

**COMMISSION DECISION (EU) 2016/154****of 22 July 2015****on State aid SA.13869 (C 68/2002) (ex NN 80/2002) — reclassification as capital of the tax-exempt accounting provisions for the renewal of the high-voltage transmission network (RAG) implemented by France in favour of EDF***(notified under document C(2015) 4959)***(Only the French 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 <sup>(1)</sup>,

Having called on interested parties to submit their comments pursuant to that Article <sup>(2)</sup>,

and having regard to their comments,

Whereas:

- (1) By decision of 16 October 2002 the Commission initiated the formal investigation procedure under Article 108(2) of the TFEU (‘the opening decision’) into the advantage resulting from the non-payment by Établissement Public à Caractère Industriel et Commercial ‘Électricité de France (E.D.F.), Service National’ (‘EDF’, which became the public limited company Électricité de France SA towards the end of 2004) of the corporation tax due, when it restructured its balance sheet in 1997, on some of the accounting provisions created free of tax for the renewal of the high-voltage transmission network (*réseau d’alimentation général* — RAG) and reclassified as capital.
- (2) The French authorities, in their comments submitted to the Commission by letter dated 11 December 2002, denied that EDF had received a tax concession and argued that the additional capital contribution corrected an under-capitalisation and was therefore justified.
- (3) By letter dated 21 January 2003, the Commission forwarded to France the only observations received from one interested third party and invited the French authorities to submit their comments. France did not present any comments on these observations.
- (4) A technical meeting between the Commission and the French authorities was held on 12 February 2003, followed by a request for information by the Commission dated 4 July 2003.
- (5) On 11 November 2003, France provided additional information. On 17 November 2003, a further technical meeting was held between the Commission, the French authorities and representatives of EDF. The French authorities provided additional information on 20 November 2003.
- (6) By decision of 16 December 2003 <sup>(3)</sup>, the Commission declared the aid measure in favour of EDF incompatible with the internal market and requested recovery of the aid with interest. The aid was repaid in February 2004.

<sup>(1)</sup> With effect from 1 December 2009, Articles 87 and 88 of the EC Treaty have become Articles 107 and 108, respectively, of the Treaty on the Functioning of the European Union (‘TFEU’). The two sets of provisions are, in substance, identical. For the purposes of this Decision, references to Articles 107 and 108 of the TFEU should be understood as references to Articles 87 and 88, respectively, of the EC Treaty, where appropriate. The TFEU also introduced certain changes in terminology, such as the replacement of ‘Community’ by ‘Union’, ‘common market’ by ‘internal market’ and ‘Court of First Instance’ by ‘General Court’. The terminology of the TFEU is used throughout this Decision.

<sup>(2)</sup> OJ C 280, 16.11.2002, p. 8.

<sup>(3)</sup> OJ L 49, 22.2.2005, p. 9.

- (7) By judgment of 15 December 2009, the General Court annulled the Commission's decision <sup>(1)</sup>. France repaid to EDF the amount of aid which had been reimbursed in 2004.
- (8) By judgment of 5 June 2012, the Court of Justice rejected the appeal lodged by the Commission against the judgment of the General Court <sup>(2)</sup>.
- (9) By decision of 2 May 2013, the Commission extended the formal investigation procedure ('the extension decision') <sup>(3)</sup>.
- (10) The French authorities submitted their comments to the Commission on 1 July 2013.
- (11) By letter dated 13 August 2013, the Commission forwarded to France the observations dated 29 July 2013 received from one interested third party, namely EDF, and invited the French authorities to submit their comments. On 11 October 2013, France submitted its comments on the observations by EDF.
- (12) On 18 October 2013, EDF sent to the Commission a study prepared by a consultant (Oxera) dated 15 October 2013. On 22 October 2013, the Commission sent this study to France and invited the French authorities to submit their comments. However, the invitation was subject to the reservation that the study had been submitted more than two and a half months after the deadline set by the extension decision and, furthermore, it had been drawn up after the decision to invest in EDF on which France was relying. On 6 November 2013, France submitted its comments on the study.
- (13) A meeting between the Commission and the French authorities was held on 14 November 2013. On 15 November 2013, the Commission asked for further information and clarifications on the observations by France, which were submitted on 23 December 2013.
- (14) On 22 November 2013, EDF sent to the Commission a legal opinion commissioned by EDF further to and in support of its observations of 29 July 2013.
- (15) At the request of EDF, a meeting with the Commission in the presence of the French authorities was held on 12 March 2014.
- (16) On 13 May 2014, the Commission requested comments on the legal opinion submitted by EDF and clarifications and additional information from France, which the latter provided by letter dated 19 June 2014.

## 1. DETAILED DESCRIPTION OF THE MEASURE

### 1.1. THE BENEFICIARY: EDF, CHANGES IN ITS STATUS AND ITS CAPITAL

- (17) EDF was set up by Act No 46-628 of 8 April 1946 on the nationalisation of electricity and gas ('Act No 46-628'), which, in its first article, nationalised the production, transport, distribution, and import and export of electricity in France. This Act entrusted the management of the nationalised electricity enterprises to a national public industrial and commercial establishment called 'Électricité de France (E.D.F.), Service National'.
- (18) Article 16 of Act No 46-628 provided that the net balance of the assets, rights and obligations transferred to EDF constituted its capital, belonged to the nation, was inalienable and, in the event of operating losses, had to be reconstituted using the results of subsequent years. Under Article 1 of Decree No 56-493 of 14 May 1956 on capital contributions to EDF, those contributions were subject to the rules laid down by Article 16 of the above Act. Article 2 of the same Decree stipulates that the capital contributions give rise to payment to the state of interest and a dividend.

<sup>(1)</sup> Judgment of the General Court in Case T-156/04 *EDF v Commission* [2009] ECR II-4503.

<sup>(2)</sup> Judgment in *Commission v EDF* C-124/10 P, EU:C:2012:318.

<sup>(3)</sup> OJ C 186, 28.6.2013, p. 73.

- (19) By virtue of Act No 46-628, EDF had been since its creation, and still was in 1997, a national public industrial and commercial establishment that was not governed by the provisions applicable to public limited companies. A national public industrial and commercial establishment does not have any share capital, unlike a limited company governed by public law, which is owned by its shareholders<sup>(1)</sup>. Despite the terms 'capital' and 'capital contribution' used in the relevant instruments, EDF, because of its status as a legal person governed by public law, did not have any share capital. Act No 2004-803 of 9 August 2004 on the public electricity and gas service and on electricity and gas enterprises ('Act No 2004-803') provided for a future change to this status. Article 24 of Act No 2004-803 stipulated that EDF, in which the state had to hold more than 70 % of the capital, would be governed by the laws applicable to public limited companies, save as otherwise provided by statute. Article 47 of the Act also provided for the subsequent conversion of the public establishment EDF into a public limited company, subject to the publication of a decree on its new status. Article 46 laid down that the balance sheet of the company EDF at 31 December 2004 would be based on the balance sheet at 31 December 2003 and the income statement of the public establishment EDF for the 2004 financial year.
- (20) The conversion of EDF into a public limited company became effective by application of Decree No 2004-1224 of 17 November 2004 on the statutes of the public limited company *Électricité de France*. The statutes annexed to the Decree provided that EDF would now be a public limited company governed by the laws and regulations applicable to commercial companies, in particular the Commercial Code, unless otherwise specified by more detailed provisions, including the statutes themselves.
- (21) Article 6 of the EDF statutes provides that the company's share capital, which was initially wholly owned by the state, is set at EUR 8,129 billion, divided into 1 625 800 000 shares of EUR 5 each. The share capital of the new public limited company EDF was set in November 2004 at the same amount as the cumulated capital and capital contributions of the publicly owned industrial and commercial establishment EDF at that time, i.e. EUR 8,1 billion. This amount of capital and capital contributions had been reached under application of Act No 97-1026 of 10 November 1997 on various economic and commercial measures ('Act No 97-1026') and had remained unchanged since 1997.
- (22) As stipulated by Act No 2004-803 and the EDF statutes, the state had — and has — to hold more than 70 % of the company's capital at any time. In November 2005, new EDF shares accepted for listing on Euronext were offered at an open price, thereby effectively opening EDF's capital to shareholders other than the state.

#### 1.2. THE CREATION OF ACCOUNTING PROVISIONS FOR THE RENEWAL OF THE HIGH-VOLTAGE TRANSMISSION NETWORK (RAG)

- (23) Article 36 of Act No 46-628 transferred all the nationalised electricity concessions to EDF. Under Article 37 of the Act, the concessionaire is required to comply with a standard set of terms and conditions in relation to the concessions. In 1958, the various electricity transmission concessions that had been transferred to EDF by the state were converted into a single concession known as the '*réseau d'alimentation générale*' (RAG) (high-voltage transmission network).
- (24) In the absence of specific accounting rules for concessions, as early as 1946 EDF considered that it was the owner of the assets comprising the RAG and included those assets in its balance sheet. Pursuant to Article 8 of the terms and conditions approved by Decree No 56-1225 of 28 November 1956, EDF was required to carry out, at its expense, all the maintenance and renewal work needed to keep the concession structures in good working order.
- (25) In 1987, following a 1982 amendment to the general accounting plan that laid down specific rules for the assets to be returned to the state at the end of the concession, EDF changed its accounting practice for the assets constituting the RAG, which had until then been considered to be own assets, and classified them under the balance sheet item 'Assets under concession'. EDF applied to those assets the special accounting rules established in France for assets under concession that have to be returned to the state at the end of the concession period, and created tax-free provisions for the renewal of the RAG.
- (26) In a 1994 report<sup>(2)</sup>, the French Court of Auditors considered that, in the presence of a sole and permanent concessionaire from the state, nominated by law, such as EDF, it was difficult to regard the assets constituting the RAG as having to be returned to the state at the end of the concession, as opposed to the RAG's own assets

<sup>(1)</sup> Reply by the French authorities dated 23 December 2013, points 71 and 72.

<sup>(2)</sup> *Rapport particulier sur les concessions d'EDF* No 1993, 10 October 1994.

belonging to EDF. In other words, the Court of Auditors took the view that the accounting change introduced by EDF in 1987, which was reflected in the setting-up of tax-free provisions, was not justified. Work to regularise EDF's situation was started rapidly between the undertaking and the supervising authorities.

- (27) In 1997, EDF's accounts contained two types of tax-exempt provisions for the renewal of the RAG: unused provisions amounting to FRF 38,5 billion, and grantor rights corresponding to renewal operations already carried out, amounting to FRF 18,345 billion.

### 1.3. RECLASSIFICATION OF THE ACCOUNTING PROVISIONS

- (28) Act No 97-1026 clarified the status of the assets constituting the RAG. Article 4 of the Act provides:

- I. The structures of the high-voltage electricity transmission network are deemed to have been owned by Électricité de France (EDF) from the time that it was granted the concession for that network.
- II. For the purposes of applying the provisions of paragraph I, as at 1 January 1997, the value of the assets in kind allocated under concession to the high-voltage transmission network appearing as liabilities on EDF's balance sheet is to be entered, net of the corresponding revaluation differences, under the item "Contributed capital" ...'

- (29) Reference to the Act was necessary for any operation relating to EDF's capital. Article 16 of Act No 46-628, in the version in force in 1997, provided that EDF's capital was inalienable and belonged to the nation. Therefore, under French law, the capital contributions to EDF resulting from the reclassification of the provisions for the renewal of the RAG were a matter for the law.

- (30) Act No 97-1026 establishes the ownership of the assets constituting the RAG. EDF's balance sheet was therefore reorganised by Act No 97-1026. The provisions set up by EDF between 1987 and 1996 for the renewal of the RAG with a view to returning those assets to the state, whether or not they had been used, would become superfluous if EDF were deemed to own the assets constituting the RAG.

- (31) Annex 1 to a letter addressed to EDF on 22 December 1997 by the Minister for Economic Affairs, Finance and Industry, the Secretary of State for the Budget and the Secretary of State for Industry ('the letter from the Minister for Economic Affairs') explained the restructuring of the upper part of EDF's balance sheet pursuant to Article 4 of Act No 97-1026 of 10 November 1997:

'— Reclassification of "Grantor rights" (FRF 18 345 563 605):

Consolidation as capital contributions of the value of assets in kind allocated under concession to the RAG, amounting to FRF 14 119 065 335.

Amalgamation of the revaluation reserves for the RAG in 1959 (FRF 2 425 million) and 1976 (non-depreciable fixed assets: FRF 97 million) with the item "Revaluation reserves RAG", which is thus increased from FRF 1 720 million to FRF 4 145 million.

Amalgamation of the statutory provisions for the revaluation of depreciable fixed assets in 1976 (FRF 1 704 million), the item thus increasing from FRF 877 million to FRF 2 581 million.

Reclassification of the renewal provisions which have become unwarranted (FRF 38 520 943 408) as retained income, in accordance with National Accountancy Council Opinion No 97-06 of 18 June 1997 on accountancy changes.'

- (32) In reorganising EDF's balance sheet, the French authorities followed National Accountancy Council Opinion No 97-06 of 18 June 1997 on changes to accounting methods, changes to estimates, changes to tax options and corrections to errors ('the National Accountancy Council Opinion'), which states that corrections to accounting errors, which by their very nature relate to the posting of past transactions, 'should be posted in the accounts for the financial year in which they are discovered'.

- (33) In accordance with Act No 97-1026 of 10 November 1997 and the letter from the Minister for Economic Affairs, the revaluation reserves were transferred to the item 'Own funds' without incurring any tax since they corresponded to revaluation surpluses realised free of tax or under a tax neutrality arrangement pursuant to the 1959 and 1976 Revaluation Acts.

#### 1.4. TAX IMPLICATIONS OF THE RECLASSIFICATION OF THE ACCOUNTING PROVISIONS

- (34) Annex 3 to the letter from the Minister for Economic Affairs also sets out the tax implications of the reorganisation of EDF's balance sheet. A net asset variation results from the reclassification of the unused renewal provisions amounting to FRF 38,5 billion as retained income and is subject to corporation tax at the rate of 41,66 % applicable in 1997. The unused provisions amounting to FRF 38,5 billion were thus correctly taxed by the French authorities. However, the part of the tax-free provisions consolidated as a capital contribution corresponding to the grantor rights was not taxed.
- (35) A memorandum by the Directorate-General for Taxation dated 9 April 2002, sent to the Commission by the French authorities, stated that 'the grantor rights in respect of the RAG represent an unowed debt which was unjustifiably exempted from tax by being incorporated into the capital' and that 'before this reserve was incorporated into the capital, it should have been transferred from the enterprise's liabilities, where it was incorrectly posted, to a net assets account, thereby resulting in a positive variation in net worth that was taxable under Article 38(2)' of the General Tax Code. They noted that 'the tax concession thus obtained [by EDF in 1997] can be estimated at FRF 5,88 billion (14,119 × 41,66 %)'.

#### 2. OPENING DECISION

- (36) In its opening decision, the Commission concluded that the irregular creation of additional provisions for the renewal of the RAG between 1987 and 1996 had favoured EDF within the meaning of Article 107(1) of the TFEU. This operation had conferred on EDF a selective economic advantage resulting from the difference between the capitalised value of the unpaid corporation tax on the provisions during the same period and the amount of corporation tax paid by EDF in 1997, following the entry into force of Article 4 of Act No 97-1026.
- (37) Despite the fact that EDF engaged in activities in France on a series of markets subject to monopoly rights before the entry into force of Directive 96/92/EC of the European Parliament and of the Council <sup>(1)</sup> liberalising the electricity sector, the Commission considered that the aid measures in question in favour of EDF had distorted or threatened to distort competition and affected trade between Member States within the meaning of Article 107(1) of the TFEU. This resulted in particular from the fact that, despite the exclusive rights enjoyed by EDF in engaging in certain activities in France, there was nevertheless a degree of trade between Member States on those markets. Moreover, free competition also existed on related markets where EDF had already diversified its activities beyond its exclusive rights in both geographic and sectoral terms. These effects already existed well before the liberalisation of the electricity sector.
- (38) The Commission also concluded that it was new aid which did not appear, at that stage, to meet the requirements that must be fulfilled for finding that the conditions laid down in Article 107(2) and (3) of the TFEU were fulfilled. Furthermore, the French authorities did not rely on the application of Article 106(2) of the TFEU.

#### 3. COMMENTS BY AN INTERESTED PARTY

- (39) By letter dated 6 January 2003, the National Association of Independent Thermal Electricity Producers (SNPIET) submitted comments to the Commission in the context of the formal investigation procedure. In relation to the non-payment in 1997 of corporation tax on some of the tax-free provisions created for the renewal of the RAG, SNPIET alleged that EDF had not complied in its operations with normal practice in industrial and commercial enterprises, contrary to the provisions of Act No 46-628 of 8 April 1946.

#### 4. COMMENTS BY FRANCE ON THE DECISION TO INITIATE THE FORMAL INVESTIGATION PROCEDURE

- (40) The French authorities submitted their comments to the Commission by letter of 11 December 2002. They challenged the classification as State aid of the non-payment in 1997 of corporation tax on some of the accounting provisions created free of tax for the renewal of the high-voltage transmission network.

<sup>(1)</sup> Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity (OJ L 27, 30.1.1997, p. 20).

- (41) First of all, they disputed the amount of the provisions created for the renewal of the high-voltage transmission network (RAG) advanced by the Commission. Second, the French authorities claimed that, even if EDF had not set aside provisions for the renewal of the RAG, it would still not have been liable for the payment of corporation tax between 1987 and 1996 because of the carry-over of large tax losses. Furthermore, since the state was both the owner of EDF and the grantor of the concession on the RAG, they considered that the grantor rights did not provide it with a genuinely enforceable claim. Consequently, when the balance sheet was restructured in 1997, they assigned those rights to EDF's capital and reserves in order to correct its under-capitalisation, but without subjecting them to corporation tax.
- (42) The French authorities took the view that the restructuring of EDF's accounts in 1997 could be interpreted as a capital contribution of an amount equivalent to the partial tax exemption, the aim of which was also to correct under-capitalisation. EDF and the state would have liked to allocate the quasi-own assets to capital, leaving aside the question of corporation tax. It was thought that it would be more efficient and more neutral to allocate the grantor rights directly, and in their full amount, to own funds, rather than to carry out the equivalent transaction, which would have entailed assigning to capital a net amount after corporation tax, requesting EDF to pay corporation tax in an amount equal to the variation in net worth and, finally, making an additional capital contribution in an amount equal to the tax paid.
- (43) The French authorities took the view that an additional contribution was justified by EDF's projected profits in 1997, which were in fact achieved during subsequent years. According to the French authorities, in comparable circumstances, a private investor in a market economy would have made such a capital contribution.
- (44) They also denied that the remuneration of the state had been unduly reduced between 1987 and 1996 as a result of the creation of the provisions in question. They argued that, even if the net result had been higher, the remuneration of the state would not have been increased since, during that period, the level of that remuneration did not correspond to a predetermined percentage of EDF's net result. The level was determined freely by the state in absolute terms and did not necessarily depend on EDF's financial situation. Nor did the remuneration have to be deducted from the net profits for each year. In view of the foregoing, and given the losses carried over by EDF, the French authorities stressed that between 1987 and 1996 the state had in fact taken a dividend considerably in excess of the limits laid down by company law.
- (45) The French authorities also considered that, even if the creation of provisions for the renewal of the RAG had resulted in an advantage, that advantage had to be regarded as cancelled out by the increase in corporation tax paid in 1997. They claimed that, over the period from 1987 to 1996, EDF paid more to the state overall than the corporation tax that would have been paid by a commercial company which did not create provisions for the renewal of the RAG and which paid its shareholder a dividend equal to 37,5 % of its net result after tax.
- (46) The French authorities also argued that, if EDF were found to have benefited from an undue advantage, it would constitute existing aid and not new aid on account of the expiry of the 10-year limitation period laid down in Article 15 of Council Regulation (EC) No 659/1999 <sup>(1)</sup>, which started to run from the date on which the initial aid was granted. Since the Commission's first request for information was made on 10 July 2001, any aid granted before 1991 would be time-barred. The French authorities took the view that the legislative measures adopted in 1997 did not suspend the limitation period since only action by the Commission could have that effect. The French authorities argued finally that the measure would constitute existing aid in any event since it was granted prior to the liberalisation of the electricity market.
- (47) In their letter dated 20 November 2003, the French authorities reiterated their arguments concerning the revaluation reserves included in the amount of the grantor rights appearing in the accounts and concerning application of the limitation rule. Moreover, they claimed that the rate of corporation tax that should have been applied when EDF's balance sheet was restructured was the 1996 rate (36,67 %) and not the 1997 rate (41,66 %). They considered that the restructuring was carried out on the basis of a tax return filed on 23 December 1997, after closure of the accounts for 1996 but before the 1997 accounts were finalised.
- (48) The French authorities thus disputed the Commission's claim that EDF benefited from an advantage in 1997 on account of the non-payment of corporation tax on some of the provisions created free of tax for the renewal of the high-voltage transmission network.

<sup>(1)</sup> 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).

## 5. JUDGMENTS BY THE EU COURTS

- (49) By its judgment of 15 December 2009, the General Court annulled the Commission's decision of 16 December 2003 on the ground that it was incumbent on the Commission to determine whether a private investor would have invested a comparable amount in similar circumstances. The General Court took the view that the Commission should have checked whether the operation satisfied the private investor test. The General Court therefore considered that the Commission had committed an error of law and infringed Article 107 of the TFEU.
- (50) In its judgment of 5 June 2012, the Court of Justice dismissed the appeal brought by the Commission against the judgment of the General Court. The Court of Justice considered that the finding made by the General Court, to the effect that the obligation for the Commission to verify whether the capital had been provided by the state in circumstances corresponding to normal market conditions existed regardless of the way in which that capital had been provided by the state, was not vitiated by an error of law. The Court of Justice also took the view that the General Court did not err in law either in finding that the private investor test may be applicable even where fiscal means have been employed.

## 6. DECISION TO EXTEND THE FORMAL INVESTIGATION PROCEDURE

- (51) As a result of the annulment of the decision of 16 December 2003, the Commission had to adopt a new decision under Article 266 of the TFEU and Article 13 of Regulation (EC) No 659/1999 terminating the procedure by complying with the points of law established definitively by the judgment of the General Court. Since the decision of 16 December 2003 had been annulled, the Commission had to re-examine the questions relating to Articles 3 and 4 of that decision.
- (52) On the one hand, neither the Court of Justice nor the General Court had found that the opening decision was irregular. It could therefore form the basis for a new final decision. On the other hand, the General Court clearly laid down the conditions governing the applicability and application of the private investor test. These criteria were based on the existence of objective and verifiable evidence showing that the decision by the Member State was to make an investment in the public undertaking on the basis of economic evaluations comparable to those which a rational private investor would have had carried out, before making the investment, in order to determine its future profitability <sup>(1)</sup>.
- (53) In the decision to extend the formal investigation procedure, the Commission noted that, at that stage of the administrative procedure, there was no evidence, demonstration or document to support the statement by the French authorities that the accounting reform of 1997 could be interpreted as a capital contribution of an amount equivalent to the partial tax exemption. Contrary to the observations by the French authorities, nor was such a capital contribution an investment rather than an aid measure which a rational private investor in a market economy would have made in comparable circumstances, justified by EDF's projected profits in 1997, which were in fact achieved during subsequent years.
- (54) Accordingly, in the extension decision, the Commission set out, in the light of the available information and documents, its preliminary analysis of the potential economic advantage arising from the non-payment by EDF in 1997 of corporation tax on the part of the provisions corresponding to the FRF 14,119 billion in grantor rights which were reclassified as capital contributions.
- (55) In that regard, the overall assessment of the facts of the case seemed to indicate that that measure involved the public authorities, thereby precluding the applicability of the principle of the private investor. In support of their claim, the French authorities had not provided any information or business plan preceding or contemporaneous with the decision not to levy the tax on EDF demonstrating the profitability of such an operation. From a substantive perspective, having regard to the criteria laid down by the General Court, the Commission noted that it was for France to duly establish the date of the documents provided and the evidence that they had been examined by the relevant ministers and officials and the Houses of Parliament before the contested decision was adopted.
- (56) In the absence of this information, however, it was in the exercise of its powers of taxation that France appeared to have reserved a more favourable tax treatment for the restructuring of the upper part of EDF's balance sheet, in relation to the reclassification of the grantor rights provided for in Article 4 of Act No 97-1026. No specific budgetary provision earmarked this tax resource to EDF, just as the rules and checks relating to investments had not been implemented to provide a legal basis for the alleged investment.

<sup>(1)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 84.

- (57) Likewise, in its extension decision, the Commission noted in the alternative that, even if the principle of the private investor in a market economy had been applicable, application of the principle resulted in the conclusion at that stage that a private investor would not have invested FRF 5,88 billion in the capital contribution to EDF in 1997. In the absence of information provided by the French authorities, it seemed excluded that a private shareholder under normal market conditions would have gone ahead with the alleged investment without previously examining objective and reliable studies, preferably carried out by an impartial independent investment adviser, rather than, for example, by the beneficiary enterprise, which stated, in particular, the return on capital invested, the return period on the investment and the inherent risks in absolute terms and in relation to the remuneration arrangements linked to such an investment.
- (58) In that regard, the Commission added to the factors which a rational private investor would have examined before committing funds the uncertainty about the amount and the future course of the pension financing costs facing EDF in 1997, under its specific pension scheme, and the assessment that an investor would make at that time.
- (59) Under those conditions, the partial exemption from corporation tax in 1997 was not a productive investment by the state shareholder but rather a tax exemption measure likely to have conferred an economic advantage on EDF.
- (60) Furthermore, it appeared that the failure to levy the corporation tax owed by EDF involved state resources and was likely to distort competition and affect trade between Member States, thereby fulfilling the conditions for the application of Article 107(1) of the TFEU.
- (61) In the absence of a legal basis justifying the compatibility with the internal market of operating aid that strengthened EDF's position in relation to its competitors, the Commission, in its decision of 2 May 2013, doubted whether the aid was compatible with the internal market. Similar doubts had already been raised in the opening decision.

#### 7. COMMENTS BY THIRD PARTIES

- (62) By letter dated 29 July 2013, EDF submitted its comments on the extension decision. EDF levelled three main criticisms at the arguments set out in that decision: (i) the decision ignored the lessons of the judgment of the General Court and failed to recognise the true nature of the recapitalisation of EDF carried out by the state; (ii) the decision was excessively formalistic in that it wrongly postulated the need for a business plan linked to the investment, whereas the recapitalisation was the fruit of a lengthy reflection process, as attested by many documents from that period; and (iii) the decision argued, without any demonstration, that no investor in a situation as close as possible to that of the state would have made a comparable investment, contrary to the information provided by EDF in support of its observations.
- (63) EDF took the view that the Commission was therefore continuing to analyse the measure adopted by the French state in 1997 from the sole perspective of its alleged tax implications, even though the General Court had clearly rejected that approach. As the General Court had confirmed, the measure implemented by the state when it reclassified the grantor rights as capital contributions constituted a recapitalisation of EDF intended to correct the imbalance on EDF's balance sheet with view to the opening-up of the energy markets to competition. The letter from the Minister for Economic Affairs dated 22 December 1997 did not contain a tax decision that departed from the 1997 Act but served to point out the tax implications. It was that this single and indivisible recapitalisation measure that should be examined, not the alleged tax implications, which were artificially dissociated in the decision to extend the formal investigation procedure.
- (64) According to EDF, a business plan specific to the investment was not required by the case-law, which did not establish any formalism on that question but requires objective and verifiable evidence pre-dating or contemporaneous with the measure under examination. Incidentally, such a business plan would not have been essential for the state in 1997. The state had five representatives on EDF's management board, had held all of EDF's capital since 1946 and, at the time, had detailed knowledge of the enterprise and was involved in its management and in setting its strategic objectives, with a long-term time horizon. According to EDF, such a long-term time horizon was particularly relevant in the case of EDF because of the capital intensiveness of its activity and the decades-long useful life of its installations, ranging from 30 to 75 years in some cases.



- (65) EDF took the view that it was as a shareholder and not as a public authority that the state, as attested by many contemporary documents, had carried out an investment on the basis of precise forward-looking analyses and assessments. Thus, as early as 1995 discussions had begun between EDF and its line ministries in order to draw the conclusions from the opinion of the Court of Auditors referred to in recital 26. These discussions focused on the reorganisation of the balance sheet of the undertaking and the return on capital. They resulted in the signature, on 8 April 1997, of the contract for services between the state and EDF for the period 1997-2000 and the concomitant tabling, on 2 April 1997, of a draft law on various economic and financial measures, Article 45 of which was identical to Article 4 of Act No 97-1026. According to EDF, the preparatory work in the National Assembly and the Senate, and even the Act itself, demonstrated that the nature of the intervention by the state was that of a shareholder: a capital contribution recapitalising EDF.
- (66) As attested by some 40 contemporaneous documents that EDF attached to its accounts, the state had been guided in its analyses and reflections by four main concerns:
- taking into consideration the new competitive context of the gradual opening-up of the markets following Directive 96/92/EC,
  - normalising its financial relations with EDF on the basis of ordinary law by putting an end to the ambiguities which had existed in the past,
  - rectifying the significant imbalance which was affecting the structure of EDF's balance sheet by strengthening its own funds,
  - facilitating international comparisons to increase the credibility of the enterprise within the financial community.
- (67) Lastly, for EDF, the criterion of the prudent private investor in a market economy was not only applicable because of the considerations referred to above but was also satisfied in this case since the state had acted as a private investor would have done. In the view of EDF, according to the Court of Justice (paragraphs 78 and 89 of the judgment), the question was one of determining whether EDF, in circumstances which corresponded to normal market conditions, could have obtained the same advantage as that which had been made available to it through state resources and whether the advantage, because of its effects, distorted or threatened to distort competition.
- (68) Here again, many contemporaneous documents demonstrate that the state had indeed examined and quantified the profitability of its investment, as would have done an investor who was the sole shareholder in the undertaking operating to a long-term time horizon. It was on that basis that the remuneration of the state had been set in the contract for services between the state and EDF for the period 1997-2000. At the time, the remuneration was consistent with the remuneration of shareholders in comparable companies. The estimates of the amounts that EDF would have to pay to the state from 1997 to 2000 had therefore been examined by the latter before the contract was concluded.
- (69) Moreover, in its comments of July 2013, EDF had anticipated a study commissioned from Oxera, which had not yet been finalised when EDF made its submission. EDF had claimed that the Oxera study would compare the internal rate of return expected on the investment by the state in 1997 with that required by the capital markets for a similar investment and would show that a private investor would have made the investment under the conditions set in the contract for services for 1997-2000.
- (70) On 18 October 2013, EDF had sent to the Commission the study by Oxera, which was dated 15 October 2013 <sup>(1)</sup>, without further comment. As EDF had anticipated in its comments in July 2013, the study by Oxera concluded that a prudent private investor in a market economy would have invested in the increase in the amount of capital in EDF. This conclusion resulted from the fact that the profitability (internal rate of return) that an investor could have expected in 1997 lay somewhere between 35 % and 15 %, with an average of 27 %, over five years, which in any event was higher than the return of 12,7 % that such an investor would have required. The return was calculated by taking into account the value, at the start and end of the period, of the sale of the rights in EDF held by the state.

<sup>(1)</sup> Does the 1997 recapitalisation of EDF by the French State meet the private investor test? Final Report of 15 October 2013.

- (71) EDF took the view that, apart from the weakness in own funds, its economic fundamentals were healthy in 1997, as analysts had commented at the time, without expressing any concerns about its financial viability or its commercial prospects at the time the state made its investment. EDF's credit rating was excellent (Aaa for Moody's between 1992 and 1997, AAA for Standard & Poor's in 1996-1997) and remained so despite it having been necessary to lower it by one or two notches to take account of the state guarantee available to EDF as a public industrial and commercial establishment. Several contemporaneous documents showed that the level of remuneration of the French state by EDF was comparable to the rate of return from dividends from companies listed on the French stock exchange (CAC 40) (4,5 % to 5 % on capital) and from undertakings active in the energy sector in Europe (estimated at 4,7 % and 5,27 % for 1996 and 1997 respectively). Moreover, this demonstrated that EDF could have obtained the same amount of capital on the capital market, so the measure, because of its effects, had not been of such a nature as to distort competition.
- (72) In particular, EDF took the view that a private investor holding the entire share capital in a subsidiary would have been able to make, under comparable conditions, a similar investment in that subsidiary by converting any type of claim held against the subsidiary into capital. This analysis was supported by a legal opinion issued at the request of EDF. In seeking to rectify a financial structure that was distorted by the weakness of its own capital compared with the financial indebtedness, the state would also have allowed the undertaking to compete with other leading operators in the sector in the EU. The same shareholder would not, therefore, have left untouched a significant imbalance in the balance sheet of its subsidiary with sound economic fundamentals, while it had an easy method of correcting the imbalance by converting a claim into capital.
- (73) In the view of EDF, it was therefore reasonable to think that a private investor in a situation as close as possible to that of the state, i.e. the sole shareholder in the company, operating to a long-term time horizon, in a highly capital-intensive market on the verge of being opened up to competition, would have made the same investment.

#### 8. COMMENTS BY FRANCE ON THE DECISION TO EXTEND THE FORMAL INVESTIGATION PROCEDURE

- (74) The French authorities considered, first, that the state had acted as a prudent investor in a market economy when it reclassified, free of corporation tax, the grantor rights as capital contributions to EDF. They took the view that, contrary to the presentation in the decision to open the investigation procedure of 16 October 2002 and in the decision to extend the procedure of 2 May 2013, the measure that the Commission should analyse was a single measure to recapitalise EDF through the adoption of Article 4 of Act No 9-1026 and not the measure to grant a tax exemption on the reclassification of the grantor rights as a capital contribution, which was separable under the said Act. They relied on the information presented in a number of documents dating from 1996 and 1997 annexed to their comments, which they believed supported and corroborated that argument. These documents are referred to in recitals 87 to 108. As far as the French authorities were concerned, other documents submitted by EDF backed up their comments.
- (75) In the alternative, the French authorities pointed out that they disputed the amount of aid and reiterated their comments of 20 November 2003 to the effect that the rate of the relevant tax to be applied should be the 1996 rate and not the 1997 rate, as set out in recital 47.

#### **On the applicability of the principle of the private investor in a market economy**

- (76) The French authorities disputed that France had granted the tax exemption at issue in its capacity as a public authority, which made the principle of the prudent private investor in a market economy inapplicable. They considered that the General Court did not require the Member State to submit a genuine business plan relating to the contested measure.
- (77) In that regard, first, they pointed out that in 1997 EDF was a public industrial and commercial establishment placed under the supervision of the state, which, therefore, had a detailed knowledge of the undertaking and of its industrial strategy and financial prospects. Accordingly, they took the view that the submission of the information and evaluations available to the state before it took the contested measure, which demonstrated the profitability of the investment, was admissible. The Commission had to carry out an overall analysis, including in particular this information and any other relevant information.

- (78) Second, given the nature and purpose of Article 4 of Act No 97-1026, the French authorities took the view that the state had acted in its capacity as shareholder by granting a tax exemption on the reclassification of the grantor rights. Thus, this Act had been preceded by the signature on 8 April 1997 of the contract for services between the state and EDF for the period 1997-2000, the performance of which involved the adoption of legislative measures to restructure EDF's balance sheet. Previously, in a letter dated 12 July 1996, the supervisory authorities had informed EDF that the contract should set it an ambitious target for the remuneration of the state. Title III of the contract provided for a remuneration of the state comprising two elements: (i) a remuneration on the capital contributions at a fixed rate of 3 %; and (ii) an additional remuneration equal to 40 % of EDF's net income, whereby the combined amount of the two elements could not, however, exceed 6 % of the amount of the capital contributions.
- (79) The state had examined this remuneration in the form of prospective dividends and quantified the additional remuneration at FRF 3,5 billion, which could reach FRF 6 billion over the period, as documented by a letter dated 22 April 1997 from the supervisory authorities to EDF. This estimate was based on the economic-financial prospects that EDF had sent to the Ministry of Finance on 19 February 1997 and on the assumptions underlying the contract for services. The report from September 1997 by the rapporteur to the Senate on Act No 97-1026 also included analyses by the Ministry's departments of the expected impact on the remuneration of the state as shareholder for 1998, i.e. FRF 2,6 billion, of which FRF 1,5 billion was fixed interest and FRF 1,1 billion was additional remuneration. The state had therefore estimated the projected remuneration before adopting the measure at issue, as would any shareholder wishing to take part in a capital increase in their company.
- (80) Third, the French authorities considered that the reclassification of the grantor rights and, more broadly, the restructuring of EDF's balance sheet and the strengthening of own funds had rectified the weakness in the financial structure of the enterprise. If this weakness had persisted, EDF would probably have had to face an increase in the interest rate on its debt and a difficulty with its commercial partners because of a negative perception of the counterparty risk. That the state as shareholder had had such a concern emerged from the explanatory memorandum to Article 4 of the draft law which then became Act No 97-1026 and from the speech by the minister responsible when he tabled the draft law before the Senate on 2 October 1997.
- (81) Furthermore, the reports by the deputy and senator who acted as rapporteurs on the draft law before the National Assembly and the Senate respectively had stressed the positive effect of restructuring EDF's balance sheet on the debt-equity ratios: the first report had judged the equity (FRF 24,2 billion) to be insufficient in relation to the loan debts (FRF 131,9 billion) and the net assets (FRF 696,4 million); the strengthening of own funds had given EDF a balance-sheet structure that better reflected its economic reality, while enabling more relevant comparisons with its European competitors; the second report, moreover, had stressed the positive effect for EDF of greater credibility among the financial community and with its potential partners. The French authorities took the view that strengthening the financial structure of an enterprise was a concern of a prudent private investor in a market economy in a comparable situation.
- (82) According to the French authorities, the outcome was that the prudent private investor in a market economy test was indeed applicable since the state had acted as shareholder in reclassifying, free of tax, the provisions for grantor rights as capital contributions to EDF.

#### **On the applicability of the principle of the private investor in a market economy**

- (83) First of all, the French authorities pointed out that the contract for services between the state and EDF had provided for a remuneration of the state resulting from two elements: (i) a fixed rate of 3 % on its capital contributions; and (ii) additional remuneration of 40 % of EDF's net income, which demonstrated that the state had information on the expected yield on the invested capital. As attested, moreover, by the report by the member of the National Assembly referred to above, given the existence of a fixed rate on the capital contributions, the reclassification of the grantor rights as capital had had the effect of increasing in absolute terms the value of the remuneration of the state, because of the broadening of the capital base.
- (84) Next, the French authorities considered that the profitability of the investment in EDF in 1997 should be looked at from a long-term perspective, having regard to the future payments to the state and to the increase in the value of the enterprise. Substantial generation of resources between 1997 and 2000, of almost FRF 70 billion, as forecast by the contract for services, had to be added to the positive net results after taxation and remuneration of the state (FRF 1,4 billion in addition to FRF 2,5 billion remuneration of the state in 1998). As underlined by the letter from EDF dated 19 February 1997, the state had indeed set a target for the increase in the asset value of the enterprise of this amount, resulting from debt reduction, asset formation and investments in development, providing prospects for growth in the capital value of EDF.

- (85) Lastly, in assessing the risks of the investment, the state as shareholder had taken into account the characteristics of EDF's main activity, which was conducted principally in France, on the basis of a principle of regulated tariffs which would have to cover the company's costs. These characteristics reduced the risk associated with the investment and, consequently, the profitability requirement. Furthermore, a memo from EDF dated 27 July 1996, which was sent to the Senate on 15 September 1997, showed that the shareholder remuneration in foreign companies differed markedly, depending on the institutional and regulatory environment in the sector in each country.
- (86) According to the French authorities, the result was that the state had behaved as a prudent private investor in a market economy when it reclassified the provisions for grantor rights as capital contributions without levying corporation tax. Furthermore, this conclusion was also confirmed by EDF's comments, including the studies and analyses on which it relied, as set out in recitals 62 to 73. In particular, as regards the economic study by Oxera submitted by EDF, the French authorities took the view that the Commission should carry out the same analysis in order to determine whether or not the recapitalisation of EDF by the state in 1997 was a prudent investment.

### **Documents submitted by France in support of its comments**

- (87) In support of their reply to the extension decision, the French authorities sent the Commission nine documents in attachment to their comments of 1 July 2013. They submitted these nine documents in support of the argument they had already put forward in their comments of 11 December 2002 to the effect that an additional capital contribution equivalent to the revenue from the uncollected tax was justified by EDF's projected profits in 1997, which were achieved in the subsequent years. Without prejudice to the documentary evidence cited by France in its comments, a systematic analysis of the evidence contained in these documents is required.
- (88) The documents relate either to the preparation or implementation of the contract for services for 1997-2000 between EDF and the French state or to debates on the draft law which became Act No 97-1026. They date from 1996 to 1997 and thus from the same period as the supposed investment decision. The documents concerned are the 1997-2000 contract for services <sup>(1)</sup>, letters from the line ministers responsible for supervising EDF <sup>(2)</sup>, letters from EDF to the Ministry or the Senate <sup>(3)</sup> and documents and two reports from the National Assembly and the Senate in preparation for debates on the draft law <sup>(4)</sup>. Their content is outlined in more detail below.
- (89) In a letter of 12 July 1996 to the Chairman of EDF, the line ministers welcomed the results of the 1993-1996 Plan contract between EDF and the state and, as it was due to expire on 31 December 1996, launched the preparation of the next Plan contract for 1997-2000. They explained that the financial equilibrium in the 1997-2000 contract would be determined as part of a new tax and accounting framework for EDF, following work conducted since 1995. They asked for discussions to start between the relevant departments and EDF and outlined the three primary objectives for the future contract:

- first, the ministers wanted: 'the productivity gains achieved by the undertaking [to] allow it to continue its price reduction policy, thereby helping to boost the competitiveness of French industry and the purchasing power of domestic consumers',
- at the same time EDF was to continue its debt reduction efforts and to set an ambitious target for the remuneration of the state, with an income-growth incentive mechanism for EDF,
- lastly, the contract was to set strategic guidelines for developing EDF worldwide, in order of priority.

<sup>(1)</sup> 1997-2000 State-EDF contract for services, signed on 8 April 1997.

<sup>(2)</sup> Letter of 12 July 1996 from the Minister for Economic and Financial Affairs and the Minister for Industry, Posts and Telecommunications to the Chairman of EDF, letter of 22 April 1997 from the Minister for Economic and Financial Affairs, the Deputy Minister for the Budget and the Minister for Industry, Posts and Telecommunications to the Chairman of EDF.

<sup>(3)</sup> Letter dated 19 February 1997 from EDF's finance director to the Head of Financing and Holdings at the Treasury Department; EDF memo dated 27 July 1996 on the shareholder's remuneration, sent to the Senate on 15 September 1997.

<sup>(4)</sup> Explanatory memorandum to Article 45 of the draft law laying down various economic and financial rules, adopted by the Council of Ministers on 5 April 1997; report by the National Assembly's Committee on Finance, the General Economy and the Plan, submitted by Member of the National Assembly Didier Migaud on 10 September 1997, on draft law No 201 on urgent tax and financial measures; report by Member of the Senate Alain Lambert on the draft law on urgent tax and financial measures submitted on 24 September 1997; speech by the Minister for Economic Affairs, Finance and Industry presenting the draft law on urgent tax and financial measures to the Senate on 2 October 1997.

- (90) As part of the ongoing preparatory work on the contract, on 19 February 1997 EDF's finance director sent the Treasury Department a memo dated 18 February 1997. It contained the main hypotheses regarding the financial scenario underpinning the contract for services between EDF and the state for 1997-2000, including in particular the projected annual income statements and cash flow statements for the period.
- (91) The memo forecast a price reduction each year (– [...] (\*) %, – [...] %, – [...] %, – [...] %), industrial investment of FRF [...], of which FRF [...] for international development, and investment of FRF [...] in the core business over the period 1997-2000. It also mentioned a tax-deductible remuneration for capital contributions of 3 % on an estimated base of FRF 50 billion after restructuring of the balance sheet and of 40 % of income after the fixed remuneration component and corporation tax. Debt at end of year was expected to go from FRF [...] at end 1996 to FRF [...] at end 2000. Similarly, outstanding debt less assets was expected to go from FRF [...] at end 1996 to FRF [...] at end 2000.
- (92) Of the documents submitted in annex to their comments by the French authorities, the EDF memo of 18 February 1997, sent to the supervising authorities the following day, is the only one to contain systematic quantified projections for EDF's economic and financial operating income. On the basis of these projections dating from February 1997, the state as shareholder could expect a return on the invested capital of FRF 2,1 billion in 1997, FRF 2,5 billion in 1998, FRF 2,4 billion in 1999 and FRF 2,4 billion in 2000, or an annual average of FRF 2,35 billion. EDF's projected income statement for 1997-2000 as set out in the memo was as follows:

Table 1

**F projected income statement 1997-2000 (FRF billion current value)**

	1997	1998	1999	2000
Revenue	186,3	184,2	185,7	187,5
Expenses	177,0	177,2	179,1	180,9
of which fuel and energy purchases	36,9	36,8	37,8	38,5
of which operating expenses	88,3	91,2	93,6	95,7
Income from core business	9,3	7,0	6,6	6,6
Income before remuneration of the state	6,8	6,5	6,1	6,1
Remuneration for capital contributions	1,5	1,5	1,5	1,5
Additional remuneration	0,6	1,0	0,9	0,9
Corporation tax	3,9	2,6	2,4	2,3
Net income	0,9	1,4	1,3	1,4

Source: EDF memo of 18 February 1997 'Contract for services — economic and financial prospects'.

- (93) As mentioned in the EDF memo, the remuneration paid to the state was tax deductible. This marked a departure from the principle of corporation tax being levied on income after interest and depreciation, thereby reducing net income and thus the amount that could potentially be paid out in dividends. This ad hoc departure potentially increased the state's remuneration as shareholder but decreased by the same amount the tax to be paid to the state as revenue collector. In their reply of 23 December 2013, the French authorities stated that the remuneration for the capital contributions was treated as a standard dividend from 2001 onwards, as a result of which it ceased to be tax deductible. This treatment was used for the group contract between EDF and the state for 2001-2003, which replaced the 1997-2000 contract.

(\*) Business secret..

- (94) On 8 April 1997 a contract for services between EDF and the state for the 1997-2000 period was agreed and signed by the line ministers and the EDF Chairman and CEO. The contract set out the main direction EDF's medium-term action should take and contained reciprocal commitments by the parties, stating that these commitments had been entered into in the light of broad reference hypotheses and could be called into question only if there was a significant change in the business environment. The contract contained various commitments under three headings: reaffirming the core tasks of a public undertaking (Title I), preparing the undertaking's future today (Title II) and a new financial and institutional framework for the undertaking (Title III). Two annexes to the contract set out performance indicators used for implementation (Annex I) and price movements forecast per year between 1997 and 2000 (Annex II).
- (95) The main commitments and guidelines laid down in the contract which relate to the scope of this Decision are described below:
- The state confirmed that it wanted the undertaking to retain its legal status, which had proved its effectiveness and should remain a stable point of reference for future developments; this was in compliance with the EU Directive on the internal market in electricity <sup>(1)</sup>. For its part, EDF was to contribute to spatial planning and national solidarity through an ambitious policy to support economic activity and employment by helping local authorities to create jobs and by improving the situation of its poorest customers (Title I).
  - EDF's development was intended to 'boost the competitiveness of French business'; the productivity gains to which it was committing were to be allocated as a priority to a reduction in the average level of its prices. The price adjustments should result in an average reduction at constant prices of [...] % in April 1997, [...] % in April 1998 followed by [...] % in April 1999 and [...] % in April 2000. At the same time, EDF's development should be geared towards winning new markets, particularly in Europe (Title II).
  - EDF's balance sheet was to be restructured with the two-fold aim of strengthening its net assets and stabilising its financial relationship with the state on a basis more akin to ordinary law. To this end the Government undertook to present to Parliament a legislative measure restructuring EDF's balance sheet in 1997, with an effective restructuring date of 1 January 1997. The contract provided for a remuneration of the state as shareholder comprising two elements: a remuneration on the capital contributions at a rate of 3 % and an additional remuneration equal to 40 % of net income, whereby the combined amount of the two elements could not exceed 6 % of the amount of the capital contributions, though no estimate of the absolute amounts involved was included. In addition, for the period 1997-2000 EDF undertook to allocate FRF [...] to industrial investment worldwide, to cut its gross debt by FRF [...] to bring it to FRF [...] at end 2000, with a view to an ultimate objective of zero debt by the time the generation system was renewed. Lastly, the contract provided that, if targets were exceeded and a surplus resulted, this should be allocated 'as a priority to additional price reductions' before paying out any dividends to the state as shareholder or profit-sharing bonuses to staff (Title III).
- (96) A letter dated 22 April 1997 to the EDF Chairman from the ministers who co-signed the contract for services confirmed that the reference hypotheses and financial projections contained in the EDF memo of 18 February 1997 and which underpinned the 1997-2000 contract for services were consensual and fixed. The letter made express reference to the prior concertation between EDF and the public authorities in preparing the financial scenario. It mentioned the target of an average [...] % reduction in EDF's prices in four years.
- (97) The letter of 22 April 1997 referred to the provisions of the Decree of 14 May 1956, as amended, and the arrangements for the remuneration of the state included in Title III of the contract for services. In accordance with these provisions, the letter stated that 'the reference scenario gave an additional remuneration amount of FRF 3,5 billion over the period' 1997-2000 and that in these circumstances it would be possible to achieve a total value of payments to the state of FRF 5,1 billion in 1997, including the fixed interest rate and the advance on corporation tax. These amounts are consistent with those contained in the EDF memo of 18 February 1997. The consistency between the amounts of additional remuneration calculated on the basis of income demonstrates that all the amounts (revenue, expenses, net income, etc.) included in EDF's projected income statement for the period 1997-2000 were examined, validated and approved by the supervising authorities.

<sup>(1)</sup> The contract refers to Directive 96/92/EC. This Directive, like those which have succeeded it, did not contain any rules on the legal form to be taken by companies generating, transmitting or distributing electricity in the internal market.

- (98) The letter of 22 April 1997 from the ministers also stressed that the means of achieving equilibrium in the contract came under the accounting and tax framework accompanying the restructuring of EDF's balance sheet, which was to take effect, subject to the necessary legislative provisions, on 1 January 1997. The letter stated, 'the detailed arrangements for implementing this restructuring, on both the accounting and the tax fronts, will be the subject, on the basis of the plan now adopted, of further discussions between the line ministries and the undertaking'.
- (99) Not long before this letter, the Government had tabled a draft law before the National Assembly. The draft law on various economic and financial measures was adopted by the Council of Ministers on 5 April 1997. Article 45 provided for the reclassification of EDF's accounting provisions. The explanatory memorandum to the draft law stated that the planned accounting adjustments would give EDF a balance sheet that better reflected its real economic circumstances, with a level of own funds proportionate to its volume of activity. The draft law was not examined on account of the National Assembly's being dissolved on 21 April 1997.
- (100) After the transmission to Parliament of the draft law on urgent tax and financial measures, subsequently adopted as Act No 97-1026, the National Assembly and the Senate appointed their rapporteurs. National Assembly Report No 204 described the background to the need to clarify the ownership of EDF's transmission structures, which would nullify the accounting practices contested by the Court of Auditors in its special report on the EDF concessions, No 1993 of 10 October 1994. It explained the accounting changes needed and provided estimates of their effects on the various balance-sheet items as follows:

Table 2

**Effects of the reorganisation of EDF's own funds as a result of Article 4 of the urgent tax and financial measures Act on the accounts for 1996 (FRF billion)**

	End 1996	Effect of Article 4
Own funds	24,2	79,8
of which (liabilities):		
Paid-in capital	2,6	2,6
Contributed capital	36,6	50,7
Revaluation reserves	2,1	6,2
Statutory reserves	0,15	0,15
Retained income <sup>(1)</sup>	20,2	18,3
Income after remuneration of the state	1,9	1,9

Source: Ministry of Economic Affairs and Finance

<sup>(1)</sup> The changes to retained income are not a direct effect of Article 4, but a logical consequence.

- (101) The National Assembly report stressed the draft law's effects that made comparisons with the debt ratios of European competitors (Austria, United Kingdom, Sweden, Spain, Germany) more meaningful: after the restructuring of the balance sheet, EDF's net debt/equity ratio would go from 480 % to 148 %.
- (102) The report also stressed the changes in the financial relations between EDF and the state. It explained the legal regime and the remuneration for the capital contributions to EDF, governed by Decree No 56-493 of 14 May 1956, as amended by Decree No 86-1360 of 30 December 1986. This regime provided for a fixed-rate remuneration capped at 8 % and additional remuneration as a percentage of EDF's income after tax and fixed interest. The payments made by EDF from 1991 to 1996 as described in the report total FRF 3,41 billion per year on average during the period; proportional to own funds at the end of 1996, these payments gave an average operating profitability of 14,1 % for the state as shareholder <sup>(1)</sup>. They are summarised in the table below.

<sup>(1)</sup> The profitability for the State as shareholder is explained by the low capital contribution base of FRF 36 billion (denominator) and the size of the accounting provisions. Until 1996, once they had been entered into the accounts, EDF ended up with a negative annual net income. The loss carried over from the income statement was reflected in the balance sheet as depleting the own funds set at FRF 24,2 billion (see Table 2, 'End 1996' column, showing how EDF's own funds were slashed by negative retained income of FRF 20,2 billion before the amendment introduced by Article 4 of Act No 97-1026). As tax was not levied on negative income, the high profitability for the State as shareholder was at the expense of the State as revenue collector.

Table 3

**Financial relations between the state and EDF (FRF million current value)**

	1991	1992	1993	1994	1995	1996
Interest on capital contributions (GB — line 407)	1 816	1 816	1 816	1 816	1 816	1 816
Additional remuneration on capital contributions (GB — line 116)	500	665	965	1 938	1 500	4 002
Total	2 316	2 481	2 781	3 754	3 316	5 818

Source: National Assembly report, p. 77, Committee calculations for 'total'

- (103) The National Assembly report stated with respect to the changes envisaged for the EDF balance sheet that 'as the capital contributions form the base for the fixed interest, increasing them as a result of this Article would increase the payment burden on EDF. An amendment to the terms of remuneration was therefore included in the state-EDF contract for 1997-2000 signed on 8 April 1997. The fixed interest rate has been brought down to 3 % in order to offset the effect of the base'. The report pointed out that, despite the profits earned since 1990, EDF had not paid corporation tax and that moving the provisions linked to the RAG concessions up would wipe out in one go the accumulated tax and accounting deficit. The report noted that, according to the line ministry, this would leave the public establishment (EDF) owing corporation tax of FRF 3 billion in 1997 and FRF 2,5 billion in 1998.
- (104) The National Assembly report referred to a parliamentary amendment to the draft law, which was scrutinised and rejected by the Committee. The amendment specified that the reclassified accounting provisions should be converted to own funds by an accounting entry that bypassed EDF's income statement, in order to avoid showing a very high profit that the state might be tempted to tax in part. To this end, the amendment proposed that the Act should define the accounting process and stipulate that no additional revenue could be collected from EDF by the state on the ownership of the RAG assets being transferred. The report indicated that 'the inclusion of the accounting process for converting the provisions to own funds in the Act was ruled out at the request of the Council of State on account of its not being of a legislative nature'; in the discussion the report cited a number of parliamentary opinions to the effect that the state should be able to impose other charges on EDF, the undertaking should pay corporation tax on its profits and the real question was 'how much the Government was to collect from EDF and by what means'.
- (105) As for the Senate, its report preparatory to the debate on the draft law found that there was no justification for creating accounting provisions for the renewal of the RAG assets from 1987 onwards. When the draft law was presented to the Senate on 2 October 1997, the minister responsible stressed the 'fictitious' nature of EDF's losses from a tax point of view, as well as the non-payment of corporation tax resulting from the provisions. The minister reassured the Senate that the arrangements did nothing to call into question EDF's monopoly position. The Senate report outlined the consequences of the Article under scrutiny on the items in EDF's balance sheet before and after reclassification of the provisions, along similar lines to the National Assembly report, as set out in Table 2. It pointed out that cleaning up the balance sheet would make it easier to compare it with the balance sheets of EDF's competitors; this would make EDF more credible to the financial world, which was all the more important considering that the cost of debt renegotiation depended in particular on the debt/equity ratio.
- (106) As part of the 'clarification' of EDF's financial relations with the state, the Senate report stated that 'in exchange for the tax revenue that the public establishment would now pay to the state, the contract for services signed on 8 April 1997 for 1997 to 2000 provides for a slight reduction in EDF transfers to the state'. As a result of the writing back of the renewal provision of FRF 38,5 billion, making EDF liable for corporation tax, the Senate report stated that 'the financial relations between EDF and the state have been revised downwards'.



- (107) The other documents submitted by France include a cover letter dated 15 September 1997 from EDF's finance department to the Senate administration, to which were attached a table quantifying the effects of Article 4 of the draft law, and showing the effects on the balance sheet, a copy of the instruction of 27 July 1993 on the electricity distribution concessions and an internal EDF memo discussing foreign experiences of remunerating shareholders in the electricity sector, dated 27 July 1996. This memo explained the key principles applicable to remunerating shareholders, the disparity and return figures for certain undertakings in the sector: 60-80 % of profits in the US, 40 % for National Power and Power Gen, 78 % for Union Fenosa and 30 % for Endesa, giving the Spanish state a return of 28 % for the period 1991-1996 taking account of dividends and the increase in share price.
- (108) Despite the two further documents sent by EDF to the Senate with its letter of 15 September 1997, the principles, figures and their application to shareholder remuneration by EDF as set out in the memo of 27 July 1996 were not analysed or included in the Senate report. On the contrary, the Senate report, like that of the National Assembly, stated that the planned reduction in the remuneration on the capital contributions paid by EDF to the state as shareholder was: 'to take account of the increase in capital contributions brought about by this Article'.

#### 9. ASSESSMENT OF THE MEASURES: EXISTENCE OF STATE AID

- (109) Article 107(1) TFEU provides: 'Save as otherwise provided in the Treaties, any aid granted by a Member State or through state resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market'. The question whether these cumulative tests apply to the tax exemption granted by France to EDF is examined below.

##### 9.1. SELECTIVE ADVANTAGE TO AN UNDERTAKING

- (110) Since Act No 97-1026 established that EDF was deemed to have been the owner of the high-voltage transmission network (RAG) for which it had been granted the concession, it has to be ascertained whether the Act involved a transfer of ownership of the RAG.
- (111) According to the information provided by the French authorities, EDF can reasonably be regarded as the owner of the RAG before the entry into force of the Act. This finding is supported by the following considerations: the features of the different types of concession contract under French law; the special features of the original concession granted to EDF, which did not include an explicit retrocession clause; the procedure for the acquisition of the assets concerned, for which EDF had to pay a fee similar to compensation under a compulsory purchase procedure; and the conditions for the financing, maintenance and extension of the RAG at EDF's expense. The 'clarification' of the ownership of the RAG provided by Act No 97-1026 does not therefore in itself appear to confer an economic advantage on EDF.
- (112) It therefore has to be examined whether Act No 97-1026 addressed all the tax implications of the 'clarification' of ownership of the RAG and, if not, whether an economic advantage in the form of a tax concession was granted to EDF.

##### 9.1.1. *Waiving the tax owed by EDF constitutes prima facie a selective advantage*

- (113) During the period between 1987 and 1996, EDF created tax-free provisions for the renewal of the RAG, provisions which were identified as irregular by the French Court of Auditors. Article 4 of Act No 97-1026 declaring that EDF was deemed to be the owner of the RAG rendered those provisions superfluous and they therefore had to be reallocated to other items in the balance sheet.
- (114) The letter from the Minister for Economic Affairs setting out the tax implications of the restructuring of EDF's balance sheet shows that the unused provisions for renewal of the RAG were subjected by the French authorities to corporation tax at 41,66 %, the rate applicable in 1997.

- (115) On the other hand, the provisions corresponding to renewal operations already carried out, also called grantor rights, were reclassified as capital contributions amounting to FRF 14,119 billion without being subjected to corporation tax. The tax authorities acknowledge that this transaction was illegal, as can be seen from the memorandum dated 9 April 2002 addressed by the Directorate-General for Taxation to the Commission and quoted in recital 35.
- (116) In line with the National Accountancy Council opinion, corrections to accounting errors should be posted in the accounts for the financial year in which they are discovered. Moreover, since the unused provisions amounting to FRF 38,5 billion that had been created free of tax were subjected to corporation tax at the rate of 41,66 % in 1997, there is no objective reason why the rest of the provisions created free of tax should not have been taxed at the same rate.
- (117) The grantor rights should have been taxed at the same time and at the same rate as the other accounting provisions created free of tax. This means that the FRF 14,119 billion in grantor rights should have been added to the FRF 38,5 billion in unused provisions and taxed at the rate of 41,66 % applied to the restructuring of EDF's balance sheet. By not paying all the corporation tax due when it restructured its balance sheet, EDF made tax savings of FRF 5 882 849 762.
- (118) The tax measure was advantageous to EDF in 1997, as the amount of FRF 5,88 billion exempted from tax and included in the amount of FRF 14,119 billion was recorded in EDF's balance sheet as grantor rights reclassified by the state when it implemented Act No 97-1026 with retroactive effect from 1 January 1997. The tax implications of the Act are set out in the letter from the Minister for Economic Affairs with effect from the same date of 1 January 1997.
- (119) The French authorities claim that, even if EDF had not set aside provisions for the renewal of the RAG, it would still not have been liable for payment of corporation tax between 1987 and 1996 because of the tax loss carry-forward. That argument misses the point. The tax advantage dates from 1997, not from the preceding years. Moreover the irregular provisions were in part responsible for the tax loss carry-forward. The carry-forwards would have been gradually absorbed between 1987 and 1996 and the amount of tax payable by EDF would have been significantly higher, even without taking account of the non-payment of tax for the reclassification of the grantor rights.
- (120) The French authorities also take the view that, even if the creation of provisions for the renewal of the RAG resulted in an advantage, that advantage should be regarded as cancelled out by the increase in corporation tax paid in 1997. However, as the French authorities themselves acknowledged in their memorandum dated 9 April 2002 and quoted in recital 35, although the unused replacement provisions were correctly taxed, the grantor rights were reclassified as capital contributions without being subjected to corporation tax. The tax paid by EDF in 1997 is therefore lower than the tax normally due.
- (121) The French authorities also claim that, over the period from 1987 to 1996, EDF paid more to the state overall than the corporation tax that would have been paid by a commercial company which did not create provisions for the renewal of the RAG and which paid its shareholder a dividend equal to 37,5 % of its net income after tax. Moreover, the rate of corporation tax that should have been applied when EDF's balance sheet was restructured was the 1996 rate and not the 1997 rate.
- (122) First, as stated in recitals 32 and 116, the National Accountancy Council takes the view that corrections to accounting errors should be posted in the accounts for the financial year in which they are discovered. Since the provisions for renewal of the RAG became superfluous following Act No 97-1026 of 10 November 1997, they should have been reclassified in the accounts for the 1997 financial year and therefore taxed at the rate of corporation tax applicable to that year. Second, the French authorities themselves applied the 1997 rate of corporation tax to the share of the provisions that was taxed, as set out in recital 34.
- (123) The non-payment by EDF, in 1997, of FRF 5 882 849 762 in corporation tax constitutes an economic advantage for the undertaking. EDF was able to use this amount to increase its own funds without having to raise outside finance. If the tax had in fact been paid and the increase in own funds financed by the undertaking's operating profit, it would have had to cut costs, increase profit or refrain from investment expenditure. By having at its disposal amounts that should have been paid to the French state by way of corporation tax, EDF benefited from a selective measure which placed it at an advantage over French undertakings in a similar situation, and which had to pay corporation tax on the reclassification of irregular provisions under Article 38-2 of the General Tax Code in force in 1997, as set out in recital 35.

- (124) However, in its comments of 11 December 2002, France called for application of the principle of the prudent private investor in a market economy. As pointed out by the EU courts in their judgments referred to in recitals 7 and 8 in this case, a further capital contribution to EDF of an amount equal to the tax owed could not be regarded as conferring an economic advantage on the undertaking within the meaning of Article 107(1) TFEU, if it was established that a hypothetical private shareholder would have invested an equivalent amount in EDF, on similar terms and in similar circumstances, in accordance with the prudent private investor in a market economy test.
- (125) In paragraph 99 of its judgment of 5 June 2012, the Court of Justice stated that, by the judgment under appeal, the General Court had not prejudged the applicability of that test to the present case or the outcome of applying that test. The applicability and application of that test to the facts of the case must therefore now be examined in the light of the criteria set out by the Court of Justice.

#### 9.1.2. *Applicability of the principle of the prudent private investor in a market economy*

- (126) To determine whether the principle of the prudent private investor in a market economy is applicable, an overall assessment must be made of whether the French Republic granted the tax exemption in its capacity as shareholder or in its capacity as public authority. In its judgment of 5 June 2012, the Court of Justice set out a number of factors that should be taken into account in this overall assessment. These factors, examined in more detail below in relation to the circumstances of the case, are:
- the Member State must, where there is doubt, establish unequivocally and on the basis of objective and verifiable evidence that the measure implemented falls to be ascribed to the state acting as shareholder <sup>(1)</sup>; 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 make an investment, by means of the measure actually implemented, in the public undertaking <sup>(2)</sup>,
  - in that regard, it may have to produce evidence showing that the decision was based on economic evaluations comparable to those which, in the circumstances, a rational private investor 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 its future profitability <sup>(3)</sup>; the Commission may refuse to examine evidence established after the decision to make the investment in question <sup>(4)</sup>,
  - the nature and subject-matter of the measure are relevant in that regard, as is its context, the objective pursued and the rules to which the measure is subject <sup>(5)</sup>,
  - application of the private investor test must make it possible to determine whether, in similar circumstances, a private shareholder would have subscribed, to an undertaking in a situation comparable with that of EDF, an amount equal to the tax due <sup>(6)</sup>.
- (127) In their comments of 11 December 2002 referred to in recital 42, the French authorities argued that it was thought to be more efficient and more neutral for EDF to allocate the grantor rights directly, and in their full amount, to own funds, without paying corporation tax. However, none of the documents prior to or contemporaneous with the supposed decision not to levy tax, that were submitted by France or EDF in support of their comments on the decision to extend the formal investigation procedure, made any direct or indirect mention of the supposed decision to invest, with its implications, benefits or costs, or of the corresponding decision to increase the amount of contributed capital by not levying tax. The documents submitted by the French authorities as described in recitals 87 to 108 do not mention, still less analyse, the benefits or costs for the state of the decision not to levy corporation tax on the part of the grantor rights reclassified as capital under Act No 97-1026 of 10 November 1997.
- (128) It is for France, in the event of any doubts, such as those formulated by the Commission, about the applicability of the prudent private investor in a market economy test, to establish unequivocally and on the basis of objective

<sup>(1)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 82.

<sup>(2)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 83.

<sup>(3)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 84.

<sup>(4)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 104.

<sup>(5)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 86.

<sup>(6)</sup> Judgment in *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 95.

and verifiable evidence that the measure implemented falls to be ascribed to the state acting as shareholder. However, in the light of the evidence provided, the decision to make an investment by way of waiving the tax EDF should have paid must be deemed to have been taken tacitly, without a reasoned legal act that would reveal the precise content of the decision, its grounds and legal basis or by what authority and on what date it was taken. In the light of the factors set out by the Court of Justice for establishing the applicability of the prudent private investor in a market economy test, namely the need for objective and verifiable evidence, a measure that has actually been implemented or economic evaluations carried out in advance, the absence of references or material evidence must be regarded as an initial indication that the test is not applicable.

- (129) In the absence of any documentary evidence tracing the supposed decision, the investment measure that the French state might have taken needs to be described. In this case, the Court of Justice found that application of the private investor test must make it possible to determine whether, in similar circumstances, a private shareholder would have subscribed FRF 5,88 billion to an undertaking in a situation comparable to that of EDF. An investment by France would constitute waiving the collection of this amount with a view to making a profit greater than the resources initially invested. The analysis must therefore be made with reference to the amount of corporation tax due.
- (130) The absence of any specific studies, references or analyses of the profitability of the investment in the amount of the tax exemption makes it difficult to isolate the effects of the supposed investment in the information submitted by France or by EDF. This difficulty is not insurmountable if, for the purposes of analysing most of the factors relevant for determining the applicability and the application of the prudent private investor principle, the additional capital contribution to EDF equivalent to the amount of unpaid tax is regarded as benefiting from the rights attaching to all the capital contributions. So, if the capital contributions were remunerated at a certain rate, this rate had to be, and indeed was, applied to the amount of unpaid tax. If, on the other hand, the marginal or incremental effect is taken into account, the information provided by France or EDF does not at first sight demonstrate that the amount of contributed capital was increased by the amount of unpaid tax.
- (131) The non-collection of the tax had the effect of increasing the capital contribution to EDF, and thus EDF's own funds, by an additional FRF 5,88 billion, within the overall amount of FRF 14,119 billion of reclassified provisions. These provisions, which did not correspond to a prior injection of fresh capital by the state as shareholder, were reclassified as capital contributions and posted under the corresponding item in the upper part of EDF's balance sheet, together with the other equity items (paid-in capital, contributed capital, etc., see Table 2). Without the tax exemption, EDF's own funds, which were to reach FRF 79,8 billion in 1997, would have reached FRF 72,1 billion, according to the documents examined at the time (see Table 2, recital 100). Instead of FRF 50,7 billion, the state contributions to EDF's capital would have stood at FRF 44,8 billion.

#### Supposed investment decision: factors for analysis

- (132) First, as pointed out by the French authorities, given that the amount in unpaid tax was included in the capital contribution base, and that this was remunerated at a fixed rate (3 %), the absolute value of the remuneration to the state was increased by the tax exemption (or non-collection, see recital 83). However, the increase in the capital contribution by the amount of the tax exemption did not have the effect of increasing the state's remuneration in relative terms. It is common ground that the remuneration for the capital contributed to EDF by the state was laid down as from Decree No 56-1360 of 30 December 1956 (recitals 18 and 103). Different types of remuneration were therefore included in the contracts which preceded and succeeded the 1997-2000 contract for services, as set out in recitals 93 and 102. The principle of remuneration pre-dated the supposed decision and was maintained afterwards.
- (133) Moreover, an examination of the facts demonstrates that the tax exemption had the effect of reducing the state's return on its investment. The report produced by the National Assembly in September 1997 unequivocally shows that the increase in the total capital contribution was the reason for the reduction in the remuneration so as not to 'increase the payment burden on EDF' (recital 103). The Senate report confirms this deliberate reduction by the public authorities (recital 108).
- (134) Between 1991 and 1996, EDF gave the state a higher return for a lower capital contribution base compared with what was offered between 1997 and 2000 for a higher base. The average annual remuneration in absolute terms

of FRF 3,41 billion for 1991-1996, when the amount of the capital contribution came to FRF 36,6 billion, was well above the FRF 2,35 billion put in place for a base increased to FRF 50,7 billion during the 1997-2000 period (recitals 92 and 102-103, Table 3). It follows that the current marginal return on the FRF 5,88 billion increase in the amount of contributed capital expected in the 1997-2000 period by the state as shareholder was lower than in the period 1991-1996.

- (135) The French authorities saw to it that the remuneration paid to the state on its capital contribution fell, in absolute and relative terms, as the contribution base increased, as unequivocally established by the National Assembly and Senate reports. It follows that, by increasing the total capital contribution with a lower return than the contribution which pre-dated Act No 97-1026, the decision to grant a tax exemption did not necessarily constitute an investment.
- (136) Second, the way in which the remuneration on the increased capital contribution was determined is not what a prudent private investor in a market economy might have chosen.
- (137) As demonstrated by the references contained in the letters from the line ministers and the parliamentary reports referred to in recitals 97, 103 and 106, in making their 1997 scrutiny of the French state's remuneration after the restructuring of EDF's balance sheet, the French authorities took account both of the return on the capital contributions due to the state as shareholder in the strict sense, and of the expected amount of tax that the state, acting as a tax-raising public authority, would collect after 1997 following several years of tax loss carry-over. As set out in recital 93, the remuneration on the capital contributions was in its turn deductible from income tax, by way of exception to the ordinary law.
- (138) The concept examined and adopted by the French authorities in 1997 was therefore one of the overall amount collected from EDF, tax and shareholder remuneration combined. The overall amount of tax collected from EDF, above and beyond the contested exemption, under the state's tax-raising powers, and the remuneration paid to the state as shareholder, are mixed up together in the evidence submitted by the French authorities. Nevertheless, in their view, this evidence points to the existence of an investment decision. On the contrary, the fact that the payment of tax due by EDF to the state as revenue collector, including by the regularisation and discharge of the tax that had not been collected prior to Act No 97-1026, was constantly taken into account for the purposes of examining and setting the remuneration to the state as shareholder tends to indicate that the disputed tax exemption was adopted by the state acting as a public authority and not as an investor.
- (139) This impression is reinforced by the nature of the objectives set for EDF by the state in 1997 in the light of the concerns and goals of a public authority, not a shareholder. These concerns are reflected in the setting of EDF's tariffs, as agreed in the 1997-2000 contract for services, under which the state as shareholder was remunerated. The state asked EDF to help boost the competitiveness of French industry and the purchasing power of French households. Not only would such concerns have been alien to a prudent private investor in a market economy, they would have run counter to the hypothetical investor's financial interests. The same goes for the objective laid down for EDF in the 1997-2000 contract for services to put in place an ambitious policy to support economic activity and employment by helping local authorities (recitals 89 and 95).

#### Economic evaluations to determine the profitability of the supposed investment

- (140) The contract for services between EDF and the state signed on 8 April 1997 contained a prior evaluation of the financial scenario, including projections of the return for the state as shareholder on the investment in the form of contributions to EDF's capital (recital 92). The documents and analyses put forward by the French authorities relate to the expected effects of reclassifying all the provisions constituted by EDF, whether mandatory or not, whether resulting from Act No 97-1026 or not. The only systematic evaluation presented by the French authorities in the EDF memo of 18 February 1997 (recital 92) is general and confined to the statutory remuneration on the capital contributions, including those pre-dating the restructuring of EDF's balance sheet, but excluding, for example, remuneration on other capital or own funds.
- (141) None of the documents submitted by France or by EDF demonstrate that the supposed investment decision, namely to make a bigger capital contribution to EDF by waiving tax on the reclassification, was the subject of specific scrutiny, study or analysis. However, given the amounts involved, a prudent private investor in a market

economy would in all probability have conducted a financial and economic analysis of the investment before deciding whether, in view of the statutory return on the capital contributions, the amount of FRF 5,88 billion in tax exemption was needed for the undertaking to guarantee the long-term profitability of its overall investment and for the shareholder to be sufficiently remunerated. This type of prior economic study, cited by the Court of Justice in paragraph 84 of its judgment as one of the conditions for the private investor test to apply, is absent.

- (142) It is particularly striking that, apart from the remuneration to be paid to the state over the 1997-2000 period, no study of the remuneration or return in the longer term was carried out, although France claims precisely to have made a long-term investment. However, a prudent private investor in a market economy would not have neglected to conduct an analysis of the profitability of the investment for the period after the year 2000.
- (143) While it is reasonable to suppose that a prudent private investor in a market economy would have taken into account the effects of the reduction in EDF's debt ratio, it must be noted that the advantage to EDF of lower-cost borrowing on account of an improved debt/equity ratio is referred to in general terms in some of the documents furnished by France (recitals 101 and 105) and EDF. However, none of the documents mentions the advantages and the profitability for the state as shareholder of a reduction in EDF's borrowing costs or a lower debt ratio. According to the figures produced at the time as set out in recital 101, EDF's net debt/equity ratio was to drop to 148 % as a result of the new capital contribution overall, which came to FRF 50,7 billion, including the FRF 5,88 billion by way of the contested exemption. Without the tax exemption, the ratio would have been around 163 %, or some three times lower than the ratio of 480 % before Act No 97-1026. Considered separately from the other effects of the reclassification of the various provisions, the contribution of the tax exemption to the improvement in the ratio is negligible and it is very doubtful that it had a real effect in terms of reducing the cost of borrowing for EDF (recitals 170 to 172). In any event, the documents submitted by the French authorities do not mention or analyse in investment terms the return for the shareholder resulting from a ratio of 148 %, still less a ratio of 163 %. In this connection, there are no prior economic evaluations comparable to those which a rational private investor in a market economy would have had carried out, as referred to by the Court of Justice in paragraph 84 of its judgment.
- (144) The economic study submitted by EDF in support of its comments (recitals 69-70) does not find that France acted as an investor rather than a public authority. The study was produced after the supposed investment decision taken in 1997 and was not examined by the authorities responsible for taking such a decision. For this reason alone, the study is not admissible as evidence, as set out by the Court of Justice (recital 126, paragraph 104 of the judgment of 5 June). The fact that the study used authentic basic data available at the time does not invalidate this conclusion. The study was commissioned to support the case following the extension of the investigation procedure in May 2013 and the conclusions it would reach were apparently known to EDF in July 2013, although the study dates from October 2013. Other grounds also invalidate the quantified findings of the study, and consequently undermine the conclusions that EDF draws from it in support of its comments; these grounds are:
- The study uses basic data almost exclusively from the time and applies widely recognised methodological approaches for evaluating enterprise value, subject to the major reservations set out below. For all that, it constitutes a particularly complex economic evaluation, following relatively thorough data research, which took some three months to carry out and validate. This complex process comprised successive and various methodological choices, some of which are questionable. Without this process, it is quite impossible, from the basic data drawn from scattered and diverse sources, to form an overall view or make a quantified projection of the profitability that the French state could expect in 1997, as the study does. However, the Court of Justice requires the private investor test to be based on evaluations which were foreseeable at the time when the decision to make the investment was taken (paragraph 105 of the judgment of 5 June 2012). Contrary to what is claimed by EDF, the very fact that, with data available in 1996-1997, the relevant authorities of the French state did not themselves carry out or commission a study on this scale and with this level of complexity indicates that the profitability of the investment for the shareholder was not the sole relevant consideration for the French authorities when they took their decision.
  - The study analyses the conduct of the French state in the light of the private investor principle using information and hypotheses that are very different from those outlined in recitals 87 to 108 and which, according to the French authorities, formed the basis for the supposed decision. However, it is not EDF which took the investment decision, and, according to the Court of Justice (paragraphs 82 and 83 of its judgment of 5 June 2012), it falls to France to produce evidence of the nature and context of the decision taken. Since

France alleges that it was in the light of the information and data submitted by it that it took its decision, the study, and EDF, are *de facto* substituting themselves for the alleged investor and claiming to know better than the French state the concerns and information that supposedly underpinned the decision taken and the hypotheses used to reach it. As such, the study is based on speculation and conjecture with respect to the data, information and hypotheses that the French authorities might have taken into account (among other possible options) in 1997 and has no force as evidence in 2015 (or October 2013, when it was carried out) to explain the decision taken by the French authorities in 1997, which these authorities themselves explain with reference to different data and hypotheses.

- The study's value as evidence is undermined still further by the fact that, to reach the findings outlined in recital 70, the study relies on hypotheses which are arbitrary or random, or uncorroborated by the facts, or counter to the information contained in the evidence provided by the French authorities and which, according to them, illustrates that the private investor test is applicable and does in fact apply in this case. So, first, the study conjectures that after 2000, the remuneration paid to the state as shareholder would not be regulated by decree and contained in a contract between the state and EDF but would be set by reference to the dividends which other undertakings in the sector paid in 1996-1997 <sup>(1)</sup>. However, the remuneration on the capital contributions to EDF had been regulated by decree since 1956 (recital 102) and was statutory and reflected in the multiannual contracts before and after 1997, in the light of considerations unrelated to the dividends paid by undertakings in the sector operating in markets other than France (recitals 94 and 95). Likewise, and in second place, the study, with no good reason, reintroduced into EDF's income statement provisions from EDF's company accounts worth FRF 11,6 billion (before tax) and FRF 7,3 billion (after tax) <sup>(2)</sup>, artificially increasing EDF's value by that amount without taking account of the information which was available and the developments which were foreseeable in 1997 with respect to EDF's commitments under its staff pension scheme (recitals 168-169).
- Thirdly, the increase in the value of EDF resulting from the increase in return and results is calculated in the study on the basis of the 'market expectations' in 1997 <sup>(3)</sup>. However, the French authorities had specific and quantified projections for EDF's revenue and income for 1997 to 2000, validated as part of the process of drawing up the contract for services for the same period and stated that they relied on these projections and data to take their decision (recitals 78-79, 90, 94, 96); they also had in 1997 detailed knowledge of the undertaking and its financial prospects (recital 77). The use of 'market expectations' from third parties to estimate EDF's value in these circumstances is neither reliable nor consistent with the arguments put forward by France to explain the decision which its authorities are supposed to have taken, all the more so since the French authorities argue that most of EDF's business in 1997 was conducted in France subject to regulated tariffs (recital 85). Moreover, these tariffs were set at a low level with a view to boosting the competitiveness of French industry and the purchasing power of French households (recitals 89 and 95). The study fails to explain, still less to justify, why the remuneration, dividends and results of listed companies which had no significant presence in France and operated in markets subject to different competitive and regulatory constraints (such as Endesa, Gas Natural and Union Fenosa in Spain, RWE, EON and Verbund in Germany, Fluxys in Belgium, etc.) should determine the results, remuneration and dividends of EDF, which is one of the hypotheses on which the findings set out in recital 70 are based <sup>(4)</sup>.
- Lastly, and in fourth place, the study postulates with no justification that increasing the capital contribution to EDF in 1997 was, at least potentially, equivalent to acquiring a liquid financial asset <sup>(5)</sup>. However, in 1997 EDF was a public industrial and commercial establishment with no share capital (recital 19), with the French authorities and EDF affirming at the time that it would retain this status in the future (recitals 95, 105). The arbitrary nature of this postulation, on which the findings of the study none the less crucially depend, is demonstrated in more detail in recitals 179 to 181.

Nature and subject-matter of the measure, its context and the rules to which it is subject

- (145) The Court of Justice states that the nature of the measure is one of the relevant factors to take into account when ascertaining whether the private investor principle is applicable (paragraph 86 of its judgment). The decision to

<sup>(1)</sup> Oxera study, points 3.3, 3.24-3.25.

<sup>(2)</sup> Oxera study, Table A2.2.

<sup>(3)</sup> Oxera study, point 3.3.

<sup>(4)</sup> Oxera study, points 3.3, 3.15, Table 3.2, Table 3.8 for beta coefficient and Annex 5.

<sup>(5)</sup> Oxera study, points 3.5, 3.13, 3.20 to 3.23.

contribute additional capital to EDF by waiving the tax on the reclassification of the irregular RAG provisions is both an accounting decision on moving amounts between different items on EDF's balance sheet (recitals 100 and 105) and a tax decision, since the authorities responsible deemed that the corporation tax should be levied before reclassification (recital 35), even though tax was paid on other reclassified accounting provisions. Contrary to what is claimed by the French authorities, it has not been established that the two accounting and tax strands are indissociable within a single measure put in place by Act No 97-1026 of 10 November 1997.

- (146) Article 4(2) of the Act provides that the value of the assets in kind allocated under concession to the RAG and appearing as liabilities on EDF's balance sheet should be entered, net of the corresponding revaluation reserves, under the item 'contributed capital' (recital 28). It could be concluded that, under the Act, any revaluation reserves aside, no further accounting or tax treatment was to reduce the value entered as a capital contribution to EDF. However, in accordance with Article 34 of the French Constitution, the decision to levy tax or not is not a matter regulated by law, and Act No 97-1026 could not therefore legitimately settle this question. Under this Article, Parliament's legislative powers in tax matters are confined to setting the base, rates and collection procedures for tax of all kinds. EDF paid corporation tax on some accounting provisions and not on others following the same reclassification operation provided for in the Act.
- (147) Furthermore, the preparatory documents submitted by the French authorities and referred to in recital 104 show that the Council of State took the view in 1997 that non-legislative provisions should be eliminated from the draft law; a draft amendment designed to limit the amounts that the state could collect from EDF under the Act was also rejected. Lastly, the line ministers took the view in April 1997 that the detailed arrangements for implementing EDF's restructuring, on both the accounting and the tax fronts, should be the subject of further discussions between the supervising authorities and the undertaking (recital 98).
- (148) These implementation arrangements, detailed and quantified in the letter from the line ministries to EDF on 22 December 1997, following the adoption of the Act (recital 31), suggest that the tax elements were dissociable from the provisions of Act No 97-1026 of 10 November 1997. In their letter the ministers explain the restructuring of the upper part of EDF's balance sheet pursuant to Article 4 of Act No 97-1026 of 10 November 1997 and appear to reach a tacit decision on the tax implications of the restructuring, without there being any question of a profitable investment or of any mandatory requirements of the law.
- (149) As regards the context of the measure, this being one of the factors cited by the Court of Justice for the purposes of ascertaining the applicability of the private investor test, the preparatory meetings and supporting documents dating from the period, and which resulted in the contract for services between the state and EDF signed on 8 April 1997, demonstrate that the reclassification of the provisions took place in the light of the prospect of the partial liberalisation of energy markets in the EU, planned as from 1996. Hence the concern for EDF's activities to become more international evident in the 1997-2000 contract and the preparatory documents, as well as the parliamentary documents. The contract itself presupposes that its implementation will require a regularising legislative measure such as that laid down in Act No 97-1026, thereby establishing a *de facto* link between the objectives of the contract and of the legislator. However, neither the contract concluded in April 1997 nor the preparatory documents or exchanges with EDF's line ministries take a position on the precise amount of tax.
- (150) This context, outlined by the evidence cited by France in its comments, does not, however, establish beyond doubt that the measure could be ascribed to a shareholder making an investment. The need to correct the irregularities identified by the Court of Auditors in October 1994 is also part of the picture. While, on one side, there was a need to correct an accounting irregularity that had allowed EDF to avoid paying corporation tax for years, on the other, the French authorities stressed that the measure did not call into question EDF's monopoly (recital 105) and that the stable framework allowed by the liberalisation of the market should be maintained (recital 95). Although liberalisation opened up possibilities for expansion into the national markets of other Member States and some measures were included in the 1997-2000 contract for services so that EDF could become more international, the concern of the public authorities to place national undertakings at an advantage through financial support in the early stages of liberalisation was not confined to public undertakings; nor does it constitute typical behaviour by a prudent investor in a public undertaking.
- (151) Lastly, the Court of Justice states that the rules to which the disputed measure is subject are relevant for determining whether it constitutes an investment by the state as shareholder or a prerogative of a public authority. Classing the measure as one or the other may therefore take account of compliance with the rules governing it. The rules governing the investment of tax resources in undertakings like EDF must therefore be



examined. Without the measure, the revenue from the uncollected corporation tax would have been paid into the general revenue of the budget of the French state in 1997. Under Article 18 of Order No 59-2 of 2 January 1959 laying down an organic law for budget laws, which was in force at the time of the facts, as all revenue is used to implement all expenditure, all revenue and all expenditure of the state are posted to a single account, called the General Budget. So, tax revenue is posted to the budget for the benefit of the state, and not for the benefit of public undertakings.

- (152) The budget is subject to the constitutional principle of universality, whereby all revenue and all appropriations are posted as two separate blocks, with no specific link made, for example, between revenue from corporation tax and an allocation such as a capital contribution to a public undertaking like EDF. Of course, the pre-allocation of a tax resource to a legal person other than the state in the form of a subsidy or an investment is possible under French law, where expressly provided for. Article 18 of Order No 59-2 thus provided that, apart from in the case of loans and advances in particular, the allocation of state resources was exceptional and could take place only pursuant to a provision of a budget law, which was for the government to adopt.
- (153) However, Act No 97-1026 of 10 November 1997 was not a budget law and as such could not allocate a tax resource to EDF's capital. Moreover, there do not appear to have been any specific government initiatives to adopt budget-law provisions applicable to the 1997 budget with a view to pre-allocating the revenue from the tax owed by EDF to expenditure by the French state on any investment in EDF's capital as part of the same budget. The rule allowing the investment of a tax resource constituted for the benefit of the state in a legal entity distinct from the state, such as EDF, does not seem to have been applied here.
- (154) The vast majority of the evidence described above clearly shows that France did not, either before or at the same time as conferring the economic advantage resulting from the non-payment of the corporation tax, take a decision to make an investment in EDF by way of the tax exemption. Accordingly, the prudent private investor in a market economy principle does not appear to be applicable to this measure. The considerations set out below on the application of the private investor test are therefore provided in the alternative.

### 9.1.3. *Application of the principle of the prudent private investor in a market economy*

- (155) In its judgment of 5 June 2012 in the present case, the Court of Justice held that application of the private investor principle should make it possible to determine whether, in similar circumstances, a private shareholder would have subscribed, to an undertaking in a situation comparable to that of EDF, an amount equal to the tax due (paragraph 95 of the judgment). Any difference between the cost to the private investor and the cost to the state as investor may be taken into account when assessing whether the conditions laid down by that principle are met (paragraph 96 of the judgment).
- (156) The assessment must be carried out by reference to the objective and verifiable evidence which is available and the developments which were foreseeable, at the time when the decision to make the investment was taken (paragraphs 102 and 105 of the judgment). On that view, only the benefits and obligations linked to the situation of the state as shareholder — to the exclusion of those linked to its situation as a public authority — are to be taken into account (paragraph 79 of the judgment).
- (157) In view of the situation and the characteristics of EDF, which had existed as a public corporation fully controlled by the French state for over 50 years, it is advisable to keep in mind the benchmark of an investor pursuing an objective of long-term profitability and to examine in particular the information supplied by France as set out in recitals 87 to 108. It is this information that the French authorities relied on as the basis for their own decision in 1997.

- (158) First it is necessary to examine the rate of return that EDF gave its shareholder in 1997. This rate of return must be compared with reference values. In 1997, the average rate of return on French long-term bonds (30 years) was 6,35 %. Even for shorter maturities (10 years) — shorter than the life cycle of EDF's installations — the average interest rate on French Government securities was 5,58 % <sup>(1)</sup>. These values represent both the return on financial assets deemed to be low risk and the French state's long-term financing cost at the time. An investment in an undertaking such as EDF in 1997 was a riskier investment than holding government bonds during the same time period. As a result, a prudent private investor in a market economy would have required a better rate of return than the rate for government bonds.
- (159) Analysis of the current rate of return that the French state could expect in 1996-1997, as revealed by the documents submitted by the French authorities, does not justify the conclusion that the investment met the test of the prudent private investor in a market economy.
- (160) The French authorities forwarded EDF's projected income statement for the period subsequent to the restructuring of the balance sheet, as examined in 1997 by the authorities concerned (recital 92, Table 1). The estimates in the table are corroborated by other contemporaneous documents (recitals 96-97, 103). These EDF baseline scenario estimates for the following period had been validated by the state authorities (recital 97). From this income statement, and from the expected amounts of resources invested by the state in EDF (recital 100, Table 2), it is possible to calculate the rate of return that the state could have expected on contributions to capital, to total capital (initial capital plus contributions) and to EDF's equity (total capital, revaluation reserves, reserve requirements and retained income) <sup>(2)</sup>, as shown in Table 4.

Table 4

**Estimated remuneration from the capital on EDF's balance sheet 1997-2000 (billion FRF)**

	1997	1998	1999	2000	1997-2000
Portion fixed at 3 %	1,5	1,5	1,5	1,5	6,0
Variable portion	0,6	1,0	0,9	0,9	3,4
Fixed and variable portions	2,1	2,5	2,4	2,4	9,4
Return on equity (FRF 79,8 billion) (%)	2,63	3,13	3,01	3,01	2,94
Return on capital and contributions (FRF 53,3 billion) (%)	3,94	4,69	4,50	4,50	4,41
Return on contributions to capital (FRF 50,7 billion)	4,14 %	4,93 %	4,73 %	4,73 %	4,64 %

Source: Commission calculations based on Tables 1 and 2

<sup>(1)</sup> Annual average of the daily rate of the 30-year and 10-year French bellwether bond, source Bank of France: Benchmark rate of treasury bonds and fungible government bonds, <http://www.banque-france.fr/economie-et-statistiques/changes-et-taux>

<sup>(2)</sup> The relevance of a calculation of the rate of return on the total equity tied up in the undertaking in relation only to the capital invested in the form of capital contributions is confirmed by the fact that, in the contract between the State and EDF for the period 2001-2003, the State's remuneration calculated as a percentage (37,5 %) of net income was confined within a minimum (1,5 %) and maximum (4,5 %) range of the equity base. Reply by the French authorities of 23 December 2013, point 53.

- (161) It is clear from the documents referred to and submitted by the French authorities that in 1997 the remuneration the state as shareholder expected from EDF for the whole period 1997-2000 was FRF 9,4 billion, of which FRF 6 billion was in respect of the portion at the fixed rate of 3 % and EUR 3,4 billion for the whole period in respect of the supplementary portion, after the reclassification made by Act No 97-1026. On the basis of the estimates validated at the time, on average, the future current rate of return that the state as shareholder could expect was 2,94 % of EDF's total equity, 4,41 % of the total capital invested by the state in EDF and 4,64 % of the amount of the contributions to capital. This rate of return, applicable to the amount of the tax exemption reclassified as contribution to capital, was well below the 6,35 % paid on the bonds that the French Government issued in 1997 with a view to its own long-term financing. A prudent private investor in a market economy would have found that the expected current rate of return on an amount of FRF 5,88 billion corresponding to the tax exemption was insufficient to justify the investment.
- (162) Furthermore, the Court of Justice held in paragraph 96 of its judgment of 5 June 2012 that it is possible in the context of the application of the principle of the prudent private investor in a market economy to take into account the difference between the investment cost to a private investor and the cost to the state. This amounts to comparing the rate of return which, according to the French authorities, justified the reclassification of the grantor rights provisions at the amount of the tax exemption, with the rate that would have been obtained by a private shareholder on the same recapitalisation operation in an undertaking similar in every respect to EDF, except for the prerogative, which is not available to the private investor, to exempt the capital contribution from corporation tax.
- (163) Such an undertaking whose shareholder had FRF 5,88 billion available to recapitalise it under conditions identical to those of EDF would have had the prospect of an annual return of 4,64 % on the additional capital invested by the shareholder, i.e. FRF 272 million per year, without taking account of corporation tax. By applying the rate of corporation tax of 41,66 % applicable in 1997, the prospective rate of return would be FRF 159 million per year for the same capital contribution, or a nominal annual rate of return of 2,7 %. Such a rate for a share in the capital of a company with the risks associated with such an investment must be compared with 6,35 % paid on French bonds at that time. The low rate of return would have deterred a private investor who did not have the tax privileges of the state. With such poor prospects of return on the invested capital, it appears out of the question that a prudent private investor whose company is liable for corporation tax on contributions to capital would, instead of France, have participated in the increase in the capital of EDF in 1997.
- (164) It is therefore necessary to examine whether the evidence and information dating from the time of the decision to reclassify the provisions without levying the tax submitted by France contain additional information which would have convinced a prudent private investor to make the alleged investment notwithstanding the apparent very low rate of return. These details may relate in particular to the capacity of EDF (i) to increase its long-term operating income; (ii) to improve its operating results through efficiency gains; (iii) to increase the net value of the productive assets of the undertaking; or (iv) to provide a steady and adequate remuneration for its shareholder. These are factors which have the potential to create long-term value for the shareholder with a positive outlook, but destructive of value with a negative outlook.
- (165) In this respect, none of the documents forwarded by the French authorities contain a quantification, or even a qualitative assessment, of any potential creation of value for the shareholder that the French authorities examined and took into account for the period 1997-2000 or beyond. There are only general references to taking better account of the interests of the state as shareholder. This would indicate that the increase in the undertaking's value as an investment for the state as shareholder was not taken into account in deciding on the investment claimed. In any event, examination of four factors that potentially create value for the shareholder does not justify a conclusion of foreseeable growth on the basis of the data available in 1997, in particular EDF's forecast operating account 1997-2000 and the financial scenario forecasts used by the supervising authorities (recital 92, Table 1, recital 96).
- (166) In terms of EDF's total revenue, the state as shareholder could expect to receive a very small increase of 0,64 %. This virtual stagnation can be explained by the objective set by the state to contribute 'to the competitiveness of French industry and the purchasing power of domestic consumers', which resulted in an average reduction of [...] % in EDF's tariffs over four years (recitals 89, 95-96), which represents an annual decrease of [...] %. EDF conducted its business mainly in France since, for the period from 1997 to 2000, it was envisaged that more than 89 % of EDF's revenues would come from the French market. Therefore, the majority of its revenue depended on the choices the state made in setting electricity tariffs. A prudent private investor would not have failed to note that the setting of public policy objectives contrary to its interests as shareholder was prejudicial to its proprietary interests. No prudent private investor would have agreed to lower earnings from its investment to foster the competitiveness of French undertakings.

- (167) The item in the projected income statement 1997-2000 showing the income from EDF's core business was also set to decrease by 29 % during the period, from FRF 9,3 billion in 1997 to FRF 6,6 billion in 2000. Operating expenses were, for their part, set to increase by 2,2 %, mainly owing to the increase in day-to-day operating expenditure, since financial charges, depreciation and interest, excluding return on capital, were set to decrease. Adding depreciation and financial charges to the income from the core business, the outlook for the period 1997-2000 was also negative, because this aggregate was set to decrease from FRF 62,6 billion to FRF 53,9 billion, i.e. by 13,9 %. However, it is the trend in income from everyday operations before depreciation and interest that determines the future capacity of the undertaking to generate value and a positive cash flow. In addition to the projected deterioration, in pursuit of economic policy or regulatory objectives, the state had set EDF the objective of allocating any earnings from efficiency and productivity gains to further reducing tariffs, which was to take priority over a better return for the shareholder (recital 95). It follows that EDF's ongoing activities, weighed down by the state's economic policy objectives, would not have offered the prospect of satisfactory future earnings.
- (168) As the Commission pointed out in the extension decision, a prudent private investor would have taken account of the uncertainty about the amount and evolution of the pension financing charges facing EDF in 1997 under the specific scheme for the electricity and gas industries. In the case of EDF in 1997, the cost of pensions and, a fortiori, the related off-balance-sheet commitments represented an encumbrance in anticipation of additional drains on the undertaking's already poor net result.
- (169) Whereas EDF's pension bill amounted to FRF 12,2 billion in 1997, assuming no change in legislation, the pension bill for the entire scheme (including GDF and non-nationalised undertakings) was expected to grow significantly in the following years to reach FRF 20 billion in 2010 and FRF 25 billion in 2020 <sup>(1)</sup>. By applying an allocation key of 78,4 % for EDF, reflecting the weight of its wage bill in the industrial sector covered by the scheme, EDF's share would have been FRF 15,7 billion in 2010 and FRF 19,6 billion in 2020, without taking account of any provision made for future commitments, assuming no change in legislation <sup>(2)</sup>. The expected increase in pension costs was therefore bigger than net earnings, after remuneration of the state and tax, foreseen for the period 1997-2000, as illustrated in Table 1. Therefore, any appraisal by a prudent private investor in a market economy in 1997 with, like the French state, a thorough knowledge of the situation of the undertaking, would have led the investor to accentuate the future liabilities of the undertaking and to downplay accordingly the profitability prospects of the investment.
- (170) In addition, the prudent private investor could expect a considerable reduction in EDF's debt, which was set to fall from FRF [...] to FRF [...] over four years (recitals 91 and 95). However, it has been shown that between 1992 and 1996 EDF kept its Aaa credit rating by the credit rating agency Moody's with a debt ratio of 480 %. The French authorities also refer rather vaguely to the generation of resources of FRF 70 billion by EDF for the period 1997 to 2000 (recital 84). However, EDF's debt reduction and its automatic effect on the undertaking's net asset value was not to result in improved remuneration of the French state during the same period, but rather in a marked deterioration compared with the period between 1991 and 1996 (recital 134).
- (171) As indicated by EDF, despite a deterioration in the rating assigned to EDF by credit rating agencies such as Moody's or Standard & Poor's, EDF still retained an excellent rating (recital 71). Moreover, one of the objectives set between 1997 and 2000 was to reduce EDF's indebtedness to FRF [...]. A substantial reduction in the total interest charges incurred by EDF was therefore expected to follow. Consequently, neither the reduction in EDF's total debt nor its cost, nor any advantages arising for the state as shareholder would have been compromised by a lesser contribution to capital of FRF 44,8 billion instead of FRF 50,7 billion. A debt-to-equity ratio of 163 % instead of the 148 % foreseen as a result of the tax exemption would not have been detrimental to the interests of the shareholder. In this area, there is no optimal financial structure, and the report of the National Assembly (recital 100) shows ratios in the sector ranging from 250 % (Verbund, Austria) to 10-15 % (Veba, Germany and PowerGen, UK).
- (172) Indebtedness enabled EDF to finance its growth and its results without additional funds from the shareholder, using the leverage effect of the debt to increase the rate of return on the funds already invested by the state. However, priority was given to debt reduction, even though EDF's credit rating was excellent before the envisaged debt reduction (recital 71). Moreover, the excellent credit rating before 1996, reflecting EDF's capacity to repay its

<sup>(1)</sup> EDF Annual Report 1997, p. 103.

<sup>(2)</sup> By Article 2 of the Decision of 16 December 2003 (C(2003) 4637 final) (OJ L 49, 22.2.2005, p. 9), the Commission decided not to raise any objections to the reform of the pension scheme for the electricity and gas industries to which EDF was subject. The effect of the reform was to transfer to the general social security scheme the pension liabilities and commitments of the specific scheme for the staff of EDF and other participating companies.

creditors, is not incompatible with poor remuneration of the shareholder. On the contrary, the less drawn down by its shareholder, the better the credit rating of the debt instruments that EDF issued. Within the time-frame put forward in the projections submitted by the French authorities, the foreseeable reduction in the leveraging effect and, in any event, the low impact of the amount of tax on the debt ratio would have led a prudent private investor in a market economy either to reduce the profitability prospects of its investment or to not consider that the equity investment equivalent to the amount of tax was justified by the need to improve the debt situation of EDF in 1997.

- (173) Finally, a prudent private investor would likely have based its investment decision on an assessment of the undertaking's capacity to provide it with stable and adequate remuneration. In this regard, the remuneration for the state as shareholder for the period 1997-2000 described by the French authorities was well below the 6,35 % paid on French bonds during the same period. In addition, this remuneration could in practice be reduced to take account of the tax paid to the state as revenue collector (recitals 103 and 106). The remuneration of the shareholder was also considerably reduced at the very time the state was making the alleged investment. Any shareholder would have taken into account negatively the sudden and very significant reduction in the return on contributions of capital. This return was to decrease from an actual average of 9,32 % over the period 1991-1996 to 4,64 % for the period 1997-2000, which is a reduction of more than half. In terms of equity capital, the rate of return fell from an average of 14,1 % at the end of 1996 to 2,94 % in the same period (recitals 92 and 102, Tables 1 and 3).
- (174) Admittedly, a prudent private investor may accept a reduction in its current return in the expectation that the growth of the undertaking will result either in better future earnings or in an increase in the undertaking's value which is likely to generate a value-added on the sale of its asset reflecting an ownership right over the undertaking. In that regard, first, the current rate of return that could be expected in 1997 would not have been sufficient to offset the sharp reduction in the past rate of return. Secondly, analysis of the four factors with the potential to create value for the shareholder identified in recitals 164 to 173 does not support the conclusion that growth in the value of the company was foreseeable by the shareholder from the data available in the documents forwarded by the French authorities.
- (175) Moreover, the available evidence does not support the conclusion that a prudent private investor acting in the place of the French state in 1997 could have counted on a capital appreciation to offset the low current rate of return paid to the state, in the light of the information available. The French authorities did not carry out any assessment of the value of EDF before and after reclassification of the provisions in 1997.
- (176) Moreover, in 1997, EDF had, for more than fifty years, been a public industrial and commercial establishment and not a public limited company. Under Article 16 of Act No 46-628, its capital belonged to the French nation and could not be alienated (recital 18). Furthermore, it should be pointed out that, even after the restructuring of EDF's balance sheet under Act No 97-1026, in 1997 EDF's total net debt of FRF 118 billion far exceeded the value of its equity capital, which stood at FRF 79,8 billion (recital 101, Table 2).
- (177) None of the documents shedding light on the alleged investment decision of the French authorities records a plan for a possible privatisation of EDF through the sale of all or part of the capital held by the state. This would have required the prior adoption of the status of public limited company and the abandonment of the status of publicly owned industrial and commercial establishment. On the contrary, the only reference to the status of EDF contained in those documents was the reaffirmation by the state of its intention to maintain the specific status of EDF 'which should remain a stable point of reference for future developments' within the internal market for electricity (recital 95). It is on the basis of this information that France claims the investment decision was taken. These facts must therefore remain the reference framework for analysis of the alleged decision.
- (178) Accordingly, it would not have been reasonable or wise for an investor to expect a capital gain which depended on the action by the legislature contrary to both the provisions of law adopted by the French authorities in 1946

and applied unflinchingly and the express intention of the state, affirmed by the Minister responsible for state holdings at the material time in 1997, to maintain the specific legal status of EDF in a liberalised internal market for energy at EU level. The assumptions underpinning EDF's conclusions as to the return on investment that a prudent private investor would have expected, based on the initial and future value of EDF's shares in 1997 (recitals 69 and 70), do not take account of the status of EDF in 1997, and are contradicted by the evidence submitted by the French authorities referring thereto.

- (179) As the French authorities emphasise, as a public industrial and commercial establishment, in 1997 EDF had no share capital, unlike, for example, a public limited company whose capital is owned by the shareholders (see recital 19), who may sell their shares at any time. Thus, in 1997 the reference investor would have had in particular to determine a number of factors or make assumptions that were necessarily open to question; namely: (i) the amount at which the state would set the share capital of a future public limited company, and in particular the inclusion or otherwise of quasi-own assets, which determines the company's capacity to provide a stable dividend; (ii) the number of shares into which this capital would be divided, bearing in mind that a greater or lesser number partially determines their attractiveness in the market; (iii) the form of any share flotation and the amount to be raised, which determines the potential level of dilution of its holding; finally (iv) when the operation would be implemented, which, owing to the poor recovery prospects offered by EDF's projected income until 2000 (recital 167), could be envisaged only in the distant future. There is nothing in the information submitted by the French authorities for the period preceding the alleged investment to suggest that these unknowns could have been cleared up in 1997.
- (180) Accordingly, any increase in the value of the right held by the state in the capital of EDF resulting from the contested capital contribution, assuming the increase was established — which is manifestly not the case — would have involved a prudent investor speculating about at least four key factors over which, unlike the legislator and the regulator, it had no influence or, in any event, no valid information available in 1997. A prudent private investor would not have ignored the virtual absence of liquidity of its investment. It follows that a prudent private investor would have taken that fact into account when deciding whether or not to invest. This lack of liquidity is likely to reduce the benefit of any increase in the value of the company.
- (181) Furthermore, as mentioned in recital 144, the test of the prudent private investor in a market economy must be based primarily on the information and evidence submitted by the Member State in a situation where the decision has already been taken, since it is the Member State that is arguing that these are the elements that the Member State has taken into account, and not others which are more hypothetical or even contradictory in relation to those submitted. However, the Court of Justice requires the application of the principle of the prudent private investor in a market economy to be based on assessments foreseeable at the time the decision was taken (paragraph 105 of the judgment of 5 June 2012). Thus, the French authorities claimed in 1997 that the status of EDF, which did not allow the creation and disposal of EDF shares, would be maintained as a stable point of reference, including in the liberalised European market (recital 95). Adopting assumptions which contradict the assertion of the French authorities amounts to placing the test in a situation which is not as close as possible to that of the Member State, contrary to what the case-law requires (recital 126).
- (182) However, even assuming for the purposes of the analysis that a prudent private investor could have taken into account a future increase in the value of its investment at an uncertain date in addition to the regular returns offered, in deciding on the alleged investment the investor would have borne in mind the capacity of the undertaking to generate dividends over the long term, thereby following the time horizon of the French state, which had been controlling EDF since 1946. In estimating the value of its ownership interest in EDF, the prudent private investor would have disregarded the book value of the undertaking's net assets, even if it was counting on the debt reduction and generation of resources underlined by the French authorities (recital 84). The value of the assets, the amounts of investment or debt reduction do not necessarily coincide with the real economic value with a view to fixing a transaction price. One should therefore not focus on the fact that full repayment of EDF's debts in 1997 would have required amounts far exceeding the equity capital of EDF (recital 177). In the long term, an undertaking's value is a function of its capacity to generate value for its shareholders in the form of dividends or capital appreciation rather than in terms of the book value of its assets.

- (183) Among the various methods used in finance to estimate the opportunity cost or the rate of return required of an ownership interest transferable against consideration in the capital of an undertaking, the most common is that of the capital asset pricing model (CAPM) <sup>(1)</sup>. As shown in Table 5, application of the CAPM model to an investment in the capital of EDF in 1997 gives a target value for the required rate of return of approximately 12 %, and as high as 13,4 %, for a liquid asset such as an EDF share. However, this target value must be seen as a minimum. It presupposes not only that an ownership right in EDF such as a share is possible and transferable but also that there is a liquid market, whereas the state held 100 % of the capital and EDF could not issue shares. A premium of between 0,5 and 1,5 % <sup>(2)</sup> must be added to the required rate of return on a liquid asset to reflect the great uncertainty resulting from the factors examined in recitals 179 and 180 as regards the liquidity of the EDF securities that a prudent private investor could entertain in 1997.
- (184) In any event, the validity of the order of magnitude of 12 %, excluding a liquidity premium, is close to, although lower than, the current rate of return on equity capital of 14 % used by EDF to remunerate the French state between 1991 and 1996 (recital 102, Table 3). The actual rate of return obtained is normally the starting point for the expected rate of return in the future. The validity of this order of magnitude of 12 % is also corroborated by the use of other parameters based on figures available at the time, including those used in the study carried out for EDF referred to in recital 70, which gives a target value in a range of between 11,9 % and 13,5 %, with an average of 12,7 %. Since the results of the analysis do not change when a liquidity premium is added to the target rate of return of around 12 %, or when the 14 % actual rate of return in the recent past is applied from 1997, it is not necessary to take this premium and the actual rate of return into account.

Table 5

**Target rate of return required for an investment in EDF shares in 1997: calculation values**

Parameter	Value	Source
Risk-free rate	6,35 — 5,58	Annual average in 1997 of the daily rate of the 30-year and 10-year French bellwether bond, source Bank of France: Reference rate treasury bills and fungible government bonds, <a href="http://www.banque-france.fr/economie-et-statistiques/changes-et-taux">http://www.banque-france.fr/economie-et-statistiques/changes-et-taux</a>
Beta of EDF (leveraged)	0,45 — 0,54 — 0,62	1. Beta of EDF — Vernimmen et al. op cit., graph p. 427. 2. and 3. Oxera Study, Table 3.8, Beta of EU companies in the sector.
Indebtedness (%)	60	Capital structure of EDF after 1997 restructuring
B of EDF (deleveraged)	0,84 — 0,89 — 1,36	1. and 2. Commission calculation. 3. Oxera Study, Table 3.8

<sup>(1)</sup> The model estimates the target rate of return required by an investor in an undertaking's capital ( $k$ ) as the result of an addition to the rate of return on a financial asset deemed to be risk free or low risk, namely, a sovereign bond in the reference financial market ( $r_f$ ), a market-risk premium reflecting the higher risk of an investment in shares ( $K_m - r_f$ ) multiplied by a risk coefficient specific to the share of the undertaking concerned ( $\beta$ ) which can be, preferably, that of the undertaking itself or, failing this, that of comparable undertakings used as a reference. Parameter  $\beta$  must be estimated for an undertaking with no debt (gearing) in order to measure the inherent risk of (the share of) the undertaking in relation to the market. The model is  $k = r_f + \beta \times (K_m - r_f)$ . The Commission has applied the CAPM model to estimate the required rate of return on capital investments in an undertaking, endorsed by the General Court of the European Union: T-319/12 — *Spain v Commission, 'Ciudad de la Luz'*, EU:T:2014:604, paragraphs 48 to 66. For a fuller description, see Vernimmen et al. *Corporate Finance* John Wiley & Sons ed. 2nd edition, 2009, Chap. 22; for the findings of surveys of the frequency of use of estimation methods, see p. 460. The theoretical bases and a numerical application of the CAPM model to the present case are also contained in the study carried out by Oxera on behalf of EDF (recital 70), in particular Annex I.

<sup>(2)</sup> Vernimmen et al. *Corporate Finance* John Wiley & Sons ed. 2nd edition, 2009, pp. 433-4.

Parameter	Value	Source
Market risk premium	6,3 — 7,3	1. Vernimmen op cit. p. 423, citing Mehra Prescott 2/2003 T.2 FR 1973-98. 2. Forward risk premium in France on average 1988-1996 (this premium was 10,1 % in 1996). 'An examination of Equity Risk Premium Forecasts in the G-6 Countries', Khorana, Moyer & Pattel, I/B/E/S Working Paper, August 1997, p 25.
Target return range	11,7 — 12,1 — 13,4	Commission calculation
Median return	12	Commission calculation

- (185) In making its investment decision in 1997, a prudent private investor in a situation as close as possible to that of the French authorities would have used the regular estimates of EDF's future earnings validated by the competent authorities and used as a financial scenario, as contained in the EDF's projected income statement 1997-2000 (recitals 90-92, Table 1, recital 97). The tax exemption represented 11 % of the FRF 53,3 billion of EDF's capital and capital contributions in 1997, after the restructuring of the balance sheet. It can therefore be assumed that the investment conferred a right to receive 11 % of the dividends (remuneration of the capital contributions as estimated in Tables 1 and 4) and of the value of EDF. In order to determine this value, a model for calculating the long-term value of an undertaking should be applied, i.e. the dividend discount model (DDM) <sup>(1)</sup>.
- (186) The results of the DDM analysis of an investment of FRF 5,88 billion based on the dividends foreseen in EDF's projected income statement 1997-2000 (remuneration for capital contributions and additional remuneration in Table 1) are presented in Table 6, noting the internal rate of return (IRR) of financial flows and the net present value (NPV) for the target rates of return of 12 %, 6,35 % and 5,58 % <sup>(2)</sup>. These results are calculated for a baseline scenario based on standard analysis practice (Table 6.1), with three less plausible sensitivity analyses which loosen the assumptions of the baseline scenario and thus simulate a higher rate of return for the shareholder than the reference scenario (Tables 6.2, 6.3 and 6.4).

Table 6

**Estimate of the return (NPV) on an investment of FRF 5,88 billion using the MDD model based on the projected income statement of EDF 1997-2000 (Table 1) (billion FRF)**

6.1. Baseline scenario (Growth of dividends foreseen for end of period 1999-2000)

	1.1.1997	31.12.1997	31.12.1998	31.12.1999	31.12.2000	31.12.2000
	Investment	Dividend	Dividend	Dividend	Dividend	DDM value
	- 5,88	0,23	0,28	0,26	0,26	2,21
NPV at 12 %	- 3.43					
NPV at 6,35 %	- 3.17					
NPV at 5,58 %	- 3.12					
IRR	- 13 %					

NB: The table reads as follows: For financial flows between 1.1.1997 and 31.12.2000, the NPV with a discount rate of 12 % is FRF - 3,43 billion (...) and the IRR is - 3 %

<sup>(1)</sup> The DDM model gives the value of the undertaking from the (last) dividend paid (Dt), the growth rate of the dividends (d'D) and the target return, or opportunity cost of the capital (K), applying the formula  $Vr = Dt (1 + d'D) / (K - d'D)$ . The MDD model is also used in the Oxera study on behalf of EDF (points 3.27-3.31, Table 3.4), but with different and sometimes highly unrealistic values. The Oxera study uses a dividend growth rate of 9,3 % per year. In a perpetuity formula such as the DDM model, dividend growth rates are associated with the growth of the undertaking. Growth rates of 9,3 %, which are well above inflation and the long-term growth rate of gross domestic product (GDP), mean that, ultimately, EDF would monopolise the entire GDP of France.

<sup>(2)</sup> A negative net present value for a given interest rate (updating-financing) indicates that the investment is not viable at that interest rate. The internal rate of return (positive — IRR-) indicates the effective interest rate at which the expected financial flows remunerate an investment.



## 6.2. Sensitivity 1 (d' dividends = 4,51 % annual rate 1997/2000)

		1.1.1997	31.12.1997	31.12.1998	31.12.1999	31.12.2000	31.12.2000
		Investment	Dividend	Dividend	Dividend	Dividend	DDM value
		- 5,88	0,23	0,28	0,26	0,26	3,69
NPV at 12 %	- 2,68						
NPV at 6,35 %	- 2,14						
NPV at 5,58 %	- 2,05						
IRR	- 4,7 %						

## 6.3. Sensitivity 2 (Base scenario + additional 11 % quasi-equity capital)

		1.1.1997	31.12.1997	31.12.1998	31.12.1999	31.12.2000	31.12.2000
		Investment	Dividend	Dividend	Dividend	Dividend	DDM value
		- 5,88	0,23	0,28	0,26	0,26	4,93
NPV at 12 %	- 2,06						
NPV at 6,35 %	- 1,29						
NPV at 5,58 %	- 1,16						
IRR	0,3 %						

## 6.4. Sensitivity 3 (Sensitivity 1 + additional 11 % quasi-equity capital)

		1.1.1997	31.12.1997	31.12.1998	31.12.1999	31.12.2000	31.12.2000
		Investment	Dividend	Dividend	Dividend	Dividend	DDM value
		- 5,88	0,23	0,28	0,26	0,26	6,41
NPV at 12 %	- 1,30						
NPV at 6,35 %	- 0,26						
NPV at 5,58 %	- 0,08						
IRR	5,2 %						

(187) The estimates from Table 6 show that, if the amount of FRF 5,88 billion allegedly invested had conferred entitlement to a proportional percentage of the dividends and the value of EDF, the operation would have produced a large negative net present value (FRF - 3,43 billion). In order for the investment to be financially advantageous for a private market economy investor, on the most widely used assumption (Table 6.1), it would have been necessary for the prudent private investor to be satisfied by a rate of return well below an opportunity cost of capital of 12 % for an investment in liquid EDF shares, and indeed also below the rate paid on French Government bonds with maturities of 30 years (6,35 %) and 10 years (5,58 %) in 1997. Clearly, a prudent private investor would not have made the investment in those circumstances.

- (188) These conclusions do not change qualitatively if, as sensitivity test, other assumptions are used which, although less plausible, value the alleged investment more (Tables 6.2 to 6.4) <sup>(1)</sup>. In any event, the rate of return provided is below 12 %, and indeed also even lower than the return on French Government 30-year and 10-year bonds in 1997. Finally, examination of other variables available in EDF's projected operating results, such as the revenue estimates, core business income or the net income (recitals 166 to 168) would not have allowed the prudent private investor to expect a complete trend reversal leading to a better return or the creation of value for the state as shareholder down the line. These developments, which were foreseeable and foreseen in 1997, further corroborate the conclusions and their extension to the period after 2000, as foreseeable by a prudent private investor in 1997 on the basis of the information supplied by the French authorities.
- (189) Even supposing that the prudent private investor would have expected a capital gain in addition to a regular return from EDF, which nothing in the information and data sent by the French authorities indicates, and which moreover would be too risky to expect having regard to the status of EDF in 1997, it can be ruled out that it would have made the alleged investment. Accordingly, the application of the test of the prudent private investor in a market economy shows that, even if the tax exemption of FRF 5,88 billion was in fact an investment decision on the part of the state as shareholder, the operation would not have been carried out by a prudent private investor in possession of the information put forward by the French authorities.
- (190) In this connection, the comments by EDF reproduced in recital 71, according to which the tax exemption had no detrimental effect on competition and did not provide an advantage since EDF could in any event have found equivalent financing on the capital markets, are contradicted by the facts. It is common ground that EDF could not have issued shares on the markets to obtain this amount. Even if EDF would probably have been able to find a lender, the corresponding loan or bond issue would have had to be remunerated, in all likelihood, at a higher rate than the rate that the French state anticipated for capital contributions to EDF for the period 1997-2000 and higher than the refinancing cost equivalent to the government bonds in 1997. If EDF could have had an equivalent amount in principal, the financing costs would have been greater than that of the alleged investment. Even then, without taking into account a repayment of principal, which EDF was not required to make, in the amount of the tax exemption or the equivalent amount in capital contributions in 1997, the measure would have provided an economic advantage to EDF by reducing its financing costs.
- (191) Even if the principle of the prudent private investor in a market economy were applicable, in the light of the documents provided by the French authorities shedding light, according to them, on the profit expectations and risks attached to the alleged investment in the form of a tax exemption, application of the test of the private investor in a market economy leads to the conclusion that a prudent private investor would not have invested an amount equal to the tax due in the EDF capital increase in 1997.
- (192) The non-payment by EDF of FRF 5,88 billion in corporation tax does not appear to be a productive investment by the state as shareholder in application of the principle of the prudent private investor in a market economy. It appears rather to be an ad hoc derogating tax exemption that provided an economic advantage to EDF equal to the amount of tax not paid. Such an advantage necessarily strengthens the position of EDF vis-à-vis its competitors, since the amount of equity capital determines, among other factors, the external financing capacity and conditions of an undertaking while, moreover, the resources saved in this way could be used for other purposes such as, for example, investment in France or in other Member States where competitors conducted their business in 1997.

<sup>(1)</sup> The assumption that the EDF dividend would increase by 4,51 % (sensitivity 1, Table 6.2) appears optimistic; it is obtained by smoothing the forecast growth rate for the four forecast years 1997-2000. Besides the fact that in usual practice the dividend growth used is the end-of-period growth (baseline scenario), in actual fact the dividends to be paid by EDF were to decrease in 1997-2000 compared with 1991-1996, and in 1999 and 2000 compared with 1998. In any event, a rate of 4,51 % in perpetuity is high in absolute terms. The assumption (sensitivity 2, Table 6.3) that the shareholder would add — or the buyer would pay for — (a pro rata) quasi-equity capital of EDF as estimated in 1997 to the objective value of EDF as calculated, does not take into account the regulatory character of certain types of equity capital (reserves). This assumption combined with the MDD model is also optimistic as it amounts to allocating to the shareholder (a pro rata of 11 %) quasi-equity capital (excluding subscribed capital) which allows the undertaking to absorb possible losses and, in the long term, to be able to provide regular dividends and remuneration for the shareholder. It presupposes that the quasi-equity capital of EDF set in 1997-2000 would be permanently available, whereas the MDD disregards sources of remuneration other than the dividend. It is therefore an unjustifiable assumption. The combination of the two assumptions (sensitivity 3, Table 6.4) magnifies their respective disadvantages or weaknesses and makes the results of the calculation even more unlikely and arbitrary.

- (193) The economic advantage therefore distorts competition within the meaning of Article 107(1) of the TFEU. The advantage is selective, since the non-payment of corporation tax on some of the accounting provisions constitutes an exception to the tax treatment normally applicable to such an operation and, in the present case, this exception was applied only to EDF.

## 9.2. STATE RESOURCES

- (194) The concept of aid embraces not only positive benefits, such as subsidies, but also interventions by the public authorities which mitigate the charges that are normally included in the budget of an undertaking and which have the same effect as subsidies <sup>(1)</sup>. The EU Courts have consistently held <sup>(2)</sup> that the non-collection by the state of a tax which should normally have been collected is equivalent to the consumption of state resources.
- (195) The non-collection of the full amount of corporation tax due in respect of the 1997 financial year derived directly from a measure adopted by the state, namely Act No 97-1026 of 10 November 1997.

## 9.3. DISTORTION OF COMPETITION AND EFFECT ON TRADE BETWEEN MEMBER STATES

- (196) From its creation in 1946 to the entry into force of Directive 96/92/EC, EDF enjoyed a monopoly position in the French market with exclusive rights for the transmission, distribution, and import and export of electricity. However, EDF competed with other producers in other Member States already ahead of the entry into force of Directive 96/92/EC. Moreover, free competition existed in related markets not subject to exclusive rights where EDF had already diversified its activities beyond its exclusive rights in both geographic and sectoral terms. Effects on competition did therefore exist well before the liberalisation provided for by Directive 96/92/EC.
- (197) Electricity was the subject of significant, growing trade between Member States in which EDF was actively engaged. These exchanges, reinforced by the adoption of Council Directive 90/547/EEC <sup>(3)</sup>, were taking place on the basis of commercial agreements between the various operators of the high-voltage electricity networks in the Member States. In the European OECD member countries, electricity imports grew at an average annual rate of over 7 % between 1980 and 1990. Between 1981 and 1989, EDF multiplied the surplus on its balance of trade in electricity nine fold, achieving net exports of 42 TWh, representing 10 % of its total production. In 1985, EDF already exported 19 TWh to other Member States.
- (198) Even before Directive 96/92/EC entered into force in February 1999, some Member States acted unilaterally to open up their electricity market. In particular, the United Kingdom opened up its market completely for large industrial customers in 1990. Sweden opened up its market completely in 1996, Finland began the process in 1995 and reached 100 % market opening in 1997, Germany completely opened up its market in 1998 and the Netherlands opened up its market completely for industrial customers in 1998. In those circumstances, even before the deadline set by the Directive for opening up the market to competition, State aid granted to enterprises enjoying a monopoly in a Member State that took an active part in intra-Union trade, as in the case of EDF, was likely to affect trade between Member States within the meaning of Article 107(1) of the Treaty.
- (199) In its annual report for 1997, EDF stated that it ranked 'among the world's leading operators in the electricity industry, with, outside France, more than FRF 13 billion invested, a total installed production capacity equal to nearly 11 % of the figure for France and over 8 million customers'. The report also stressed that in 1997 EDF had 'increased the number and size of its investments in Europe by extending its presence to Austria and Poland' and had 'exported over 70 TWh in Europe'. These exports were delivered in competition with alternative suppliers in the markets concerned.
- (200) The 1997-2000 management contract, signed on 8 April 1997 between the French state and EDF, stipulated that EDF was to allocate some FRF 12-13 billion to its international investments, assigning priority to regions in Europe. Between 2000 and 2002, EDF acquired one third of the capital of the German company EnBW,

<sup>(1)</sup> Judgments in *Gezamenlijke Steenkolenmijnen v High Authority*, 30/59, EU:C:1961:2; judgment in *Banco de Crédito Industrial C-387/92*, EU:C:1994:100; judgment in *SFEI*, C-39/94, EU:C:1996:285; judgment in *France v Commission*, C-241/94, EU:C:1996:353; judgment in *FFSA v Commission*, T-106/95, EU:T:1997:23.

<sup>(2)</sup> See in particular *Ladbroke v Commission*, T-67/94, EU:T:1998:7, paragraph 109.

<sup>(3)</sup> Council Directive 90/547/EEC of 29 October 1990 on the transit of electricity through transmission grids (OJ L 313, 13.11.1990, p. 30).

increased the production and distribution capacities of its United Kingdom subsidiary London Electricity, took direct control of the Italian enterprise Fenice and set up a partnership with Fiat for the purchase of Montedison (now Edison).

- (201) In 1997, SDS, a wholly owned subsidiary of EDF, brought together its activities associated with the provision of services to individual customers, businesses and local authorities. SDS was active in waste treatment, street lighting and other energy-related services and generated turnover equivalent of EUR 685 million in 1998 as against EUR 650 million in 1997. In 2000, EDF established a partnership with Veolia Environnement via the company Dalkia, the European leader in energy services to businesses and local authorities. Dalkia offers energy engineering and maintenance services, manages heating plants and technical services to do with the operation of buildings and operates district heating networks, combined heat and power schemes, and energy production and industrial fluid systems.
- (202) EDF has also developed its activities in the market for renewable energy sources. In 1997, the holding company Chart, a wholly owned EDF subsidiary, brought together its activities in the renewables sector, e.g. geothermal energy and wind power. Its contribution to consolidated turnover that year was EUR 70 million.
- (203) Lastly, as an electricity producer and distributor, EDF was and still is in competition with suppliers of other substitute energy sources such as coal, oil and gas, both in its domestic market and in international markets. In France, for example, EDF has launched a successful campaign to promote the use of electricity for heating. It has thus increased its market share in comparison with its competitors who supply substitute energy sources such as oil or gas. In the steel industry, electric furnaces are in competition with gas and oil-fired furnaces. It follows that a measure such as the one at issue is liable to distort competition with alternative suppliers, such as Gaz de France.
- (204) EDF thus occupied a prominent position in electricity trading between the Member States in 1997, whereas now the French electricity market is fully open and many European suppliers are present. It is therefore clear that, in 1997, EDF was already well established in certain markets in other Member States and that the aid resulting from the non-payment by EDF of corporation tax on some of the accounting provisions created free of tax for the renewal of the RAG inevitably affected competition between Member States.
- (205) The above considerations were detailed in the extension decision. Neither France nor EDF disputed in their comments that the aid was likely to affect trade between Member States.
- (206) Thus, since the four criteria set out in Article 107(1) TFEU are fulfilled, the non-payment by EDF of corporation tax on some of the accounting provisions created free of tax for the renewal of the high-voltage transmission network constitutes State aid. The compatibility of the aid with the internal market must now be assessed.

#### 10. ASSESSMENT OF THE COMPATIBILITY OF THE AID WITH THE INTERNAL MARKET

- (207) Article 107(1) of the TFEU provides that aid fulfilling the criteria laid down therein is in principle incompatible with the internal market. According to settled case-law, it is for the Member State to cite the reasons and evidence of any kind for which State aid is compatible with the internal market <sup>(1)</sup>. In the present case, the French Republic has cited no reason nor provided any information in this regard.
- (208) The exceptions laid down in Article 107(2) of the TFEU are not applicable in the case in point because of the nature of the aid since it does not pursue the objectives listed in that paragraph.
- (209) Nor does the aid in question fulfil the conditions laid down for exceptions in Article 107(3)(a) and (c) of the TFEU in respect of aid intended to promote the economic development of certain regions, particularly since it corresponds to operating aid. It is not conditional on investments or on job creation as envisaged in the Guidelines on regional State aid <sup>(2)</sup>.

<sup>(1)</sup> C-364/90 — *Italy v Commission*, EU:C:1993:157, paragraph 20.

<sup>(2)</sup> Guidelines on regional State aid (OJ C 209, 23.7.2013, p. 1).

- (210) Article 107(3)(c) of the TFEU also allows an exception to be made for aid to facilitate the development of certain economic activities, where such aid does not adversely affect trading conditions to an extent contrary to the common interest. The aid measure under examination does not qualify for this exception. The derogation from the applicable tax law, granted for the benefit of a single enterprise, cannot be regarded as being intended to facilitate the development of an activity. Its sole purpose is to assist an enterprise by reducing its operating costs.
- (211) As regards the exceptions allowed by Article 107(3)(b) and (d) of the TFEU, the aid measure under examination is not intended to promote the execution of a project of common interest, remedy a serious disturbance in the French economy or promote culture and heritage conservation.
- (212) The compatibility criteria set out in Article 107(2) and (3) of the TFEU are therefore not met. Furthermore, as regards compensation for public service costs, the French authorities have not cited Article 106(2) of the TFEU in defence of the tax concession, but they have stressed the fact that EDF performs public service tasks. They have not, however, provided any assessment of the cost incurred by EDF in carrying out those tasks. The Commission cannot therefore determine whether or not the tax concession in question compensates for any additional cost linked to the public service tasks entrusted to it. In any event, if the non-payment of the tax must be qualified as compensation for the provision of a service of general economic interest, it has not been established that such compensation was determined in advance in accordance with transparent and objective criteria and calculated by reference to the costs of an efficient undertaking.
- (213) It is consequently not possible in the case in point to examine whether the conditions set out in the judgment in *Altmark* <sup>(1)</sup> for escaping the application of Article 107(1) of the TFEU, and the criteria for qualifying for the exception allowed by Article 106(2) of the TFEU, which, moreover, the French authorities do not cite, are fulfilled.
- (214) In the light of the foregoing considerations, it appears that the aid under examination constitutes operating aid which has had the effect of strengthening EDF's competitive position in relation to its competitors. In those circumstances, it would be incompatible with the internal market.
- (215) The Commission also considers that, contrary to what is claimed by the French authorities, the rule on limitation periods does not apply in the case in point. Admittedly, EDF created the accounting provisions free of tax between 1987 and 1996. However, it should be pointed out, firstly, that corrections to accounting errors, which by their very nature relate to the posting of past transactions, should according to the National Accountancy Council be posted in the accounts for the financial year in which they are discovered and, secondly, that the Act providing that the grantor rights were to be reclassified as capital contributions without being subject to corporation tax dates from 10 November 1997. The tax concession therefore dates from 1997 and any new aid paid on that date is therefore not time-barred because the first Commission instrument concerning this measure dates from 10 July 2001. Furthermore, under Article 15 of Regulation (EC) No 659/1999, legal proceedings suspend the period of limitation.

## 11. CONCLUSIONS

- (216) The Commission finds that France has unlawfully implemented the aid in question in breach of Article 108(3) of the TFEU. The Commission considers that the exemption from corporation tax in the amount of FRF 5 882 849 762 relating to the reclassification as a capital contribution, provided for by Act No 97-1026, of accounting provisions for the renewal of the high-voltage transmission network, already implemented to the tune of FRF 14 119 065 335, constitutes aid that is illegal and incompatible with the internal market.
- (217) Under Article 108(2) of the TFEU, when the Commission has found that aid is incompatible with the internal market, it is competent to oblige the Member State concerned to abolish or alter it. According to Article 14 of Regulation (EC) No 659/1999 'where negative decisions are taken in cases of unlawful aid, the Commission shall decide that the Member State concerned shall take all necessary measures to recover the aid from the beneficiary (hereinafter referred to as a "recovery decision"). The Commission shall not require recovery of the aid if this would be contrary to a general principle of Community law'.

<sup>(1)</sup> C-280/00 — *Altmark Trans and Regierungspräsidium Magdeburg*; EU:C:2003:415.

- (218) The Commission's objective in requiring the Member State concerned to recover the aid incompatible with the internal market is to restore the previously existing situation <sup>(1)</sup>. In this context, the Court of Justice has established that that objective is attained once the recipient has repaid the amounts granted by way of unlawful aid, thus forfeiting the advantage it enjoyed over its competitors. In this way, the situation prior to payment of the aid is restored <sup>(2)</sup>.
- (219) In the present case, it appears that no general principle of EU law would run counter to the recovery of the unlawful aid found to exist. In particular, neither France nor the interested parties presented any arguments to that effect.
- (220) It follows that France must take all necessary measures to recover from EDF the aid unlawfully paid in the form of exemption from corporation tax in the amount of FRF 5 882 849 762 relating to the reclassification of part of the provisions to the tune of FRF 14 119 065 335 as capital.
- (221) For the purposes of recovery, the French authorities must also add to the amount of the aid the recovery interest due from the date on which the incompatible aid was made available to the undertaking, i.e. the date on which the corporation tax in respect of tax year 1997 became payable, until it is actually recovered <sup>(3)</sup>, in accordance with Chapter V of Commission Regulation (EC) No 794/2004 <sup>(4)</sup>.
- (222) In the context of France's obligation of loyal cooperation within the framework of the recovery procedure, this amount will have to be established more precisely during the procedure, on the basis of information to be supplied by the French authorities, and which will take account, inter alia, of the exchange rates between the ECU/EUR and the French franc (FRF) that may apply to the instalments of corporation tax paid by EDF during 1997 and of the reimbursement to EDF of the aid following the annulment of the first negative decision in 2009. In the present case, interest is not due for the period during which the aid was no longer at the disposal of the undertaking, namely the period between the actual recovery of the aid by France and the repayment to EDF. Any interest paid by France to EDF will nevertheless have to be taken into account.
- (223) The French authorities must recover the above amount within four months from the date of notification of this Decision.
- (224) In accordance with settled case-law, in the event that a Member State encounters unforeseen and unforeseeable difficulties or perceives consequences overlooked by the Commission, it may submit those problems for consideration by the Commission, together with proposals for suitable amendments. In such a case, the Commission and the Member State concerned must work together in good faith with a view to overcoming the difficulties while fully observing the provisions <sup>(5)</sup> of the TFEU.
- (225) The Commission therefore requests France to submit to it without delay any problems with which it would be faced in implementing this Decision,

HAS ADOPTED THIS DECISION:

#### Article 1

1. The exemption from corporation tax in favour of *Électricité de France* for an amount of 5 882 849 762 French francs, relating to the reclassification as capital of the provisions corresponding to the value of the assets in kind allocated under concession to the high-voltage transmission network, constitutes State aid within the meaning of Article 107(1) of the TFEU.

<sup>(1)</sup> Judgment in *Spain v Commission*, C- 280/92, EU:C:1994:325, paragraph 75.

<sup>(2)</sup> Judgment in *Belgium v Commission*, C-75/97, EU:C:1999:311, paragraphs 64-65.

<sup>(3)</sup> See Article 14(2) of Regulation (EC) No 659/99 (cited above).

<sup>(4)</sup> Commission Regulation (EC) No 794/2004 of 21 April 2004 implementing Council Regulation (EC) No 659/1999 laying down detailed rules for the application of Article 93 of the EC Treaty (OJ L 140, 30.4.2004, p. 1).

<sup>(5)</sup> Judgment in *Commission v Germany*, C-94/87, EU:C:1989:46, paragraph 9, and judgment in *Commission v Italy*, C-348/93, EU:C:1995:95, paragraph 17.

2. The aid mentioned in paragraph 1, unlawfully granted by the French Republic, is incompatible with the internal market.

*Article 2*

1. The French Republic is required to recover from the beneficiary the equivalent in euro of the aid referred to in Article 1.

2. The sums to be recovered shall bear interest from the date on which they were placed at the disposal of the beneficiary until that of their actual recovery.

3. The interest shall be calculated on a compound basis in accordance with Chapter V of Regulation (EC) No 794/2004.

*Article 3*

1. Recovery of the aid referred to in Article 1 shall be immediate and effective.

2. The French Republic shall ensure that this Decision is implemented within four months of the date of its notification.

*Article 4*

1. Within two months of notification of this Decision, the French Republic shall provide the following information to the Commission:

- (a) the total amount (principal and interest) to be recovered from the beneficiary;
- (b) a detailed description of the measures already taken and planned to comply with this Decision; and
- (c) the documents proving that the beneficiary has been ordered to repay the aid.

2. The French Republic shall keep the Commission informed of the progress of the national measures adopted pursuant to this Decision until the recovery of the aid specified in Article 1 has been concluded. At the Commission's request, it shall immediately submit information on the measures already adopted and planned for the purpose of complying with this Decision. It shall also provide detailed information on the amounts of aid and the interest already recovered from the beneficiary.

*Article 5*

This Decision is addressed to the French Republic.

Done at Brussels, 22 July 2015.

*For the Commission*  
Margrethe VESTAGER  
*Member of the Commission*

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