II

(Acts adopted under the EC Treaty/Euratom Treaty whose publication is not obligatory)

DECISIONS

COMMISSION

COMMISSION DECISION

of 11 December 2007

on State aid C 32/07 (ex N 389/06) temporary Defensive Mechanism to Shipbuilding — Portugal

(notified under document number C(2007) 6063)

(Only the Portuguese version is authentic)

(Text with EEA relevance)

(2008/315/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 those provisions [1] and having regard to their comments,

Whereas:

I. PROCEDURE

(1) Portugal notified the measure on 20 June 2006. The Commission, by letter dated 6 July 2006, requested additional information from Portugal and proposed to extend the period within which the Commission would take a Decision on the notified measure, in conformity with Article 4(5) of Regulation (EC) No 659/1999 [2], until such time as the Commission would reach a Decision on a previous similar notification by Portugal that was under assessment [3]. Portugal, by letter dated 25 July 2006, accepted this proposal.

(2) The Commission, by letter dated 11 May 2007, resumed the assessment of the notification and reminded Portugal that the notification was incomplete. Portugal provided additional information by letters dated 5 July 2007 and 26 July 2007.

(3) By letter dated 10 August 2007, the Commission informed Portugal that it had decided to initiate the procedure laid down in Article 88(2) of the EC Treaty in respect of the aid.

(4) By letter dated 17 September 2007 the Portuguese authorities presented their comments in the context of the above-mentioned procedure.

(5) The Commission Decision to initiate the procedure was published in the *Official Journal of the European Union* [4]. The Commission called on interested parties to submit their comments. There were no comments from third parties.

[1] OJ C 221, 21.9.2007, p. 8.

[2] Council Regulation (EC) No 659/1999 laying down detailed rules for the application of Article 93 of the EC Treaty, (OJ L 83, 27.3.1999, p. 1).

[3] Case C 26/2006 (ex N 110/2006) on which the Commission took a final negative decision on 24 April 2007 (OJ L 219, 24.8.2007, p. 25).

[4] See footnote 1 above.

II. DESCRIPTION OF THE AID MEASURE

(6) The beneficiary of the aid would be Estaleiros Navais de Viana do Castelo S.A. ('ENVC') a Portuguese shipyard employing about 1 000 people.

(7) Portugal proposes to grant ENVC direct aid amounting to EUR 6 575 558 in relation to seven shipbuilding contracts, signed between 4 February 2005 and 31 March 2005. The details concerning the contracts and the corresponding proposed aid are the following:

Multipurpose heavy lift vessel	Date of signature of the contract	Ship owner	Proposed State aid (EUR)
C 228	24.2.2005	JMS Schiffahrtsgesellschaft mbH & CO KG MS	1 212 766
C 229	24.2.2005	JMS Schiffahrtsgesellschaft mbH & CO KG MS	1 212 766
C 230	4.2.2005	MARE Schiffahrtsgesellschaft	1 212 766
C 231	4.2.2005	MARE Schiffahrtsgesellschaft	661 102
C 232	4.2.2005	MARE Schiffahrtsgesellschaft	630 328
C 233	4.2.2005	MARE Schiffahrtsgesellschaft	433 064
C 210	31.3.2005	Mutualista Açoreana	1 212 766

(8) According to the information supplied in the notification, the request for aid in relation to all seven contracts was submitted by the shipyard in July 2005, i.e. **after** the signature of the contracts. Portugal authorized the aid, on condition of approval by the Commission, by decision of the Ministry of Finance, Public Administration, Economy and Innovation of 7 August 2006.

(9) The vessels were delivered, or are expected to be delivered, at the following dates:

Vessel	Delivery date
C 228	30 September 2007
C 229	30 December 2007
C 230	28 July 2006
C 231	30 October 2006
C 232	3 January 2007
C 233	24 April 2007
C 210	10 July 2007

(10) Portugal proposes to grant the aid on the basis of Council Regulation (EC) No 1177/2002 concerning a temporary defensive mechanism to shipbuilding [5] as amended by Council Regulation (EC) No 502/2004 [6] (the 'TDM-regulation'). The TDM-regulation entered into force on 3 July 2002 and expired on 31 March 2005. This Regulation was, thus, no longer in force at the time when Portugal approved and notified the aid.

(11) Portugal argues that the contracts fall within the scope of application of the TDM-regulation because they were signed while this regulation was still in force.

III. GROUNDS FOR INITIATING THE FORMAL INVESTIGATION PROCEDURE

(12) The Commission, in its decision to initiate the formal investigation procedure in the present case, noted that it had doubts on the compatibility of the aid with the common market based on the TDM-regulation for the following reasons.

(13) First, the Commission had doubts regarding the incentive effect of the aid. The Commission noted that the application for aid was only submitted after the contracts had been signed. Also Portugal only approved the aid internally (on condition of approval by the Commission) more than a year after the application for aid was submitted. Portugal had not provided evidence that at the time ENVC signed the contracts there were any assurances that the shipyard would obtain the aid. The Commission, therefore, had doubts that ENVC was induced in any way by State aid to carry out the projects concerned.

[5] OJ L 172, 2.7.2002, p. 1.
[6] OJ L 81, 19.3.2004, p. 6.

(14) Second, the Commission questioned the legal basis for approving the aid. The Commission noted that the TDM-regulation expired on 31 March 2005 and was therefore no longer in force at the time Portugal approved and notified the aid. The Commission also noted that in its decision concerning Case C 26/2006 (ex N 110/2006) ([7]) it had explained in detail why it considers that the TDM-regulation can no longer be a valid legal basis for approving new operating aid to shipbuilding. Portugal, in the present case, had not submitted any new information that would modify the Commission's assessment in this respect and therefore the Commission could not consider at that stage that the aid was compatible with the common market.

IV. COMMENTS SUBMITTED BY PORTUGAL

(15) Portugal noted, in general terms, that for the contracts in question the yard was mainly competing with non-Community shipyards, notably with regard to unfair competition from Korean shipyards which was the subject of the TDM regulation. Further, the contracts did not affect or threatened to affect competition in the EU because all shipyards in the EU had equal access to aid under the TDM regulation that had direct application in all Member States. As a consequence, the notified measures could not be considered to affect trade between Member States.

(16) Regarding the incentive effect of the aid, Portugal argued that it was not materially possible for ENVC to submit a request for aid duly motivated, prior to signing the contracts, because of aspects linked to the negotiation. The contacts with the ship owners were initiated prior to ENVC requesting the aid. Also, Portugal sustains that, although ENVC signed the contracts without public assurances that it would receive the aid, the shipyard negotiated and signed the contracts and built the vessels on the expectation of both the Portuguese authorities and the Commission authorizing the aid, given that the objective conditions for receiving the aid were fulfilled in this case.

(17) Concerning the legal basis for approving the aid Portugal referred to its comments submitted in the context of Case C 26/2006 ([8]) that it considers applicable to the present case. Portugal noted that the contracts in question were signed during the period of application of the TDM regulation, i.e. before 31 March 2005 and before the WTO Dispute Settlement Body adopted the panel report condemning the TDM-regulation. Portugal also stated that it was not possible to notify the aid before the expiry of the TDM-regulation because the contracts were only signed in February and March 2005 (i.e. just before the expiry of the TDM-regulation). However, in Portugal's view this does not annul the validity of these contracts which fulfilled the objective conditions of the TDM-regulation at the time they were signed.

V. ASSESSMENT

Existence of aid

(18) According to Article 87(1) of the EC 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, in so far as it affects trade between Member States, be incompatible with the common market.

(19) The Commission considers that the proposed measures constitute State aid within the meaning of Article 87(1) of the EC Treaty. The measures take the form of a grant financed by State resources. Even if the TDM-regulation applied in all Member States, and all shipyards were eligible for aid under the TDM-regulation, as argued by Portugal, the measures are selective as in this case they are limited to ENVC. This selective grant is likely to distort competition, by providing ENVC with an advantage over other competitors not receiving the aid. In this respect, the fact that ENVC might be competing with shipyards in Korea does not detract from the fact that it was also competing with other shipyards in the common market. Finally, shipbuilding is an economic activity involving extensive trade between Member States and the measures are thus likely to affect trade between Member States.

(20) The Commission thus confirms that the notified aid measure falls within the scope of Article 87(1) of the EC Treaty.

Compatibility with the common market

The incentive effect

(21) As a general principle, State aid may only be considered compatible with the common market if it is necessary to induce the recipient firm to act in a manner which assists attainment of the objectives envisaged by the relevant derogation ([9]).

([7]) See footnote 3.
([8]) See footnote 3.
([9]) See judgment in Case 730/79 Philip Morris v Commission [1980] ECR 2671, paragraphs 16 and 17.

(22) The Commission notes in this respect that the objective of the TDM-regulation was to *'effectively enable Community shipyards to overcome unfair competition from Korea'* (see paragraph 6 of the preamble). Direct aid up to 6 % of contract value before aid could thus be authorized provided there had been competition for the same contract from a shipyard in Korea offering a lower price (Article 2).

(23) Portugal argues in this case that even if ENVC had no assurances of receiving the aid when it signed the contracts, it had expectations of receiving the aid because the contracts fulfilled the objective conditions to be eligible for aid under the TDM-regulation.

(24) However, the Commission considers that in this case there is not sufficient evidence that the aid was determinant for ENVC to sign the contracts.

(25) As already noted in the decision to initiate the investigation procedure, Portugal submitted copy of a letter from a ship owner stating that for six of the contracts in question (vessels C 228 to C 233) the ship owner had received lower offers from Korean shipyards. However, this letter is dated 9 March 2005, i.e., it was only sent to ENVC after the shipyard had already signed the contracts relating to these offers. Thus, it appears that the shipyard, when it signed the first six contracts, could not have had the certitude that the contracts fulfilled all the eligibility conditions. As regards the seventh contract (vessel C 210) the situation also appears doubtful, since the indication that lower offers were received from Korea was also only sent to ENVC on 31 March 2005, i.e. the very same day when ENVC signed the contract.

(26) Portugal has not submitted any evidence that, formally or informally, ENVC had received indication from the Portuguese authorities, prior to signing the contracts, that the aid could be granted in relation to these contracts ([10]). Rather, it would appear that ENVC was prepared to undertake these contracts even without guarantees of receiving aid. For example, Portugal in its submission following the initiation of the investigation procedure also stated that ENVC was legally bound to build the vessels even if the aid would not be authorized. It adds that in the present case, ENVC only applied for aid after the expiry of the TDM-regulation which appears to confirm that the shipyard was prepared to carry out the projects at the risk of not receiving aid.

(27) Also, generally, the Commission considers that the aid has an incentive effect if an application for aid was submitted before the start of the project ([11]). This was not the case here. The application for aid was only submitted after the contracts had been signed (i.e. in July 2005, whereas the contracts were signed in February and March 2005). Also, Portugal only approved the aid internally (on condition of approval by the Commission) more than a year after the request for aid was presented. So, also from a formal point of view, the incentive effect is not fulfilled

(28) The Commission therefore concludes that Portugal has not submitted sufficient evidence to prove the incentive effect of the aid.

The legal basis

(29) Regarding the legal basis for approving the aid, Portugal has not submitted any new arguments that would allay the doubts expressed by the Commission in its Decision to initiate the formal investigation procedure. Portugal's main argument in this respect is that the contracts are eligible for aid because they were signed during the period of application of the TDM-regulation. Portugal also notes that the fact that the aid was only notified after the expiry of the TDM-regulation has no impact on the eligibility of the contracts for aid.

(30) However, the Commission, in a previous Decision ([12]) has already explained why it does not consider that the TDM-regulation is still a valid legal basis for approving new operating aid to shipbuilding.

(31) The Commission notes that the temporal application of the TDM-regulation is defined in Article 5 ([13]) of the regulation, which states the regulation *'shall expire on 31 March 2005'*. The fact that Article 4 of the TDM-regulation states that this regulation *'shall be applied to final contracts signed from the entry into force of this Regulation until its expiry (…)'* is, in the Commission's view, a condition of compatibility and not a definition of the application in time of the regulation.

([10]) See, by contrast, case C 26/06 (footnote 3). In this case the Commission concluded that the incentive effect was shown by a letter from the Portuguese authorities to the shipyard acknowledging receipt of the request for aid prior to the signature of the contracts and indicating willingness to grant the aid if the eligibility conditions were fulfilled. This type of evidence was not submitted with regard to the present case.

([11]) See, by analogy, Article 38 of the Guidelines on National Regional Aid 2007-2013 (OJ C 54, 4.3.2006, p. 13): 'aid may only be granted (…) if the beneficiary has submitted an application for aid and the authority responsible for administering the scheme has subsequently confirmed in writing that subject to detailed verification, the project in principle meets the conditions of eligibility (…) before the start of the work on the project'.

([12]) Case C 26/2006 (ex N 110/2006) — footnote 3.

([13]) As modified by Council Regulation (EC) No 502/2004, see footnote 4 above.

(32) The above is also confirmed by the second part of Article 4, which provides that the TDM-regulation **shall not apply** to 'final contracts signed **before** the Community gives notice in the Official Journal of the European Communities that it has initiated dispute settlement proceedings against Korea (…) and final contracts signed on month or more **after** the Commission gives notice in the Official Journal of the European Communities that these dispute settlement proceedings are resolved or suspended'.

(33) From the above, it is clear that the TDM-regulation was only to be applied as long as there was a pending dispute with Korea ([14]) and in any event, no later than 31 March 2005.

(34) This interpretation is supported by the very objective of the TDM-regulation: it was designed 'as an exceptional and temporary measure, in order to assist Community shipyards in those segments that have suffered adverse effects in the form of material injury and serious prejudice caused by unfair Korean competition (…) [which] should be authorised for limited market segments and **for a short period only**' ([15]) (recital 3).

(35) In the present case, the application for aid was only submitted by ENVC to the Portuguese authorities, approved by Portugal and notified to the Commission **after** the expiry of the TDM-regulation, so clearly, the measures fall outside the temporal application of the TDM-regulation.

(36) The Commission further notes that, as already explained in the decision to initiate the formal investigation procedure in the present case, the interpretation of the TDM-regulation must also be seen in the light of the Community's international obligations. According to the settled case law of the Court of Justice, Community legislation must, so far as possible be interpreted in a manner that is consistent with international law, including the EC's WTO obligations. ([16])

(37) In this context, the Commission recalls that Korea challenged the compatibility of the TDM-regulation with WTO rules. On 22 April 2005, a Panel issued its report concluding that the TDM and several national TDM schemes — existing at the time when Korea initiated the WTO dispute — were in breach of Article 23.1 of the Understanding on rules and procedures governing the settlement of disputes (DSU) ([17]). On 20 June 2005, the WTO Dispute Settlement Body (DSB) adopted the Panel report including its recommendation that the Community brings the TDM-regulation and the national TDM schemes into conformity with its obligations under the WTO Agreements ([18]). On 20 July 2005, the Community informed the DSB that it had already brought its measures into conformity with the DSB ruling and recommendations since the TDM-regulation had expired on 31 March 2005 and Member States could no longer grant operating aid under this regulation.

(38) The Panel report and the DSB ruling adopting that report condemned the TDM-regulation *per se* for being in breach of WTO rules and oblige the Community to no longer apply the TDM-regulation. The obligation of the Community to implement the DSB ruling also covers future decisions to grant new aid in application of the TDM-regulation ([19]). The Community, by informing the DSB that it had already brought its measures into conformity with the DSB ruling and recommendations, since the TDM-regulation had expired on 31 March 2005 and Member States could no longer grant operating aid under this regulation, took a commitment to no longer apply this regulation for allowing the granting of new aid. Accordingly, approving the present aid would result in a breach of the Community's international commitments.

(39) The fact that the Council did not renew this Regulation following its expiry is a clear indication that the Council did not intend to continue to authorize the Commission to approve aid under the TDM-regulation. This corresponds with the fact that the Community informed the DSB that the Member States could no longer grant operating aid under this regulation.

(40) There were no new arguments from Portugal to counter the Commission's views as expressed in the decision to initiate the formal investigation procedure and reiterated above.

(41) The Commission, therefore, concludes that the notified aid cannot be approved under the TDM-regulation. Since no other exemption clause under Article 87(2) or (3) of the EC Treaty applies, the aid is thus incompatible with the common market,

([14]) Recital 7 confirms this assessment: 'the temporary defensive mechanism should only be authorised after the Community initiates dispute settlement proceedings against Korea (…) and may no longer be authorised if these dispute settlement proceedings are resolved or suspended (…)'.

([15]) Emphasis added.

([16]) Case C-53/96, Hermes, [1998] ECR I-3603, para. 28; Case C-76/00 P, Petrotub, [2003] ECR I-79, para. 57.

([17]) See *EC — Measures affecting trade in commercial vessels*, WT/DS301/R, paragraphs 7.184-7.222 & 8.1(d).

([18]) See WTO document WT/DS301/6.

([19]) See *EC — Measures affecting trade in commercial vessels*, WT/DS301/R, para. 7.21.

HAS ADOPTED THIS DECISION:

Article 1

The notified aid of EUR 6 575 558 proposed by Portugal to Estaleiros Navais de Viana do Castelo S.A. in relation to seven contracts signed by this shipyard cannot be authorized under Council Regulation (EC) No 1177/2002 concerning a temporary defensive mechanism to shipbuilding [20] as amended by Council Regulation (EC) No 502/2004 [21] and is therefore incompatible with the common market. The aid must not be implemented.

Article 2

This Decision is addressed to Portugal.

Done at Brussels, 11 December 2007.

For the Commission
Neelie KROES
Member of the Commission

[20] OJ L 172, 2.7.2002, p. 1.
[21] OJ L 81, 19.3.2004, p. 6.