COMMISSION

COMMISSION DECISION

of 19 July 1995

concerning aid for the operation of air routes granted under the Law of the Region of Sardinia of 20 January 1994

(Only the Italian text is authentic)

(Text with EEA relevance)

(96/110/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 93 (2) thereof,

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

Having given the interested parties notice to submit their comments, in accordance with the abovementioned provisions, and in view of the fact that no comments were submitted,

Whereas :

I

By letter of 8 March 1994, the Italian authorities informed the Commission, in accordance with Article 93 (3) of the Treaty, of the aid scheme for the operation of third-level air services introduced by the Law of the Autonomous Region of Sardinia of 20 January 1994 (hereinafter 'the Law of 20 January 1994').

On 30 March 1994, the Commission sent the Italian authorities a request for further information to enable it to determine whether the aid scheme was compatible with the common market. The Commission's request concerned the definition of the routes to and from Sardinia which may have received or may in future receive operating aid, the definition of routes which could have benefited under the Law of 20 January 1994, the possible application by the Italian authorities of certain provisions of Council Regulation (EEC) No 2408/92 of 23 July 1992 on access for Community air carriers to intra-Community air routes [1], (Articles 3 (2) and (4), 4 and 5) as amended by the Act of Accession of Austria, Finland and Sweden which might restrict market access and lastly, the rules for the payment and calculation of the subsidies and the amount concerned.

By letter dated 3 June 1994, the Italian authorities sent the Commission a memorandum from the Region of Sardinia which partly complied with the request for information of 30 March 1994. It stated that the Region had not in the past granted any aid to airlines, that a list of the routes which might receive aid under the scheme had not yet been drawn up, that the financial compensation concerned was available to all Community airlines meeting the requirements and, lastly, that the amount of the aid was limited by the budget allocated to it. No detailed information, however, was given as to the possible application of the restrictive provisions of Regulation (EEC) No 2408/92 on market access, in particular Article 4 which makes provision for public service obligations, including where appropriate financial compensation to the operating companies, in particular in respect of regional routes with light traffic. Although a reminder was sent to the Italian authorities on 1 August 1994 concerning this last point, the Commission has not to date received the information requested.

On the basis of the information in its possession, the Commission decided to initiate the Article 93 (2) procedure and informed Italy of its decision by letter of 17 January 1995. The letter gave the Italian Government notice to submit its comments to the Commission within one month, together with the information required by the Commission to pursue its examination of the matter. It was published in the *Official Journal of the European Communities* [2], and other interested parties were invited to send their comments within one month of the date of

[1] OJ No L 240, 24. 8. 1992, p. 8.
[2] OJ No C 117, 12. 5. 1995, p. 2.

publication. No reply was received from the Italian authorities to the Commission's letter giving notice, nor were any comments sent, or further details provided as to the aid scheme introduced by the Law of 20 January 1994, or on the possible existence of public service obligations on the air routes to and from Sardinia. Nor were any comments received under the procedure from other interested parties.

II

The Commission decided to examine the case under Articles 92 and 93 of the Treaty and Article 61 of the Agreement on the European Economic Area (hereinafter 'the EEA Agreement') solely on the basis of the information in its possession. Since the time limit for the submission by the Italian Government of the comments and information requested under the Article 93 (2) procedure has expired without such information or comments being submitted, the Commission is empowered to terminate the procedure and make its decision, on the basis of the information available to it, on the question whether or not the aid is compatible with the common market, in accordance with the Court of Justice judgment in Case 301/87, *French Republic* v. *Commission* (1). In Joined Cases C-324/90 and C-342/90, *Germany and Pleuger Worthington* v. *Commission* (2), the Court also held that, prior to taking a decision, the Commission need order a Member State to submit information only if the information in its possession did not allow it to determine whether the aid was compatible with the common market. The Commission considers in the present case that, although the information in its possession, forwarded by the Italian authorities when notifying the aid scheme and in response to a request for information sent before the procedure was initiated, is incomplete, it is sufficient to allow it to take a decision on the compatibility with the common market of the aid scheme introduced by the Law of 20 January 1994.

III

The Law of 20 January 1994 is intended to strengthen air services to and from Sardinia by authorizing the Regional Executive to grant subsidies to companies or bodies which provide scheduled third-level services for the transport of passengers by air. Third-level services within the meaning of the Law are air services provided by aeroplanes or helicopters with a capacity of between nine and 50 passengers.

The subsidies concerned are intended to compensate for the losses incurred by carriers as a result of empty seats. They are paid only up to 55 % of the seats offered on the routes specified each year by the Regional Executive, in accordance with the regional transport plan. Inasmuch as Sardinia already has direct air services to the main Italian cities and to a number of other European cities, it would seem that the routes concerned are essentially low-density regional routes. In addition, the subsidies are granted for only three consecutive years as from 1994, their amount being equal to 100 % of the fares approved the first year, 75 % the second year and 50 % the third year.

The grant of the subsidies is subject to an administrative procedure provided for in the Law of 20 January 1994. Firms wishing to receive such subsidies must submit an application, together with supporting documents (annual report, technical report, financial management plan, forward budget, etc.) to the Regional Transport Department by 31 October of the year preceding that for which the subsidy is requested. For 1994 the final date for submission of the files is set at 30 days following the publication of the Law in question in the Official Gazette of the Autonomous Region of Sardinia. Applications considered to be admissible must then be included in the annual intervention plan adopted by the Regional Executive, which takes account of budgetary resources available. Lastly, the grant of subsidies to airlines is subject to the signing of an agreement with them which must in particular stipulate that it is prohibited to modify or to disrupt the operating programme approved by the Regional Transport Department, that the fares approved by it must be applied, that the provisions laid down by law and agreement concerning staff must be complied with and that the staffing levels approved by the Regional Transport Inspectorate must be maintained.

The expenditure arising from the application of the subsidy measures is estimated at Lit 2 billion for each of the years 1994, 1995 and 1996. The subsidies are paid *ex post* to the recipient firms every six months, once the Department has checked the empty seats on the aircraft assigned to the routes concerned. An advance of 50 % of the subsidy may, however, be paid once a deposit has been lodged.

IV

Article 92 (1) of the Treaty and Article 61 (1) of the EEA Agreement provide that 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 is incompatible with the common market.

(1) [1990] ECR I-307.
(2) [1994] ECR I-1173.

In the case in point, the Region of Sardinia has decided, by means of the Law of 20 January 1994, to grant aid to firms or bodies providing third-level scheduled air services to and from Sardinia.

State aid means aid granted by the central, regional or local authorities of a Member States 'or by public or private bodies established or appointed by it to administer the aid', as the Court of Justice held in Case 78/76, *Steinike & Weinlig* [1]. The subsidies in question are granted direct by the Region of Sardinia and are included in its budget; they therefore constitute State aid. Furthermore, they are liable to affect trade between Member States as they are granted to firms engaged in air transport activities which, by their nature, are directly linked to trade and may cover the whole of the common market and the European Economic Area. This has particularly been the case since the entry into force of Council Regulations (EEC) No 2407/92 [2], (EEC) No 2408/92 and (EEC) No 2409/92 [3] (the 'third air transport package') on the liberalization of air transport, the harmonization of conditions for granting licences to carriers, and the definition of rules for the application, within the civil avaiation sector, of the principle of freedom to provide services within the Community. Lastly, the Commission considers that the subsidies distort competition by favouring certain enterprises, since the aid is granted only to airlines operating routes specified by the Law of 20 January 1994, namely airlines providing scheduled air services with aircraft having a capacity of between nine and 50 passengers. In addition, companies wishing to benefit under the scheme are subject to a procedure which amounts to a selection procedure, inasmuch as they are required to submit a complete file which is examined by the Regional Transport Department; the latter then decides to include a certain number of airlines in its programme in accordance with the regional transport plan and according to budget availabilities. In any event, the granting of operating aid under such conditions to certain air carriers in order to operate certain routes is liable to jeopardize competition by favouring those carriers in the operation of those routes. The distortion is even greater since, under the Law, all recipients are required to apply fares approved by the Department and are expressly prohibited from charging fare supplements, which means they are unable to adjust fares to costs, as they are required to maintain a minimum price level which no competitor could offer without such subsidies. In addition, the calculation of the subsidies does not take account of revenue generated and costs borne by the aid recipients in operating the routes in question. Thus there is no guarantee that the carriers will not realize an excessive profit, likely to be transferred to routes where they are in competition with other Community carriers. Lastly, in the absence of specific information from the Italian authorities on this point, it is probable that freedom of access to the routes in question, a list of which has not been communicated to the Commission, will be restricted until 1 April 1997 to the detriment of Community carriers licensed in a Member State other than Italy. These restrictions further increase the risks of distortion of competition resulting from the aid scheme introduced by the Law of 20 January 1994.

The Commission therefore considers that the Law of 20 January 1994 establishes subsidies which constitute State aid within the meaning of Article 92 (1) of the Treaty and Article 61 (1) of the EEA Agreement.

The aid set up under the Law in question cannot be regarded as compatible with the common market under Article 92 (2) of the Treaty and Article 61 (2) of the EEA Agreement since it does not qualify for any of the exceptions provided for therein. Article 92 (2) (b) and (c) and Article 61 (2) (b) and (c) do not apply as the aid is not intended to make good the damage caused by natural disasters or exceptional occurrences or to assist the economy of certain areas of Germany. Point (a) of those provisions, relating to aid having a social character, is not applicable either, since the subsidies in question are paid to the airlines or other bodies and it is not possible to identify the individual consumers. Indeed, the method of calculating the subsidies does not take account of the number of passengers carried. What is more, in view of the probable access restrictions on the routes in question until 1 April 1997 to the detriment of Community airlines not licensed in Italy, serious doubts exist as to the possibility of discrimination in connection with the origin of the services.

Article 92 (3) of the Treaty and Article 61 (3) of the EEA Agreement list the aid which may be regarded as compatible with the common market. Such compatibility must be examined in the context of the Community and not of a single Member State. The exceptions provided by the

[1] [1977] ECR 595.
[2] OJ No L 240, 24. 8. 1992, p. 1.
[3] OJ No L 240, 24. 8. 1992, p. 15.

relevant provisions apply only if the Commission establishes that, without the aid, market forces alone would not be sufficient to persuade the recipient to act in such a way as to achieve one of the desired objectives.

In order to safeguard the orderly functioning of the common market and having regard to the principles set out in Article 3 (g) of the Treaty, the exceptions to the principles of Article 92 (1), as defined in Article 92 (3), must be interpreted strictly when examining an aid scheme or any individual measure.

Article 92 (3) (b) of the Treaty and Article 61 (3) (b) of the EEA Agreement are not applicable to the case in question since the subsidies provided for in the Law of 20 January 1994 are not aimed at promoting the execution of an important project of common European interest or at remedying a serious disturbance in the economy of a Member State. Nor is the exception provided for in Article 92 (3) (c) concerning aid to facilitate the development of certain economic activities applicable since, on the one hand, the subsidies in question are operating aid rather than investment aid and, on the other hand, they are aimed solely at increasing flights to and from Sardinia and have no sectoral purpose.

The whole of Sardinia is covered by Article 92 (3) (a) of the Treaty and Article 61 (3) (a) of the EEA Agreement. Hence, the existence of low-density air services within Sardinia or linking it to other Community or EEA regions could be regarded as promoting the economic development of the island within the meaning of these provisions. In addition, the aid in question is temporary (three years) and degressive, thus satisfying two of the main conditions which the Commission generally imposes for acceptance of operating aid under Articles 92 (3) (a) of the Treaty and 61 (3) (a) of the Agreement. However, on 16 November 1994 the Commission adopted a communication on State aid to civil aviation [1] which takes account in particular of the liberalization measures which entered into force on 1 January 1993 and which create an integrated single market in air transport and which in particular introduce cabotage. As a result, direct aid for the operation of regional air services cannot in principle be exempted on the basis of Article 92 (3) (a) of the Treaty and Article 61 (3) (a) of the Agreement. Such aid results in cross-subsidies within airlines between subsidized unprofitable routes and profitable routes on which the airlines are in competition with other Community airlines, thereby distorting competition to the advantage of the airlines receiving operating aid in certain regions. In the present case, two aggravating factors should also be taken into account: first, the calculation of the subsidies takes no account of the revenue and costs to the recipients, which means that the possibility of excess profits is not ruled out; secondly, there are barriers to entry to the routes in question, due either to the possible application of the restrictive clauses of Regulation (EEC) No 2408/92 or to the strict procedural conditions for obtaining the subsidies imposed by the Law of 20 January 1994.

The Commission spelled out very clearly in its communication of 16 November 1994 that direct subsidies for the operation of regional air routes are compatible with the common market only in two specific cases, the first being exemption under Articles 92 (2) (a) of the Treaty and 61 (2) (a) of the EEA Agreement, which as demonstrated above is not possible, and the second being exemption under Article 4 of Regulation (EEC) No 2408/92 as a public service obligation imposed by a Member State. In the latter hypothesis, any financial compensation granted to an air carrier selected through a transparent tender procedure must take account of expenditure and revenue generated by the service. In the present case, however, no public service obligation on routes to and from Sardinia has been brought to the attention of the Commission, whose responsibility it would be to publish a notice to that effect in the *Official Journal of the European Communities.*

V

In the light of the foregoing, the aid scheme introduced by the Law of 20 January 1994 must be regarded as incompatible with the common market. Where legislation provides for an aid scheme that is incompatible with the common market, the Commission is entitled, in order to ensure the effectiveness of the incompatibility and hence of its decision on the incompatibility of the aid scheme, to require the Member State concerned to refrain from applying the legislation and to take the necessary steps to repeal it (see judgment of the Court in Case 130/83, *Commission* v. *Italian Republic*) [2]. As the Law provides for the granting of aid corresponding to expenditure charged to that end against the budgets for 1994, 1995 and 1996, the Italian authorities must refrain from applying it and must adopt the necessary measures to repeal it. Furthermore, where an aid scheme is incompatible with the common market but aid has been paid pursuant to legislative provisions establishing the scheme, the Commission has the power, pursuant to Article 93 (2)

[1] OJ No C 350, 10. 12. 1994, p. 5.

[2] [1984] ECR 2849.

of the Treaty and in accordance with the Court's judgments in Cases 70/72, *Commission* v. *Germany*(1) and 310/85, *Deufil* v. *Commission*(2), to require the Member State concerned to order that the aid be repaid. As the Commission has no information concerning any aid payments made pursuant to the Law in question, the Italian authorities will therefore have to recover any aid that may have been granted to firms or bodies under that Law. The aid must be recovered in accordance with the provisions of national law, in particular those relating to interest on arrears on amounts owed to the State, with interest starting to run on the date on which the unlawful aid was granted,

HAS ADOPTED THIS DECISION:

Article 1

The aid scheme established by the Law of the Region of Sardinia of 20 January 1994 is hereby declared incompatible with the common market within the meaning of Article 92 of the EC Treaty and Article 61 of the EEA Agreement.

Article 2

1. Italy shall forthwith cease to apply the Law of 20 January 1994 and shall, within two months of notification of this decision, take all the necessary steps to repeal that Law.

2. Italy shall order the repayment, within two months of notification of this Decision, of any aid granted under the Law of 20 January 1994. The aid shall be recovered in accordance with the provisions of national law, in particular those relating to interest on arrears payable on amounts owed to the State, with interest starting to run on the date on which the aid was granted. The rate applicable shall be the reference rate used in the assessment of regional aid schemes.

Article 3

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

Article 4

This Decision is addressed to the Italian Republic.

Done at Brussels, 19 July 1995.

For the Commission

Neil KINNOCK

Member of the Commission

(1) [1973] ECR 813.
(2) [1987] ECR 901.