II

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

DECISIONS

COMMISSION

COMMISSION DECISION

of 16 July 2008

relating to State aid C 29/04 (ex N 328/03) that Italy is considering granting to the Villasor sugar refinery owned by Sadam ISZ

(notified under document C(2008) 3531)

(Only the Italian text is authentic)

(2009/704/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

having regard to the Treaty establishing the European Community and, in particular, Article 88(2)(1) thereof,

having given interested parties notice to submit their comments pursuant to that Article, and having regard to those comments,

Whereas:

I. PROCEDURE

(1) By letter dated 22 July 2003, Italy notified the Commission of the aid to the Villasor sugar refinery owned by Sadam ISZ. By letters dated 19 September 2003 and 30 March 2004, Italy submitted the additional information to the Commission.

(2) By letter dated 8 September 2004, the Commission informed Italy of its decision to initiate the procedure referred to in Article 88(2) of the EC Treaty in respect of the aid in question.

(3) By letters dated 13 October 2004 and 7 April 2005, Italy forwarded to the Commission the Italian authorities' comments concerning the decision to initiate the formal investigation procedure.

(4) The Commission decision to initiate the procedure was published in the *Official Journal of the European Union* [1]. The Commission called on interested parties to submit their comments on the aid in question.

(5) The Commission received comments on this subject from interested parties. It forwarded them to Italy, giving it the opportunity to comment on them, and received Italy's comments by letter dated 18 May 2005.

(6) By letters dated 31 January 2008 and 14 April 2008, the Italian authorities forwarded to the Commission the information requested by letter dated 29 March 2007.

II. DESCRIPTION

(7) The recipient firm — the Villasor sugar refinery owned by Sadam ISZ — is a sugar beet processing facility. It is the only one in Sardinia (one of the largest islands in the Mediterranean).

(8) The Italian authorities are making EUR 3,5 million available to the refinery in order partially to compensate it for the losses it sustained following the slump in sugar production caused by the fall in sugar beet supplies following the drought in 2001-2002.

(9) Regarding sugar beet production, the competent authorities provided data showing a decrease in regional production and, consequently, of sugar beet supplies. Compared with the 1998-2000 reference period, the fall was 39 % in 2001 and 68 % in 2002 [2].

[1] OJ C 51, 1.3.2005, p. 9.

[2] The Commission authorised the granting of aid (aid N 745/2000 and aid N 331/02) to Sardinian agricultural producers under point 11.3 of the Community guidelines for State aid in the agriculture sector (OJ C 28, 1.2.2000, p. 2) for the losses they sustained following the drought concerned.

(10) The competent authorities calculated the loss sustained by the Villasor refinery on the basis of the data extracted from the company's balance sheets for the financial years 1998 to 2002 and estimated it at EUR 6 858 448 ([3]). The method for calculating the loss was as follows. The authorities calculated the proportion of the fixed costs in relation to one tonne of sugar during one reference period (1998-2000) and compared this figure to the ratio of fixed costs per tonne of sugar during the years 2001 and 2002. They viewed the following as fixed costs: permanent staff, handling (services provided by third parties, and warehousing levies), general expenditure, depreciation and financial charges ([4]). During the reference period, the effect of fixed costs on the product was EUR 166,61/tonne ([5]). For 2001-2002, the same calculation process gave rise to the following results: the effect of fixed costs on the product in 2001 was EUR 287,95/tonne ([6]) and, in 2002, EUR 569,18/tonne ([7]). The major effect of the fixed costs in relation to the reference period was obtained by subtracting the effect of the fixed costs for the reference period from the effect of the fixed costs for 2001 and 2002. The result in 2001 was EUR 121,34/tonne and, in 2002, EUR 402,58/tonne ([8]). In order to calculate the total loss sustained, total sugar production in 2001 and 2002 was multiplied by the index shown above. In 2001, the loss was quantified at EUR 2 427 278 and, in 2002, at EUR 4 431 170 ([9]), i.e. a total of EUR 6 858 448.

(11) The amount of EUR 3,5 million granted by the Italian authorities would therefore correspond to 51 % of the loss sustained. The Italian authorities explained that the amount of the aid was dictated by budgetary imperatives.

(12) This aid is not to be paid in conjunction with other forms of aid.

(13) In order to demonstrate the exceptional nature of the drought affecting Sardinia in 2001-2002, the Italian authorities submitted a dossier, drawn up by Sardinia's Regional Agro-Meteorological Service (Italian acronym: SAR) ([10]). These data indicate, for example, the duration of the drought and the level of water reserves. There are also data concerning the agro-climatological situation in Sardinia in 2001-2002.

(14) The Italian authorities also indicated that sugar beet growing had benefited from aid on a number of occasions. During the period 1990-2002, aid had been granted in 1995, 2000, 2001 and 2002.

(15) The Italian authorities considered the aid to be compatible with the common market under the terms of point 11.3.1 of the Community Guidelines for State aid in the agriculture sector for the period 2000-2006 (henceforth referred to as the Guidelines) ([11]) since, in their view, such aid is designed to make good the loss sustained by the sugar refinery following a decrease in sugar beet production caused by an adverse weather condition assimilated to a natural disaster.

(16) The Italian authorities considered that this interpretation was in line with Commission practice in such matters ([12]) in cases where primary agricultural production and the procedures of agricultural processing were closely interdependent, and particularly in an instance where the agricultural processing undertaking concerned had no alternative sources of supply available to it.

(17) With this in view, the Italian authorities maintained that, in the beet-based sugar industry, the agricultural and industrial components were closely linked and interdependent. The existence of a sugar beet processing facility depends on there being an appropriate supply basin, and the Villasor refinery's activity consists exclusively in converting the beet produced in Sardinia's 'supply basin' into sugar. The Italian authorities maintain that, because of its physiological characteristics, sugar beet grown in the Mediterranean basin has to be harvested over the short period of time in which the sugar content is at its highest. It also has to be transported to the processing facility quickly (within 36 hours of being harvested), otherwise it loses its sugar content and is attacked by fungi, making it unusable. For these reasons, supply basins are usually situated within a radius of 80 to 100 kilometres from processing facilities, and harvesting and processing periods are very short. The source of supply closest to the Villasor

([3]) The competent authorities sent the Commission the balance sheet and their estimate of the value of the loss by letter dated 27 November 2003.

([4]) The competent authorities deducted a rate of 27,2 % for depreciation for 2000-2002, equivalent to the percentage of aid received by Sadam Spa as State aid in relation to the investment made in restructuring the Villasor processing facility. State aid N 157/99, decision (2000) D/103781, 19 May 2000 (OJ C 175, 24.6.2000, p. 20).

([5]) For the complete reference period, the total fixed costs were EUR 15 762 413,37 and total sugar production was 94 609 tonnes (15 762 413,37/94 609 = EUR 166,61/tonne).

([6]) In 2001, fixed costs amounted to EUR 5 760 061,14 and sugar production to 20 004 tonnes (5 760 061,14/20 004 = EUR 287,95/tonne).

([7]) In 2002, fixed costs amounted to EUR 6 265 000,70 and sugar production to 11 007 tonnes (6 265 000,70/11 007 = EUR 569,18/tonne).

([8]) In 2001 (287,95 – 166,61) = EUR 121,34/tonne in 2002 (569,18 – 166,61) = EUR 402,58/tonne.

([9]) In 2001 (121,34 × 20 004) = EUR 2 427 278 in 2002 (EUR 402,58 × 11 007 tonnes) = EUR 4 434 170.

([10]) The SAR is Sardinia's public agro-meteorological service.

([11]) OJ C 28, 1.2.2000, p. 1.

([12]) In this connection they cite the Commission decision of 5 December 2000, taken within the framework of State aid N 185/2000 (OJ C 19, 20.1.2001, p. 6). In this case, the Commission had considered the compensation paid to shellfish-cleaning enterprises following the mucilage pollution in 1997 to be compatible with Article 87(2)(b) of the Treaty.

refinery is in continental Italy, more than 250 km away (including 180 km across the sea).

(18) The Italian authorities pointed out that sugar production is regulated at Community level by the common organisation of the markets in the sugar sector (sugar CMO Regulation) ([13]). This stipulates that, in order to benefit from prices and revenues guaranteed by the CMO, refineries must enter into contracts with their supply basin's sugar beet producers for the 'A + B' sugar production quotas granted to them by the State. Sugar produced over and above the 'A + B' quotas can neither benefit from internal support measures nor be freely marketed within the common market. As a result, refineries and the farms that normally supply them factor into their cultivation contracts acreages that produce no more than the 'A + B' quotas granted by the State to the refineries. In this context, it is difficult for a refinery to obtain supplies from a sugar beet production basin other than its own because of the limited quantity of sugar beet available for processing outside the cultivation contracts and because of the need for supply agreements between sugar processing companies. In the Mediterranean Basin, moreover, alternative sugar beet basins have to be situated sufficiently close by to guarantee the supply of a usable product.

(19) The Italian authorities were also willing to consider the possibility of the Villasor facility having been able to find its raw material for processing somewhere else, but the refinery is so far away from the production areas in continental Italy as to make it uneconomic to transport the sugar beet, quite apart from the fact that the raw material would arrive at its destination in an unusable condition.

(20) The Italian authorities provided the Commission with simulations of the periods required for transporting sugar beet from an 'alternative' basin in continental Italy and of the costs of doing so. The period required for transporting sugar beet to Sardinia would be in the region of 2,5 days as from the time of loading. Given that the sugar beet necessarily has to be processed within 36 hours (1,5 days) of harvesting, it would arrive at its destination in an unusable condition. The cost of such an operation, as calculated by the competent authorities, would be approximately EUR 10 188 000 for the two periods.

(21) With regard, specifically, to the drought and to the drought-related water management policy conducted in Sardinia, the Italian authorities indicated that a water emergency had been declared in 1995 and that a special administrator (*Commissario Governativo per l'Emergenza Idrica*) had been appointed, with special powers for managing water resources and for having urgent infrastructure work done.

(22) The Italian authorities also indicated that Sardinia's regional development plan for 2000 to 2006 provided for specific measures for cultivating sugar beet. These measures included hydro-agricultural land development, the acquisition of irrigation equipment and installations by farms and the introduction of more modern machinery and of machinery for protecting plants and facilitating their fertilisation.

III. GROUNDS FOR INITIATING THE PROCEDURE

(23) The Commission initiated the procedure laid down by Article 88(2) of the EC Treaty because it doubted that the measure was compatible with Article 87(2)(b) of the Treaty, according to which aid to make good the damage caused by natural disasters or exceptional occurrences is compatible with the common market. Because they constitute exceptions from the general principle of the incompatibility of State aid with the common market, laid down by Article 87(1) of the Treaty, the Commission has a restrictive interpretation of the notion of 'natural disaster' contained in Article 87(2)(b). Until now, the Commission has accepted that earthquakes, avalanches, landslides and floods may constitute natural disasters.

(24) The Commission has consistently held that adverse weather conditions such as frost, hail, ice, rain or drought cannot of themselves be regarded as natural disasters within the meaning of Article 87(2)(b). However, because of the damage that such events may cause to agricultural production or the means of agricultural production, the Commission has accepted that such events may be treated as natural disasters once the level of damage reaches a certain threshold (which has been fixed at 20 % of normal production in less-favoured regions and 30 % in other regions). Point 11.3 of the Guidelines ([14]) states that aid designed to make good losses resulting from adverse weather conditions may only be paid for farmers or to a producer organisation of which the farmer is a member. The Commission regards the aid that comes under point 11.3 as being compatible with the common market under Article 87(3)(c) of the Treaty, provided that certain conditions are complied with.

(25) The Commission has consistently held that the provisions of point 11.3 of the Guidelines are not applicable to agricultural processing undertakings that, in its view, have the flexibility necessary for managing their supplies. This may of course result in additional raw material costs and/or a loss of profitability, but it does not warrant the direct application of the rules applicable to agricultural production.

([13]) At the time of the notification, the market was governed by Council Regulation (EC) No 1260/2001 of 19 June 2001 on the common organisation of the markets in the sugar sector (OJ L 178, 30.6.2001, p. 1).

([14]) See footnote 11.

(26) Since the Italian authorities have proposed no other legal basis for the assessment and possible approval of the aid, the Commission could not, at this stage of the procedure, exclude the possibility of the anticipated aid constituting operating aid, that is to say a form of aid that seeks to relieve enterprises of the costs they would normally have to bear as part of their day-to-day management or normal activities.

(27) Moreover, the information provided by the Italian authorities and the information available to the Commission appeared to suggest that Sadam ISZ and the companies to which it belonged directly or indirectly — in particular, Società Adriatica Marchigiana (SAM) ([15]) and FINBIETICOLA Spa ([16]) — could have absorbed the reduction in the facility's profitability.

(28) Finally, even if it had been considered acceptable (which was not the case at this stage of the procedure) to apply to Sadam ISZ the principle governing the payment of compensation under point 11.3 of the Guidelines, the reference period chosen by the Italian authorities for calculating the aid would have been incorrect.

IV. COMMENTS FROM INTERESTED PARTIES

(29) When the procedure was initiated, the Commission received comments from Sadam ISZ ([17]), the President of Sardinia Region ([18]) and Brumar Srl ([19]).

Sadam ISZ

(30) In its comments, Sadam ISZ repeated the reasons, expressed in points 12 to 36 of the letter initiating the formal investigation procedure, that had led the Italian authorities to consider granting the aid: the exceptional nature of the drought; the impossibility of obtaining supplies from other basins due to the particular structure of the organisation of the market in sugar; the impossibility of obtaining suitable transport due to the refinery's island location; and the importance of the agricultural sugar processing industry for Sardinia's economy. It also provided information about the changing ownership of Sadam ISZ, which is at present owned exclusively by the Eridania Sadam group, with Finbieticola's share having also been transferred to the Eridania Sadam group in October 2004 since Sviluppo Italia SpA's withdrawal in December 2003. Sadam ISZ provided a copy of the agreement concluded between the various private and public authorities with a view to guaranteeing the continued production of sugar beet in Sardinia. Within this framework, Sardinia region committed itself to taking every initiative necessary for recommencing investment in the sugar beet sector — in particular, in water resource management — and to losing no time in obtaining the Commission's authorisation of the aforesaid EUR 3,5 million in aid to offset the losses due to the drought.

(31) Sadam ISZ considers that what it produces has no influence at all on the development of the European market, not only because it represents only 0,2 % of that market but also because 98 % of its production is intended for the Sardinian market, covering almost 50 % of that market's needs, whereas the Eridania Sadam group produces 35 % of Italian sugar, equal to 1,7 % of European sugar, and has 23 % of the national market, equal to 2,15 % of the European market.

President of Sardinia Region

(32) The President of Sardinia Region emphasised the quite exceptional nature of the situation characterising the years 2001-2002, stating that it could in no way constitute a precedent applicable in the future to other situations. The region's President stressed the bad effects that closure of the only Sardinian refinery would have on the island's economy, given the need for rational management of agricultural production as a whole (with sugar beet an important rotation crop) and given the importance of the sugar beet industry in Sardinia, the number of farms concerned (1 300 employing approximately 5 000 people) and the number of permanent and seasonal employees at the refinery (83 and almost 200, respectively), not counting the jobs created by the sugar beet industry (for hauliers, enterprises responsible for growing and harvesting the sugar beet and undertakings tasked with handling the facilities). The region's President pointed out the importance attached by the regional administration to the sugar beet industry and its commitment to safeguarding the industry.

Brumar Srl

(33) Brumar Srl stated that the Sadam refinery had not sustained losses since it had had the option of buying sugar in France, Germany, Slovenia and Croatia; that all Italian refineries had increased the price of white sugar by EUR 50 per tonne as from 1 October 2003, with a net profit of EUR 80 million in favour of the five sugar refineries on Italian territory. According to Brumar Srl, Sadam ISZ would have been the main recipient of this profit, given that it is responsible for most of Italy's sugar production. In its conclusion, Brumar Srl considered that aid should be granted both to sugar beet producers (to offset the losses sustained due to the failed harvest caused by the drought) and to the workers who had not been employed by the processing facilities.

([15]) SAM srl is a company controlled by Sadam Spa. The Sadam group accounts for 35 % of Italian sugar production.
([16]) FINBIETICOLA Spa's particular task is to play a part in those Italian sugar manufacturers in which it holds shares.
([17]) Letter dated 31 March 2005.
([18]) Letter dated 10 December 2004.
([19]) Fax dated 7 March 2005.

V. COMMENTS MADE BY ITALY

(34) The Italian authorities sent their comments when the procedure was initiated by letters dated 13 October 2004 and 7 April 2005 and submitted their comments in response to the letter from Brumar Srl by letter dated 17 May 2005.

(35) The Italian authorities contested Brumar Srl's comments in their entirety, deeming them to be of no relevance at all to the case in question, given that the Villasor refinery had never imported sugar from the countries listed by Brumar Srl and given that the increase in the prices of white sugar applied to Italy's production as a whole and related to the marketing year 2003, postdating the years for which the aid was to be granted. Finally, the authorities contested the calculations of the presumed profits made in 2003 by Italian sugar companies in general and by the Eridania Sadam group in particular. The Eridania Sadam group, of which Sadam ISZ is a part, produced 34 % of Italian sugar in 2003.

(36) In their letter of 13 October 2004, the Italian authorities acknowledged that the Commission had been most thorough in presenting all the factors in the case and all the data supplied during the phase prior to the investigation procedure being initiated, particularly in relation to the legal basis, the compensatory nature of the measure proposed, the means of calculating the aid, the legal basis important for authorising the measure, the interdependence of the sugar beet industry's agricultural and industrial components, the impossibility of obtaining supplies from other production basins for Sardinia-based processing, and the importance of the sugar beet industry for Sardinia's economy.

(37) The Italian authorities consider that the aid measure would have no impact on intra-Community trade, as its effects would not be felt beyond the region. Ninety-eight per cent of what is produced by the Villasor refinery is absorbed by the local market and is not therefore in competition with the production of other Community undertakings, whether in continental Italy's market or in the Community or international market. The Italian authorities consider that the Commission, in accordance with its Draft Communication on new guidelines for the evaluation of State aid with limited effects on intra-Community trade, should attach greater importance to the economic impact of the intervention concerned, in view in particular of its limited impact on trade. According to the Italian authorities, the Commission's statement ([20]) to the effect that Italy has an important position in sugar production should at least be seen in relation to the references to Italy's being only the fourth largest EU sugar producer and to the Eridania Sadam group's having, in this context, a market share of slightly more than 1,5 % of the European market, while Sadam ISZ's production amounted to 0,06 % (data for the marketing year 2002).

(38) Regarding the legal basis for the measure, the Italian authorities cite a series of previous decisions by the Commission (in particular, State aid cases N 83/2000, N 185/2000, N 657/02 and N 729/02), in which the Commission authorised aid in the agricultural and agricultural processing sector on the basis of Article 87(2)(b) of the Treaty and in the light of the implementation criteria specified in point 11.3 of the Guidelines, maintaining that, in the case in question, the implementation criteria had been met.

(39) The Italian authorities also draw the Commission's attention to point 3.4 of the Guidelines which stipulates that the fact that an aid measure is not in all points comparable to one of the possible cases listed in the Guidelines themselves does not exonerate the Commission from carrying out an examination on a case-by-case basis, taking into account the principles set out in Articles 87, 88 and 89 of the Treaty and the Community's common agricultural and rural development policies. Accordingly, the Italian authorities consider that if the Commission finds that Article 87(2)(b) is not applicable to the proposed measure, the measure should be allowed under Article 87(3)(c).

(40) According to the Italian authorities, the proposed intervention would enable the refinery partially to offset the large losses sustained as a result of the absence of sugar production due to the lack of raw materials to be processed following the severe drought of 2001-2002. In Sardinia, a normal sugar beet harvest would enable the processing facility to achieve financial equilibrium. The support provided, again characterised as contingent and exceptional by the Italian authorities, would also allow completion of the whole restructuring project launched in 1999 and involving major investment at industrial and agricultural level ([21]) (see measure 4.9 N in the regional development plan for Sardinia approved by the Commission), with benefits for the economic development of the region as a whole.

([20]) See point 38 of the letter initiating the investigation procedure.
([21]) See footnote 4.

(41) The Italian authorities maintain that the reference to the Sadam Eridania group's internal relations are not at all relevant to the assessment of the case in hand. In response to the large trading deficit in 2003, the Sadam Eridania group and FINBIETICOLA Spa recapitalised the company in December 2003 with a payment of EUR 5 039 393, thereby honouring their obligations towards the company they controlled, given the normal business risks borne by Sadam ISZ in 2003 (management year/normal production). Following this recapitalisation, Sviluppo Italia — the public shareholder — withdrew as it had not taken part in the recapitalisation. The Italian authorities do not consider that the controlling company might have an obligation, in the context of prudent planning of the group's business activities, to compensate by financial transfers within the group for losses caused by an event of an exceptional and unforeseeable nature. The Italian authorities maintain that the supervising shareholders' responsibility has to be limited to the requirements arising from the undertaking's normal activities.

(42) With regard, finally, to the reference period established for calculating the compensation, the Italian authorities consider that they have complied with the principles laid down in point 11.3.2 of the Guidelines. Moreover, the amount of the difference between the value of the loss in fact borne by the company (EUR 6 858 448) and the amount of the aid proposed (EUR 3,5 million) excludes excessive compensation. The Italian authorities point out that the Commission has already accepted methods of calculating loss that are different from those indicated in the Guidelines, provided that the methods adopted were not in danger of providing excessive compensation for the losses sustained ([22]).

(43) In their latest letters of 2008, the Italian authorities have provided additional details at the Commission's request. In particular, the Italian authorities provided data (expressed in tonnes) on the subject of sugar production. These are presented in the table below:

Marketing year	Villasor prod.	Sadam group prod.	'A + B' quota, Sadam group	Deficit/excess
1999/2000	34 310,13	334 851,41	308 119,70	26 731,71
2000/2001	26 608,50	290 403,52	298 910,30	– 8 506,78
2001/2002	20 004,60	242 879,84	305 996,50	– 63 116,66
2002/2003	11 007,06	283 729,55	290 072,50	– 6 342,95
2003/2004	9 143,18	284 895,25	533 961,70	– 249 066,45
2004/2005	9 520,30	341 327,21	540 996,50	– 199 669,29
2005/2006	8 193,55	623 281,50	484 356,20	138 925,30

(44) The Italian authorities also indicated that the Villasor refinery had definitively ceased its activities within the framework of a process of restructuring the sector because of the reform of the sugar CMO. In the light of this, Eridania Sadam submitted a 'restructuring plan for the Villasor refinery' to the Ministry of Agricultural, Food and Forestry Policy on 30 April 2007.

(45) According to the Italian authorities, it will be possible for the aid that has been notified to be incorporated within the process of restructuring the industry and the company — a process that remains vital in terms of safeguarding jobs and outlets for the Sardinian agro-energy industry.

VI. **ASSESSMENT OF THE AID**

Market organisation

(46) The measure considered is aid to be granted to a sugar refinery. In accordance with Article 36 of Council Regulation (EC) No 318/2006 of 28 February 2006 on the common organisation of the markets in the sugar sector ([23]) and, prior to this, Article 45 of Regulation (EC) No 1260/2001, Articles 87, 88 and 89 of the EC Treaty apply to the products that come under these Regulations. Consequently, the sector to which the aid measure relates comes under the Community provisions on State aid.

([22]) See State aid N 661/01, decision (2003) C/130, 13 February 2003 (OJ C 68, 21.3.2003, p. 17).
([23]) OJ L 58, 28.2.2006, p. 1.

Prohibition of State aids within the meaning of Article 87(1) of the EC Treaty

(47) 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.

(48) The measure in question corresponds to the definition of aid referred to in Article 87(1) of the Treaty, given that it confers an economic advantage (in the form of non-refundable financial aid) to a specified company (Sadam ISZ of Villasor), that it amounts to funding from (regional) public resources and that the aid concerned is likely to affect trade. Moreover, it emerges from the data supplied by Sadam after the investigation procedure had been initiated that the company is active not only in the Italian market but also in the intra-Community market (see recital 31, above). Even if the sugar produced in the Villasor refinery is intended almost exclusively for the Sardinian market, it is no less the case that the aid in question is likely to place a possible competitor in this market from another Member State at a disadvantage.

(49) According to the case law of the European Court of Justice, an improvement in the competitive position of an undertaking as a result of State aid generally leads to distortion of competition in relation to competing undertakings not receiving such assistance ([24]). Case law has indicated that the relatively small size of aid or the relatively small size of the company that benefits from it does not as such exclude the possibility that trade between Member States might be affected ([25]).

(50) A measure affects trade between Member States when it hinders imports from other Member States or facilitates exports to other Member States. The crucial factor is that intra-Community trade develops, or is in danger of developing, differently because of the measure in question.

(51) The product benefiting from the aid scheme is the subject of trade between Member States ([26]) and is therefore exposed to competition.

(52) The existence of a common organisation of the market in the sugar sector, as indicated in recital 46, is also proof of the importance of intra-Community trade in sugar and of the desire to ensure undistorted conditions of competition on the common market.

(53) The draft Commission Communication on the new guidelines for the evaluation of State aid with limited effects on intra-Community trade to which the Italian authorities have referred (see recital 37) has not been adopted by the Commission and cannot undermine the foregoing reasoning.

(54) The criteria concerning the effect on trade and the distortion of competition are therefore fully met.

(55) The measure is in effect, therefore, State aid within the meaning of Article 87(1) of the EC Treaty.

(56) The prohibition referred to in Article 87(1) of the EC Treaty is not unconditional. In order to be considered compatible with the common market, the proposed measure must benefit from one of the derogations provided for by Article 87(2) and (3) of the Treaty.

Derogations provided for by Article 87(2) of the EC Treaty

(57) The provisions of Article 87(2)(b) of the EC Treaty invoked by the Italian authorities — declaring aid to make good the damage caused by natural disasters or exceptional occurrences to be compatible with the common market — are not applicable.

(58) Since no definitions of the terms 'exceptional occurrence' and 'natural disaster' are given by the Treaty, it needs to be verified whether the drought affecting Sardinia can be considered a 'natural disaster' within the meaning of Article 87(2)(b) of the Treaty. The Commission has always adopted a restrictive interpretation of 'natural disasters' and 'exceptional occurrences' as referred to in Article 87(2)(b).

(59) The need for such a restrictive interpretation has constantly been confirmed by the European Court of Justice ([27]).

(60) Hitherto, the Commission has accepted earthquakes, avalanches, landslides and floods as natural disasters. Exceptional occurrences that have hitherto been accepted include war, internal disturbances or strikes and, with certain reservations and depending on their extent, major nuclear or industrial accidents and fires that result in widespread loss.

(61) Because of the inherent difficulties in foreseeing such events, the Commission will continue to evaluate proposals to grant aid in accordance with Article 87(2)(b) on a case-by-case basis, having regard to its previous practice in this field. Such analysis is particularly necessary within the framework of aid to a sensitive sector, such as the sugar sector, where any intervention measure could come up against the measures laid down by the common organisation of the markets.

([24]) European Court of Justice, Judgment of 17 September 1980, Case C-730/79 [1980] ECR 2671, paragraphs 11 and 12.

([25]) Court of Justice, Judgment of 21 March 1990, Case-142/87 [1990] ECR I-959, paragraph 43, and Judgment of 14 September 1994, joined cases C-278/92 and C-80/92 [1994] ECR I-4103, paragraphs 40 to 42.

([26]) Intra-Community trade is important in the sugar sector. In 2002, Italy imported 366 539 tonnes of sugar from other Member States (the EU-15), while exports amounted to 37 564 tonnes.

([27]) European Court of Justice, 11 November 2004, *Spain* v *Commission*, Case C-73/03, paragraph 37; CJEC, 23 February 2006, Cases C-346/03 and C-529/03, *Giuseppe Atzeni* and others, paragraph 79.

(62) The Commission has consistently held that adverse weather conditions such as frost, hail, ice, rain or drought cannot of themselves be regarded as natural disasters within the meaning of Article 87(2)(b) (see point 11.3.1 of the 2000-2006 Guidelines).

(63) Drought, even on a large scale, has hitherto never been recognised as a natural disaster within the meaning of Article 87(2)(b) of the Treaty.

(64) In general, an exceptional occurrence must at least present the characteristics of an occurrence that, by its nature and its effect on the operators concerned, is clearly distinguished from usual conditions and is outside the framework of the normal conditions under which a market operates.

(65) Moreover, the data submitted by Italy lead to the conclusion not that the drought was of an exceptional character but, rather, that it is a recurring phenomenon. Since autumn 1999 (and with the exception of November 2001), there has been a long period of drought. The year 2001-2002 was characterised by lower, but not exceptionally lower, rainfall than average. During the period 1990-2000, there were in fact three years when the drought was more severe (1994-1995, 1998-1999 and 1999-2000). Since 1970 there has apparently been a general trend towards reduced rainfall ([28]).

(66) Another factor in the light of which drought may be considered a recurring phenomenon is the fact that a water emergency was declared in Sardinia in 1995 ([29]) — a state of affairs that ended on 31 December 2004 ([30]).

(67) The fact that aid has been granted on four occasions to sugar beet producers to make good the losses due to drought in the period 1990–2002 also indicates that the drought was not exceptional.

(68) Moreover, production subsequent to the period considered (2001-2002) shows a large decrease in production by the Villasor refinery, even though there was no drought during this period (see table in recital 43).

(69) As a result, the aid proposed by the Italian authorities cannot be authorised on this legal basis.

Derogations provided for by Article 87(3) of the EC Treaty

(70) It needs to be examined whether the measure proposed may be considered to be compatible with the common market within the meaning of Article 87(3) of the Treaty. The provisions of point (c) are of more precise relevance. According to these, aid to facilitate the development of certain economic activities or of certain economic areas may be considered to be compatible with the common market where such aid does not adversely affect trading conditions to an extent contrary to the common interest.

(71) In its interpretation of the aforesaid derogation relating to the agriculture sector, the Commission begins by verifying the applicability of Commission Regulation (EC) No 1/2004 (of 23 December 2003) on the application of Articles 87 and 88 of the EC Treaty to State aid to small and medium-sized enterprises active in the production, processing and marketing of agricultural products ([31]). If the aforesaid Regulation is inapplicable, the Commission proceeds on the basis of the Guidelines.

(72) In the case in question, Regulation (EC) No 1/2004 is not applicable since the aid is intended for a processing company as a result of losses due to adverse weather conditions — a state of affairs not anticipated by the Regulation referred to. As a result, the Commission should evaluate the measure on the basis of the Guidelines.

(73) Point 11.2 of the Guidelines regulates State aid designed to make good the damage caused by natural disasters or exceptional occurrences. This point will not be discussed below as it comes under the application of Article 87(2)(b) of the Treaty, already examined above.

(74) Point 11.3 of the Guidelines regulates State aid designed to compensate farmers for losses due to adverse weather conditions such as frost, rain, ice or drought — occurrences that cannot of themselves be regarded as natural disasters within the meaning of Article 87(2)(b) of the Treaty.

(75) When such events cause damage to agricultural production or to the means of agricultural production of a value greater than 20 % of normal production in less-favoured areas and greater than 30 % in other areas, the Commission treats the events as natural disasters and authorises the granting of aid to farmers, designed to offset the losses concerned under Article 87(3)(c) of the Treaty.

(76) In general, drought may in fact be put on the same footing as a natural disaster, as happened in the case of Decision No 331/02 ([32]) because the damage sustained by farmers or producer organisations exceeded a certain threshold. As pointed out in its letter initiating the investigation procedure, the Commission has, however, always considered that the provisions of point 11.3 of the Guidelines were not applicable to agricultural processing undertakings that, in its view, enjoy a degree of flexibility in the management of their supplies. This may of course result in additional raw material costs and/or a loss of profitability, but seems not to warrant the direct application of the rules applicable to agricultural production.

([28]) Data sources: *SAR: Le precipitazioni sulla Sardegna da Settembre 2001 ad Agosto 2002* ['SAR: Rainfall in Sardinia from September 2001 to August 2002'].

([29]) Prime Minister's Decree of 20 June 1995, *Dichiarazione dello stato di emergenza* ['Declaration of the state of emergency'], on the basis of Act 225/92.

([30]) http://www.regione.sardegna.it/j/v/138?s=1&v=9&va=3&c=1219

([31]) OJ L 1, 3.1.2004, p. 1.

([32]) Commission letter C(2002) 3211 of 2 September 2002, http://ec.europa.eu/community_law/state_aids/agriculture-2002/n331-02.pdf

This approach, referred to in point 11.3.8 of the Guidelines, was also confirmed in a recent judgment of the Court of First Instance ([33]).

(77) According, then, to point 11.3 of the agricultural Guidelines, aid designed to compensate agricultural processing undertakings from losses resulting from adverse weather conditions is incompatible with the common market.

(78) The Italian authorities had based a part of their argument on the fact that the refinery concerned did not have the flexibility to manage its supplies and that, as a result and in view of the close link between sugar beet production and the refinery, the aid should be extended to include the refinery. In this context, the Italian authorities had referred to several Commission decisions as precedents. The first series of decisions referred to cannot be considered to be comparable as they refer to occurrences characterised in themselves as natural disasters (aid N 729/02 ([34]) refers to compensation following flooding in the south-east of France) or exceptional occurrences (aid N 83/2000 ([35]) relates to dioxin contamination in Belgium, aid N 185/2000 ([36]) makes good the damage following the proliferation of algae in the Adriatic in Italy and aid N 657/02 ([37]) relates to the Belgian forestry sector, damaged by an exceptional proliferation of bark beetles and fungi). As indicated previously, drought cannot in itself be characterised as a natural disaster or exceptional occurrence and, as a result, the decisions cited cannot be considered as precedents similar to the case in question.

(79) The Italian authorities had also referred to decisions N 745/2000–C 4/01 ([38]) and N 331/02 ([39]). In these two cases, the Commission concluded that drought could be likened to a natural disaster because of the threshold of damage exceeded. In both cases, the aid was granted to primary producers and to 'consorzi di bonifica' (land reclamation consortia). The Commission concluded that the agricultural Guidelines did not apply to these 'consorzi di bonifica' because of the fact that water is not a product that comes under Annex I of the Treaty.

(80) However, these 'consorzi di bonifica' cannot be likened to normal undertakings, as is the case with the refinery in question. The 'consorzi di bonifica' are autonomous public undertakings that manage drainage areas. In exchange, they receive payments from farmers for the irrigation water provided. This difference between the 'consorzi di bonifica' and undertakings for processing or marketing agricultural products has also been confirmed by the fact that, in the aforesaid case N 745/2000–C 4/01, the Commission decided to initiate the investigative procedure for the portion of the aid concerning undertakings and cooperatives active in the processing and marketing of agricultural products while indicating that, in application of the agricultural Guidelines, aid to these processing undertakings could not be approved. Notification having subsequently been withdrawn, no final decision was taken where this case was concerned.

(81) With regard to the refinery's difficulty in obtaining supplies from elsewhere, the Italian authorities put forward arguments aimed at demonstrating the inherent difficulties faced by every refinery in obtaining supplies from a sugar beet production basin different from its own because of a contract system linking the sugar beet producers to the refineries, because of the island location of the refinery concerned and because of the short period for which sugar beet can be preserved. The fact that it is impossible for refineries to obtain supplies from elsewhere is a result, however, of Regulation (EC) No 1260/2001 which introduced a system of contracts between sugar beet producers and refineries. The Italian authorities have themselves pointed out that, in normal conditions, it is not possible to obtain supplies from other sugar beet production basins intended for other undertakings without causing these other undertakings' final production to fall and therefore preventing them from achieving their quotas. The authorities have therefore indicated that, in general, it is not often that a refinery is able to obtain supplies from production basins other than its usual ones.

(82) Because of the aforesaid Regulation (EC) No 1260/2001, any refinery, whatever its location, has the inherent inflexibility invoked as an argument by Italy. Such an argument would thus apply to all processing undertakings whose link with producers is an integral part of the organisation of the market in which they are active. Acceptance of this argument would go against a strict interpretation of the agricultural Guidelines — a strict interpretation that does need, moreover, to be applied since we are concerned here with an exception to the general rule concerning the incompatibility of aid.

([33]) Judgment of the Court of First Instance of 14 December 2005, Case T-200/04, par. 46, according to which it may be seen from the wording and general economy of these provisions that point 11 of the Guidelines draws a distinction in principle between farmers and agricultural production, on the one hand, and processing undertakings and processing activity, on the other. Only aid designed to offset losses sustained by farmers, and this in the exercise of agricultural production, is likely to be approved on the basis of this point.

([34]) Commission letter C(2003) 910 final of 2 April 2003, http://ec.europa.eu/community_law/state_aids/agriculture-2002/n729-02.pdf

([35]) Commission letter SG(2000) D/103852 of 25 May 2000, http://ec.europa.eu/community_law/state_aids/agriculture-2000/n083-00.pdf

([36]) Commission letter SG(2000) D/108955 of 5 December 2000, http://ec.europa.eu/community_law/state_aids/peche-2000/n185-00.pdf

([37]) Commission letter of 6 December 2002, http://ec.europa.eu/community_law/state_aids/agriculture-2002/n657-02_fr.pdf

([38]) Commission Decision of 2 February 2001 (OJ C 263, 19.9.2001, p. 16).

([39]) Commission letter C(2002) 3211 of 2 September 2002, http://ec.europa.eu/community_law/state_aids/agriculture-2002/n331-02.pdf

(83) As a result, the aid proposed by the Italian authorities cannot be authorised on this legal basis.

(84) The Italian authorities had also referred to point 3.4 of the aforesaid agricultural Guidelines as the legal basis for the aid. In applying this point, the Commission will assess any aid measures that are not covered by the agricultural Guidelines on a case-by-case basis, taking account of the principles set out in Articles 87, 88 and 89 of the Treaty and of the Community's common agricultural and rural development policies. As indicated in the previous paragraphs, the aid measures concerned (aid to processing undertakings designed to make good the losses sustained due to adverse weather conditions) are specifically covered by point 11.3 of the Guidelines. These exclude such undertakings from the benefit of aid, with the result that point 3.4 does not apply.

(85) Concerned not to leave any avenue unexplored, the Commission has examined whether the guidelines for rescuing and restructuring firms in difficulty might not be applicable to the case in question. The first condition to be fulfilled by an undertaking if it is to benefit from rescuing or restructuring aid is that it should be considered as being in difficulty within the meaning of the guidelines on State aid for rescuing and restructuring firms in difficulty ([40]). It is not apparent from the information held by the Commission that the undertaking was in difficulty within the meaning of the above-mentioned guidelines when the aid was notified. The only known indication that it might have been so is the fact that it needed to be recapitalised because of a large trading deficit in 2003. The private shareholders intervened to recapitalise the company in December 2003, thereby making any public support for its restructuring superfluous. Moreover, the company had already received restructuring aid, approved by the Commission in 1999 ([41]). Since fewer than 10 years have elapsed since the end of the restructuring period, no new restructuring aid can be granted because of the 'one time, last time' principle referred to in point 3.2.3 of the guidelines on rescuing and restructuring. In any case, the Commission wishes to point out that it is up to the Member State concerned to fulfil the duty of cooperation it has towards the Commission by providing all the elements required for the Commission to be able to check that all the conditions of the derogation from which it is asking to benefit have been met ([42]). In the case in question, the Italian authorities have never called for the guidelines on rescuing and restructuring to be applied nor supplied any document enabling the Commission to assess the data in the light of these guidelines, and this in spite of the information provided by the Commission in recital 44 of the decision to initiate the investigative procedure.

Other doubts expressed by the Commission when the procedure was initiated

(86) The data held by the Commission when the procedure was initiated seemed to indicate that Sadam ISZ and the companies to which Sadam ISZ directly or indirectly belonged — in particular, SAM and FINBIETICOLA Spa — would have been in a position to cope with the fall in Sadam ISZ's profitability.

(87) Sadam ISZ having passed entirely under the control of Eridania Sadam during the procedure, the Commission notes that the lead company has been in a position to honour its obligations towards the controlled company, enabling it to pursue its activity, partly because of the considerable investment made within the framework of the restructuring plan launched in 1999-2000 and of the recapitalisation that took place in 2003-2004. As indicated in recital 75, the undertaking seems not, therefore, to be in difficulty, meaning that the guidelines on rescuing and restructuring are not applicable.

(88) The decision to initiate the procedure also stated, as a subsidiary point, that, even if it were deemed acceptable (*quod non*, at this stage of the procedure) to apply the compensation principle described in point 11.3 of the Guidelines to Sadam ISZ, the reference period chosen by the Italian authorities for calculating the aid would be wrong. Since it was not deemed acceptable, for the reasons explained above, to apply point 11.3 of the Guidelines, there is no reason for examining this last doubt raised when the decision was taken to initiate the procedure.

VII. **CONCLUSION**

(89) In view of the foregoing considerations, the Commission considers that the State aid of EUR 3,5 million that Italy is considering granting to the Villasor sugar refinery belonging to Sadam ISZ is not compatible with the common market,

HAS ADOPTED THIS DECISION:

Article 1

The State aid of EUR 3,5 million that Italy is considering granting to the Villasor sugar refinery belonging to Sadam ISZ is not compatible with the common market.

([40]) OJ C 288, 9.10.1999, p. 2.
([41]) Commission letter SG(2000) D/103781 of 19 May 2000. http://ec.europa.eu/community_law/state_aids/agriculture-1999/n157-99.pdf
([42]) Judgment of the Court of First Instance of 15 June 2005, *Regione autonoma della Sardegna* v *Commission*, Case T-171/02 [2005] ECR II-2123, paragraph 129.

Accordingly, the granting of the aid is not authorised.

Article 2

This Decision is addressed to the Italian Republic.

Done at Brussels, 16 July 2008.

For the Commission
Mariann FISCHER BOEL
Member of the Commission