STATE AIDS (ELECTRONICS): THE SELECO CASE

Subject: State aids
Recovery
Statement of reasons

Industry: Electronics

Parties: Italian Republic
SIM 2 Multimedia SpA
Commission of the European Communities
Seleco SpA
Ristrutturazione Elettronica SpA

Source: Judgment of the Court of Justice of the European Communities, dated 8 May 2003 in Joined Cases C-328/99 and C-399/00 (*Italian Republic and SIM 2 Multimedia SpA v Commission of the European Communities*)

(Note. This action, which was partly successful, challenged a Commission decision requiring the recovery of illegally paid state aid. The Commission's case failed partly on account of its inadequate statement of reasons for its decision and partly for providing no evidence on the valuation of the financial benefits to the firm in question. The judgment offers an invaluable guide to the law on the recovery of illegally paid state aid.)

Judgment

1. By application lodged at the Court Registry on 1 September 1999 and registered under the number C-328/99, the Italian Republic brought an action under the first subparagraph of Article 230 of the EC Treaty for:
- annulment of Commission Decision 2000/536/EC of 2 June 1999 concerning State aid granted by Italy to Seleco SpA (hereinafter, the contested decision), and
- in the alternative, annulment of that decision in so far as it requires the Italian Republic to take the necessary measures to recover from Seleco SpA the incompatible aid granted by Ristrutturazione Elettronica SpA (hereinafter, REL) in 1996 and in so far as it requires the Italian Republic to adopt the necessary measures to recover from Seleco Multimedia Srl (hereinafter, Multimedia) and from any other undertaking which benefited from asset transfers the incompatible aid granted to Seleco, for the part not recoverable from the latter.

2. By application lodged at the Registry of the Court of First Instance on 6 September 1999 and registered under number T-195/99, SIM 2 Multimedia SpA (hereinafter, SIM Multimedia), legal successor to Multimedia, brought an action to annul Article 2(1) of the contested decision in so far as it requires the Italian Republic to take all the necessary measures to recover from Multimedia the

incompatible aid granted to Seleco, with regard to the part not recoverable from the latter.

[Paragraphs 3 and 4 concern the transfer of the second case to the Court of Justice and the joining of the two cases for the purposes of oral procedure and judgment.]

Legal background

5. Under Article 87(1) of the EC Treaty:
Save as otherwise provided in this 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.

6. The first subparagraph of Article 88(2) of the EC Treaty provides:
If, after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the common market having regard to Article 87, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission.

7. In accordance with Article 88(3) of the EC Treaty:
The Commission shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. If it considers that any such plan is not compatible with the common market having regard to Article 87, it shall without delay initiate the procedure provided for in paragraph 2. The Member State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision.

Facts in the proceedings

The parties concerned

8. Seleco was active in the consumer electronics market and, more specifically, in the sector of colour television sets, decoders for encrypted programmes and video projectors and monitors.

9. Multimedia was established in 1995. In March 1996 Seleco hived off its most profitable activities (video projectors and monitors) to Multimedia, providing ITL 29 billion in capital and becoming its sole owner. In June 1996, Multimedia was converted into a company limited by shares. In July 1996, Seleco sold 33.33% of the shares which it held in Multimedia to Italtel and 33.33% to Friulia SpA. Each package of shares was sold for ITL 10 billion. The remaining shares were transferred to a shell company belonging to Seleco and then sold to a private company at a public sale by court order which took place on 20 December 1997 in the context of the liquidation of Seleco.

[Paragraphs 10 to 16 amplify the foregoing facts.]

17. After it learned that the aid granted to Seleco, which had been notified to it by the Autonomous Region of Friulia-Venezia Giulia, had already been

implemented and that REL had partly written off its claims on Seleco under an agreement concluded in 1994 for the purpose of covering the losses for the financial year 1993, the Commission decided on 27 September 1994 to initiate the procedure laid down in Article 93(2) of the EC Treaty (now Article 88(2). After subsequently learning from press reports that other public aid had been granted to Seleco, the Commission extended that procedure to those other measures by decision of 3 February 1998.

18. That procedure ended in the adoption of the contested decision, the operative part of which is worded as follows:

Article 1
The following aid granted by Italy to Seleco SpA is hereby declared incompatible with the common market:
(a) the partial write-off in 1994 by Ristrutturazione Elettronica SpA of ITL 16.8 billion on a loan of ITL 82 billion;
(b) the repurchase in 1996 by Seleco SpA of its outstanding debt to Ristrutturazione Elettronica SpA of ITL 65.2 billion for ITL 20 billion;
(c) the conversion into shares by Friulia SpA of an ITL 6 billion loan granted by it in 1992;
(d) a capital injection of ITL 7 billion by Friulia SpA in 1994;
(e) a convertible loan of ITL 12 billion at 7% granted by Friulia in 1996 and guaranteed by a lien on four industrial brands owned by Seleco.

Article 2
1. Italy shall take all the necessary measures to recover the aid referred to in Article 1, which has already been granted unlawfully, from Seleco SpA and, additionally, with regard to the part not recoverable from Seleco, from Seleco Multimedia srl and any other firm which benefited from asset transfers designed to frustrate the effects of this decision.
2. Recovery shall be effected in accordance with the procedures of national law. The aid to be recovered shall include interest from the date on which it was made available to the recipient until the date of its recovery. Interest shall be calculated on the basis of the reference rate used for calculating the net grant equivalent of regional aid applicable at the time the aid was granted.

Article 3
Italy shall inform the Commission, within two months of notification of this Decision, of the measures taken to comply with it.

Article 4
This Decision is addressed to the Italian Republic.

19. In those circumstances, the Italian Republic and SIM Multimedia brought the present actions against the contested decision.

Substance

20. The action brought by the Italian Government calls in question the categorisation of the operations by REL and Friulia as State aid, the requirement to recover from Seleco the alleged aid which REL granted to it in 1996 and the requirement to cover the so-called State aid from SIM Multimedia.

Classification of the operations by REL and Friulia as State aid

[Paragraphs 21 et seq set out the arguments of the parties.]

Findings of the Court

31. It is appropriate, first, to consider whether the operations carried out by Friulia referred to in Article 1(c), (d) and (e) of the contested decision, mentioned *inter alia* in paragraph 18 of the present judgment, must be regarded as having been carried out by means of State resources within the meaning of Article 87(1) of the EC Treaty.

32. In that regard, although the Italian Government claims that Friulia's private partners have wide powers of decision-making and of disinvestment, it does not deny the Commission's claim that the company was under the control of the Region of Friulia-Venezia Giulia.

33. The financial resources of a private-law company such as Friulia, 87% of which is held by a public authority such as the Region of Friulia-Venezia Giulia and which acts under the control of that authority, may be regarded as State resources within the meaning of Article 87(1) of the EC Treaty (see, to that effect, Case 323/82, *Intermills* v *Commission*, paragraph 32, and Joined Cases 67/85, 68/85 and 70/85, *Van der Kooy* v *Commission*, paragraphs 36 and 38). The fact that Friulia participated using its own funds is irrelevant in that regard. For those funds to be categorised as State resources, it is sufficient that, as in the present case, they constantly remain under public control and therefore available to the competent national authorities (see, to that effect, Case C-482/99, *France* v *Commission*, paragraph 37).

34. It follows that the Commission was right in holding in the contested decision that Friulia's operations were carried out by means of State resources, within the meaning of Article 87(1) of the EC Treaty.

35. Next, it must be borne in mind that the aim of Article 87 of the EC Treaty is to prevent trade between Member States from being affected by advantages granted by public authorities which, in various forms, distort or threaten to distort competition by favouring certain undertakings or certain products. The notion of aid can thus encompass not only positive benefits such as subsidies, loans or direct investment in the capital of enterprises, but also interventions which in various forms mitigate the charges which are normally included in the budget of an undertaking and which therefore, without being subsidies in the strict sense of the word, are of the same character and have the same effect (see Case 234/84, *Belgium* v *Commission*, paragraph 13, and Case C-39/94, *SFEI and Others*, paragraph 58).

36. It is settled case-law that investment by the public authorities in the capital of an undertaking, in whatever form, may constitute State aid where all the conditions set out in Article 87(1) of the EC Treaty are fulfilled (see, in particular, Case C-142/87, *Belgium* v *Commission* (*Tubemeuse*), paragraph 25; Joined

Cases C-278/92 to C-280/92, *Spain* v *Commission*, paragraph 20, and *France* v *Commission*, cited above, paragraph 68).

37. It should also be noted that, pursuant to the principle that the public and private sectors are to be treated equally, capital placed directly or indirectly at the disposal of an undertaking by the State in circumstances which correspond to normal market conditions cannot be regarded as State aid (Case C-303/88, *Italy* v *Commission*, paragraph 20).

38. Therefore, in accordance with equally settled case-law, it is necessary to determine whether, in similar circumstances, a private investor of a dimension comparable to that of the bodies managing the public sector could have been prevailed upon to make capital contributions of the same size (Case C-261/89, *Italy* v *Commission*, paragraph 8; *Spain* v *Commission*, cited above, paragraph 21; and Case C-42/93, *Spain* v *Commission*, paragraph 13), having regard in particular to the information available and foreseeable developments at the date of those contributions (*France* v *Commission*, paragraph 70).

39. Since that involves a complex economic appraisal, in reviewing an act of the Commission which has necessitated such an appraisal, the Court must confine itself to verifying whether the Commission complied with the relevant rules governing procedure and the statement of reasons, whether the facts on which the contested finding was based have been accurately stated and whether there has been any manifest error of assessment or a misuse of powers (see *inter alia* Case C-56/93, *Belgium* v *Commission*, paragraph 11).

40. In this case, therefore, it is necessary to assess whether, in similar circumstances, a private investor of a dimension comparable to that of REL or Friulia could have been prevailed upon to make capital contributions of the same size, having regard in particular to the information available and foreseeable developments at the date of those contributions.

41. First, the parties agree that, at the time of the first recapitalisation of Seleco, that company's financial situation was poor...

42. Secondly, Seleco's restructuring plan for 1993 to 1996, which was the second since the beginning of the decade, forecast a return to profitability in 1995, while the first plan, which covered the period 1990 to 1993, had forecast a return to significant profits in 1993 (point 68 of the grounds of the contested decision). However, at the request of Friulia, the restructuring plan for 1993 to 1996 was studied by KPMG Peat Marwick Corporate Finance, an independent outside expert, which came to the conclusion that it was too ambitious, on the basis of both the firm's position and the plan's underlying assumptions...

43. Thirdly, it is clear from the minutes of Seleco's general meeting of 1 February 1994, a copy of which is attached to the Italian Government's application, that REL, whose representatives took part in several meetings with representatives of the Ministry of Industry and the Presidency of the Council, had stated that it was ready, in view of the interests linked to employment, to cover the amount of the

losses which exceeded the company's net assets in proportion to its shares, by partially waiving the debt owed it by Seleco.

44. It follows from the foregoing that, as regards the recapitalisation of Seleco in 1994, neither Friulia nor REL acted like a private investor operating under normal market conditions. A private investor would not, under those conditions, have made the capital contributions made by Friulia or REL to an undertaking in difficulty such as Seleco without having a credible and realistic restructuring plan or taking social concerns into account (see, as regards the latter point, Case C-303/88, *Italy* v *Commission*, cited above, paragraphs 18 and 24), and thus not seeking to ensure the likelihood of profitability for such contributions.

45. The Commission was therefore right to consider that REL and Friulia could not expect that the capital contributions made in the context of the 1994 recapitalisation of Seleco would generate an acceptable profit for a private investor operating under normal market conditions.

46. Accordingly, it must be held that the interventions by REL and Friulia in the first recapitalisation of Seleco constitute State aid within the meaning of Article 87(1) of the EC Treaty.

47. As regards the second recapitalisation of Seleco, it must be pointed out that Seleco showed a loss of ITL 64.2 billion for the financial year 1995, almost twice the amount of its equity capital, although the company's restructuring plan for 1993 to 1996 counted on a return to profitability in 1995.

48. Since Seleco's restructuring plan had proved to be unachievable, and in the absence of any information concerning any other restructuring plan which would make it possible in the present case to consider that second intervention acceptable, the Commission was entitled to take the view that no informed private investor operating under normal market conditions would have made the capital contributions that REL and Friulia made to Seleco at the time of its recapitalisation in 1996, since its financial situation remained poor, and indeed critical.

49. Therefore, the interventions by REL and Friulia in the second recapitalisation of Seleco also constituted State aid within the meaning of Article 87(1) of the EC Treaty.

50. The first plea put forward by the Italian Government must therefore be rejected.

The obligation to recover the aid REL granted Seleco in 1996

[Paragraphs 51 and 52 set out the arguments of the parties.]

53. In that respect, it must be borne in mind that it is settled case-law that recovery of unlawful aid is the logical consequence of a finding that it is unlawful

(see, in particular, *Tubemeuse*, cited above, paragraph 66, and Case C-261/99, *Commission* v *France*, paragraph 22).

54. Accordingly, since the repurchase in 1996 by Seleco of its outstanding debt to REL of ITL 65.2 billion for ITL 20 billion constitutes unlawful State aid, the Commission is entitled to order the Italian Republic to take the necessary measures to recover it (see, to that effect, Case 310/85. *Deufil* v *Commission*, paragraph 24).

55. The fact that REL must return ITL 20 billion to the bankrupt company and apply for its earlier unsecured claim of ITL 65.2 billion to be registered among the liabilities of Seleco, even assuming it to be established, cannot in this instance call in question the principle that unlawful aid must be recovered.

56. Accordingly, the second plea of the Italian Government must be rejected.

The obligation to recover State aid from Multimedia

57. The contested decision, in so far as it requires the Italian Republic to recover the aid at issue from Multimedia, is the subject of several pleas in law put forward as grounds for annulment. The Italian Government and SIM Multimedia both put forward a plea alleging infringement of the right to a fair hearing. SIM Multimedia also puts forward pleas alleging the non-existence of State aid to Multimedia, inadequacy of and contradictions in the statement of reasons for the contested decision, and disproportion between the recovery order to the detriment of Multimedia and the size of the branch of the undertaking at issue.

58. It is appropriate first to consider the plea alleging non-existence of aid to Multimedia.

[Paragraphs 59 et seq set out the arguments of the parties.]

65. As a preliminary observation, it should be pointed out that, in accordance with Community law, when the Commission finds that aid is incompatible with the common market, it may order the Member State to recover that aid from the recipient (Case 70/72, *Commission* v *Germany*, paragraph 20).

66. The recovery of unlawful aid is the logical consequence of a finding that it is unlawful (see *Tubemeuse*, paragraph 66) and seeks to re-establish the previously existing situation (Case C-382/99, *Netherlands* v *Commission*, paragraph 89).

67. Article 2(1) of the contested decision provides that the Italian Republic is to take all the necessary measures to recover the incompatible aid identified by the Commission, and which has already been granted unlawfully, from Seleco SpA and, additionally, with regard to the part not recoverable from Seleco, from Multimedia and any other firm which benefited from asset transfers designed to frustrate the effects of the contested decision.

68. The Commission, in giving the reasons for that element of the operative part of the contested decision, was right to observe in point 113 that in order to ensure that the decision is implemented correctly the Member State is required to act like a private creditor.

69. The Commission was also right to state in points 113 to 115 of the grounds of the contested decision, that:
- ... To ensure that the Commission decision is implemented correctly, the Member State is required ... to recover the aid without delay, using all the legal means at its disposal, including seizure of the firm's assets and, where necessary, its liquidation if it is unable to repay the amounts in question. The proceeds of the sale of the assets allow the creditors, including the Member State, to be repaid even if they are not sufficient to cover all the debts of the firm and even if, consequently, the aid is not recovered in full. In such circumstances, the liquidation of the firm is still important from a competition standpoint as it frees the market segment previously held by the firm and makes it available to creditors, while giving them the opportunity to acquire the assets and reallocate them more effectively.
- There are, however, circumstances which can hamper that process, jeopardise the effectiveness of the recovery decision and frustrate the rules on State aid. Such is the case when, following a Commission investigation or decision, the assets and liabilities of the firm as an ongoing concern are transferred to another firm controlled by the same persons at below-market prices or by way of procedures that lack transparency. The purpose of such a transaction can be to place the assets out of reach of the Commission decision and to continue the economic activity in question indefinitely.
- As in any other recovery procedure, the Member State must, like any other diligent creditor, exhaust all the legal instruments available under its own legal system, such as those used to combat fraud against creditors in the form of acts carried out by the firm in liquidation during the suspect period prior to the bankruptcy, which would allow such acts to be declared invalid.

[Paragraphs 70 et seq describe the arrangements made for hiving off Seleco's activities, assets and debts. The facts were not disputed.]

72. In the present case, it is also common ground that the value of the multimedia branch transferred by Seleco to Multimedia in exchange for all of the latter's shares had been estimated by a sworn expert appointed by the national court for that purpose. It is also common ground that the price Friulia and Italtel paid for the purchase of two thirds of the shares which Seleco held in Multimedia, which took place several months after that transfer, in effect corresponded to two thirds of the value of the multimedia branch, as estimated by the above-mentioned sworn expert. The Commission has not put forward any concrete evidence that that expert estimated the value of the multimedia branch transferred by Seleco to Multimedia taking into account the risk that the latter company might be required, should the case arise, to repay all or part of the aid granted to Seleco.

73. It is further not in dispute that the administrator appointed by the court in Seleco's bankruptcy did not act to revoke the transfer by Seleco of the two thirds of the shares which it held in Multimedia.

74. Finally, it is clear from the documents before the Court that the expert's report produced at the end of 1997 at the request of the bankruptcy court set the value of Multimedia's trading capital considerably lower than what had been estimated in the previous expert's report.

75. In those circumstances, the question arises whether Multimedia should also be considered as having been a beneficiary of the aid.

76. In that regard, it is appropriate to point out that the possibility of a company in economic difficulties taking measures to rehabilitate the business cannot be ruled out *a priori* because of requirements relating to recovery of the aid which is incompatible with the common market.

77. However, as the Commission is essentially maintaining before the Court, if it were permissible, without any condition, for an undertaking experiencing difficulties and on the point of being declared bankrupt to create, during the formal inquiry into the aid granted it, a subsidiary to which it then transfers its most profitable assets before the conclusion of the inquiry, that would amount to accepting that any company may remove such assets from the parent undertaking when aid is recovered, which would risk depriving the recovery of that aid of its effect in whole or in part.

78. Thus the Commission pointed out at points 116 and 117 of the grounds of the contested decision that:
- in order to prevent the effectiveness of the decision to recover the aid from being frustrated and the market from continuing to be distorted, the Commission may be compelled to require that the recovery is not restricted to the original firm but is extended to the firm which continues the activity of the original firm, using the transferred means of production, in cases where certain elements of the transfer point to economic continuity between the two firms;
- the elements examined by the Commission include the purpose of the transfer (assets and liabilities, continuity of the workforce, bundled assets, etc.), the transfer price, the identity of the shareholders or owners of the acquiring firm and of the original firm, the moment at which the transfer was carried out(after the start of the investigation, the initiation of the procedure or the final decision) and, lastly, the economic logic of the transaction.

79. In this case, it is, admittedly, relevant to point out, as the Commission does in points 118 and 119 of the grounds of the contested decision, that:
- Seleco hived off in March 1996 its most profitable assets to Multimedia, injecting ITL 29 billion into the capital of that company;
- that transaction, which helped to deprive Seleco of its substance in two respects (activities and capital), occurred at a time when the Commission had initiated the procedure laid down in Article 93(2) of the Treaty;

- it is likely that the transaction was not limited to a transfer of assets and that the transfer of Seleco's main activities was accompanied by the transfer to Multimedia of the corresponding workforce (or part of it) and hence of its social security debts at the very least;
- after Seleco sold two thirds of its shares in Multimedia, the latter remained under the control of Seleco and/or Friulia (which was itself Seleco's third shareholder and which had granted Seleco a convertible loan of ITL 12 billion).

80. However, it must be observed that, in that statement of reasons, the Commission makes no mention of the price of the transfer, although it referred to that element in the contested decision as one of the two which had to be taken into account.

[Paragraphs 81 to 83 refer to the Commission's assumptions.]

84. In addition, the Commission did not take into account in the contested decision the consequences of the obligation on the part of the Italian Republic to recover the unlawful aid from Multimedia with regard to the private company which, at a court-ordered public sale as part of the liquidation of Seleco, bought the final third of the shares in Multimedia.

85. In the light of the foregoing, it is apparent that the statement of the reasons on which the contested decision is based is inadequate for the purposes of Article 253 of the EC Treaty, in particular as regards the alleged irrelevance of the fact that the shares in Multimedia were bought at a price which seemed to be the market price, although that point was required also to be taken into account in the present case.

86. In those circumstances, Article 2(1) of the contested decision must be annulled in so far as it provides that the Italian Republic is to take all the necessary measures to recover the aid referred to in Article 1 from Multimedia, with regard to the part not recoverable from Seleco.

87. The remainder of the application is dismissed.

[Paragraphs 88 and 89 deal with costs, referred to in the ruling below.]

Court's Ruling

The Court hereby: 1. Annuls Article 2(1) of Commission Decision 2000/536/EC of 2 June 1999 concerning State aid granted by Italy to Seleco SpA in so far as it provides that the Italian Republic is to take all the necessary measures to recover the aid referred to in Article 1 from Seleco Multimedia Srl with regard to the part not recoverable from Seleco SpA;
2. Dismisses the remainder of the application;
3. Orders, in Case C-328/99, the Italian Republic and the Commission of the European Communities to bear their own costs;
4. Orders, in Case C-399/00, the Commission of the European Communities to pay the costs. ■