COMMISSION DECISION

of 23 July 2003

on the State aid C 61/2002 which the United Kingdom is planning to implement for a newsprint reprocessing capacity support under the WRAP programme

(notified under document number C(2003) 2010)

(Only the English text is authentic)

(Text with EEA relevance)

(2003/814/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

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

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

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

Whereas:

1. **PROCEDURE**

(1) By letter dated 20 December 2001 and registered on 21 December 2001 under number A/40145, the Commission received a complaint about a planned aid measure by the United Kingdom government for the erection of a newsprint reprocessing facility under the Waste and resources action programme (hereafter 'WRAP'). The complaint was registered by the Commission under number CP 219/01. Following that complaint, the Commission asked the United Kingdom for clarification by letter dated 24 January 2002 and registered under number D/50289. The United Kingdom replied by letter dated 5 February 2002, and registered on 7 February 2002 under number A/30923. The Commission asked further questions by letter dated 14 February 2002, and registered under number D/50655. The United Kingdom replied by letter dated 7 March 2002, and registered on 11 March 2002 under number A/31885.

(2) By letter dated 20 March 2002, and registered on 20 March 2002, under number A/32132, the United Kingdom authorities notified the Commission of an aid project for a newsprint reprocessing capacity under the WRAP. The notification was registered under number N 196/02. The Commission informed the United Kingdom authorities that the notification was considered to be incomplete, and asked for further information by letter dated 15 May 2002 and registered under number D/52364. The United Kingdom submitted the answers by letter dated 14 June 2002, and registered on 19 June 2002 under number A/34497. By letter dated 26 July 2002, and registered on the same date under number A/35727, the United Kingdom asked for a meeting, and agreed to extend the time limit for the Commission to take a decision until 20 October 2002. A meeting was held on 29 August 2002 between the Commission and representatives of the United Kingdom government and of the WRAP programme. The United Kingdom provided further information by letter dated 6 September 2002 and registered on 9 September 2002 under number A/36527.

(3) By letter dated 16 July and registered on the same day under number A/7212, the United Kingdom notified the WRAP scheme. That scheme was registered under number N 474/02. The Commission took the decision to approve part of the scheme, and to open the formal investigation procedure with regard to the remaining part on 20 March 2003. The procedure was registered under number C 21/03, and will be the subject of a separate decision.

(4) By letter dated 4 October 2002, the Commission informed the United Kingdom that it had decided to initiate the procedure laid down in Article 88(2) of the EC Treaty in respect of the aid measure. The case was registered under number C 61/02.

(5) By letter dated 24 October 2002, and registered on 14 November 2002 under number A/38393, the United Kingdom asked for an extension to the deadline for submitting its comments. By letter dated 15 November

([1]) OJ C 283, 20.11.2002, p. 7.

2002, and registered the same day under number A/38470, the United Kingdom replied to the letter informing it of the initiation of the procedure.

(6) The Commission decision to initiate the procedure was published in the *Official Journal of the European Communities*. The Commission invited interested parties to submit their comments on the aid.

(7) The Commission received 19 comments from interested parties within the time limit of one month. It forwarded them to the United Kingdom, which was given the opportunity to react, by letter dated 20 January 2003, and registered under number D/50382. The United Kingdom's comments were received by letter dated 20 February 2003, and registered on 21 February 2003, under number A/31417.

(8) On 20 March 2003, Commission officials visited the UPM-Kymmene Shotton paper mill.

(9) A meeting was held on 8 April 2003 between the Commission and representatives of the UK government, of the company involved and of the WRAP programme. Following that meeting, the Commission sent further questions to the United Kingdom by letter dated 15 April 2003 and registered under number D/52501.

(10) The United Kingdom replied by letter dated 12 May 2003, and registered on 14 May 2003 under number A/33317.

(11) A new meeting was held on 20 May 2003 between the Commission and representatives of the UK government, of the company involved and of the WRAP programme. Following that meeting, the Commission asked further information by letter D/54603 of 15 July 2003 and the United Kingdom sent further information by letters dated 23 May 2003 and 17 July 2003, registered under numbers A/33640, A/33641 and A/35092.

2. DESCRIPTION OF THE MEASURE

2.1. The WRAP Programme

(12) The aid is given within the framework of the Waste and resources action programme. According to the information submitted by the United Kingdom, the programme and its executive body (hereinafter 'WRAP') have been established to promote efficient markets for recycled materials and products, by stimulating demand for recycled materials and products. WRAP's members comprise the charity Wastewatch, the Environmental Services Association as well as the Secretary of State for Environment, Food and Rural Affairs. It is responsible for administering the aid, and is funded by the government for the period 2001 to 2004. WRAP functions as an adjunct to the government, and implements government policies, although it has the form of a private company. The financial support in itself is provided through the Waste and Resources Environmental Body Limited (WREB), a subsidiary of WRAP, with responsibility for the selection of beneficiaries.

(13) In this case, WRAP wished to address the problem that too much waste newsprint is being put into landfill sites. In the UK newsprint sector, there is an established demand for recycled products, but according to the United Kingdom, a market failure has led to a shortage of reprocessing capacity. The United Kingdom identified the main cause of this market failure to be the lack of sufficient reprocessing capacity for waste newsprint, which has led to difficulties in sourcing waste paper in the last decade, and attendant price fluctuations ([2]). For this reason, an increase in reprocessing capacity has been hampered by lack of investor confidence. In order to correct this market failure, WRAP decided to offer support to the private sector to increase newsprint reprocessing capacity which utilises waste newspapers and magazines as its raw material input.

2.2. The tender process

(14) WRAP issued a competitive tender in July 2001, inspired by Community public procurement procedures ([3]), with a view to promoting the creation of newsprint reprocessing capacity. The tender stipulated two key conditions: first, the reprocessing facility had to produce newsprint, and be located within the United Kingdom. Secondly, the reprocessing facility had to use an agreed tonnage of waste paper per year recovered

([2]) According to the information submitted by the United Kingdom, each time the recycling capacity increased in the United Kingdom, the price of mixed waste paper and magazines increased. The supply responds very slowly to the increasing demand, and causes upward pressure on prices.

([3]) According to the United Kingdom, since the process related to the award of financial support rather than the procurement of a work, supply or service, there could be no publication in the Official Journal. The structure of the process was however inspired by the Community procurement rules.

from the municipal waste stream as raw material input for the duration of the life of the facility. The agreed tonnage had to be in excess of the aggregate amount of waste paper used by the successful bidder in a previous calendar year in its newsprint manufacturing facilities in the United Kingdom. WRAP's target for the agreed tonnage was to exceed 300 000 tonnes per year, and the facility was to enter into production in 2003, with full capacity to be reached as soon as possible thereafter. Tenderers needed to specify the level of support required to bring forward their proposals, and to demonstrate technological developments and environmental benefits. Furthermore, the tender specification stipulated that any costing included in the tender bids should only refer to the activities and investments needed to achieve the required environmental benefits.

(15) Following the tender procedure, a prequalification pack was sent to five companies, four of which did prequalify and received a tender invitation document. Applications were finally received from two companies: Aylesford Newsprint Limited, and UPM Kymmene-Shotton (hereinafter 'Shotton'). Aylesford Newsprint was appointed preferred bidder in November 2001, but during the discussion between WRAP and Aylesford Newsprint, it appeared that Aylesford Newsprint would not be able to enter into the level of contractual commitment which would enable WRAP to achieve its objectives. WRAP therefore reviewed its position, and appointed Shotton as preferred bidder. The decision to appoint Shotton as preferred bidder was taken on 18 January 2002. Discussions then followed between WRAP and Shotton, regarding the completion of the funding arrangements to enable the overall investment to proceed. The funding is subject to State aid clearance. A funding agreement was entered into on 21 February 2002.

(16) According to the United Kingdom, the fact that there has been a competitive tender to ensure that the minimum necessary is paid to secure the environmental benefits, means there can be no distortion of competition. That is why the UK authorities consider that the funding does not constitute State aid. However, in order to obtain complete legal certainty, the United Kingdom decided to notify the project.

2.3. **The beneficiary: Shotton**

(17) Shotton is based in Shotton, Flintshire, in North Wales, being an area eligible for regional aid under Article 87(3)(c) of the Treaty. Shotton is owned by UPM-Kymmene Corporation, a Finnish company and major player on the paper market. Shotton's present site has two paper machines, using locally produced pulp derived from a combination of virgin wood and recycled waste paper.

2.4. **The project**

(18) The project proposes the adaptation of the current production facilities to enable the substitution of waste paper for virgin pulp. It also proposes the enhancement of one of the de-inking lines for the recycled paper feeding one of the paper machines. According to the UK authorities, this project will make it possible to achieve an increase in waste paper consumption of approximately 321 000 tonnes per annum over that achieved in the United Kingdom in 2000. This exceeds WRAP's objective of achieving a net increase target of 300 000 tonnes per annum in the year 2000. The adaptations of the facility will be finished in 2003, and the facility will be fully operational by 2005.

(19) The UK authorities explain that the waste paper used by Shotton as raw material in its newsprint production process will source from local authorities and waste management companies. UPM-Kymmene aims to enter into long-term contractual arrangements with local authorities for the major part of its feedstock. This will enable the local authorities to implement comprehensive long-term collection systems where they do not currently exist. The excess waste paper collected prior to commissioning will be diverted to other paper mills within the UPM-Kymmene group. According to the United Kingdom, the local authorities and the waste management companies will need to build up a waste paper collection infrastructure.

(20) Apart from the fact that Shotton has to use an agreed tonnage of waste newspapers and magazines recovered from the municipal waste stream as the raw material for the new facility, the support to Shotton is subject to other environmental obligations set out in the funding agreement. These comprise:

(a) a reduction of 118 000 tonnes of CO_2 emissions;

(b) an annual reduction of some 6 500 lorry movements (this means a minimum reduction of some 325 000 lorry miles per year);

(c) an annual reduction of 53 tonnes of emissions of volatile organic compounds; and

(d) the recycling of an additional total of 54 600 m^3 of water.

(21) According to the United Kingdom, the main objective of the current project is to achieve additional newsprint recycling. But the United Kingdom argues that the investment project will bring about other environmental benefits consisting of a reduction in the waste going to landfills ([4]), the reduction of carbon dioxide and methane emissions from landfills, and the conservation of 1,9 million tonnes of virgin timber. Furthermore, they claim that this project will lead to increasing demand for a major proportion of the household waste stream in the region concerned to be recycled. This demand for waste newspapers and magazines, being 30 to 40 % of household waste by weight, would provide a stable economic platform for the establishment and maintenance of separated collections for household waste for recycling. The simultaneous collection of other recyclable materials at much higher rates could therefore also be supported. This leads to the conclusion that the facility would enable greater proportions of household waste to be recycled ([5]). This will bring benefits for the environment, as less waste will be deposited in the landfills.

(22) The UK authorities argue that the investment in the newsprint facility will enable the United Kingdom to make significant progress towards achieving its obligations within the framework of European Community waste management policy, and deliver tangible environmental benefits. These environmental benefits bring the United Kingdom to affirm that the aid qualifies for investment aid under point 29 of the Community guidelines on State aid for environmental protection ([6]) (hereafter 'environmental aid guidelines'), when firms undertake investment in the absence of mandatory Community standards. According to the UK authorities, there are no specific mandatory requirements for any newsprint manufacturer to use recycled waste paper as a raw material. As regards the waste water standards, the new investment in the facility does not involve any additional expenditure on waste water treatment. In the case of air emissions, there is only a very small part referable to mandatory air emissions standards. This investment concerns the installation of equipment for on-line monitoring of emissions, and amounts to approximately GBP 35 000.

(23) The total costs of the project were originally estimated at GBP 127,9 million. The United Kingdom notified GBP 88,2 million of this amount as eligible costs under the environmental aid guidelines. The remaining GBP 39,7 million represent enhancements to the production and quality capabilities of the existing paper machines, and do not relate to recycling.

(24) According to the United Kingdom, the switch from the current paper mills to the new paper mills using only waste paper would result in an increase in Shotton's total earnings of GBP 824 000 over the five-year period from the date of full operation.

(25) Following discussions with the Commission in May 2003, the United Kingdom modified its original project, and submitted information in order to allow the whole project to be assessed under the Guidelines on national regional aid ([7]) (hereinafter 'the regional aid guidelines'). The total cost of the modified investment project will be GBP 125,2 million.

(26) Shotton changed its project with a view to building a new type of sludge combustor, which will achieve higher environmental benefits than the one originally foreseen. The combustor will produce steam for the plant's energy needs. In the original project, it was planned that the sludge combustor would function on the basis of sludge and natural gas. In the new project, the sludge combustor will use, as well as the sludge, fuel consisting of renewable low-grade forest residues, and pretreated household waste, from which the recyclable elements have already been removed.

(27) Following requests for information from the Commission, the United Kingdom indicated in its last submission that the project will create a total of four direct jobs. Furthermore, 187 indirect jobs will be generated in the adjacent assisted areas by Shotton's commitment to purchase a higher amount of waste paper, newly recovered from the domestic waste stream.

([4]) In the region where UPM-Kymmene is located, there is an abundance of low cost landfills, therefore local authorities have not been motivated to invest in the collection of waste materials for recycling.

([5]) According to the United Kingdom, it is estimated that the demand for newsprint of the scale created by the development of this facility will allow around 596 Kt of other materials (steel, aluminium, glass, newsprint, plastic) to be recycled per year.

([6]) OJ C 37, 3.2.2001, p. 3.

([7]) OJ C 74, 10.3.1998, p. 9.

2.5. **The aid measures**

(28) Shotton has applied for support of GBP 23 million, which will be paid out by WREB. The United Kingdom provided a copy of the Support agreement between WREB and Shotton, dated 21 February 2002.

3. **REASONS TO INITIATE THE FORMAL INVESTIGATION PROCEDURE**

(29) First of all, the Commission doubted whether the aid could be assessed under the environmental aid guidelines.

(30) According to the information available to the Commission, the use of waste paper for the production of newsprint seems to be the current state of the art. Even if there is an environmental benefit in using waste paper instead of virgin wood pulp, the Commission doubted whether the investment could qualify as an investment within the meaning of point 29 of the environmental aid guidelines ([8]), as Shotton already uses waste paper in its current plant. Furthermore, the investment seeks to improve the state of the environment as such and not the environmental performance of the company itself. The Commission also doubted whether there could be an environmental justification for requiring the recycling to take place within the United Kingdom, which was a condition in the tender, since waste paper is not a hazardous waste.

(31) The Commission also indicated that similar projects had been approved under the regional aid guidelines. In this case, the aid would be notifiable under the multisectoral framework ([9]) as the project is fulfilling the conditions set out in this framework. But the Commission did not have sufficient information to allow it to assess the case under the environmental aid guidelines.

(32) Furthermore, even if point 29 of the environmental aid guidelines applied, doubts arose as to the calculation of the eligible costs and the amount of the benefits for the undertaking concerned.

([8]) Similar projects have already been approved by the Commission on the basis of the multisectoral framework, but not under the current environmental guidelines (for example, Hamburger AG (C 72/01), Commission decision 9 April 2002 (not yet published); Kartogroup (N 184/2000), Commission decision 18 July 2001 (http://europa.eu.int/comm/secretariat_general/sgb/state_aids/industrie/n184-00.pdf).

([9]) Multisectoral framework on regional aid for large investment projects (OJ C 107, 7.4.1998, p. 7).

4. **COMMENTS FROM INTERESTED PARTIES**

4.1. **Introduction**

(33) The Commission received comments from 19 interested parties. Two interested parties expressed the desire to keep their identity confidential. They will be referred to in this decision as 'paper producer A' and 'paper producer B', which is the original complainant. The Commission also received comments from several members of the UK Parliament as well as from the European Parliament, which have been duly taken into account. However, these comments are not discussed in detail in this decision since those persons cannot be considered as interested parties within the meaning of Article 1(h) of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty ([10]).

4.2. **Comments from paper producer A**

The paper market

(34) Producer A is a competitor of Shotton. It indicates, first of all, that newsprint is a cyclical industry with excess capacity. The demand for newsprint paper depends on the demand for advertising, which is itself closely linked to the performance of the economy. The excess newsprint capacity is likely to continue to exist for at least two to three years. Shotton might start its production already within this period. Newsprint industry is extremely capital intensive, and investments in new capacities tend to occur in large and infrequent lumps. Usually, decisions about the amount and the timing of the investment are made taking into account the existing capacity/demand balance, the investments already decided by others, and the long-term growth trend of the market.

(35) As regards the market for fresh fibres and the market for recycled fibres, neither product is sold on the open market in appreciable quantities, since newsprint producers generally have integrated pulp production facilities. There is a well-developed market for used paper and recycled fibres since the increase in environmental awareness. Recycled fibres have become an essential raw material for the paper industry, and they can be reused up to six times, if they are mixed with fresh fibres. Usually, recycling happens in densely

([10]) OJ L 83, 27.3.1999, p. 1.

populated areas, because of the large supply of paper, and the short distances for transporting. There is a wide variety of recycled fibres, and it is estimated that around 40 to 43 million tonnes of recycled paper are collected in Europe annually, in addition to 350 000 tonnes of imported recycled paper. In 2000, the newsprint industry as a whole used 16,9 % of the total European recycled fibre market for raw material. Around 41 million tonnes of recycled paper are used within general paper production. According to producer A, there is a trend amongst customers to prefer newsprint made of recycled fibres if other commercial/technical factors are equal or similar to newsprint made of fresh fibres.

Notion of aid

(36) Paper producer A asks the Commission to declare the aid incompatible with the Community rules on State aid. According to that producer, the grant constitutes State aid, as it grants an advantage to one selected company, covering the costs the beneficiary would otherwise have to bear. Producer A argues that the funding does not meet requirements similar to those a private investor would have applied.

(37) Producer A states that the conditions set out in the tender are not strictly necessary to meet environmental objectives. More specifically, the requirement that the plant should be located in the United Kingdom goes beyond what is necessary, as there is significant cross-border trade in recovered paper. The objectives pursued by the United Kingdom could be reached with less negative impact on trade between Member States and on competition, and with less inefficiencies. Producer A suggests WRAP should have tried to stimulate the collection rates, building a direct incentive system for the collectors and sorters of waste paper, rather than favouring one single producer of newsprint.

The distortion of competition

(38) Producer A argues that the funding could cause a distortion of competition on the market for newsprint. The funding would first of all influence the decisions of investors in the field of newsprint paper. As a result, there would be a direct effect on competition in the newsprint market as well as on trade between Member States, not only in the newsprint market, but also on markets upstream and downstream to newsprint, including the market for recovered papers. Secondly, Shotton will have a cost advantage in comparison with its competitors, as it will not have to bear all investment costs in connection with the de-inked pulp facility. If Shotton receives the aid, it will be able to accept lower prices for its product than its competitors, and still have a positive gross margin on its sales.

(39) As regards a distortion on the geographical market, although it is apparent from previous cases that the relevant market would be the EEA market, producer A holds that the market could be defined more narrowly, due to the high transportation costs. However, according to producer A, statistics show that there are significant intra-Community cross-border trade flows of recovered paper. To conclude, producer A states that the funding would affect intra-Community trade.

Existence of a market failure

(40) Producer A strongly disagrees with the fact that there is a market failure leading to a shortage of reprocessing capacity in the United Kingdom. Recovered paper is a scarce resource, and there would be demand for recovered paper should supply increase.

Applicability of the environmental aid guidelines

(41) The objectives of WRAP do not only include the achievement of environmental objectives. They also aim to create stable and efficient markets for recycled products and materials. Points 29 and 40 of the environmental aid guidelines do not apply, as producer A claims that the funding does not aim at improving on standards directly applicable to the beneficiary, or in the absence of any community standards. The proposed aid merely aims at satisfying Community standards under the landfill of waste Directive ([11]) directly applicable to the United Kingdom.

([11]) Council directive 1999/31/EC of 26 April 1999 on the landfill of waste (OJ L 182, 16.7.1999, p. 1).

(42) Producer A expresses strong doubts as to whether Shotton could achieve the objectives established by WRAP within the agreed timetable.

Definition of the eligible costs under the environmental aid guidelines

(43) Producer A takes the view that the investment does not concern an initial investment only, but is, for a large part, also a replacement investment. In order to integrate the new de-inking pulp line, Shotton will have to rebuild fibre line 1, which will most probably be done by increasing capacity of existing equipment and enhancing quality on the existing line. Furthermore, producer A believes that increasing the de-inking pulp capacity by the amounts stated would require more combustion and sludge dewatering capacity than already in place. The new sludge combustion and sludge dewatering equipment would be built with capacity to handle the total sludge combustion and sludge dewatering needs for the whole mill. This means that either the existing equipment would be closed down and fully replaced or, it would be replaced and the previous equipment maintained and kept as back-up. Producer A therefore concludes that the aid would be used for replacing existing machines, which should not be considered as eligible costs under the environmental aid guidelines.

Applicability of the regional aid guidelines

(44) Producer A finally states that the regional aid guidelines and the multisectoral framework are not applicable. It urges the Commission to take into account the current and future excess de-inked pulp capacity in the newsprint market and the overall size and position of Shotton.

4.3. **Comments from paper producer B**

Notion of aid

(45) Producer B claims that the measure constitutes State aid as it fulfils the conditions of Article 87(1) of the Treaty. The fact that there was an open tender process does not change anything in that respect. The argument of an open tender procedure is only relevant when the tender procedure serves to fix the consideration for a service, work, or an acquisition, in order to be sure that the market price has been paid for the service by the tendering public authority. In this case, WRAP does not wish to acquire a service or goods so this argument is not useful to conclude that there is no State aid. The grant clearly alleviates Shotton of the cost burden it should normally have to bear.

(46) Producer B argues that the aid lacks any incentive effect, since it is granted for an investment that is necessary for Shotton to remain competitive. The use of waste paper instead of wood pulp will reduce the high production costs, as a large amount of electricity is needed to process primary wood into wood pulp, in comparison to the costs for the flotation process to produce recycled fibre pulp. Furthermore, the prices for virgin timber and fresh wood pulp do not allow it to remain competitive in the mid- to long-term, without processing substantial amounts of waste paper. Shotton will most probably keep its facilities for virgin pulp, these being necessary to be able to add fresh fibres to the pulp. It will also probably only increase its output by adding waste paper reprocessing facilities. By doing so, Shotton's position on the market will be improved in comparison to competitors that do not benefit from aid to modernise or replace their facilities.

Applicability of the environmental aid guidelines

(47) Producer B considers that the aid should not be considered as environmental aid, as its purpose is not the protection of the environment, but merely the upgrading of the equipment to the current state-of-the-art. The exceptions under Article 87(3)(c) should be interpreted restrictively. In this case, the aid only incidentally happens to have positive environmental effects, which means the environmental aid guidelines do not apply in this case. As regards the environmental benefits cited (reduction of carbon dioxide, recycling of water, etc.), producer B submits that these advantages are an automatic result of the adaptation of old facilities for the increased reprocessing of recycled paper. It also states that the expected advantages in terms of reduction of waste going to landfills is very doubtful. The market for old newsprint offers opportunities to sell waste paper rather than deposit it in landfill, because it has become a required

raw material. Furthermore, the conversion from the existing thermo-mechanical pulp process to the de-inking process of waste paper leads to a higher load at the landfills in form of de-inking sludge. This sludge contains a higher amount of potentially harmful materials, such as heavy metals, per tonne.

(48) Producer B submits furthermore that the aid is linked to compliance with existing Community standards, which require a minimum amount of waste to be recycled, rather than sent to landfills. Therefore, the aid may not be granted, as it is intended solely to fulfil the mandatory standards.

(49) Furthermore, according to producer B, undertakings that help fulfilling mandatory Community standards have to use the 'best available techniques' ([12]). Producer B states that these 'best available techniques' consist of using waste paper as raw material to produce newsprint paper.

Definition of the eligible costs under the environmental aid guidelines

(50) According to producer B, the aid granted should be considered as operating aid and not as investment aid, as it concerns the mere replacement and updating of old facilities. Under the environmental aid guidelines, operating aid may only be granted if it is absolutely necessary to implement the Community strategy for waste and only for the polluters. Producer B also claims that the operating costs will be reduced for Shotton, as the aid will allow Shotton to upgrade its plant to the current state-of-the-art and, to use less fresh wood pulp or virgin timber.

(51) As regards the intensity of the aid, producer B states first of all that the costs exposed by Shotton are not all eligible costs. The modifications of Shotton's paper machines represent the current standard technology. Therefore, they can not claim all or part of the investment costs to be eligible for environmental aid. Producer B states furthermore that the investment costs to be taken into consideration should be the net eligible costs. However, the costs of similar projects have been 50 % lower than what is suggested for the Shotton plant. The investment costs seem inflated. Producer B also notes that the conversion to a production by de-inking waste paper does not require any particular investments on the actual paper production lines.

(52) Producer B expects the amount of the benefits of the investments and the earnings of the first five years to be higher than the amount proposed by the United Kingdom. This assumption is based on the forecast that the local collection of waste paper will be cheap, and that the demand for recycled paper will increase.

Applicability of the regional aid guidelines

(53) As regards an eventual assessment of the aid under the guidelines for national regional aid, producer B states that the purpose of the aid is not to enhance regional development as it does not aim to create or to maintain working places. It does not seem to have any positive effects for the development of the Flintshire region. Therefore, the aid should not be considered as regional aid.

4.4. **Comments from UPM — Shotton**

Introduction

(54) Shotton first gives a general picture of the facts. The United Kingdom's capacity to recycle waste paper is lower than that of other northern European countries. Paper recycling should be improved to allow the United Kingdom to respect its obligations under the landfill Directive. WRAP considered an indirect approach to stimulate collecting of waste paper but dismissed it as it would not have had a sustainable long-term benefit. If only collection were aided, there would be no guarantee that the collected product would find a sustainable demand. Furthermore, this solution would cost more in the medium term. Therefore, WRAP has chosen to stimulate the demand of waste paper.

Notion of aid

(55) As regards Shotton, the existing plant is still profitable. The existing fibre pulp mill, which will be decommissioned, has a further profitable operating life of at least 10 years. The remaining existing paper machines have at least 20 years of operating life. There is no economic or legal reason why existing profitable

([12]) Footnote 6 of the environmental guidelines.

mills that do not use 100 % waste newspapers should be decommissioned or adapted to the use of waste paper. The use of a tender procedure was meant to ensure that the costs of conversion of a well-functioning plant into a plant using only recycled fibres were limited to the minimum necessary.

(56) As regards the tender procedure, Shotton concludes from previous Commission decisions, that State aid for recycling may be granted in three circumstances. One of those circumstances is State aid to an undertaking which is not obliged to recycle under national or Community standards, but where funds are nevertheless provided to support the entity performing the recycling. State aid is allowed to the extent that it is paid over and above market rates for the job in question. In that case, the recycling company is performing a service of general economic interest to the State. The amount of aid should be determined taking into account whether the State is paying a market rate or not for the service provided. In this case, the fact that there was a tender procedure ensures the market price has been paid. Therefore, no aid has been granted.

(57) Furthermore, the competition was open to non-UK firms. The fact that the company had to be located in the United Kingdom is justified, as the investment is aimed at increasing recycling capacity in the United Kingdom. All other conditions are essential to meet the environmental objectives pursued by the United Kingdom. The condition that the successful tenderer should be involved in the manufacture of newsprint is justified, as newsprint can be made out of 100 % waste paper. It again serves to achieve the environmental objectives of the United Kingdom. The mere collection of newspaper is not in itself recycling and is very different from using newspaper in an economic and useful way.

Distortion of competition and effect on trade

(58) Shotton's capacity will be unchanged after the conversion, as will its costs and the quality of the final product. Therefore, Shotton argues, that there will be no adverse effect on competition.

(59) Shotton will not be relieved from costs it would normally have to bear, as the plant is perfectly profitable in the way it is working now. It has an estimated further profitable operating life of 10 to 20 years.

(60) The funding of the project will have no effect on trade, as Shotton operates on the local market of the United Kingdom for the purchase of raw materials, as well as partly for sales of newsprint (50 % will be delivered to customers within 70 miles of the mill, and Shotton aims to supply all its products to customers in the United Kingdom by 2005). The current raw materials also come from the United Kingdom. Shotton also argues that UK exports of waste newsprint and magazines originate from the south of the United Kingdom, outside Shotton's catchment area.

(61) The funding does not distort competition, as it does not strengthen Shotton's position vis-à-vis other undertakings. There will be no changes to the capacity of the plant or to the production costs. Shotton will not compete for existing supplies of waste newspapers, but will generate new supplies of recovered newspapers from UK landfill. The conversion relates to the pulp mill and the pulp will exclusively be used in Shotton, without being sold to third parties.

Applicability of the environmental aid guidelines

(62) The investment fits perfectly within the environmental aid guidelines: the project is designed to prevent damage to our physical surroundings (point 6). There is no reason to limit the environmental benefits to the reduction of pollution, but if that were to be the case, Shotton emphasises that the investment will in any case reduce pollution. It will also correspond to the objectives of sustainable development set out in point 3 of the environmental aid guidelines, by promoting the use of waste paper and the collection of other waste materials. Furthermore, the investment is in line with point 36 of the environmental aid guidelines, as it is meant to adapt production methods with a view to protecting the environment. According to Shotton, investment aid should be compatible up to 30 % of the eligible investment costs, in the absence of mandatory Community standards, which is the case here, as Shotton is under no obligation as regards the purchase

or use of waste paper. The argument that the investment concerns an activity which is 'state-of-the-art' makes no sense, according to Shotton, as the existing plant still has a long life to run. Things would be different for a new investment. Without the aid, there would be no incentive for Shotton to change its production methods.

Definition of the eligible costs

(63) As regards the calculation of the eligible costs, the calculation has been done properly. Shotton maintains that the costs are investment costs and do not constitute a replacement investment. Therefore, all costs incurred should be considered as being eligible.

Notion of service of general economic interest

(64) Shotton claims that it will provide a service of general economic interest, as it will help the United Kingdom to fulfil its obligations under Community law. The United Kingdom issued a tender to ensure the supply of this service. As regards the performance of a service of general economic interest, Shotton quotes the FFAD ([13]) case, where the management of waste was considered to be a service of general economic interest. In view of the Ferring case ([14]), the funding merely constitutes compensation for this service which does not involve State aid. If the cost were to be higher than the market price for this service, the aid would nevertheless be compatible under Article 86(2) of the Treaty.

4.5. **Comments from the other interested parties**

(65) Comments were introduced by the Paper Federation of Great Britain, the Paper Industry Technical Association, Professor John Roberts of the Department of Paper Science of the UMIST ([15]), the Local Authority Advisory Committee, the Local Government Association, the Greater Manchester Waste Disposal Authority, Cleanaway, St Regis Paper Company, the Environmental Industries Commission, the Environment Agency, Albion Water Limited, London Remade, the Merseyside Waste Disposal Authority, Viridor Credits and Forum for the Future.

Distortion of competition

(66) As regards the effects of the investment on competition, several parties argued that there would be no effects on competition as Shotton's capacity would not increase. There would be no impact on downstream markets for finished newsprint.

(67) Concerning the market failure, the Paper Federation of Great Britain states that recovered paper usage has increased by 144 % since 1991. Newsprint is the second largest recovered paper using sector. Imports account for 65 % of the market, and the United Kingdom has the largest newsprint market in Europe. However, despite the strong apparent investment potential, only one newsprint machine has been built in the United Kingdom during the past decade with a government grant. This shows, according to the Paper Federation, that there is a clear market failure. The Paper Federation also states that the United Kingdom newspaper publishers and British newsprint manufacturers agreed with the government on certain targets for the recycled fibre content of newspapers (for example, 60 % by the end of 2001). The target for 2001 has been reached but not by increasing the amount of recovered fibre used by UK newsprint manufacturers. It was the result of the increased import of already degraded fibres which have to be used sooner than virgin fibres.

The environmental benefits of the project

(68) The parties in recital 65 mention the fact that the investment in the Shotton plant will divert 1,6 million tonnes of waste paper from landfills. This will result in a reduction of 352 000 tonnes in carbon dioxide and methane emissions. The switch to the use of waste paper as a raw material for newsprint will allow savings of virgin pulp. For the Environmental Industries Commission, the WRAP funding for the Shotton investment is a good example of how industries can use new technologies to meet key environmental challenges such as using resources more efficiently. The diversion of 1,6 million tonnes of waste paper from landfills will result in an increase in the UK recycling rate of 7 %.

([13]) Case C-209/98 *Entreprenørforeningens Affalds/Miljøsektion (FFAD)* v *Københavns Kommune* [2000] ECR I-3743, paragraphs 75 and 76.

([14]) Case C-172/00 *Ferring Arzneimittel GmbH* v *Eurim-Pharm Arzneimittel* [2002] ECR I-6891.

([15]) University of Manchester Institute of Science and Technology.

(69) The new investment will lead to the closure of the existing energy-intensive thermo-mechanical pulp plant. This will result in the elimination of 53 tonnes/year of emissions of volatile organic compounds. These emissions arise from the wood components, and contain resin acids from the softwoods used. The Shotton project will eliminate the discharge of these toxic compounds both as volatiles and in waste water discharges.

(70) The project will also make it possible to reduce the number of lorry vehicle journeys by 6 500. The internal water re-use will increase by 500 000 m^3/year. This will enable the strategic value of scarce water resources to be optimised elsewhere in the region. According to Albion Water Limited, Shotton's move to 100 % recycled fibre will allow it to impose targets on Shotton for water consumption that will save about 500 000 m^3 of process water a year.

(71) The increased recycling of waste paper, and the long-term commitment from Shotton to take up this waste paper, will allow the area to set up an improved collection infrastructure. The aid to Shotton is deemed to be necessary in order to be able to invest in the institution of a widespread kerbside collection scheme, which will benefit the UK environmental obligations.

5. **COMMENTS FROM THE UNITED KINGDOM**

Introduction

(72) The United Kingdom considers that the project fits within the general environmental policy of the Community, more specifically the waste management policy, and that it should be approved under Article 87(3)(c) of the Treaty. The project aims at direct environmental benefits, namely the creation of a long-term demand for waste paper. The United Kingdom stresses that it has the right to choose the best way to achieve the environmental objectives, on the basis of the principle of subsidiarity. It is not up to the Commission to decide how it should achieve a reduction in waste going to landfills.

Notion of aid

(73) The United Kingdom stresses that Shotton is a consistently profitable and modern mill, with a high return on capital employed. Shotton currently takes advantage of the use of two different materials (virgin fibre and waste newspaper), which will no longer be possible after the switch to 100 % waste paper. This implies a loss of flexibility. Shotton will also lose the quality advantage derived from the current pulp mix in terms of strength characteristics of the paper.

(74) The United Kingdom claims that the conditions put in the tender are not excessive, but constitute the essence of the environmental project, being the aim to encourage recycling of waste newspaper in the United Kingdom. With this project, WRAP wanted to address the specific market failure in the United Kingdom, which exists in recycling capacity and not in waste collection. The requirement in the tender that the successful bidder be located in the United Kingdom is a response to the specific market failure in the United Kingdom. The focusing on newsprint can be explained by the fact that it constitutes a large proportion of household waste and that newsprint is the highest grade of paper which can use waste newspaper and magazines. There is no restriction of nationality or location.

(75) As regards the effects on competition, these will be reduced to a minimum, as WRAP has ensured that the recipient of State aid takes a number of steps to minimise any possible impact on the market. Furthermore, the United Kingdom intervenes at a point in the supply chain which will require the least State aid with the maximal environmental benefits.

(76) The United Kingdom also stresses that the UK situation is a specific one, as there is a large deficit in recycling capacity, without any constant demand. Shotton took the commitment to use exclusively waste paper recovered from landfill. This means there will be no increased competition for waste paper that already, in the current situation, is collected for recycling. Even if the Shotton project is successful, UK recycling levels will still be well below European averages. The impact on competition would be greater if the United Kingdom were to subsidise the collection of waste paper. If more waste paper were on the market, the prices would go down without any guarantee that recycling capacity would be stimulated to stabilise the situation again.

(77) The United Kingdom argues there will be no effect on the market for virgin pulp, as the wood used by Shotton

comes from the State Forestry Commission and other private woodland owners. The market for newsprint (downstream market) will also not be affected by the aid, since none of the pulp produced in Shotton will be sold to third parties, and there will be no changes to the capacity and life of the plant. The financial benefits will be minimal and the customers of Shotton are expected to remain the same. There will be no net increase in revenue flow for Shotton. Therefore, its position will not be strengthened and there is no risk of distortion of competition.

(78) The effect on trade is deemed to be minimal. The customers are local, all the raw wood materials are grown in the north-west of England and in Wales, the waste paper will be collected within a 70/100 mile radius of Shotton, and Shotton aims to supply virtually all its products to customers in the United Kingdom by 2005. Exports of waste paper from the United Kingdom originate mainly from the south-east of the United Kingdom, outside Shotton's primary catchment area.

(79) In response to the argument that the investment constitutes the current state-of-the-art, the United Kingdom replies that this is correct, but that the aid was strictly necessary to meet the environmental objectives pursued by the United Kingdom. Even if a new plant directly invested in a mill functioning only with recycled fibre, there would be no economic justification for the conversion of an existing mill which still has a long life. The existing mill will be decommissioned. Without aid, due to the technical risks and the low return, the investment would not take place. The investment is therefore not a commercial investment, but an environmental investment. In the present case, the United Kingdom takes the view that the planned aid is proportionate to the environmental effect achieved, and that this effect outweighs any distortive effect the aid may have on competition.

Applicability of the environmental aid guidelines

(80) As regards the applicability of the environmental aid guidelines, the United Kingdom considers that there is no reason to limit the application of those guidelines to the pollution caused by the beneficiary, as stated by the Commission in its decision to open the formal investigation procedure. The investment fits in the broad objectives of the environmental aid guidelines. Furthermore, there are no mandatory Community standards applicable to the firm which means that point 29 of the environmental aid guidelines applies to this case. The United Kingdom also claims that the aid has direct environmental effects, namely diversion from landfill and reduction of pollution. The United Kingdom also insisted on the efficient use of resources (wood and water). The environmental benefits constitute a condition for receiving the aid presented in the tender, and will be monitored by independent WRAP experts.

(81) Furthermore, the environmental aid guidelines allow aid to go beyond merely helping the company to do what the company is already legally obliged to do under Community law. There is no prohibition on granting aid to support companies assisting Member States to comply with the Member States' obligation under Community law.

(82) The United Kingdom shows that the project fits within the general environmental policy of UPM-Kymmene. Shotton has a 'local mill concept', meaning that the waste newspapers will be caught within a radius of 100 miles (and later 70 miles) from Shotton. Newsprint will be sold within a radius of 70 miles of the mill. Shotton has concluded long-term agreements with local authorities, in order to provide the security and incentive to invest in the recycling of newspapers and magazines. These contracts will last for five to ten years, and prices are generally fixed over a five to seven year period. Shotton offers to purchase every tonne of waste paper and is creating a 'recycling culture' in the local community. Shotton assists local authorities to establish the necessary infrastructure to collect waste newspaper, and has launched local initiatives. All this is financed exclusively by Shotton, without any State aid.

(83) As regards the compulsory use of the best available techniques suggested by paper producer B, the United Kingdom considers that these do not put an obligation on newsprint producers to use recycled paper as raw material otherwise, Shotton would have been infringing this for a long time. Furthermore, the United Kingdom states that the use of recycled paper pulp is not considered to be the 'best available technique' in the pulp and paper industry. There is also no economic reason to switch to the use of waste paper.

Calculation of the eligible costs

(84) All of the eligible costs are necessarily incurred if all the identified benefits are to be obtained. As regards the amount of the benefits during the first five years, the United Kingdom refers to the explanations on those benefits given in the notification and subsequent correspondence, where they showed that the benefits were related to the switch to the 100 % use of waste paper. However, the United Kingdom would agree to appoint an independent technical expert to assess the net benefits and undertakes to monitor Shotton to ensure that it does not derive any financial benefits from the aided project, other than the benefits indicated in its former correspondence ([16]). The United Kingdom adds that Shotton derives no economies of scale from the increased use of recycled fibres. The fact that the earnings seem so low may result from a misunderstanding of the current efficiency of the existing pulp mills and paper plant. The current use of virgin fibre by Shotton is extremely cost-effective.

(85) There are also other costs related to the investment which were not included in the eligible costs: extra winding machine, capital outlay of […] (*) on the basis of a wheel bin scheme and costs of setting up and running the collection of waste newspaper by a large number of local authorities. These last costs are deemed to be far more than the amount of aid over two years. A further contribution of […] in seed corn will be made to stimulate collection initiatives.

(86) The United Kingdom also emphasises that the aid is investment aid and not operating aid. The aid is granted to a one-off investment to decommission the thermo-mechanical pulp mill, and to install a mill capable of using 100 % recycled fibre. Therefore, the investment is clearly an 'initial investment'.

(*) represents business secrets omitted from the text.

([16]) In particular, if benefits are made due to the sale of assets, this will be reported to the United Kingdom, and deducted by the United Kingdom from the support provided.

6. ASSESSMENT OF THE AID

6.1. Existence of aid under Article 87(1) of the Treaty

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

(88) In this case, the measure is funded by resources granted by the State under the WRAP programme through its subsidiary WREB. The measure is granted to an individual beneficiary, Shotton, for the adaptation and modification of the existing plant.

The tender procedure

(89) In the present case, the grant has been offered through an open and competitive tender process. Therefore, the United Kingdom and Shotton argued that there was no aid, as the tender procedure ensures that the market price has been paid.

(90) Even if a tender ensures that the aid is limited to the minimum, there is still an advantage granted to the beneficiary of the tender. On the notion of advantage, it should be noted that advantages are usually defined as 'measures which, in various forms, mitigate the charges which are normally included in the budget of an undertaking' ([17]). It can not be denied that Shotton benefits from the aid, as it will receive money for new equipment, with a longer life than the current equipment.

(91) In the case of an open and competitive tender process, it should still be considered whether the conclusion of contracts by the State is a normal commercial transaction whereby the State acts as a market operator. If not, the contract may contain elements of State aid. According to settled case-law, Article 87(1) makes no distinction according to the causes or aims of the aid in question, but defines it in relation to its effects.

([17]) Case 30/59, *Gezamenlijke Steenkoolmijnen in Limburg* v *High Authority of the ECSC* [1961] ECR, p. 1.

(92) In the present case, there has been an open tender where the United Kingdom imposed obligations on a newsprint producer to use a certain amount of waste paper for the production of newsprint in return for remuneration. The choice made by the UK authorities to subsidise the recycling of waste paper is motivated by the fact that the diversion of waste paper from the municipal waste stream would lead to a substantial reduction in waste going to landfills and that this would help the United Kingdom to achieve its commitments under the EC landfill Directive ([18]).

(93) On the basis of these considerations, the Commission considers that the United Kingdom was not acting as a private market investor but as a public authority driven by environmental considerations. Therefore, the Commission concludes that the measure is imputable to the State and cannot be considered as a commercial transaction.

Qualification as a service of general economic interest

(94) Shotton argued that it is helping the United Kingdom to achieve its environmental standards and resolving a specific market failure. In that case, Shotton would be performing a service of general economic interest to the State.

(95) In its decision to open the formal investigation procedure, the Commission expressed its doubts as to the conditions of the tender and qualified them as excessive. In particular, the conditions that the successful bidder should be located in the United Kingdom, and should use a certain amount of waste paper for the production of newsprint, were considered to be excessive.

(96) The Commission's doubts were confirmed by paper producers A and B. The United Kingdom and Shotton argued in their comments that the conditions set out in the tender were essential to achieve the environmental targets: the United Kingdom identified newsprint as constituting a large proportion of household waste. Newsprint is the highest grade of paper which can use waste newspaper and magazines. The condition for the successful bidder to be located in the United Kingdom was a response to the specific market failure existing in that country.

(97) Services of general economic interest should be available to all citizens, and should be necessary for the citizen ([19]). This would be the case for a service consisting in the collection of waste paper. But this is not the case here, as the tender in itself was not aimed at the collection of waste paper but at the taking up of a certain amount of waste for reprocessing into newsprint.

(98) The realisation of an infrastructure, which is economically not profitable, could constitute a service of general economic interest if it does not favour one specific undertaking, if it is necessary to provide a service which the State should normally provide to the public and is limited to the needs of this service, or if the market would never be able to realise the service in the same conditions ([20]). According to the Commission, there is an abuse of the notion of SGEI when the economic activity does not present specific characteristics with regard to other economic activities, or when the economic activity in question is already carried out in a satisfactory manner by the market ([21]).

(99) In the present case, the investment aid benefits one single undertaking, and the service in question, which is not simply waste paper recycling but the production of newsprint on the basis of a defined amount of waste paper, is not a service which should normally be provided by the State. Furthermore, it is unlikely that the market would not be able to provide the service under the same conditions because there is a clear market failure. The comments submitted by producers A and B showed clearly that there was no real market failure on the market of recycling of waste paper. Waste paper is a scarce resource and constitutes the state-of-the art raw material for the production of newsprint. If there were any market failure, it would be in the collection of waste paper and in the cyclical nature of prices. However, the tender was not drafted in this way: it was targeted to the production of newsprint and the successful tenderer had to be located in the United Kingdom.

([18]) Directive 1999/31/EC. See footnote 11.

([19]) Services of General Interest, Communication from the Commission (OJ C 17, 19.1.2001, p. 4, points 9 to 11).

([20]) Services of General Interest, Communication from the Commission (OJ C 17, 19.1.2001, p. 4, point 14).

([21]) See also, *mutatis mutandis*, Case C-205/99 *Analir* [2001] ECR I-1271.

(100) It should finally be noted that the United Kingdom itself did not invoke the notion of service of general economic interest.

(101) Therefore, the Commission concludes that the service in question does not constitute a service of general economic interest, and that Article 86(2) of the Treaty does not apply to this case.

Distortion of competition

(102) In order to be qualified as aid, in the sense of Article 87(1) of the Treaty, the measure should distort or threaten to distort competition.

(103) The possible distortion of competition has been highlighted by paper producers A and B. Producer A states that Shotton will have a cost advantage in comparison with other competitors, as it will not have to bear all investment costs in connection with the de-inked pulp facility. Shotton's position will be improved in comparison to competitors that do not benefit from aid to modernise or replace their facilities.

(104) The United Kingdom and Shotton argued that Shotton will not be relieved from costs it should normally have to bear, as the plant is perfectly profitable as it is working now, and has an estimated further operating life of 10 to 20 years. Shotton's capacity will remain unchanged after the conversion, as will its costs and the quality of the final product. The benefits deriving from the aid are minimal and there will be no net increase in revenue flow for Shotton. Shotton's position will not be strengthened. Shotton and the United Kingdom argue that there will therefore be no adverse effect on competition.

(105) The Commission considers that there is a serious risk of distortion of competition, as the aid will be granted to one single undertaking which will benefit from aid in order to modernise its equipment and its production process. If Shotton had carried out the project without aid, it would have been in a much worse position than its competitors. Therefore, the Commission takes the view that the aid will relieve Shotton from a cost it might have to bear to remain competitive, or to adapt its facilities to different raw materials, which leads to a strengthening of its position vis-à-vis other undertakings.

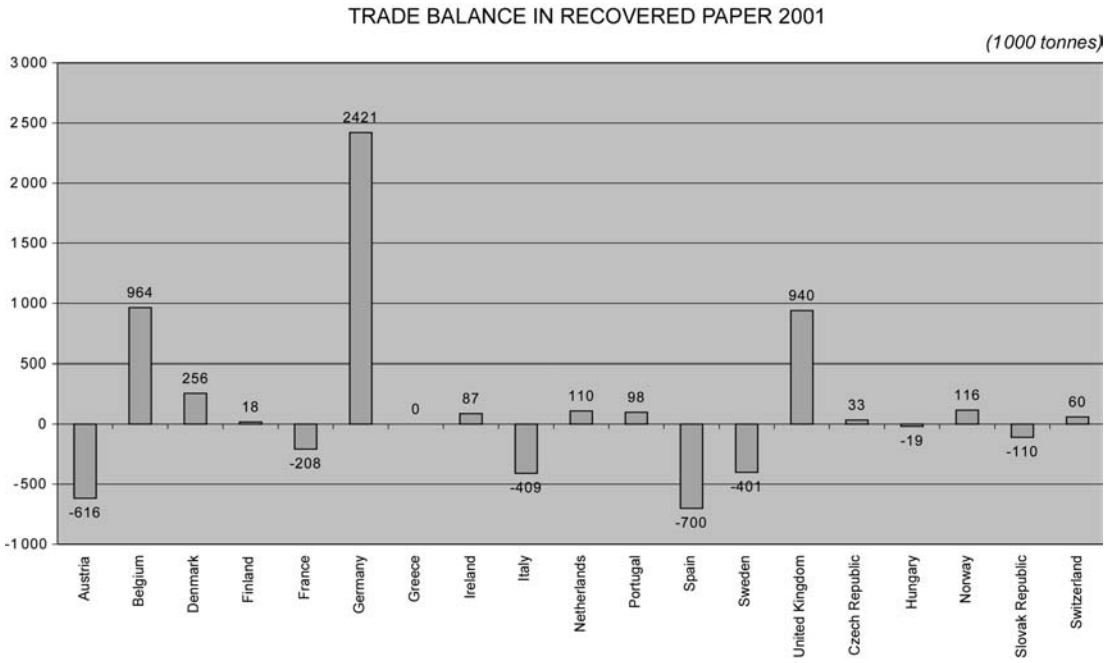
Effect on trade

(106) Paper producers A and B showed very clearly that there are significant cross-border trade flows of recovered paper, and provided the necessary figures to support this argument. In fact, a huge amount of the United Kingdom paper consumption is imported, mainly from other Member States. Producer A showed that there would be a direct effect on trade between Member States, not only in the newsprint market, but also on markets upstream and downstream to newsprint.

(107) In contrast, Shotton and the United Kingdom argued that the planned aid measure would have no effect on trade between Member States. Shotton is operating on the local market of the United Kingdom for the purchase of raw materials, as well as partly for sales of newsprint. The United Kingdom and Shotton also added that the UK exports of waste newsprint and magazines originate from the south of the United Kingdom, outside Shotton's catchment area.

(108) As illustrated in the chart below, waste paper is an internationally traded product. The statistics from the Confederation of the European Paper Industry (CEPI) and provided by producer B have demonstrated that there is cross-border trade in finished newsprint and in waste paper ([22]).

([22]) http://www.cepi.org/files/Recycling.stats2002-153648A.pdf — The Confederation of European Paper Industries (CEPI) is a non-profit-making organisation, representing 19 member countries (13 European Union Member States plus Norway and Switzerland with four Associate Members (Hungary, the Czech and Slovak Republics and Poland) and through its member countries, some 1 000 pulp, paper and board-producing companies across Europe, from small and medium-sized enterprises to multinationals.



(109) Therefore, the Commission considers that the planned measure is capable of affecting inter State trade.

(110) According to the Commission and to settled case-law, no 'actual' effect on trade is required. In order to assess whether the measure does affect inter State trade, it is sufficient to prove that the measure is 'capable' of affecting inter State trade ([23]). It is not necessary to show that the beneficiary undertaking itself engages in cross-border activity. When aid is granted, this may maintain or increase domestic production of a product thus reducing the opportunities for undertakings established in other Member States to export to the market of that Member State ([24]).

(111) On the basis of the assessment above, the Commission concludes that the measure is to be regarded as State aid as referred to in Article 87(1) of the Treaty.

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

(112) The Commission has assessed whether the exemptions set out in Article 87(2) and (3) of the Treaty apply. The exemptions in Article 87(2) of the Treaty could serve as a basis to consider aid compatible with the common market. However, the aid, (a) does not have a social character and is not granted to individual consumers, (b) does not make good the damages caused by natural disasters or exceptional occurrences and (c) is not required in order to compensate for the economic disadvantages caused by the division of Germany.

(113) The exemptions in Article 87(3)(a), (b) and (d) of the Treaty which refer to promotion of the economic development of areas where the standard of living is abnormally low, or where there is serious underemployment, to projects of common European interest and to the promotion of culture and conservation, do not apply.

(114) The United Kingdom has not attempted to justify the aid on the grounds enumerated in the foregoing paragraph.

(115) As far as the first part of the exemption in Article 87(3)(c) of the Treaty is concerned, namely aid to facilitate the development of certain economic activities, the Commission notes that the aid did not have purposes such as research and development, or investment by small and medium-sized enterprises. It also seems unlikely that the aid had the purpose to

([23]) Case C-387/92 *Banco Exterior de Espana* v *Ayuntamiento de Valencia* [1994] ECR I-877, paragraph 15.

([24]) Case T-55/99 *CETM* v *Commission* [2000] ECR II-3207, paragraph 86.

rescue and restructure Shotton. Therefore the aid can not be found compatible with the common market on this ground.

(116) It is therefore necessary to examine whether the aid qualifies for an exemption under Article 87(3)(c) of the Treaty on any other grounds, in particular, whether the environmental aid guidelines and the regional aid guidelines apply to this case.

6.2.1. *Assessment under the environmental aid guidelines*

6.2.1.1. Applicability of the environmental aid guidelines

(117) It is difficult to deny that there are environmental benefits: the reuse of waste paper is more environmentally-friendly than putting it into landfill.

(118) According to point 29 of the environmental aid guidelines, investment aid may be granted 'to enable firms to improve on Community standards applicable, or when the firms undertake investment in the absence of Community standards applicable […]'.

(119) The aid is granted to Shotton to improve the United Kingdom's environment in general and to help the United Kingdom to achieve its obligations under the landfill Directive ([25]) and under the packaging Directive ([26]). It is not granted to improve on the standards applicable to the firm directly. The first situation referred to in point 29 of the environmental aid guidelines, which allows aid to be granted in order to enable firms to improve on Community standards applicable therefore does not apply in this case.

(120) The second situation referred to in point 29 of the environmental aid guidelines concerns aid for firms to undertake investments in the absence of Community standards applicable. The United Kingdom argued that there were no standards applicable to the firm, but to the Member State, and that investment aid under the environmental guidelines could therefore be allowed.

([25]) Council directive 1999/31/EC. See footnote 11.

([26]) Directive 94/62/EC of the European Parliament and Council of 20 December 1994 on packaging and packaging waste (OJ L 365, 31.12.1994, p. 10).

(121) According to the general principles of law, an exception should be interpreted in a restrictive manner. The guidelines define the conditions under which the Commission may consider that aid is compatible with the common market in accordance with Article 87(3)(c) of the Treaty, and therefore form an exception to the general principles laid down in Article 87(1) of the Treaty. It should also be recalled that the environmental aid guidelines are based on the general principle of 'the polluter pays', and that every interpretation of the guidelines should strictly comply with this underlying principle.

(122) Therefore, this case, which concerns State aid intended to promote recycling and which relieves polluters from charges they should normally bear, does not qualify for an application of the second part of point 29. It must be noted that the aid is not intended to reduce the quantity of waste paper that results from Shotton's sales. It rather encourages Shotton to take up waste paper that may originate from products sold by any paper producer. The Commission considers that point 29 of the environmental aid guidelines concerns cases where an undertaking invests to improve its own environmental record and to reduce its own pollution. In such cases, aid can be allowed as an incentive to improve the environmental situation of the company. Otherwise, the rules could be easily circumvented by granting aid not to the polluters, but to the companies taking care of the pollution.

(123) This interpretation is confirmed by point 18(b) of the environmental aid guidelines, which states that aid 'may act as an incentive to firms to improve on standards or to undertake further investment designed to reduce pollution from their plants'.

(124) Furthermore, the interpretation suggested by the UK authorities might result in Member States subsidising large investments, with high intensities, in all those sectors where use of secondary raw materials is possible. Such aid could be granted in non-assisted areas or, in any event, without having to comply with regional aid rules and might have serious consequences on the relevant markets.

(125) In addition, in this case, the incentive effect of the aid is not clear. The Commission considers that the aid lacks

the required incentive effect, as it concerns an investment which is the current state-of-the-art. That view is confirmed by comments from paper producers A and B. The use of recovered paper for the production of newsprint is common practice, and the necessity of the measure is doubtful ([27]).

(126) The Commission observed, furthermore, when visiting the Shotton plant, that the whole investment project, with the exception of the sludge combustor, had already started and was well-advanced. This confirmed the Commission's opinion that the aid lacked any incentive effect, as required by the environmental aid guidelines.

(127) The Commission considers that no other provisions of the environmental aid guidelines apply to this case. Operating aid to promote waste management may be authorised if it is shown to be absolutely necessary under the conditions specified in points 42 to 46 of the guidelines. However, the measure in question, which constitutes investment aid, does not fulfil those conditions.

(128) The Commission concludes in this case that the environmental guidelines are not applicable to the investment as a whole insofar as it concerns the recycling of waste paper.

(129) However, the environmental guidelines might be applicable to some parts of the investment, which are not related to the recycling of waste paper, but aim at the reduction of Shotton's own pollution.

(130) According to the information submitted by the United Kingdom, the investment cost relating to the treatment of the pollution containing sludge coming from de-inking of waste paper is eligible for environmental aid. The conversion to the use of 100 % recycled fibre as a raw material implies an increase in the quantity of sludge produced per year from […] to 200 000 tonnes. In this respect, Shotton has changed its initial project, and will build a totally new type of sludge combustor. This combustor will function on the basis of sludge, low-grade forest residues and pretreated household waste, instead of non-renewable gas as was first foreseen ([28]). The combustor will produce steam and electricity for the plant's energy needs. The building of the sludge combustor has not yet started, which means that the aid will have a clear incentive effect in this case.

(131) The combustion of the sludge is not necessary for the production process, since Shotton could otherwise use 62 500 tonnes of sludge for the production of steam in the existing combustor, use 10 000 tonnes for animal bedding and spread the remainder, 127 500 tonnes, on agricultural land. This option would be fully in accordance with the relevant legislation ([29]). The combustor will not use natural gas but renewable sources, namely forest residues (which are not currently being used for anything else) and pretreated household waste (from which the recyclable elements have already been removed). Furthermore, if landspreading would become more costly, it is possible that part of the sludge may actually end up in landfill. Taking into account in particular the large quantities of sludge produced, the little nutritional value of the sludge in case of landspreading ([30]) and the very high cadmium:phosphorus ratio ([31]), recovery of the calorific value through combustion is preferable from the environmental point of view ([32]). This is confirmed by an analysis carried out by the Environmental Agency for England and Wales, based on the Integrated Pollution Prevention and Control regulatory system which itself is based on the Best Available Technique reference document (BREF) produced by the European Commission ([33]).

(132) The Commission concludes therefore that point 29 of the environmental aid guidelines applies to the sludge combustor investment.

([27]) According to the president of the British Recovered Paper Association, Ron Humphries, 'recovered paper exports will have to grow if the UK is to cope with increased levels of the material' (see website http://www.letsrecycle.com/paper/news.jsp?story= 2142).

([28]) The use of pretreated household waste implies that the investment falls within the scope of Directive 2000/76/EC of the European Parliament and of the Council of 4.12.2000 on the incineration of waste (OJ L 332, 28.12.2000, p. 91).

([29]) UK Waste Management Licensing Regulation 1994, S.I. Nr. 1056.

([30]) The nitrogen content is estimated at 3 920 mg/kg, the phosphorus at 228,2 mg/kg.

([31]) The concentration of cadmium is estimated at 1,54 mg/kg, thus the cadium: phosphorus ratio is more than 100 times higher than the corresponding average ratio for urban sewage sludge produced in the UK.

([32]) The combustion process allows the hazardous substances in the sludge, such as cadmium (1,54 mg/kg), mercury (0,7 mg/kg) and lead (12,3 mg/kg) to be separated and treated in accordance with the Community provisions on waste. Without combustion, most of these substances would end up spread on land without a clear agronomic benefit.

([33]) IPPC reference document on Best Available Techniques in the pulp and paper industry, European Commission, see website http://eippcb.jrb.es.

6.2.1.2. Application of the environmental aid guidelines to the item 'sludge combustor'

(133) According to point 29 of the environmental aid guidelines, investment aid may be authorised up to not more than 30 % of the eligible investment costs. As Shotton is situated in a region eligible for regional aid under Article 87(3)(c) of the Treaty, a bonus of five percentage points can be added, on the basis of point 34(a) of the environmental aid guidelines.

(134) According to point 36 of the environmental aid guidelines, 'the investments concerned are investments in land which are strictly necessary in order to meet environmental objectives, investments in buildings, plant and equipment intended to reduce or eliminate pollution and nuisances, and investments to adapt production methods with a view to protecting the environment.'

(135) According to point 37 of the guidelines, the eligible costs must be confined strictly to the extra costs necessary to meet the environmental objectives. They must be calculated net of the benefits accruing from any increase in capacity, cost savings engendered during the first five years of the life of the investment and additional ancillary production during that five-year period.

(136) The Commission considers that the costs presented by the United Kingdom concerning the sludge combustor are indeed investment costs, and not operating costs, as they concern investments in equipment.

(137) The cost for building a totally new sludge combustor is higher than was foreseen in the notification, GBP 42,50 million instead of GBP 26,2 million. As explained above, with the conversion to the use of 100 % recycled fibre, nearly twice as much sludge will be produced by the newsprint plant, i.e. around 200 000 tonnes/year in total. The original sludge combustor notified would have had a capacity of around 200 000 tonnes/year, and was estimated to cost around GBP 26,2 million. But, since the original notification, Shotton has had an opportunity to consider whether the environmental benefits can be further enhanced by replacing non-renewable gas as a fuel within the sludge combustor with a fuel consisting of renewable low-grade forest residues and pretreated household waste. As sludge derived from recycled fibre has a very much lower calorific value than sludge from virgin pulp and recycled pulp mix, in order to burn some 200 000 tonnes/year of sludge, a large quantity of solid fuel is required ([34]). As a result, the overall physical size of the sludge combustor and associated infrastructure will increase.

(138) As regards the new techniques used, Shotton commissioned a formal study on this topic. Several options were presented to Shotton, one of these being the replacement of natural gas as the primary fuel to combust the paper/de-ink sludge, by a combination of fuel from local forests and from the adjacent local community waste streams.

(139) The Commission notes that this modification by the United Kingdom authorities is consistent with the comments made by paper producer A, which indicated that the increase of de-inked pulp capacity would require more combustion and sludge dewatering capacity than already in place. The new sludge combustion and sludge dewatering equipment would most likely be built with capacity to handle the total sludge combustion and sludge dewatering need for the whole mill.

(140) The costs related to the sludge combustor are distributed as follows:

Category	Cost (GBP million)	Description
Sludge combustor	[…]	Equipment in which the combustion takes place.
Sludge handling/ storage	[…]	Contained storage of sludge to prevent contamination of fuel or run-off to groundwater and conveyor transport from storage combustor. This amount concerns only the cost that would not have been necessary if all sludge would have been spread on land and used for animal bedding, or if the existing combustor would continue to be used.
Biofuel/RDF ([35]) infrastructure	[…]	Pre-preparation of fuel to ensure homogenous quality and ease of transport.

([34]) About 150 K tonnes/year of forest residues and around 175 K tonnes/year of pretreated household waste.

([35]) Refuse derived fuel.

Category	Cost (GBP million)	Description
Ash handling	[…]	Ash storage and conditioning to enable dust free loading and transport of ash.
Site preparation	[…]	Investigation of ground conditions and subsequent preparation of the site to accommodate the construction of the combustor.
Sludge dewatering	[…]	Increasing sludge dryness to increase calorific value prior to combustion. In case of landspreading such dewatering is not necessary.
Total	42,50	

(141) For calculating the eligible cost under point 29 of the environmental aid guidelines the Commission can take into account only the extra cost necessary for combustion of the sludge by the most economical means. The additional costs of the increased capacity for the incineration of pretreated household waste, where forest residues and sludge serve as additional fuel, are not strictly necessary for the combustion of the sludge. The Commission therefore, as a first step, assessed the eligible cost by comparing a hypothetical, most economical, sludge combustor that deals only with sludge combustion to the situation where the existing combustor would continue to be used for steam production, where a small part of the sludge would be used for animal bedding and where the remainder would be spread on land. The hypothetical combustor can be assumed to correspond to a gas-fuelled combustor as was originally foreseen, with an investment cost of GBP 26,2 million.

(142) In accordance with point 37 of the environmental aid guidelines, the eligible cost has to be calculated net of the benefits accruing from any increase in capacity, cost savings engendered during the first five years of the life of the investment and additional ancillary production during that five-year period. In this first step of the assessment, the 'five-year benefits' concern the following:

(a) landspreading of sludge is no longer necessary, and there will be no more costs related to the use of sludge for animal bedding. The cost of animal bedding amounts to GBP […] per tonne. The cost of landspreading is estimated at GBP […] per tonne. The avoided cost for 10 000 tonnes of animal bedding and 127 500 tonnes of landspreading per year amounts to GBP […] per year. For five years, taking the net present value in the first year ([36]), this amounts to GBP […];

(b) the combustor as originally foreseen would have supplied 45 kg steam per second, whereas the existing combustor would produce only 27 kg steam per second. So, in case the existing combustor would continue to be used, Shotton would have buy an additional of 18 kg steam per second from third parties at a price of GBP […] per tonne. Consequently, the annual benefit amounts to GBP […]. For five years, discounted to the first year, this amounts to GBP […];

(c) the combustor as originally foreseen would have to be fuelled by natural gas. Combustion of 200 000 tonnes of sludge would have required […] British thermal units (BTU)/h of natural gas at a price of GBP […] per BTU. The annual cost would amount to GBP […]. For five years, discounted to the first year, this would amount to GBP […]. Since the calculation should be based on net benefits, this item must be deducted from the five year benefits;

(d) the existing combustor would have to be fuelled by 35 000 tonnes of bark per year. Because of the shift away from the use of virgin fibre, Shotton would have to buy the bark from third parties. The cost per tonne is estimated at […]. The annual cost would amount to GBP […]. For five years, discounted to the first year, this would amount to GBP […].

(143) Based on these assumptions, the Commission calculated therefore, as a first step, the maximum aid allowable under point 29 of the environmental aid guidelines applied to the sludge combustor in the following manner: 35 % (GBP 26,2 million — […] — […] + […] — […]) = GBP 9 305 000.

([36]) The reference rate for the UK at the moment of the assessment is 5,42 %.

(144) As a second step, the Commission calculated the eligible cost when comparing the sludge combuster as foreseen presently to the situation where the existing combustor would continue to be used. This involves a much higher investment cost of GBP 42,5 million. It involves as well the following costs and benefits over 5 years:

(a) landspreading of sludge is no longer necessary and there will no more be costs related to the use of sludge for animal bedding;

(b) Shotton will receive a 'gate fee' for the use of refuse derived fuel (pretreated household waste);

(c) the combustor supplies electricity which otherwise would have to be bought from third parties or produced by own installations;

(d) the combustor supplies more steam than the existing combustor. This additional quantity otherwise would have to be bought from third parties or produced by own installations;

(e) Shotton is expected to benefit from renewable obligation certificates due to the use of 'green energy';

(f) the existing, old combustor would have to be fuelled by bark. This is not directly available anymore, since the plant switches from virgin fibre to waste paper as a raw material. Therefore, this bark would have to be acquired from third parties;

(g) the disposal of the toxic ashes implies an additional cost;

(h) the new combustor is fuelled by forest residues which implies an additional cost.

The table below provides a detailed calculation of the five-year benefits.

	Unit/tonnes per annum	Proceeds or cost GBP/tonne or unit	Benefit (cost) per annum (GBP)
Avoided cost of landspreading of sludge	127 500	[…]	[…]
Avoided cost of animal bedding	10 000	[…]	[…]
Benefit of refuse derived fuel	[…]	[…] ([37])	[…]
Benefit of electricity	[…]	[…]	[…]
Net benefit of additional steam	[…]	[…]	[…]
Benefit of renewable obligation certificates	[…]	[…]	[…]
Avoided cost of bark	35 000	[…]	[…]
Cost of ash disposal	[…]	[…]	[…]
Cost of forest residues	[…]	[…]	[…]
Total net derived benefit per annum			3 256 327
Total net derived benefit for five years ([38])			14 686 035

(145) Based on these facts, the Commission calculated therefore, as a second step, the maximum aid allowable under point 29 of the environmental aid guidelines applied to the sludge combustor in the following manner: 35 % × (GBP 42,5 million — GBP 14 686 035) = GBP 9 735 000.

(146) The Commission notes that combustion of forest residues and urban waste has no link with the newsprint production process and that, therefore, only sludge combustion provides a benefit for the environment that can be taken into account for the purposes of the environmental guidelines. When an environmental benefit can be obtained in different ways, aid can be granted only for the option that involves

([37]) The 'gate fee' Shotton may expect for taking up refuse derived fuel is relatively uncertain because of the innovative character. However, based on actual information from Shotton, as confirmed by the UK authorities, this 'gate fee' will in all likelihood be well below GBP [...] per tonne. One estimate arrives even at a value as low as [...] per tonne.

([38]) Net present value at the first year.

lowest eligible cost. In this case, it is clear from the above that the combustor as originally foreseen, combusting only the sludge and fuelled by gas, constitutes the option that involves lowest eligible cost. The Commission consequently concludes that the maximum amount of aid allowable under the environmental aid guidelines is GBP 9 305 000.

(147) The gate fee Shotton expects to receive for the pretreated household waste will in all likelihood be below GBP […] per tonne. However, the Commission must take into account the uncertainty to this figure due to the innovative character of the treatment process, the unknown developments in the landfill tax and other factors that influence this price. If in reality it turns out to be higher ([39]), Shotton would obtain more benefits that should be deducted from the investment cost. If the gate fee would increase beyond GBP […] on the average over the five year period, the minimum eligible cost would be the one calculated on the basis of the new combustor. Therefore the aid amount, as approved in this decision, would be too high, since the proper calculation should have been based on the cost of the new combustor and not the hypothetical one as foreseen above. For this reason the Commission can approve the aid only under the condition, should the gate fee for pretreated household waste turn out to be higher than GBP […] per tonne, the UK authorities have to calculate the proper aid amount again and have to ensure that the aid does not surpass the level of 35 % of the eligible cost as calculated in the second step described above, taking into account the actual figure for the gate fee. Shotton has given a written undertaking that it will provide the necessary information to WRAP and repay with interest to the UK authorities any aid paid in excess if this situation occurs.

6.2.2. *Applicability of the regional aid guidelines*

(148) Point 4(1) of the regional aid guidelines provides that aid can be granted for a productive investment (initial investment) or job creation which is linked to the investment.

(149) Producers A and B argued that the regional aid guidelines do not apply, as the investment does not aim to create or to maintain working places. It does not seem to have any positive effects for the development of the region. Furthermore, on basis of the costs presented, the planned aid for Shotton should not be qualified as investment aid, but as operating aid, as it concerns the mere replacement and updating of old facilities.

(150) The investment project in this case aims at introducing a completely new production process for pulp to be used as raw material. According to point 4(4) of the regional aid guidelines, an initial investment could be 'the extension of an existing establishment, or the starting up of an activity involving a fundamental change in the product or production process of an existing establishment (through rationalisation, diversification or modernisation)'. Therefore, the Commission considers that the investment is eligible for aid under the regional aid guidelines. However, since the eligible costs related to the combustor, including additional costs linked to the combustion of forestry residues and urban waste, have already been taken into account under the environmental guidelines and, as the following calculations will show, they benefit from a higher aid intensity under these guidelines, they cannot qualify for further aid under the regional aid guidelines.

(151) As regards the incentive effect of the aid, point 4(2) of the regional aid guidelines requires that the application for aid must be submitted before the work is started on the projects. It appears from the information submitted by the United Kingdom that Shotton did not start the works before being appointed as preferred bidder following the tender procedure. Therefore, the Commission takes the view that the aid at stake has an incentive effect as required under the regional aid guidelines.

(152) Under the multisectoral framework on regional aid for large investment projects ([40]) (hereafter 'multisectoral framework'), point 2(1)(i), projects are notifiable when the total project cost is at least EUR 50 million, and the cumulative aid intensity expressed as a percentage of the eligible investment costs is at least 50 % of the regional aid ceiling for large companies in the area concerned and aid per job created or safeguarded amounts to at least EUR 40 000. In this case the total project cost

([39]) In real terms, i.e. taking into account general inflation.

([40]) See footnote 9.

amounts to GBP 125,21 million (EUR 175 million), the cumulative aid intensity is 18 % whereas the regional aid ceiling is 15 % and the aid per job is around GBP 5,75 million. Hence, the aid is notifiable under the multisectoral framework.

(153) Following the Commission's request, the United Kingdom provided information in order to allow the Commission to assess the case under the multisectoral framework.

(154) The United Kingdom first of all presented a new breakdown of the costs:

(in GBP)

Rebuild of recycled fibre mill line 1	[…]
RCF 3 new build	[…]
Paper machine (PM) 1 conversion	[…]
PM 2 conversion	[…]
PM 2 finishing	[…]
Contingencies	[…]
RCF warehouse	[…]
Power distribution	[…]
PM 1 white water	[…]
Land and site works	[…]
Package boiler	[…]
PM 1 modifications	[…]
PM 2 modifications	[…]
Mill infrastructure improvements	[…]
Effluent treatment improvements	[…]
Mill site safety and efficiency investments	[…]
RCF local authority initiatives	[…]
Commissioning costs	[…]
Sludge treatment and related investment ([41])	42 500 000
Total	125 210 000

([41]) See point 6(2) for a detailed breakdown of the costs related to the sludge treatment.

(155) Compared to the initial costs presented in the notification, the United Kingdom was able to reduce the overall amount of the costs for several reasons, such as the strong purchasing power of UPM-Kymmene, the current depressed state of the European market for the manufacture of manufacturing equipment, and greater knowledge of the advancing recycling technology.

(156) The Commission notes that the reduction in the costs is consistent with the comments made by paper producer B, which stated that the costs presented in the original notification were inflated. Paper producer B added that it had been able to carry out a similar investment with less costs.

(157) However, the Commission does not consider that all the costs presented by the United Kingdom are eligible for regional aid. Point 4(5) of the regional aid guidelines states that eligible costs consist in land, buildings, or plant/machinery. According to point 4(6), eligible expenditure may also include certain categories of intangible investment up to a limit of 25 % of the standard base in the case of large firms.

(158) On the basis of the foregoing, the Commission takes the view that the 'local authority initiatives', involving the education of people to favour recycling at a cost of GBP 2 100 000, cannot be considered as intangible investment and therefore is not eligible for regional aid.

(159) Therefore, the total eligible costs amount to GBP 123 110 000.

6.2.3. *Multisectoral framework assessment*

(160) Under the multisectoral framework, the Commission, in order to determine the maximum allowable aid intensity for a proposal to award aid, has to identify the maximum aid intensity (regional aid ceiling) which a company could obtain in the assisted area concerned within the context of the authorised regional aid system applicable at the moment of the notification.

(161) Taking into account that Shotton has to be considered a large undertaking, the maximum allowable aid intensity (R) in this case is 15 % gross.

(162) A range of adjustment factors then have to be applied to the percentage figure of 15 %, in accordance with three specific assessment factors, in order to calculate a maximum allowable aid intensity for the project in question. Those three factors are the competition factor (T), the capital-labour factor (I) and the regional impact factor (M).

6.2.3.1. The relevant market and its evolution

(163) The market concerned by the investment is the production of newsprint.

(164) According to the multisectoral framework, the relevant geographic market comprises usually the EEA or, alternatively, any significant part of it if the conditions of competition in that area can be sufficiently distinguished from other areas in the EEA.

(165) Based on the statistics available from CEPI (see recital 108), the Commission considers that the relevant geographic market is the EEA. Furthermore, the United Kingdom did not provide any information indicating that the relevant geographic market would be different from the EEA. The relevant geographic market is therefore considered to be the EEA.

(166) In 2001, UPM-Kymmene's share of newsprint sales within the EEA was 10,5 %, of which Shotton contributed 4,8 %. The United Kingdom submitted data from Amec Consultancy forecasting that the annual growth of EEA newsprint consumption is expected to be 1,6 % during the five-year period 2002 to 2007.

6.2.3.2. The competition factor (T)

(167) The authorisation of aid to companies operating in sectors which are in structural overcapacity poses particular risks for the distortion of competition. Any capacity expansion, which is not compensated by capacity reductions elsewhere, will exacerbate the problem of structural overcapacity. The sector or subsector will be established at the lowest available segmentation of the NACE classification.

(168) As newsprint represents only a small share in the relevant NACE code (21.12 'Manufacture of paper and cardboard'), the Commission based its assessment on the apparent consumption in the EEA for the period 1996 to 2001, pursuant to point 3(4) of the multisectoral framework. That point states that, in the absence of sufficient data on capacity utilisation, the Commission will consider whether the investment takes place in a declining market. A market is deemed to be declining if, over the last five years, the average annual growth rate of apparent consumption of the product is more than 10 % below the annual average of EEA manufacturing industry as a whole, unless there is a strong upward trend in the relative growth rate of demand for the product. The market is deemed to be absolutely declining if the average annual growth rate of apparent consumption over the last five years is negative.

(169) The United Kingdom submitted the following data concerning the apparent consumption of newsprint in the EEA for the period 1996 to 2001 ([42]):

(EUR million)

	Total value
1996	5 070
1997	4 060
1998	4 615
1999	4 771
2000	4 905
2001	5 611

(170) Those figures show an average annual growth of 2,05 %. The average annual growth rate of the manufacturing industry as a whole in the same period was 5,23 %.

(171) On the basis of the data on annual consumption set out above, the sector concerned can be considered to be in relative decline, as the average annual growth of newsprint is more than 10 % below the annual average of EEA manufacturing industry as a whole, and as there is no strong upward trend in the product.

(172) The United Kingdom argued that the competition factor should be set at 1, due to the fact that there was no capacity increase as a result of the investment. However, the fact that the equipment will be completely modernised, and that the plant will be able to run at higher speed in the future means that the Commission cannot conclude that there is no risk of distortion of

([42]) Sources: Cepiprint and Pulp and Paper International.

competition. Furthermore, the fact that Shotton will have a plant with a longer economic life than the current one and, due to the subsidies, with production costs lower than those of its competitors using similar technology but not benefiting from aid, may lead to distortion of competition.

(173) Hence, the Commission concludes that the competition factor should be set at 0,75.

6.2.3.3. The capital-labour factor (I)

(174) The multisectoral framework lays down a capital-labour factor which aims at adjusting the maximum intensity with a view to favouring those projects that effectively and better contribute to the reduction of unemployment through the creation of a relatively more important number of new jobs respectively safeguarded jobs. This criterion also takes into account possible distorting effects of the aid on the price of the final product.

(175) According to the United Kingdom, the project creates four jobs. Two of those jobs relate principally to encouraging recycling and facilitating the procurement of waste newspapers and magazines in the local communities. The other two jobs will be created in the recycled fibre warehouse.

(176) Investment costs amount to GBP 125,21 million (EUR 177,56 million) ([43]). The adjustment factor for an investment of EUR 177,57 million, which results in the creation of four jobs, is the one corresponding to the ratio of EUR 44,39 million/job, and should hence be set at 0,6.

6.2.3.4. The regional impact factor (M)

(177) The regional impact factor takes into account the beneficial effects of a new aided investment on the economies of the assisted regions. The Commission considers that job creation can be used as an indicator of a project's contribution to the development of a region. A capital intensive investment may create a significant number of indirect jobs in the assisted region concerned and any adjacent assisted region. Job creation in this context refers to jobs created directly by the project together with jobs created by first-tier suppliers and customers in response to the aided investment.

([43]) Exchange rate on 18 July 2003.

(178) The UK authorities estimated that 187 jobs would be created in the adjacent NUTS III level assisted areas of St Helens, Merseyside, Wigan and Wirral. These jobs will be generated as a result of Shotton's commitment to purchase a further 321 000 tonnes of waste newspaper and magazines newly recovered from the domestic waste stream. The United Kingdom provided a list of the suppliers.

(179) The agreements between Shotton and the current wood suppliers will not be breached due to the switch to the use of waste paper instead of wood, but will continue for at least five years. The project will therefore not directly result in job losses in those companies.

(180) Based on these figures, the Commission considers that there is a high degree of indirect job creation, and therefore, the regional impact factor is set at 1,2.

6.2.3.5. *Ex post* monitoring

(181) The United Kingdom undertook to insert the following conditions in the contract between WRAP and Shotton, in order to comply with the requirement of point 6(4) of the multisectoral framework: first of all, a provision was inserted requiring reimbursement if Shotton failed to comply with the decision granting the aid, and secondly, the final 25 % will be paid only when Shotton has satisfied WRAP that the execution of the project is in compliance with the Commission' s decision.

(182) The United Kingdom also undertook to submit a copy of the contract to the Commission, as well as an annual report on the project.

6.2.3.6. Conclusion

(183) In view of the foregoing, the maximum allowable aid intensity (R × T × I × M) should be calculated as follows: 15 % × 0,6 × 0,75 × 1,2 = 8,1 %. Therefore, the maximum amount which the United Kingdom is allowed to grant to Shotton under the multisectoral framework is 8,1 % × GBP 123 110 000 = GBP 9 972 000.

6.3. **Cumulation of the different types of aid**

(184) Point 74 of the guidelines provides that 'aid authorised under the guidelines may not be combined with other forms of State aid […] if such overlapping produces an aid intensity higher than that laid down in the guidelines. In the case of aid serving different purposes, and involving the same eligible costs, the most favourable aid ceiling will apply'.

(185) In this case, the sludge combustor qualifies for an exemption under both the environmental guidelines, and the regional aid guidelines. Therefore, on the basis of point 74 of the environmental aid guidelines, the sludge combustor may benefit from the most favourable aid ceiling, which is achieved by the application of the environmental aid guidelines.

(186) This leads to the following calculation:

Calculation	Explanation
8,1 % × (GBP 123 110 000 — GBP 26 200 000) = GBP 7 850 000	Application of the maximum intensity calculated on basis of the multisectoral framework to the whole project minus the sludge combustor, which is entitled to benefit from a higher intensity under the environmental aid guidelines.
35 % × (GBP 26 200 000 — […] — […] + […] — […]) = GBP 9 305 000	Application of the maximum intensity under point 29 of the environmental aid guidelines to the sludge combustor, after deduction of the five year benefits.
TOTAL: GBP 7 850 000 + GBP 9 305 000 = GBP 17 155 000	Application of point 74 of the environmental aid guidelines.

6.4. **Direct application of Article 87(3)(c) of the Treaty**

(187) It follows from the foregoing that neither under the environmental aid guidelines, nor under the regional aid guidelines not all of the notified aid of GBP 23 million can be approved. The Commission has assessed whether the aid could be exempted directly under Article 87(3)(c) of the Treaty. In order to assess this, the Commission has to consider whether the aid is proportionate and necessary for the achievement of the benefits sought, and does not lead to an undue distortion of competition.

(188) As regards the criterion of proportionality, the financing of a whole state-of-the-art recycling plant seems disproportionate to achieve the amount of waste recycling targeted. In particular, the conditions of the tender were not directly targeted to the diversion of waste from landfills, but to the production of newsprint made out of waste paper. It has been sufficiently demonstrated by paper producers A and B that the production of newsprint from waste paper is a state-of-the-art technique, to which most of the newsprint producers have switched or will switch at some time in the future.

(189) Therefore, the Commission considers that the aid does not seem proportionate to achieve the amount of waste recycling targeted.

(190) As regards the criterion of necessity, aid represents only a 'temporary second best solution' ([44]), and should only be applied when it is not possible for all costs to be internalised by firms. In most Member States, the collection of waste paper is well-organised, due partly to the landfill taxes in those countries and to the obligation on municipalities to collect paper separately. There is no real necessity to subsidise the production of newsprint by securing end-markets. Therefore, the Commission considers that the aid in question is not necessary to achieve the environmental targets set by the United Kingdom. Furthermore, the obligation on Shotton to use a certain amount of waste paper will last only for five years.

(191) Finally, the Commission examined whether the aid would not lead to an undue distortion of competition. It is concluded that such a high amount of aid, granted to one single undertaking, which is a major player in the market of newsprint, will cause an undue distortion of competition. It has been clearly emphasised by paper producers A and B that waste paper is a common traded raw material and a scarce resource.

(192) It is therefore concluded that the notified project cannot be exempted directly under Article 87(3)(c) of the Treaty.

([44]) Paragraph 18(a) of the environmental aid guidelines.

7. **CONCLUSION**

(193) It is concluded that GBP 17 155 000 out of the GBP 23 million which the United Kingdom intends to grant to Shotton is compatible with the common market. The remaining GBP 5 845 000 is incompatible with the common market.

(194) The Commission must be sure of the proper implementation of the project for which the aid is granted. Therefore, it requests the United Kingdom to submit an annual report on the implementation of the investment project for the period up to and including the first five years of operation. This report should describe the general progress of the investment and comment in particular on the actual costs and benefits derived from the construction and operation of the combustor, including costs and fees relating to other waste burned in the same installation.

HAS ADOPTED THIS DECISION:

Article 1

1. The State aid which the United Kingdom is planning to implement for UPM Kymmene-Shotton, amounting to GBP 23 million, is compatible with the common market, up to a maximum amount of GBP 17 155 000.

If during the first five years of operation of the new combustor the gate fee for pre-treated household waste is higher than GBP […] per tonne on average, so that the eligible costs of the actual combustor are lower than those taken into account in this decision, the United Kingdom shall reduce the aid amount in such a way that the aid level does not surpass 35 % of eligible costs as calculated on the basis of a comparison between the investment in the new combustor and the continued use of the existing combustor, using the actual gate fee for the calculation of the benefits derived from this investment over five years. Any aid paid in excess of the reduced aid amount shall be recovered with interest.

2. The remainder of the aid referred to in the first paragraph of paragraph 1, amounting to GBP 5 845 000 is incompatible with the common market.

That part of the aid may accordingly not be implemented.

Article 2

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

Article 3

The United Kingdom shall submit an annual report on the implementation of the investment project for the period up to and including the first five years of operation of the sludge combustor.

Article 4

This Decision is addressed to the United Kingdom.

Done at Brussels, 23 July 2003.

For the Commission

Mario MONTI

Member of the Commission