level (EUR [...] per m², or [...] % of the rent) and the expected increase ([...] % p.a.) appear reasonable. As regards the initial cost level, this finding results from NEUWOGES' own statement that, at least for the period directly following the modernisation, these costs had been set at a sufficiently high level. Secondly, the Pestel study states that, in 1997, the costs of administration and maintenance would on average amount to EUR [...] per m², which is EUR [...] lower than the provision for the same costs in the sale-and-lease-back transaction ⁽⁹¹⁾. Finally, the costs assumed in the expert valuation were also in this range. While an increase in these costs could certainly be expected, it would appear that assuming an increase of [...] % p.a. was reasonable, even somewhat cautious. Nordrevision had suggested keeping such an indexation of the administration costs in line only with the indexation of the leasing payment, namely an annual increase of [...] %, lower than that actually assumed by NEUWOGES. Incidentally, an indexation of [...] % is what NEUWOGES itself now submits could reasonably have been expected, demonstrating that [...] % p.a. was certainly not unreasonably low.

Risk of loss of rent

- (144) With respect to the risk of loss of rent, it was not unreasonable to expect a general loss of rent level of [...] %. First, it must be noted that Nordrevision did not question this level in its assessment of the contracts, despite expressing other concerns about the general economic situation and the real-estate market in Neubrandenburg ⁽⁹²⁾. Second, the 1997 valuation, despite not specifying the assumed risk of loss of rent, does not appear to assume significantly higher risks of loss of rent ⁽⁹³⁾.
- (145) BAVARIA's internal decision-making documents indicate that BAVARIA assumed that, in view of the variety of large services providers established in Neubrandenburg, the population of the city would probably remain stable and that almost all the apartments in question could be rented out after they had been modernised. Indeed, according to NEUWOGES, in 1997/98 the City of Neubrandenburg and Mecklenburg-Vorpommern *Land* assumed stable population numbers and stable income development.
- (146) Finally, the fact cannot be ignored either that NEUWOGES' management, which ran an undertaking that owned more than 30 % of the apartments in Neubrandenburg and thus had intimate knowledge of the local real-estate market, judged the risks involved in the sale-and-lease-back transaction to be bearable and based its own projections on a risk of loss of rent of [...] %. It is not clear why these experts in the local real-estate market would have based their calculations on this assumption if it had been as unreasonably low as NEUWOGES now claims.
- (147) At the same time, account has to be taken of the documents provided by NEUWOGES in connection with the issue of whether a prudent participant in the relevant real-estate market (prefabricated apartment blocks in East Germany) would have expected higher vacancy rates, in so far as the documents date from before the conclusion of the sale-and-lease-back transaction. Of the studies provided, only the Pestel study dates from before the conclusion of the contracts at issue. In this context it must be observed, however, that the Pestel study concerns East Germany as a whole and does not take into account the specific local conditions in Neubrandenburg — a state of affairs that limits its probative value in the present context. While the study points to some general problems in the East German real-estate market, the study in itself is not sufficient to establish that a MEO would not have based its investment decision on an assumed risk of loss of rent of [...] %.

⁽⁹⁰⁾ See NEUWOGES' submission of 5 November 2007, Annexes 1 and 5.

⁽⁹¹⁾ Pestel study, p. 62.

⁽⁹²⁾ Letter from Nordrevision to NEUWOGES of 20 November 1997 (NEUWOGES' submission of 25 April 2007, Annex 13), p. 3.

⁽⁹³⁾ It should be noted that, if the 1997 valuation assumed a higher risk of loss of rent, this would in turn mean that it assumed correspondingly lower administration and maintenance costs.

Rent

- (148) Moving on to the rent, it must first be observed that NEUWOGES has not submitted that the expected rent levels after modernisation were set too high. It claims, rather, that these could not be increased by as much as expected. In the light of Rostock Regional Court's finding that the average rent level of EUR [...] per m², on which the general management contract is based, was within the range set by the applicable rent table⁽⁹⁴⁾, it can be concluded that the initial average rent level was set at a realistic level.
- (149) As regards indexation of the agreed leasing payment, there is no direct evidence of what average increase of rent was generally expected in 1998. Nordrevision remarked only that the [...] % per year originally set corresponded to the general inflation rate, but was not likely to be achievable in Neubrandenburg⁽⁹⁵⁾. The fact that NEUWOGES did eventually agree to an indexation of 'only' [...] % and expected to be able to enforce rent increases of [...] % every three years (or [...] % p.a.) appears to demonstrate that it took this warning into account. The valuations did not explicitly express any expectation about future rent increases. It must, nevertheless, be noted that since the valuations did not make explicit assumptions about inflation and rent development, the underlying assumption is that the rent increase and general inflation (which had been around 3,5 % in the preceding decades) would converge⁽⁹⁶⁾. Rostock Regional Court was of the opinion that the indexation was justified in light of the average annual inflation rate of 3,52 % in the 28 years before the conclusion of the contracts⁽⁹⁷⁾. It further remarked that the development of rents was obviously difficult to predict over a period of 30 years, but that it could not recognise a clear disproportion between the indexation of the leasing payment and the development of rent levels to be expected.
- (150) The Pestel study submitted by NEUWOGES does not provide any data on what participants in the East German real-estate market actually expected, and contains no specific data on Neubrandenburg. Nevertheless, it points towards a potentially difficult market in East Germany. However, in the light of the remaining evidence, it again fails to demonstrate that agreeing an indexation of the leasing payments of [...] % p.a. and expecting to be able to enforce rent increases of [...] % p.a. was unreasonable.

Duration

- (151) As regards, finally, the duration of the contract, Rostock Regional Court reasoned that certain leasing contracts are marked by long durations (of up to 30 years) and that the contract in question is not necessarily uncommon⁽⁹⁸⁾. While the 30-year duration did, of course, involve some risks, it also offered the possibility of making stable profits and having high certainty regarding the costs. In addition, a longer duration also meant that the monthly lease payments necessary to pay back the buyer's investment were lower, or that the sale price was higher with equal leasing payments than if a shorter duration had been chosen⁽⁹⁹⁾. In this light, agreeing on a duration of 30 years does not seem unreasonable.

7.2.4.5. Conclusion

- (152) Based on these considerations, it appears that the expectations expressed by NEUWOGES in its original calculation cannot be said to have been unreasonable. Accordingly, in light of the evidence presented, it was reasonable for NEUWOGES to expect to make a profit within the framework of the general management contract. If the nominal expected profits are discounted to the relevant time (early 1998), it turns out that NEUWOGES acted on the basis of assuming that the general management contract had a cash value of EUR [...].

7.2.5. Overall assessment

- (153) As the Commission had already reached the conclusion that the land-lease and sale contract and the general management contract formed part of one integrated business transaction, the cash values of both contracts have to be added together to determine the total value of the transaction for NEUWOGES. To recap: under the land-lease and sale contract NEUWOGES could expect the following benefits:

- (a) the cash price paid by BAVARIA (EUR [...]);
- (b) the fee paid for the privatisation efforts (EUR [...]);

⁽⁹⁴⁾ Rostock Regional Court, pp. 19-20.

⁽⁹⁵⁾ Letter from Nordrevision to NEUWOGES of 20 November 1997 (NEUWOGES' submission of 25 April 2007, Annex 13), p. 3.

⁽⁹⁶⁾ In contrast, where the rent is expected to increase more slowly than general inflation, either due to non-indexed rent contracts or market developments, it is common practice to increase the property interest (*Liegenschaftszins*) by a margin reflecting the expected divergence between rent increase and inflation.

⁽⁹⁷⁾ Rostock Regional Court, p. 20.

⁽⁹⁸⁾ Rostock Regional Court, p. 19.

⁽⁹⁹⁾ For instance, the initial leasing rate would have been [...] % rather than [...] % if a duration of 20 instead of 30 years had been chosen.

- (c) the profits earned from the modernisation (EUR [...]);
- (d) the cash value of the ground rent after 2029 (EUR [...], after discounting).

(154) In addition, it was assumed (as established in section 7.2.4 above) that, based on NEUWOGES' reasonable expectations, the general management contract had a discounted cash value of EUR [...]. Thus, the sale-and-lease-back transaction had a total value of EUR [...] for NEUWOGES.

7.3. COMPARISON WITH ALTERNATIVE BUSINESS OPTIONS

(155) To determine whether NEUWOGES' decision to engage in the sale-and-lease-back transaction fell within the range of economic behaviour that a rational market economy operator would have reasonably engaged in, the value of that transaction must now be compared to that of alternative business options. If NEUWOGES had had an alternative that was economically more advantageous, the decision to engage in the sale-and-lease-back transaction could not be said to be one that a MEO would have taken.

(156) In this context, it should be noted that neither renting the buildings without first modernising them, nor demolishing them, would have been viable business alternatives. First, renting without modernisation would have resulted in limited revenues, and it was clear that unmodernised buildings would more often be left vacant than modernised buildings⁽¹⁰⁰⁾. There is thus no solid basis for concluding that the profits derived from continuing to rent unmodernised buildings could have been expected to exceed those obtained under the sale-and-lease-back transaction. Likewise, demolition would have created no revenue, but would have involved demolition costs. Thus, nor can demolition qualify as a viable alternative at the relevant time (1997/98).

7.3.1. Loan alternative

(157) A first possible alternative to consider would have been loan financing. If NEUWOGES had financed the modernisation of the buildings in question via a loan, it could have obtained some of the same profits it received from the sale-and-lease-back transaction. In the first place, it would have been able to rent out the modernised buildings, thereby generating a good revenue stream. In addition — and in contrast to the position under the sale-and-lease-back transaction — it would have remained the owner of the buildings.

(158) However, it is also clear that loan financing would have involved certain disadvantages. First, NEUWOGES would have had to provide 30 % of the investment volume from its own capital, as NEUWOGES considered that it had to maintain a capital ratio of 30 %⁽¹⁰¹⁾. In late 1997, the NEUWOGES supervisory board discussed lowering the capital ratio in order to facilitate more investment. This proposal was, however, rejected by the management as impossible from an economic point of view, since it would have led to an unacceptable degree of indebtedness⁽¹⁰²⁾. The management explained that reducing the capital ratio from 30 % to 25 % would not be feasible (degree of indebtedness)⁽¹⁰³⁾. Mr Räuber, a member of NEUWOGES' supervisory board, further stated that reducing the capital ratio was unthinkable in terms of business economics. The company's commitments had to be serviced⁽¹⁰⁴⁾. In order to finance the modernisation investment of EUR [...], NEUWOGES would therefore have had to contribute EUR [...] in own capital. It is highly doubtful that this amount of own capital was immediately available. It is clear from the supervisory board minutes that the possible total investment volume for 1998 (including loans) was approximately EUR [...], which was already earmarked for other projects⁽¹⁰⁵⁾. It is clear, then, that NEUWOGES could have resorted to a loan to finance the modernisation only if it had abandoned other projects.

(159) In contrast to loan financing, the sale-and-lease-back transaction had the advantage not only of not requiring NEUWOGES to invest own capital, but also of supplying fresh liquidity in addition to wholly financing the modernisation of the buildings.

(160) Taking all these considerations into account, it cannot be regarded as established that a loan-financed modernisation would have either been available or, if so, more beneficial to NEUWOGES than the BAVARIA deal. The fact that NEUWOGES was unlikely to have the own capital necessary for obtaining the loan and that it could use the additional liquidity to finance other investments are apt to lead to the conclusion that choosing the sale-and-lease-back transaction over loan financing was a sensible decision.

⁽¹⁰⁰⁾ See, for example, valuation GA 22b/07 (NEUWOGES' submission of 5 November 2007, Annex 5), p. 19: 'If the building is to be leased in the long term, modernisation and repairs are urgently needed. ... Unmodernised buildings, in particular, are apt to remain vacant.'

⁽¹⁰¹⁾ Minutes of NEUWOGES' supervisory board meeting of 16 December 1997, p. 3.

⁽¹⁰²⁾ Minutes of NEUWOGES' supervisory board meeting of 16 December 1997, p. 3.

⁽¹⁰³⁾ Minutes of NEUWOGES' supervisory board meeting of 16 December 1997, p. 3.

⁽¹⁰⁴⁾ Minutes of NEUWOGES' supervisory board meeting of 16 December 1997, p. 2.

⁽¹⁰⁵⁾ Minutes of NEUWOGES' supervisory board meeting of 30 October 1997, p. 3.

7.3.2. Outright sale alternative

- (161) A second serious alternative would have been an outright sale of both building and land. The crucial question is whether such a sale would have been more beneficial.

7.3.2.1. Assessment in the light of the 1997 and 2007 valuations

- (162) In attempting to compare the value of the sale-and-lease-back transaction for NEUWOGES and the benefits it could have obtained from an outright sale, the crucial question is what price NEUWOGES could have obtained from a 'normal' sale. The two valuations, from 1997 and 2007, have a certain role to play in this context.
- (163) NEUWOGES commissioned the two studies for the purpose of estimating the 1997 value of the property (buildings and land) in question. One study was carried out by an in-house expert in 1997, and the other retrospectively by an independent expert in 2007. The 1997 valuation estimated the value at EUR [...], whereas the 2007 study resulted in an estimate of EUR [...] ⁽¹⁰⁶⁾. Both studies included separate valuations of the buildings (1997: EUR [...]; 2007: EUR [...]) and the land (1997: EUR [...]; 2007: EUR [...]). Both studies are based on essentially the same methodology, the gross rental method (*Ertragswertverfahren*).
- (164) The Commission considers that, since the 2007 valuation was prepared only after the sale-and-lease-back transaction took place, it cannot be relied upon for determining the value of the property in 1997, as known to NEUWOGES at the time. NEUWOGES could not, then, have based its decision on whether or not to engage in the sale-and-lease-back transaction with BAVARIA on the retrospective 2007 valuation.
- (165) At the same time, the Commission considers that the 1997 valuation is not a reliable indicator either of the value of the property in 1997, as known to NEUWOGES at that time, since the formal investigation procedure has revealed that NEUWOGES' management was well aware that the 1997 valuation was unreliable at the time at which it entered into the contracts under investigation. The following observations are instructive:

(a) Rent

The 1997 valuation assumes rent levels of between EUR [...] and EUR [...] per m². At the same time, the first rent table for the City of Neubrandenburg, valid from 1 January 1998 onward and based on 1997 data, indicated average rent levels for modernised apartments of between EUR 3,90 and EUR 4,38 per m². NEUWOGES, as a large real-estate company active in Neubrandenburg, would necessarily have been aware of the average rent levels in the city, and ought therefore to have based its evaluation of the property on this data. Indeed, the sale-and-lease-back contract envisaged average rent levels of EUR [...] per m² for the period after modernisation (i.e. from 1999 onwards and thus two years later than the data underlying the first rent table). This figure was in line with the rent table.

(b) Modernisation costs

While the 1997 valuation was carried out in the spring of 1997 and assumed total modernisation costs of EUR [...], NEUWOGES' management indicated in a letter to BAVARIA written *at the same time* (March 1997) that it estimated the modernisation costs at EUR [...]. It is thus clear that NEUWOGES was well aware that the 1997 valuation severely underestimated the necessary modernisation costs. The lump sum agreed between BAVARIA and NEUWOGES' subsidiary, BRG, for the modernisation of the property was significantly higher still (EUR [...]), demonstrating that, when NEUWOGES concluded the contracts with BAVARIA, it knew that the 1997 valuation had underestimated the modernisation costs by almost EUR 10 million.

(c) Remaining useful life

With the envisaged modernisation in view, the 1997 valuation estimated the remaining useful life to be between 55 and 70 years. It must be noted in this context that the low estimated modernisation costs in the 1997 valuation do not fit easily with the assumption that the modernisation would significantly extend the economic lifespan of the buildings.

⁽¹⁰⁶⁾ NEUWOGES' submission of 5 November 2007, Annexes 2 and 6.

(d) Land value

It must be noted that, in evaluating the land in question, the 1997 valuation did not take into account value-reducing factors (in contrast, they were taken into account in the 2007 valuation). Such factors include existing infrastructure that cannot be moved or removed (sewage systems, pipes) and the fact that the plot of land was of an inconvenient shape. These factors typically lead to a reduction in the value of the land. As the owner of the land, NEUWOGES must have been aware of these factors and must therefore have known that the 1997 valuation overestimated the land value.

- (166) In conclusion, NEUWOGES was demonstrably aware that some of the key assumptions underlying the 1997 valuation, especially regarding the modernisation costs, were unreliable. The Commission therefore concludes that the 1997 valuation is not a reliable indication of the value of the property in 1997, as known to NEUWOGES at the time.
- (167) At the same time, the Commission is of the opinion that, on the basis of the information available to NEUWOGES at the relevant time, the *ex-ante* estimate of the property value that a MEO in the position of NEUWOGES might reasonably have obtained would probably have been very similar to that contained in the retrospective 2007 valuation. As happened with the retrospective 2007 valuation, a MEO in the position of NEUWOGES would have based its *ex ante* expectations regarding achievable rent on the relevant rent table, would have estimated the modernisation costs as being closer to those agreed between BAVARIA and BRG, and would have adjusted the land value by taking into account value-reducing factors of which it was aware. In addition, a MEO in the position of NEUWOGES would have carefully evaluated the remaining useful life in the light of the envisaged modernisation and of comparison data (as was done in the 2007 evaluation), so that it is reasonable to conclude that a MEO in the position of NEUWOGES would have based its valuation on estimates of the remaining useful life similar to those contained in the retrospective 2007 valuation.
- (168) The Commission thus considers that a MEO in the position of NEUWOGES would reasonably have estimated the value of the property, before concluding the sale-and-lease-back transaction, to have been approximately EUR [...] (as was the case in the 2007 valuation).

7.3.2.2. Comparison of outright sale and sale-and-lease-back

- (169) To recap: the total value of the sale-and-lease-back transaction for NEUWOGES was EUR [...]. In contrast, the above analysis revealed that NEUWOGES would realistically have had to assume a value for the property of EUR [...], which was a mere [...] % higher than the value of the sale-and-lease-back transaction. This small difference does not, however, mean that a MEO would have necessarily chosen the outright sale alternative:
- (a) First, it must not be overlooked that the outright sale alternative at issue related to an outright sale of the buildings *and* attached land, whereas BAVARIA bought only the buildings, while merely acquiring the rights to *lease* the land for 75 years. The land as such remained in the ownership of NEUWOGES. The land alone was estimated by NEUWOGES to have a value of EUR [...] (as in the 2007 valuation). While it is difficult to put a precise figure on the value that NEUWOGES maintained by merely leasing the land rather than selling it, it must be concluded that NEUWOGES' retaining ownership of the land justified a somewhat lower transaction price.
- (b) Second, it must be observed that there is some doubt as to whether the price that a MEO in the position of NEUWOGES would have estimated could actually have been achieved. The only concrete purchase offer that NEUWOGES has submitted information on came from Felske Immobilien, which apparently offered a price of EUR [...] per m², resulting in a total purchase price of EUR [...] ⁽¹⁰⁷⁾. This offer was well over EUR 1 million lower than the price that a MEO in the position of NEUWOGES would have estimated.
- (c) Third, NEUWOGES, in estimating the profits that it expected to make from the general management contract, erroneously calculated profits only up to and including 2027. However, as the duration of the general management contract was 30 years from the end of the modernisation works (i.e. 30 years from the beginning of 1999), the calculation should have included profits up to and including 2028. Correcting the estimate in this way would add to the value of the sale-and-lease-back transaction.

⁽¹⁰⁷⁾ Submission 97/97 to NEUWOGES' supervisory board of 17 April 1997, p. 3.

(d) In calculating the cash value of the future ground rent payments by BAVARIA to NEUWOGES, it was assumed, for the sake of simplicity, that the cost of living would not change and that the payments would therefore not need to be adjusted. It is more realistic, however, to assume that the cost of living will generally rise, so that the payments due in the future will probably turn out to be higher than assumed. This would again lead to an increase in the value of the contract.

(170) In light of these considerations, it must be concluded that preferring the sale-and-lease-back transaction to attempting an outright sale was economically reasonable.

7.3.3. Conclusion

(171) After comparing the value of the sale-and-lease-back transaction for NEUWOGES with the value of possible alternative actions, it must be concluded that the transaction was such that a MEO would also have entered into it.

7.4. BENCHMARKING

(172) After having determined that choosing the sale-and-lease-back transaction over other alternatives was behaviour that a MEO would reasonably have engaged in, the Commission also examined, as a precautionary measure, whether the transaction corresponded to other contracts in evidence at the relevant time in the relevant market and whether there were other indications to undermine the Commission's conclusion that the sale-and-lease-back transaction was in keeping with the principle of conduct by a MEO.

(173) The available information on comparable transactions relates to sale-and-lease-back agreements concluded by BAVARIA around the same time as the adoption of the measure. These contracts can indicate whether the sale-and-lease-back transaction in question was of a type that was also chosen by other market participants, including private undertakings, thereby pointing towards market conformity (section 7.4.1). In addition, the limited bidding process carried out by NEUWOGES and a comparison with other financing transactions can shed some light on the market conformity of the transaction in question (sections 7.4.2 and 7.4.3).

7.4.1. Comparison contracts

(174) Contracts related to three comparable transactions ([...]) were submitted for the purpose of comparison. However, only the [...] and [...] contracts date from around the same time as the conclusion of the sale-and-lease-back transaction between BAVARIA and NEUWOGES and can thus be taken into account. It must first be noted that both of these transactions differ from the transaction in question with respect to duration, indexation of the fixed leasing payment, and modernisation. NEUWOGES refers in particular to the difference in the indexation rate ([...]: 1,5 % per year; [...]: adjustment to changes in the cost of living) to prove that the general management contract contained provisions that were not common market practice at the relevant time (1997/98).

(175) BAVARIA indicates that the [...] and [...] transactions were examples of the implementation of its 'real-estate leasing model'⁽¹⁰⁸⁾, which suggests that the provisions of these contracts were established on the basis of calculations similar to those underlying the NEUWOGES/BAVARIA sale-and-lease-back transaction.

(176) As discussed above (see recital 131), NEUWOGES could apparently choose the contract parameters freely within the framework of the leasing model offered by BAVARIA. This means that NEUWOGES could have chosen a lower indexation or a higher deduction for costs. The consequence would, of course, have been a lower upfront cash payment. It can be assumed that the same was true for [...] and [...].

(177) Since the contract partners were apparently free to choose the precise parameters of their transaction within the framework of the model offered by BAVARIA, it does not seem central to the market conformity of the NEUWOGES/BAVARIA sale-and-lease-back transaction whether the parameters chosen by NEUWOGES were the same as those chosen by the parties to the [...] and [...] transactions. These choices simply reflected strategic business decisions by the parties involved. What is more relevant is the fact that all these transaction were based on the same transaction model.

(178) To the extent that the [...] and [...] contracts are based on the same underlying calculation model — which in the light of the available information there is no reason to doubt — they point towards the market conformity of the transaction model underlying the NEUWOGES transaction as well. In this context it is significant that the 'real-estate leasing model' was apparently chosen by both public ([...]) and private ([...]) undertakings, and was offered both to undertakings wishing to qualify for debt relief under the Inherited Debt Support Law and to parties that did not come within the provisions of that law.

⁽¹⁰⁸⁾ Germany's submission of 11 July 2008, pp. 10-11.

7.4.2. Bidding process

7.4.2.1. Background

- (179) As already indicated, NEUWOGES did not undertake a fully-fledged, open, transparent, unconditional and non-discriminatory tender with a view to privatising the buildings eventually sold to BAVARIA. However, NEUWOGES did initially solicit offers from 72 potential buyers. NEUWOGES claims that it chose the recipients more or less at random and that the selection could not be considered as representative of the entire market. Further contacts resulted after these initial calls for expression of interest were sent out, inter alia, with BAVARIA, which had not been among the recipients of the initial letter.

7.4.2.2. Result of the bidding process

- (180) Of the unknown number of offers received, five were considered 'useable' ⁽¹⁰⁹⁾. Of these, two were nevertheless rejected because the potential buyers could not present a full offer 'because of time constraints'. Two were furthermore rejected for economic reasons. The fifth offer, from Felske Immobilien was rejected because the price offered was considered too low (Felske had offered EUR [...] per m², resulting in a total buying price of EUR [...]). In addition to these five offers, three further bids were made, coming from BAVARIA and two other unsolicited bidders. While negotiations were also initiated with one of the other two unsolicited bidders, this bid was eventually also rejected for unspecified economic reasons ⁽¹¹⁰⁾.
- (181) Once the final negotiations had been concluded, NEUWOGES' board had to approve the contracts. When presenting the contracts to the board, the management argued that a higher sale price could not be obtained because the contracts concerned only a lease of the land (as opposed to an outright sale), BRG would be hired to carry out the modernisation works, and NEUWOGES would continue to manage the buildings for a further 30 years ⁽¹¹¹⁾. When asked about the difference from the 1997 valuation, the management again stated that a higher price could not be achieved for this transaction ⁽¹¹²⁾.

7.4.2.3. Assessment

- (182) While this bidding process cannot be classified as an open, transparent, non-discriminatory and unconditional tender, it nevertheless provides some indication of what offers were available on the market. In this regard it is also significant that apparently a number of unsolicited bids were received, showing that potential buyers not among the 72 originally contacted companies also had an opportunity to learn of the process and participate.
- (183) The assessment of the bids by NEUWOGES indicates that NEUWOGES perceived BAVARIA's bid to be the best available on the market at the relevant time (1997/98). NEUWOGES' argument that at least the Felske bid was actually better is unsustainable. While it is true that the price apparently offered by Felske (EUR [...]) was higher than the upfront payment eventually made by BAVARIA (EUR [...]), it must be pointed out that the sale-and-lease-back transaction has to be assessed as a whole and that its total value (EUR [...]) was higher than the price offered by Felske.
- (184) In this light, it can be stated that, even though the bidding process carried out was not such as to constitute proof in itself that BAVARIA's bid was the best available on the market, it points in this direction. In any event, the limited bidding process provides no substantiated indication that a better offer was available to NEUWOGES at the relevant time (1997/98).

7.4.3. Other types of transactions available at the relevant time

7.4.3.1. Assessment framework

- (185) It is helpful to assess the transaction in question against different, but generally similar, types of transactions offered on the market at the relevant time (1997/98).
- (186) The transaction in question is a typical sale-and-lease-back transaction. Sale-and-lease-back agreements are, by nature, *financing transactions*. By buying a property from the lessee, the lessor provides the lessee with liquidity and/or finances major investments, such as the modernisation of old buildings. In order to continue using the property, for commercial or other purposes, the lessee then leases the property back, thereby (fully or partly) paying back the lessor's investment over the duration of the lease contract.

⁽¹⁰⁹⁾ Submission 97/97 to NEUWOGES' supervisory board of 17 April 1997, p. 2.

⁽¹¹⁰⁾ See Submission 110/97 to NEUWOGES' supervisory board of 30 October 1997, p. 3.

⁽¹¹¹⁾ Submission 114/97 to NEUWOGES' supervisory board of 12 December 1997, p. 3.

⁽¹¹²⁾ Minutes of NEUWOGES' supervisory board Meeting of 16 December 1997, p. 5.

- (187) Being a financing transaction, a sale-and-lease-back agreement has a certain similarity with bank loans and mortgages. There are, however, some important differences that need to be kept in mind. A sale-and-lease-back transaction enables the seller/lessee to finance major investments and gain instant liquidity without having to rely on own capital. This means that own capital and the additional liquidity obtained are available for other investments, or that the lessee can finance investments even where a traditional loan would not be available because of the lack of own capital or a high degree of indebtedness. As the buyer/lessor has to re-finance its own initial investment and make a profit, the leasing rate is typically somewhat higher than the interest rate on a comparable bank loan (as explained in further detail in the following section). At the end of the lease contract, the lessee either has to repurchase the property or it remains in the ownership of the lessor and is available for further use. This means that the leasing rate depends on the residual value of the property at the end of the lease contract concluded between the two parties. As the residual value is often difficult to predict, especially in the case of long-term leases, it represents a risk factor for the lessor that is reflected in the leasing rate. No such risk is involved in traditional bank loans, and only to a certain degree in mortgages.
- (188) The consequence is that the leasing rates and the interest rates for loans/mortgages are not entirely comparable. By comparing the leasing rate for the transaction in question with the average interest rates on loans/mortgages available at the relevant time (1997/98), it is not possible to determine precisely whether the leasing rate charged was in line with the market conditions at the relevant time (1997/98). It is, however, possible to say whether the leasing rate was so high that it appears that no MEO would reasonably have engaged in the transaction.

7.4.3.2. Assessment

- (189) In the transaction in question, the leasing rate was initially set at [...] % p.a. of the total investment volume. Due to the indexation of the amount owed by [...] % p.a., the leasing rate will rise to [...] % at the end of the contract, resulting in an average leasing rate of [...] % p.a. For the sake of comparison, if NEUWOGES had chosen not to index the leasing rate, it would have been set at [...] % p.a. over the entire duration of 30 years. The 'premium' is then the cost of choosing lower leasing rates at the beginning, and higher leasing rates towards the end, of the contract, rather than stable rates throughout.
- (190) It must first be pointed out that Rostock Regional Court assessed the leasing rate against interest rates for other transactions. It observed that the development of the interest rates on mortgages over a time span of 30 years was difficult to predict, but that interest rates of over 10 % could be expected in periods of high interest rates. It observed that the average leasing rate charged to NEUWOGES could not, then, be seen as being out of line with market terms.
- (191) Only fairly general data is available for comparison. Of all the data gathered by the German Bundesbank for January 1998 (when the transaction in question was concluded), two types of interest rates can be considered relevant. First, the interest rates for 'mortgage loans secured by residential real estate with interest rates fixed for 10 years' are of interest, since NEUWOGES too would use residential real estate as collateral for a loan (regardless of whether or not such a loan would meet all the formal conditions of a mortgage). Second, the interest rates for 'long-term fixed-rate loans to enterprises and self-employed persons, EUR 500 000 and over but less than EUR 5 million' could also be suitable for a comparison, since NEUWOGES can be considered as an enterprise (while mortgages are usually taken out by private individuals who actually live in the property themselves rather than renting it out).
- (192) According to the Bundesbank, in January 1998 German mortgage loans with a 10-year fixed interest rate had an average interest rate of 6,40 % p.a. At that time, interest rates for this type of loan normally spanned a range of 6,17 % p.a. to 6,97 % p.a. For long-term fixed-rate loans, the average interest rate in January 1998 was 6,35 % p.a. and spanned a range of 5,55 % p.a. to 7,73 % p.a. The Bundesbank does not specify the average duration of a 'long-term' loan. However, it can be assumed that it would not be more than 10 years and would probably be shorter than that⁽¹¹³⁾.

⁽¹¹³⁾ Banks usually prefer to use variable-interest loans as this reduces the interest-rate risk they run. If they grant fixed-interest loans, it is in their interests to limit the duration of the contract in order to reduce this risk. For loans to enterprises, it is common to use revolving loan contracts where, upon expiry of the initial loan contract, a new contract is automatically started (provided that the firm's creditworthiness has not deteriorated) with a revised interest rate (reflecting the market conditions at that time). In addition to interest-rate risk, banks also bear credit risk, and this is a further reason for limiting the duration of loan contracts with enterprises (since the amounts involved are significantly higher than in a mortgage contract, which usually has a duration of 20 to 30 years).

(193) A comparison of the leasing rate paid by NEUWOGES with the available interest rates from the Bundesbank for loans that were concluded in the same time period (i.e. January 1998) must take the following elements into account:

- The average yearly leasing rate over the 30-year contract period is [...]%. However, as discussed above, this rate is the result of NEUWOGES' choosing to pay a lower leasing rate at the beginning of the contract period, offset by a higher leasing rate later on. This choice comes at a cost, because if NEUWOGES had opted for a flat leasing rate from the start it would have had to pay a rate of only [...]% per year⁽¹¹⁴⁾. The figures from the Bundesbank are for fixed-rate loans, meaning that the interest rate is equal in each of the years. If it is assumed that NEUWOGES would have been in a position to negotiate a loan with similar payment conditions (i.e. lower interest payments at the start and higher payments towards the end), this would also have come at a cost (for the same reasons as for BAVARIA)⁽¹¹⁵⁾. The Bundesbank interest rates should therefore be compared with the flat leasing rate of [...]%.
- The leasing rate has been fixed for a period of 30 years. Although it is indexed each year, it was perfectly possible, as early as at the start of the contract, to calculate the average leasing rate for the duration of the contract. The Bundesbank interest rates for mortgages are fixed for only 10 years (as explained above, it is not known for which period the interest rates for enterprises are fixed, but it can be assumed that the period is of no more than 10 years). The most suitable benchmark would be interest rates fixed for 30 years, but these figures are not published by the Bundesbank. In general, fixed-interest rate loans become more expensive the longer their duration. For example, the Bundesbank figures for January 1998 show that a mortgage with a 5-year fixed rate had an average interest rate of 5,85 %, compared to 6,40 % for a loan with a 10-year fixed rate. Therefore, it can be safely assumed that the interest on a fixed-interest loan of 30 years' duration would have been considerably higher than the Bundesbank averages of 6,35 % and 6,40 %.
- The Bundesbank figures provide both an average rate and a range of interest rates based on a large number of German loan contracts concluded in January 1998. The leasing rate that applied to NEUWOGES implicitly reflects the inherent risk of the transaction for BAVARIA. BAVARIA's greatest exposure was to credit risk, i.e. the risk that NEUWOGES would go bankrupt or otherwise not fulfil the obligation to make the required leasing payments. Similarly, a bank would have made an assessment of NEUWOGES' creditworthiness before granting a loan. Clients with a lower creditworthiness (or a higher credit risk for the bank) are usually charged a higher interest rate to compensate for the additional risk⁽¹¹⁶⁾. As discussed above (see section 7.3.1), NEUWOGES had a limited ability to obtain new loans because of its relatively high degree of indebtedness and the fact that its own capital was tied up in other investment projects. If, however, a bank had been prepared to grant a loan to NEUWOGES, it would have taken these elements into account when setting the interest rate. Loans to companies with a relatively high level of debt and a low own-capital contribution to the investment have higher interest rates. Because of this, any comparison of the leasing rate paid by NEUWOGES and the interest rates on loans available on the market should focus on the higher end of the Bundesbank interest-rate range⁽¹¹⁷⁾.
- As mentioned above, a leasing company has to refinance its initial investment (in this case mainly the purchase price for the apartment blocks and the costs of modernisation). The interest rate it has to pay for its own refinancing will depend on several factors, such as its size, its level of debt, the property in its portfolio, etc. In any event, this interest rate is just the starting point, as the leasing company (BAVARIA) also needs to be compensated for the risks it bears. These can include interest-rate risk (the risk that it will have to refinance its investment on the basis of a variable interest rate, while the lease payments have a fixed rate), credit risk (the possibility, as discussed above, that NEUWOGES will go bankrupt and that BAVARIA will not be able to

⁽¹¹⁴⁾ The reason for this premium (i.e. the higher average leasing rate compared to a fixed rate from the start) is that BAVARIA agreed to postpone part of the leasing payments to the later years of the contract period. If it had received those payments without this 'delay', it could have invested that money and earned a return on it or repaid its own loan and hence saved on interest. Postponing part of the payments thus entails a cost for BAVARIA, which is transferred to NEUWOGES via a higher average leasing rate.

⁽¹¹⁵⁾ This would no longer be a 'true' fixed rate loan (i.e. with equal yearly interest rates) but a loan where the different yearly interest rates are fixed in advance (hence, it is also not a variable rate loan).

⁽¹¹⁶⁾ If the risk is considered too high, the client's application for a loan will normally be refused. If the risk is deemed acceptable, a higher interest rate is charged and additional measures can be taken. This can include requiring additional collateral, granting a lower amount than requested, or adding conditions to the loan contract that enable the bank to monitor the borrower's financial situation.

⁽¹¹⁷⁾ See also the Pestel study cited above, published in June 1996, which assumed that housing companies in East Germany could obtain loans on the open capital market at 7,5 % interest.

recover the lease payments still due), and residual value risk (the uncertainty about the value of the property after the lease contract has expired). The leasing company is also likely to have certain overhead costs which would also be reflected in the leasing rate⁽¹¹⁸⁾. Finally, the leasing company also intends to make a profit and will take account of this factor in setting the leasing rate⁽¹¹⁹⁾. Even if BAVARIA had been in a position to refinance its investment at an interest rate lower than that which NEUWOGES would have been charged for a bank loan, the refinancing interest rate would have had to be increased in the light of these different elements (risk premium, costs and profit) in order to obtain the applicable leasing rate, which could have ended up being higher than the interest rate on a traditional loan.

- (194) Taking into account all of the above elements, a leasing rate of [...] % p.a. for a fixed leasing payment (or even of [...] % for a leasing payment indexed at [...] %, although this figure appears less suitable for comparison purposes) appears rather reasonable when compared to the Bundesbank figures for loans. The Bundesbank figures should be adjusted to reflect, for example, a fixed-rate duration of 30 years. While the correction required to arrive at a suitable benchmark cannot be precisely quantified, the difference between the average interest rates for loans and mortgages and the leasing rate seems sufficient to conclude that there are no indications that the BAVARIA leasing rate was too high. Accordingly, the Commission concludes that the leasing rate applied by BAVARIA was in line with market conditions at the relevant time (late 1997/early 1998).

7.4.4. Conclusion

- (195) The available information indicates that the NEUWOGES/BAVARIA deal was within the range of transactions that a MEO would reasonably have engaged in. The comparison contracts, the bidding process, and the comparison with other financing instruments all suggest that the transaction conformed to market conditions at the time and that the BAVARIA model was not overpriced.

7.5. SUPPLEMENTARY ASSESSMENT: REMAINING STATE AID ELEMENTS AND COMPATIBILITY WITH THE INTERNAL MARKET

- (196) The Commission's primary analysis thus demonstrates that NEUWOGES' decision to enter into the sale-and-lease-back transaction was in line with the MEO principle, which means that the transaction did not confer an advantage on BAVARIA and that no aid was therefore granted to BAVARIA. Nevertheless, the Commission has also examined whether a different result — namely that an advantage had in fact been granted to BAVARIA by NEUWOGES — would have necessarily resulted in finding that the transaction amounted to state aid incompatible with the internal market. On the hypothetical assumption that NEUWOGES had not complied with the MEO principle and that an advantage had thus been granted to BAVARIA, the Commission therefore examined whether the measures amounted to state aid in favour of BAVARIA and whether this aid could be declared compatible with the internal market.

7.5.1. Remaining state aid elements

7.5.1.1. Undertaking

- (197) Public funding granted to an entity can be classified as state aid only if that entity is an 'undertaking' within the meaning of Article 107(1) TFEU. The Court of Justice has consistently defined an undertaking as any entity engaged in an economic activity⁽¹²⁰⁾. An economic activity is any activity that consists in offering goods and services on the market⁽¹²¹⁾.
- (198) BAVARIA is involved in a series of economic activities, such as commercial investment in real estate and the leasing of such real estate to commercial and private customers. BAVARIA is thus an undertaking within the meaning of Article 107(1) TFEU.

⁽¹¹⁸⁾ Such costs would come on top of the costs charged by a bank when granting a loan. This is because, when the leasing company refinances its investment, it also has to pay for the bank's costs (and takes account of this factor in setting its leasing rate). It also has to bear its own overhead costs.

⁽¹¹⁹⁾ In the loan scenario, a client contributes to the bank's profit via the interest rate. In the leasing scenario, the client in essence contributes both to the bank's profit (as the leasing company refinances its investment with the bank, and then passes on this cost to the lessee) and to that of the leasing company itself. The fact that companies are willing to pay these additional costs indicates that the services provided by leasing companies have an added value for lessees.

⁽¹²⁰⁾ Joined Cases C-180/98 to C-184/98 *Pavel Pavlov and Others v Stichting Pensioenfonds Medische Specialisten* [2000] ECR I-6451, paragraph 74.

⁽¹²¹⁾ Case C-118/85 *Commission v Italy* [1987] ECR 2599, paragraph 7.

7.5.1.2. Use of state resources and imputability

- (199) The measure must be imputable to the State and be financed from state resources. According to the case law of the Court of Justice in *Stardust Marine* ⁽¹²²⁾, state aid that is not financed directly from the national budget can fulfil this criterion if funds are subject to the control of the State and the decision to transfer these funds is imputable to the State.
- (200) NEUWOGES is 100 % owned by the City of Neubrandenburg and is thus a public undertaking within the meaning of Article 2(b) of Commission Directive 2006/111/EC ⁽¹²³⁾, as referred to by the Court in the *Stardust Marine* judgment. The City of Neubrandenburg holds all the shares in NEUWOGES and, being the sole shareholder, can exercise significant control over the Supervisory Board and in the general meeting of shareholders. Therefore, the Commission concludes that the City is able to control the use of NEUWOGES' funds. Consequently, the sale-and-lease-back transaction involved state resources.
- (201) As regards imputability to the State, the Commission notes that the available information indicates that the City of Neubrandenburg was significantly involved in the conclusion of the sale-and-lease-back transaction. Entering into this transaction required the approval of NEUWOGES' Supervisory Board, whose members acted on behalf of the City. The records also show that the Supervisory Board was actively involved in negotiating the contracts. The Commission therefore finds that the conclusion of the sale-and-lease-back contract is imputable to the State.

7.5.1.3. Selectivity

- (202) Under Article 107(1) TFEU, a measure counts as state aid only if it favours 'certain undertakings or the production of certain goods'. Hence, only measures granting undertakings a selective advantage come under the heading of state aid.
- (203) Since the measure in question was a bilateral transaction between NEUWOGES and BAVARIA, any advantage granted by NEUWOGES to BAVARIA would have been selective, in that no other undertakings would have had access to it.

7.5.1.4. Distortion of competition and effect on trade

- (204) Public support to undertakings amounts to state aid within the meaning of Article 107(1) TFEU only if it 'distorts or threatens to distort competition' and only insofar as it 'affects trade between Member States'. A measure granted by a State is considered to distort or to threaten to distort competition when it is liable to improve the competitive position of the recipient compared to other undertakings with which it competes ⁽¹²⁴⁾. Distortion of competition is thus assumed to take place as soon as a State grants a financial advantage to an undertaking in a liberalised sector where there is, or could be, competition.
- (205) The case-law of the European Courts has established that any grant of aid to an undertaking exercising its activities in the internal market can be liable to affect trade between Member States ⁽¹²⁵⁾.
- (206) BAVARIA competes for investors and investment opportunities with other real-estate funds and corporate investors from Germany and other Member States of the Union. A financial advantage granted to BAVARIA would strengthen that undertaking's competitive position and would therefore be liable to distort competition. Since the market for real-estate investments is Union-wide, any financial advantage for BAVARIA would strengthen the latter's market position in comparison with its competitors from other Member States, thereby having an impact on trade between Member States.

7.5.1.5. Conclusion

- (207) Assuming that, contrary to the Commission's primary conclusion outlined above, the sale-and-lease-back transaction did not comply with the rational MEO principle and therefore granted an advantage to BAVARIA, it would have to be concluded that the sale-and-lease-back transaction involved state aid. Consequently, it must be assessed whether, on this hypothesis, the state aid could be considered as being compatible with the internal market.

⁽¹²²⁾ Case C-482/99 *France v Commission (Stardust Marine)* [2002] ECR-I 4397.

⁽¹²³⁾ Commission Directive 2006/111/EC of 16 November 2006 on the transparency of financial relations between Member States and public undertakings as well as on financial transparency within certain undertakings (OJ L 318, 17.11.2006, p. 17).

⁽¹²⁴⁾ Case 730/79 *Philip Morris v Commission* [1980] ECR 2671, paragraph 11; Joined Cases T-298/97, T-312/97, etc. *Alzetta Mauro and others v Commission* [2000] ECR II-2325, paragraph 80.

⁽¹²⁵⁾ Case 730/79 *Philip Morris Holland BV v Commission of the European Communities* [1980] ECR 2671, paragraphs 11 and 12; Case T-214/95 *Het Vlaamse Gewest (Flemish Region) v Commission of the European Communities* [1998] ECR II-717, paragraphs 48-50.

7.5.2. Compatibility with the internal market pursuant to Article 107(3)(c) TFEU

- (208) Under Article 107(3)(c) TFEU, an aid measure may be considered compatible with the internal market where it 'facilitate[s] the development of certain economic activities or of certain economic areas, where [it] does not adversely affect trading conditions to an extent contrary to the common interest'. The application of Article 107(3)(c) requires the Commission to weigh the positive and desired effects of an aid measure against the adverse effect on trading conditions that results from its implementation.
- (209) For an aid measure to withstand that test, it must comply with five cumulative conditions. First, the aid measure must serve a well-defined objective of common interest. Second, it must be an appropriate instrument for achieving that objective. Third, it must be necessary and have an incentive effect. Fourth, it must be proportionate. Fifth, it must not affect trading conditions to an extent contrary to the common interest.

7.5.2.1. Objective of common interest

- (210) Under Articles 3 and 174 TFEU, economic and social cohesion is a Union objective. Strengthening economic and social cohesion implies the improvement of the urban environment and the quality of life of urban dwellers. Cohesion policy can help create sustainable communities by ensuring that economic, social and environmental issues are tackled through integrated strategies for renewal, regeneration and development in both urban and rural areas. This can be accomplished in several ways⁽¹²⁶⁾.
- (211) The Commission observes that NEUWOGES' statutory purpose is to secure a 'sufficient housing supply' in the region in which it is active. The Commission also observes that, in concluding the sale-and-lease-back transaction, NEUWOGES pursued certain public policy objectives. NEUWOGES explains that:
- in the 1990s, after German reunification, it was an important political project to bring housing conditions in East Germany into line with those in West Germany, with the consequence that buildings in East Germany were hurriedly privatised and modernised, regardless of whether or not this made economic sense;
 - the efforts to privatise and modernise the buildings that were the subject of the sale-and-lease-back transaction were also directed at enhancing the future prospects of the City of Neubrandenburg: by offering people high-quality, affordable housing and by privatising it (as BAVARIA was obliged to do), NEUWOGES hoped to make Neubrandenburg more attractive to its citizens.
- (212) Finally, the Commission observes that BAVARIA accepted the obligation to attempt to sell a certain number of the apartments to the current tenants. In doing so, BAVARIA could not ask for a price freely determined by the market, but rather had to respect certain price ceilings⁽¹²⁷⁾. The contract imposing these conditions thus granted a certain advantage to the current tenants of the buildings in question.
- (213) If the sale-and-lease-back transaction between NEUWOGES and BAVARIA were, in actual fact, classified as state aid, which it is not, this aid would have been granted in pursuit of the policy objectives listed above. Supplying a region with sufficient housing, helping to achieve a national public policy objective (bringing the housing conditions in East Germany into line with those in West Germany following reunification), enhancing the future prospects of the City of Neubrandenburg by offering its population attractive and affordable housing (including by favouring the current tenants of the buildings in question) all qualify as well-defined objectives of common interest. The Commission therefore considers that the measure is to be regarded as pursuing an objective of common interest.

7.5.2.2. Appropriateness of the measures

- (214) It is not disputed that the sale-and-lease-back contract concluded by NEUWOGES and BAVARIA achieved the desired objectives, in that the transaction ensured that the buildings bought by BAVARIA were comprehensively modernised, privatised and offered to the current tenants at a capped price, and that this led to the increased supply of quality housing in the region, thereby enhancing the City of Neubrandenburg's future prospects.

⁽¹²⁶⁾ Commission Decision C(2011) 4940 final of 5 October 2011 in Case SA.31877 – The Netherlands: Land sale and housing development Apeldoorn (OJ C 343, 23.11.2011, p. 11), recitals 47 and 48.

⁽¹²⁷⁾ See Part V, Section 3(2) of the land-lease and sale contract.

- (215) In seeking a buyer for the buildings and evaluating its options, NEUWOGES took a series of steps that, in effect, ensured that, if the sale-and-lease-back transaction involved any aid, this would be limited to the amount necessary to achieve the desired objectives. In particular, NEUWOGES carried out a limited bidding process, negotiated the terms of the transaction with BAVARIA over several months, and was finally convinced that the transaction represented the best offer on the market. There is, then, no indication that, even if aid was involved in the sale-and-lease-back transaction, this aid exceeded the minimum required. The analysis above (see section 7.3) comparing the sale-and-lease-back transaction to various alternatives (such as a loan-based modernisation of the buildings or an outright sale) demonstrated that no alternative was available that would have achieved the same objectives without aid being granted or with a lower amount of aid being granted. The sale-and-lease-back transaction and any aid it may have contained were thus appropriate instruments for achieving the objectives of common interest.

7.5.2.3. Necessity and incentive effect

- (216) Assuming that the sale-and-lease-back transaction involved state aid, it must further be examined whether this aid had an incentive effect. NEUWOGES and BAVARIA negotiated the terms of the transaction over several months. It appears that BAVARIA would not have entered into a transaction that did not fit in with its 'real-estate leasing model'. If the transaction that was eventually concluded, which was based on BAVARIA's 'real-estate leasing model', involved state aid, then there is no doubt that, without this aid, BAVARIA would not have engaged in the transaction.

7.5.2.4. Proportionality

- (217) The Commission has already indicated that the policy objectives pursued by NEUWOGES in entering into this transaction must be viewed as being important. The modernisation and privatisation of the buildings, including their sale at a capped price to the tenants, made an important contribution to improving economic and social cohesion within the Union. At the same time, the amount of aid in favour of BAVARIA contained in the sale-and-lease-back transaction — if any — was, at most, limited — a state of affairs that also limited any distortion of competition by the measure. In this light, any aid that may have been contained in the sale-and-lease-back transaction between NEUWOGES and BAVARIA was proportionate to the objective pursued.

7.5.2.5. No effect on trading conditions that is contrary to the common interest

- (218) It should again be pointed out that the amount of aid in favour of BAVARIA involved in the sale-and-lease-back transaction — if any — was, at most, limited. The effect of the measure on trading conditions was thus also limited. While any aid contained in the sale-and-lease-back transaction would have improved the competitive position of BAVARIA, which was at least potentially in competition with other undertakings (including undertakings from other Member States), the extent of this effect depends on the amount of aid received. Since BAVARIA's competitive position would thus have been only marginally improved, it can be concluded that the sale-and-lease-back transaction, even if it contained aid, did not affect trading conditions to a degree contrary to the common interest.

7.5.3. Conclusion concerning the remaining state aid elements and compatibility with the internal market

- (219) On the basis of the reasons stated in section 7.5.2, the Commission has concluded that, if the sale-and-lease-back transaction granted an advantage to BAVARIA, it would amount to state aid within the meaning of Article 107(1) TFEU. The Commission further finds, however, that any state aid contained in the transaction would be compatible with the internal market under Article 107(3)(c) TFEU.

7.6. CONCLUSION REGARDING THE EXISTENCE OF AID AND COMPATIBILITY WITH THE INTERNAL MARKET

- (220) On the basis of the analysis of the value of the sale-and-lease-back transaction for NEUWOGES, the comparison with possible alternative transactions, and the examination of the transaction's conformity to market practices, it can be concluded that the transaction complies with the MEO principle. In concluding the sale-and-lease-back transaction, NEUWOGES' actions were such as a MEO would have chosen to engage in. Crucially, it is apparent neither that an economically more attractive option was available, nor that, in the light of the available benchmarks and of the other offers that had emerged from the bidding process, the conditions of the sale-and-lease-back transaction at the relevant time (1997/98) were out of line with market conditions.

- (221) It must therefore be concluded that the transaction with NEUWOGES did not confer an advantage on BAVARIA, since NEUWOGES' behaviour corresponded to that of a MEO. As the measure in question did not grant an advantage, it does not fulfil one of the conditions for being classified as state aid and does not, therefore, constitute state aid within the meaning of Article 107(1) TFEU.
- (222) In addition to the primary finding that the sale-and-lease-back transaction did not confer an advantage on BAVARIA and did not, therefore, involve state aid, the Commission reaches the additional conclusion that if the sale-and-lease-back transaction did, however, confer an advantage on BAVARIA, the transaction would indeed amount to state aid. This state aid would, however, be compatible with the internal market under Article 107(3)(c) TFEU,

HAS ADOPTED THIS DECISION:

Article 1

The legal transaction concluded on 21 January 1998 between Neubrandenburger Wohnungsgesellschaft mbH, Bavaria Immobilien Trading GmbH & Co, Immobilien Leasing Objekt Neubrandenburg KG and Bavaria Immobilien Beteiligungsgesellschaft mbH & Co. Objekte Neubrandenburg KG in the form of a land-lease and sale contract and a general management contract does not constitute state aid within the meaning of Article 107(1) TFEU.

Article 2

If, however, the transaction concluded on 21 January 1998 between Neubrandenburger Wohnungsgesellschaft mbH, Bavaria Immobilien Trading GmbH & Co, Immobilien Leasing Objekt Neubrandenburg KG and Bavaria Immobilien Beteiligungsgesellschaft mbH & Co. Objekte Neubrandenburg KG in the form of a land-lease and sale contract and a general management contract does constitute state aid within the meaning of Article 107(1) TFEU, this aid is compatible with the internal market within the meaning of Article 107(3)(c) TFEU.

Article 3

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 16 September 2014.

For the Commission
Joaquín ALMUNIA
Vice-President
