EUROPEAN COMMISSION

Brussels, 2.4.2008
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In the published version of this decision, some information has been omitted, pursuant to articles 24 and 25 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus […].

PUBLIC VERSION

WORKING LANGUAGE

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Subject: State Aid N° N 582/2007 – Germany
Aid to Propapier PM 2 GmbH & Co. KG - LIP

Sir,

1. PROCEDURE

(1) By letter dated 8 October 2007, registered at the Commission on the same day, the German authorities, pursuant to Article 88(3) of the EC Treaty, notified under the Guidelines on national regional aid ("RAG")[1] their intention to grant regional aid for a large investment project in favour of Propapier PM 2 GmbH & Co. KG.

(2) By letters of 7 December 2007 (D/54886) and 1 February 2008 (D/50445), the Commission requested supplementary information which was provided by the German authorities by letters of 3 January 2008 (A/113) and 14 February 2008 (A/2855).

(3) Two formal complaints concerning the notified aid were forwarded to Germany for comments by letter of 29 January 2008 (D/50383) to which the German authorities replied by letter of 6 February 2008 (A/2266).

1 OJ C 54, 4.3.2006, p. 13.

Seiner Exzellenz Herrn Frank-Walter STEINMEIER
Bundesminister des Auswärtigen
Werderscher Markt 1
D - 10117 Berlin

(4) On 25 January 2008 a meeting was held between the Commission services and the German authorities where also representatives of the beneficiary of the aid were present.

2. DESCRIPTION OF THE MEASURE

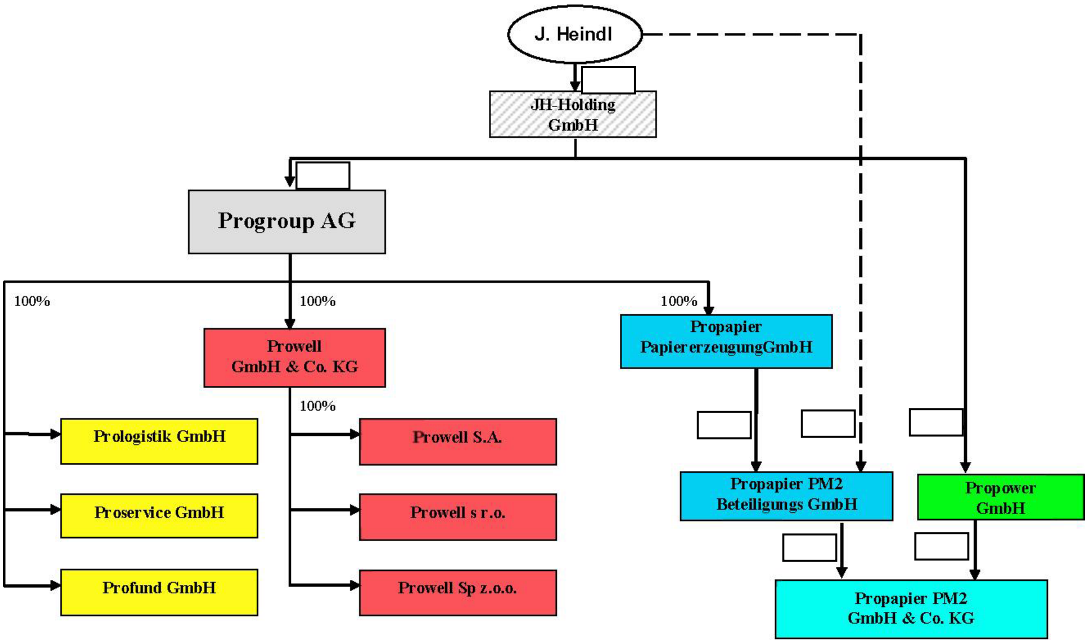
2.1. Objective

(5) Germany intends to promote regional development by providing regional investment aid to Propapier PM 2 GmbH & Co. KG (hereinafter: Propapier PM 2) for the setting up of a new paper mill and a related power plant in Eisenhüttenstadt, Brandenburg-Nordost, an assisted area pursuant to Article 87(3)(a) of the EC Treaty with a regional aid ceiling of 30% gross grant equivalent (GGE) under the regional aid map of Germany 1.1.2007 – 31.12.2013[2].

2.2. The beneficiary

(6) The German authorities specified that the beneficiary of the aid is Propapier PM 2, which is a large enterprise.

(7) The following chart shows the structure of the Progroup AG to which Propapier PM 2 belongs:



(8) The corporate relationship between the aid recipient and the group can be described as follows: […]* % of the capital of Propapier PM2 is held by

[2] State aid N 459/2006. OJ C 295, 5.12.2006, p. 6.

* Business secret

Propapier PM2 Beteiligungs GmbH in its capacity as a personally liable member. Propapier PM 2 Beteiligungs GmbH is owned […] % by Propapier Papiererzeugung GmbH and […] % by Mr Jürgen Heindl. The sole owner of Propapier Papiererzeugung GmbH is Progroup AG, in which Mr Jürgen Heindl holds […] % of the shares through JH-Holding GmbH. The remaining […] % of the shares in Progroup AG are distributed as follows: two shareholders each have a holding of […] % and a further shareholder has a share of […] %. None of these shareholders has any special voting rights.

(9) Progroup AG (hereinafter: Progroup) produces and sells corrugated case material and corrugated board through its subsidiaries. Corrugated board is produced in five (soon in six) plants in Europe by Prowell GmbH & Co. KG and its subsidiaries, i.e. Prowell S.A. in France, Prowell s r.o. in the Czech Republic and from end 2008 Prowell Sp.z.o.o. in Poland. Corrugated case material is at present produced by Propapier Papiererzeugung GmbH. The other companies belonging to Progroup offer services in connection with the sale of corrugated board.

(10) The major part of the investment project, i.e. the setting up of the paper mill, is to be carried out and operated by the beneficiary itself. The power plant providing steam end energy for the production process is, on the other hand, to be set up and financed by Propower GmbH (hereinafter: Propower), a company belonging to the same group as the beneficiary and having a […] % stake in Propapier PM 2. A leasing agreement between the parties will convey the right to use the power plant to Propapier PM 2.[3]

(11) Germany explained that under the German tax law economic goods forming part of the special business assets of a member (in this case, Propower) of a commercial partnership (in this case, Propapier PM 2) are allocated for tax purposes to the assets of the commercial partnership and not to those of the member, even if that member is the civil law owner of the asset. This is a consequence of the tax transparency of commercial partnerships. Consequently, Propapier PM 2 will be able to claim the aid for the whole investment project, including the power plant. This approach corresponds to the established practice of the German tax authorities.

2.3. The investment project

2.3.1. Products and technology

(12) The aid is granted for the setting up of a new paper mill and a related power plant in Eisenhüttenstadt, Brandenburg.

(13) The paper mill will produce two types of corrugated case material (hereinafter: CCM), namely testliner up to 150 g/m^2 and fluting made from recycled fibre. The liner constitutes a flat inner or outer layer whereas the fluting is the undulated layer. CCM is the base paper to manufacture corrugated boards (corrugated board

[3] The reason for such an arrangement is that the investor would like to avoid […] of the investment in the power plant on […] of the group in its core business, i.e. the production of corrugated case material and corrugated board.

is made by combining two layers of liner board with a layer of fluting in between), which are converted into corrugated boxes used for packaging.

(14) A large part (approx. 75 %) of the CCM produced in the aided plant will be used within Progroup for the production of the downstream product, i.e. corrugated board. Progroup sells corrugated board as their final product on the market. The part of CCM not used internally will be sold to third parties. Prougroup is not involved in producing the final product, i.e. the boxes.

(15) The paper plant will include waste paper recycling equipment, a paper machine for producing CCM, an operational building, a spare parts store, workshop buildings and a paper roll warehouse.

(16) The power plant is to be set up primarily to generate the steam which is needed for the production process. In order to make efficient use of heat energy, the power plant may be used simultaneously to generate electricity, covering approx. [<50] % of Propapier PM 2's electricity need. The power plant will mainly burn production waste and thus also reduces the dependence of the paper mill on fossil fuel.

2.3.2. Project implementation

(17) The investment project started in December 2007 and is expected to be implemented by mid-2010. Total capacity of 615 000 tons of CCM per annum is scheduled to be reached gradually by 2015.

2.4. Eligible expenditures

(18) The eligible investment costs are calculated on the basis of the costs relating to initial investment. The eligible expenditure in the meaning of the RAG amounts to EUR 643 862 500 in nominal value, which is EUR 586 722 900 in discounted value. Table 1 below provides the breakdown of eligible expenditure for the execution of the investment project in nominal values.

Table 1. Breakdown of the eligible project costs relating to initial investment (thousand EUR, nominal values)

Buildings	[…]
Installations and equipment	[…]
Other costs	[…]
Total eligible costs	**643 862.5**

(19) The category 'other costs' includes among others interior design, informatics costs and software licences. The German authorities confirmed that software licences worth EUR […] will only be used in the establishment receiving the aid, they will be regarded as amortizable assets, will be purchased from third parties and will remain in the establishment receiving the aid for five years.

2.5. Financing of the investment

(20) Some 73 % of total project costs will be financed through bank loans free of any aid (in particular, the loans will not be covered by a public guarantee). Another 14% is funded from own resources, while the balance is financed through the aid.

(21) It follows that the beneficiary will make a contribution of more than 25% of the total eligible expenditure of EUR 643.9 million which will be free of any public support.

2.6. Legal basis

(22) The indicated legal basis for the aid is the following:

- Investitionszulagengesetz 2007 vom 15. Juli 2006 in der Fassung der Bekanntmachung vom 23. Februar 2007 (BGBl. 2007 I S. 282);
- Gesetz über die Gemeinschaftsaufgabe „Verbesserung der regionalen Wirtschaftsstruktur“ vom 6.10.1969 (BGBl. I S. 1861), zuletzt geändert durch Art. 102 der Verordnung vom 25.11.2003 (BGBl. I S. 2304), in Verbindung mit dem 36. Rahmenplan der Gemeinschaftsaufgabe „Verbesserung der regionalen Wirtschaftsstruktur“ (GA) für den Zeitraum 2007 bis 2010 (BT-Drs. 16/5215 vom 27.04.2007);
- Richtlinie des Ministeriums für Wirtschaft zur Förderung der gewerblichen Wirtschaft im Rahmen der Gemeinschaftsaufgabe “Verbesserung der regionalen Wirtschaftsstruktur“ – GA – (GA-G) vom 7.12.2006 (ABl. für Brandenburg Nr. 51 vom 27.12.2006, S. 798);
- Landeshaushaltsordnung (LHO) vom 21.04.1999 (GVBl. I/99, S. 106) mit den dazugehörigen Verwaltungsvorschriften (VV-LHO).

2.7. The aid measure

2.7.1. Form and amount of the aid

(23) Aid is granted under the existing block-exempted schemes XR 6/07[4] on investment premium and XR 31/07[5] on investment grants under the joint task scheme for the improvement of regional economic structure (Gemeinschaftsaufgabe - GA).

(24) Under the scheme XR 6/07 a tax-free investment premium is paid retrospectively each year for the part of the investment costs incurred during the previous year. The amount of this aid is 15 % of the part of eligible costs incurred until end 2009, with a planned amount of EUR 81 279 300 in nominal terms (71 095 700 in discounted value). The investment premium will be paid between 2008 and 2010.

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[4] OJ C 41, 24.2.2007, p. 9. Scheme implemented under Commission Regulation (EC) No 1628 of 24 October 2006 on the application of Articles 87 and 88 of the Treaty to national regional investment aid.

[5] OJ C 102, 5.5.2007, p. 11. Scheme implemented under Commission Regulation (EC) No 1628 of 24 October 2006 on the application of Articles 87 and 88 of the Treaty to national regional investment aid.

(25) In addition, since eligible costs will also be incurred after 2009 for which no investment premium can be granted under the scheme XR 6/07, a GA grant is to be awarded under XR 31/07. The exact amount of the GA grant will depend on the investment premium paid until 2010; however, it will be established so that the combined amount of the investment premium and the GA grant respects the applicable maximum aid intensity for this project. Since the German authorities indicated that the amount of investment premium will be between EUR […] and EUR […] in nominal terms (between […] and EUR […] in discounted value), the amount of the GA-grant to be paid in 2010 will be between EUR […] and EUR […] in nominal terms (between EUR […] and EUR […] in discounted value).

(26) Consequently, the total amount of aid is limited to EUR 82 509 500 in nominal terms corresponding to EUR 72 145 700 in discounted value.

(27) The responsible granting authority is the Finanzamt Frankfurt (Oder) for the investment premium and the Investitionsbank des Landes Brandenburg for the GA-grant.

2.7.2. Cumulation

(28) The German authorities confirmed that no aid other than the above investment premium and GA-grant will be given to the notified project.

2.8. Maintenance of the assisted activity

(29) The German authorities confirmed that the investment project is required to be maintained for a period of five years from the day of its completion.

2.9. Incentive effect

(30) Before works on the project started, the beneficiary had applied for the aid and the German authorities confirmed in writing that, subject to the final outcome of a detailed verification, the project meets the conditions of eligibility (letter of the Investitionsbank des Landes Brandenburg of 24 May 2007).

2.10. Contribution to regional development

(31) Brandenburg-Nordost is a region with significant socio-economic handicaps where in 2004 GDP per capita was 76.3 % of EU-27 average[6] and the unemployment rate stood in 2005 at 19.8 %, equivalent to 220 % of the EU-27 average and 178 % of the German average.

(32) The investment project is expected to create 150 direct jobs, as well as three times as many indirect jobs. The investment in an advanced paper machine also reflects the intention of Eisenhüttenstadt to diversify its economic profile beyond that of a mono-structure focused on the metal industry. The production of CCM from

6 Measured in purchasing power standard.

recycled fibre is consistent with Eisenhüttenstadt's plan to establish a recycling industry in the city.

2.11. General commitments

(33) The German authorities have committed to submit to the Commission:

- within two months of granting the aid, a copy of the signed aid contract between the granting authority and the beneficiary;
- on a five-yearly basis, starting from the approval of the aid by the Commission, an intermediary report (including information on the aid amounts being paid, on the execution of the aid contract and on any other investment projects started at the same establishment/plant);
- within six months after payment of the last tranche of the aid, based on the notified payment schedule, a detailed final report.

3. ASSESSMENT OF THE AID MEASURE AND COMPATIBILITY

3.1. Existence of State aid in the meaning of Article 87(1) of the EC Treaty

(34) The financial support under the measure will be given by the German authorities in the form of direct grants and is financed through the budget of the state. The support can thus be considered as given by the Member State and through State resources within the meaning of Article 87 (1) of the EC Treaty.

(35) As the aid is granted to a single company, Propapier PM 2, the measure is selective.

(36) The financial support given to Propapier PM 2 will relieve the company from costs which it normally would have had to bear itself and therefore the company benefits from an economic advantage over its competitors.

(37) The financial support from the German authorities will be given for an investment resulting in the production of different types of CCM. Since these products are subject to trade between Member States, the support given is likely to affect trade between Member States.

(38) The favouring of Propapier PM 2 and its production by the German authorities means that competition is distorted or threatened to be distorted.

(39) Consequently, the Commission considers that the notified measure constitutes State aid to Propapier PM 2 within the meaning of Article 87(1) of the EC Treaty.

3.2. Legality of the aid measure

(40) By notifying the aid measure, the German authorities complied with the individual notification requirement expressed in paragraph 64 of the RAG.

3.3. Compatibility with the general provisions of the RAG

(41) The Brandenburg-Nordost region is entirely eligible for regional aid under Article 87(3)(a) of the EC Treaty.

(42) The notified aid is aid for initial investment, as defined in point 4.1 of the RAG.

(43) The eligible costs involve the costs of buildings and plant/machinery, in line with point 4.2 of the RAG.

(44) The beneficiary's own contribution free of any aid to the eligible costs is above the required 25% threshold (cf. point 4.1 of the RAG).

(45) The beneficiary applied for the aid and the German authorities confirmed in writing, before the start of work on the project that, subject to the final outcome of a detailed verification, the project meets the conditions of eligibility laid down by the scheme (cf. point 4.1 of the RAG).

(46) The investment will be maintained for at least 5 years after its completion (cf. point 4.1 of the RAG).

(47) The rules on cumulation of aid are respected (cf. point 4.4 of the RAG).

(48) The Commission therefore considers that the aid complies with the standard compatibility criteria laid down in the RAG.

3.4. Compatibility with the provisions for aid to large investment projects

3.4.1. Aid intensity (paragraph 67 of the RAG)

(49) With eligible expenditure of EUR 586 722 900 in discounted value and an applicable standard regional aid ceiling of 30% gross grant equivalent (GGE), the adjusted maximum aid intensity permitted in accordance with paragraph 67 of the RAG is 12.30% GGE.

(50) The total aid amount of EUR 72 145 700 in discounted value, which results in an aid intensity of 12.30% GGE respects this ceiling. Therefore, the proposed aid intensity is in line with the scaling down mechanism foreseen in paragraph 67 of the RAG.

(51) Germany confirmed that the indicated total amount of aid in discounted value of EUR 72 145 700 constitutes a cap which cannot be exceeded and that the maximum aid intensity to be approved (12.30%) will not be exceeded even if eligible costs in discounted value turn out to be lower than foreseen.

3.4.2. Compatibility with the rules under paragraphs 68(a) and (b) of the RAG

(52) Since the proposed total aid amount of approximately EUR 72 million exceeds the applicable notification threshold of EUR 22.5 million, the compliance of the proposed aid with paragraphs 68(a) and (b) of the RAG has to be assessed.

(53) Aid to large investment projects falling under point 68 of the RAG and where

- the beneficiary accounts for more than 25% of the sales of the product concerned before or on completion of the investment, or
- the capacity created by the project is more than 5% of the size of the market using apparent consumption data of the product concerned, unless the average annual growth rate of its apparent consumption over the past five years is above the annual growth rate of the EEA's GDP,

can be approved only after a detailed verification, following the opening of the procedure provided for in Article 88(2) of the Treaty, that the aid is necessary to provide an incentive effect for the investment and that the benefits of the aid measure outweigh the resulting distortion of competition.

(54) To carry out the relevant tests under paragraphs 68(a) and (b) of the RAG, the Commission has first to establish the relevant product and geographic markets.

Products concerned

(55) The investment project directly concerns two types of CCM, namely testliner up to 150 g/m^2 and fluting made from recycled fibre. Since an estimated 75% of the CCM produced in the aided facility will be used internally within Progroup for the production of the downstream product, the German authorities consider, in line with paragraph 69 of the RAG, that the downstream product, i.e. corrugated board, is also a product concerned by the investment project.

(56) The German authorities confirmed that feeding electricity generated by the power plant into the public grid is envisaged only exceptionally in situations where the paper machine is out of operation due to malfunction or maintenance and is, thus, unable to consume the energy which is generated. Therefore, the production of electricity is not considered as product concerned.

Relevant product market

(57) According to point 69 of the RAG, the relevant product market includes the product concerned and its substitutes considered to be such either by the consumer (by reason of the product's characteristics, prices and intended use) or by the producer (through flexibility of the production installations).

Corrugated case material (CCM)

(58) Germany submitted that the two types of CCM to be produced in the aided facility, i.e. testliner up to 150 g/m^2 and fluting made from recycled paper, belong to the overall CCM market, which includes in addition kraftliner and fluting made from virgin fibre, independently of their weight. Germany substantiated this by referring to the relations of substitutability between the different products. In particular, Germany argued the following.

(59) Flutings made from recycled fibre and from virgin fibre are substitutes both from a demand and supply side point of view. Fluting made from virgin fibre can be produced on the same production line as fluting made from recycled fibre, only an adjustment concerning the preparation of the raw material is necessary. The costs of this adjustment could however not be estimated. Moreover, fluting based on virgin fibre is in practice made from a mixture containing up to 40-50 % of recycled fibre.

(60) Fluting based on virgin fibre is approx. 15% more expensive than fluting made from recycled fibre only. However, for the consumer both products have the same basic characteristics and the same use. Consumers can substitute a heavier (e.g. 140 g/m^2) recycled fibre based fluting with a lighter (e.g. 127 g/m^2) fluting made from virgin fibre. The possibility to use lighter fluting based on virgin fibres compared to recycled fibres outweighs the price difference. The technical and price differences are, therefore, in balance.

(61) As regards substitutability between recycled fibre based testliner and virgin fibre based kraftliner the same applies: Germany claimed that they have the same use, and that the higher price for kraftliner is offset by the possibility to substitute a heavier testliner with a lighter kraftliner. Moreover, they both can be produced on the same production line with the only difference being the preparation of the raw material.

(62) Fluting and testliner are full substitutes from the supply side viewpoint, since every modern paper machine, including the beneficiary's, can produce both.

(63) Finally, CCM of different weights (i.e. below 150 g/m^2 and above) belong to the same relevant market, since their use is the same and they are substitutable for the consumer. There is moreover a tendency for heavier paper to lose market share to the benefit of lighter ones (currently CCM of more than 150 g/m^2 have a 5% share).

(64) Germany also referred to earlier State aid[7] and merger decisions[8] to substantiate its view that the relevant market is the overall CCM market. However, in earlier merger decisions referred to above, the Commission left the question of the relevant market open, especially as regards subdivision into virgin fibre based products and recycled fibre based products. Moreover, in State aid case N668/2002, Germany argued that CCM made from recycled paper and CCM made from virgin wood fibres should be considered as two distinct product markets. The reason indicated for this was that on the supply side, the use of wood instead of recycled paper would cause substantial additional costs and on the demand side, a price difference of 25% to 40% exists between the two products.

(65) Since the German authorities provided data also on the narrowest possible relevant market of testliner up to 150 g/m^2 and fluting made from recycled paper and, as shown below, the project does not raise concerns even on the basis of this market segment, the Commission considers that the question of the exact market definition can be left open in this case. The market tests were performed on the basis of two possible relevant market definitions, i.e. the overall CCM market and the market for testliner up to 150 g/m^2 and fluting made from recycled paper.

(66) As for the structure of the market, it should be noted that most producers of CCM are vertically integrated manufacturers of corrugated board and they produce

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[7] State aid N 668/2002 – Germany, Adolf Jass Schwarza GmbH; State aid C 72/2001 (ex N 361/01) – Germany, Hamburger AG.

[8] *Inter alia*, COMP/M.3935 – Jefferson Smurfit/Kappa; COMP/M.2391 – CVC/Cinven/Assidomän; COMP/M.2243 – Stora Enso/Assidomän/JV; COMP/M.2020 – Mestä-Serla/MODO.

CCM both for their own requirements as well as for sale to third parties on the open market. Some manufacturers are net buyers while others are net sellers of CCM. Detailed analysis provided by the German authorities showed that even those vertically integrated manufacturers, which produce in-house as much CCM (measured in tons) as they need for their production of corrugated board, are buying and selling CCM on the open market depending on concrete needs of sub-types of CCM and logistic requirements. Because of the dominant presence of vertically integrated manufacturers, high market shares in the open market (i.e. on the market of third party deliveries) do not necessarily mean market power. Nevertheless, for the sake of completeness, market shares were also calculated separately for the open market of CCM.

(67) It must be stressed in this respect that according to the provisions of paragraph 68 of the RAG capacity increase is calculated as a proportion of apparent consumption of the product concerned, which by definition[9] includes deliveries to third parties (i.e. sales on the open market) as well as in-house deliveries of CCM. This appears to be the appropriate benchmark to measure capacity increase since integrated producers, such as Progroup, use their production capacities to produce CCM both for in-house consumption and for sale on the open market. The size of the open market may vary according to business decisions concerning captive or open market sales much more than the overall consumption of CCM, determined by overall demand for the downstream product. Nevertheless, capacity increase relative to the size of the open market was also calculated.

Corrugated board

(68) Corrugated board will not be produced in the aided facility, but it is a downstream product concerned by the investment project.

(69) Germany submitted that corrugated board forms a standalone market from the supply side point of view, since machinery for the production of corrugated board cannot be converted even with substantial additional costs to manufacture other products.

(70) On the demand side, corrugated board packaging is closest to cardboard boxes, however, corrugated board packaging is lighter, more stable and cheaper. Therefore, consumers of corrugated board, i.e. the producers of corrugated boxes, cannot substitute it either with other products for the majority of packaging needs.

(71) Since the merger decisions referred to above also considered corrugated board to constitute a separate relevant product market, the Commission sees no reason to deviate from this previous practice and agrees with the proposal of the German authorities.

Relevant geographic market

Corrugated case material (CCM)

(72) According to Germany, the relevant geographic market for CCM is at least EEA-wide since within the EEA, there are no trade barriers or differences in technical

[9] Apparent consumption = Production – Exports + Imports

or legal requirements. There are no substantial price differences either. European producers occasionally deliver CCM even to China and the Middle East.

(73) Also in line with earlier State aid and merger decisions, the Commission considers therefore that the relevant geographic market for CCM is EEA-wide.

Corrugated board

(74) The definition of the relevant geographic market for corrugated board has to take account of the fact that corrugated board will not be produced at the aided plant, but will be manufactured by Progroup in other locations by using the CCM produced at the Eisenhüttenstadt facility. Propapier PM 2 will deliver CCM to plants belonging to Progroup located in Offenbach an der Queich, Burg and Schüttorf (Germany), as well as in Douvrin (France), Rokycany (Czech Republic) and in future (after its set up in […]) also to the plant in Strykow (Poland). These plants will in turn produce the downstream product, i.e. corrugated board.

(75) Earlier merger decisions[10] indicated that the corrugated board sheets may economically be transported for a distance of up to 400 km around the corrugator plant. Germany however submitted that for the purposes of the present decision the market should be defined EEA-wide for the following reasons.

(76) First, the largest Progroup factory in Burg ships over […] % of its corrugated board output in volume terms beyond 400 km and over […] % beyond 500 km and some […] % even between 700 and 1100 km. Considering all Progroup factories, the shipment distances are however smaller, with only […] % of the total shipments going beyond 400 km.

(77) For Progroup as a whole the share of transport costs of corrugated board remains on average below […] % of overall turnover up to a shipping distance of 600 km. This share however heavily depends on the quality type of corrugated board.

(78) Between […] and […] % of corrugated board shipments from the Progroup plants cross at least one country border, so even if markets were defined by plant, geographic markets would be supra-national.

(79) Circles with a 400 km radius around the Progroup plants producing corrugated board overlap and cover a large part of the EEA stretching from the UK to Poland and from Austria to Denmark. In this area about 68% of the total corrugated board production of the EEA takes place.

(80) Given that local markets overlap, there exists a chain of substitution effect which affects prices and competitive conditions throughout an area much larger than the selling radius of a given site. This effect works as follows: a decrease in price of one factory results in an expansion of its shipment area into one of its neighbouring competitors, which in turn reacts to decreasing demand for its product and the decline in capacity utilisation by a more aggressive price policy which will affect areas not reached by the initial expansion. The price effects are stronger the more pronounced the overlap between shipment areas is. In the corrugated board market the overlaps are substantial.

[10] E.g. COMP/M.3935 – Jefferson Smurfit/Kappa; COMP/M.2391 – CVC/Cinven/Assidomän.

(81) Finally, the average prices (calculated as the ratio of total turnover to total sales in m^2) vary by less than 10% between several different EEA countries where Progoup sells corrugated board. This should be considered as small, given that within Germany price fluctuations of a given type of corrugated board of up to 20% around the average can be observed.

(82) Given however, that Germany also provided data that allows calculating market shares only in the area covering the core delivery countries of Progroup (i.e. Czech Republic, France, Germany, the United Kingdom, the Netherlands and Poland) and these market shares, as shown below, do not give rise to concerns, the Commission leaves the question of defining the relevant geographic market for corrugated board open. Market shares are calculated both at the EEA-level and in the area covering only the core delivery countries of Progroup.

Market shares

(83) To examine whether the project is compatible with paragraph 68(a) of the RAG, the Commission has to analyse the market share of the aid beneficiary at group level before and after the investment. The investment project started in 2007 and will be implemented by 2010, while full capacity is foreseen to be reached by 2015. The German authorities indicated that independent data concerning apparent consumption on the relevant markets is not available for the year after full capacity is reached, i.e. 2016. Therefore, the Commission examined market shares in the year after completion of the investment, i.e. 2011 for which independent forecasts are already available. This is an acceptable approximation since 92% of the total capacity to be created by the project will already be available by then.

(84) To establish the market share of Progroup at group level the Commission compared its total deliveries (including sales to third parties as well as captive sales within the group) in volume and in value terms in the given year to apparent consumption on the relevant markets. Market shares were also calculated separately for the open market of CCM, i.e. taking into account non-captive sales of Progroup[11] and the total size of the market of third party deliveries.

(85) The figures on overall EEA-wide apparent consumption in volume and in value terms on the markets for CCM, for testliner up to 150 g/m^2 and fluting made from recycled paper as well as for corrugated board were compiled at the request of the beneficiary by Pöyry, a global consulting and engineering firm focusing on the energy, forest industry and infrastructure & environment sectors. Pöyry established data using its own database as well as data available in the public domain, e.g. in trade journals and from associations.

(86) Because of a lack of independent figures, data concerning the size of the open market were estimated by Germany on the basis of Pöyry capacity data for 2006. The method consisted in comparing for each integrated producer its production capacity of CCM and of corrugated board. If the capacity for corrugated board production is higher, this results in theory in a corresponding demand for the raw

[11] It should be noted in this respect that Progroup sells on the open market only recycled paper based CCM, i.e. testliner up to 150 g/m^2 and fluting made from recycled paper.

material, i.e. CCM, on the open market. To this extra demand of CCM by integrated producers comes in addition the demand for CCM on the open market by non-integrated corrugated board producers. Calculated this way, the size of the open market of CCM is approximately 37% of the total CCM market. This ratio was also used to estimate the size of the open market in 2011.[12]

(87) Since capacity data for recycled paper based CCM are not available separately, the above method could not be applied to estimate the size of the open market for testliner and fluting made from recycled paper. However, since recycled paper based CCM makes up some 70-80% of the total CCM market, this high proportion is very likely to apply also to the open market, which means that market shares of Progroup on the open market of recycled fibre based CCM are only slightly higher than on the open market of all types of CCM.

(88) Data concerning the size of the corrugated board market in the geographic area covering the core delivery countries of Progroup (i.e. Czech Republic, France, Germany, the United Kingdom, the Netherlands and Poland) was established on the basis of FEFCO[13] statistics which indicates that this area represents 58% of the total EEA-market.

(89) The market shares of Progoup in the relevant markets in the year before and after the investment are provided in Table 2 below.

Table 2: Market shares of Progroup at group level on the relevant markets

	2006		**2011**	
	In volume terms	In value terms	In volume terms	In value terms
Market share on overall CCM market in the EEA	[0-10] %	[0-10] %	[0-10] %	[0-10] %
Market share on the open market for CCM in the EEA	[0-10] %	[0-10] %	[0-10] %	[0-10] %
Market share on the overall market for testliner up to 150 g/m^2 and fluting made from recycled paper in the EEA	[0-10] %	[0-10] %	[0-10] %	[0-10] %
Market share on corrugated board market in the EEA (downstream product)	[0-10] %	[0-10] %	[0-10] %	[0-10] %
Market share on corrugated board market in core delivery countries	[0-10] %	[0-10] %	[0-10] %	[0-10] %

[12] Since, as noted above, integrated producers are active in open market transactions not only because of their insufficient capacities but also for logistic needs and depending on their concrete demand for different sub-types of CCM, this method actually underestimates the size of the open market and thus represents a worst-case scenario approach.

[13] FEFCO is Umbrella organization of European associations of corrugated board manufacturers.

(downstream product)				

(90) For all market definitions, Progroup's market share remains significantly below the 25% threshold stated in paragraph 68(a) of the RAG.

(91) Therefore, on the basis of the figures stated in the Table 2 above, the investment project under scrutiny is compatible with paragraph 68(a) of the RAG.

Production capacity

(92) The Commission also has to examine whether the investment project complies with paragraph 68(b) of the RAG. It needs to verify whether the capacity created by the project is less than 5% of the size of the market measured using apparent consumption data of the product concerned, unless the average annual growth rate of its apparent consumption over the last five years is above the average annual growth rate of the EEA's GDP.

(93) The Commission should first assess if the CCM market is underperforming in the EEA based on the average annual growth rate of its apparent consumption[14].

(94) The latest available data are those for the years 2001 to 2006. Based on these data, the compound annual growth rate (CAGR) of apparent consumption of CCM in the EEA was 2.15% in volume terms and 0.02% in value terms in the period 2001 to 2006. The CAGR of apparent consumption in the EEA of testliner up to 150 g/m^2 and fluting made from recycled paper was 3.25% in volume terms and 1.22% in value terms in the same period.

(95) As the CAGR of the European Economic Area's GDP[15] in the years 2001 to 2006 was 1.97% in constant prices (i.e. volume terms) and 3.98% in current prices (i.e. value terms), the CAGR of the consumption of CCM as well as of testliner up to 150 g/m^2 and fluting made from recycled paper was below the benchmark at least in value terms.

(96) Consequently the Commission verified whether the capacity created by the project is less than 5% of the size of the relevant market. The German authorities indicated that the total capacity to be created by the project is 615 000 tons of CCM (testliner up to 150 g/m^2 and fluting made from recycled paper) per annum, which corresponds to EUR […] million in value terms. At the same time, they indicated that apparent consumption of CCM in the EEA amounted to 23.363 million tons in 2006 (in value terms EUR 9 409.76 million). Apparent consumption in the EEA of testliner up to 150 g/m^2 and fluting made from recycled paper is indicated to have been 18.281 million tons in 2006 (in value terms EUR 6 752.698 million).

(97) Thus capacity created by the Propapier PM 2 project in Eisenhüttenstadt is 2.6% of the total CCM market ([<5] % in value terms), whereas it amounts to 3.4% of

[14] Footnote 62 of the RAG defines "apparent consumption of the product concerned" as "production minus export plus imports". Apparent consumption data was compiled by Pöyry.

[15] EU-27 data were used as a proxy.

the market for testliner up to 150 g/m^2 and fluting made from recycled paper ([<5] % in value terms). It follows that the capacity created by the project is below 5% of the markets concerned.

(98) Even if one were to calculate capacity increase as a proportion of open market sales of CCM only, the capacity created would be below 5%. In this case, only that part of total capacities created by the investment should be taken into account which is aimed at production for open market sales. According to Germany, this amounts to [<250 000] tons per annum (i.e. approximately [<40] % of the aided plant's total capacity of 615 000 tons). The German authorities expect this relatively low proportion of external sales of the aided paper mill to remain stable. The Commission considers that this is plausible, given that a new corrugated board plant will shortly be built by Progroup in Strykow, Poland, thus creating additional intra-group demand for CCM.

(99) The remaining part of capacities to be created, i.e. [>365 000] tons per annum will be applied to produce for intra-group use and therefore would have to be deducted from the size of the open market since this amount (which without the investment would have to be purchased by Progroup from third parties and would thus belong to the open market) will now be available internally within the group for further processing.

(100) Since total size of the open market for CCM in the EEA was estimated to be 8.6 million tons in 2006[16], capacity created by the project as a proportion of the size of the open market for CCM amounts to only [<3] % in volume terms[17].

(101) The size of the open market for recycled paper based CCM (i.e. testliner and fluting made from recycled paper) in the EEA could not be estimated by the German authorities. However, a complainant[18] (see section 3.5 below) indicated it to be 8.7 million tons. On this basis, capacity increase on the open market for recycled based CCM is again [<3] %[19] and remains well below the 5% threshold.

(102) As regards the downstream product, i.e. corrugated board, no production capacity is created by the project which aims to produce solely CCM (capacity increase for corrugated board 0%). This means that the 5%-threshold of paragraph 68(b) of the RAG is not exceeded for the product concerned of corrugated board.

(103) Therefore, the Commission concludes that the investment project under scrutiny is compatible with point 68(b) of the RAG.

3.5. Complaints against the notified aid measure

(104) The Commission has received three complaints from various sectoral associations against the notified aid measure. On 21 December 2007, the Swedish and Finnish

[16] On the basis of the worst case scenario approach presented in paragraph 86 of this decision.

[17] Calculated as [<250 000] / (8 600 000 – [>365 000]).

[18] Procelpac - Groupement Français des fabricants de papiers et cartons d'emballage à base de cellulose.

[19] Calculated as [<250 000] / (8 700 000 - [>365 000]).

Forest Industry Federations jointly submitted a complaint[20]. On 3 January 2008 the *Koninklijke Vereniging van Nederlandse Papier- en Kartonfabrieken* also transmitted a complaint[21] against the measure. Finally, by letter of 20 February 2008, *Procelpac - Groupement Français des fabricants de papiers et cartons d'emballage à base de cellulose* sent a complaint[22] concerning the aid at hand as well (hereinafter: "the complaints" or "the complainants"). In substance the complaints closely correspond to an informal complaint submitted by a company active on the same market which has however wished to remain anonymous.

(105) The argumentation put forward in the complaints can be summarized as follows.

Arguments put forward by the complainants: capacity created exceeds 5% of the size of the open market

(106) The complainants submit that the relevant market is the market for third party deliveries, irrespectively of whether Progroup will use part or all of its production for internal use. The reason for this would be that production for own use will replace the amount of CCM previously purchased by Progroup on the open market.

(107) According to the complainants, capacity increase pursuant to paragraph 68(b) of the RAG should be calculated as the ratio of total capacity created by the project (irrespectively of whether or not the capacity is used for in-house production) and the size of the open market (i.e. third party deliveries only) for CCM (or recycled paper based CCM) in Europe.

(108) Following this approach, total capacity created by the project would exceed 5% of the size of the open market (i.e. around 5.5% of the open market for all CCM and 7.4% of the open market for recycled based CCM).

Arguments put forward by the complainants: serious distortion of competition and trade

(109) Furthermore, it is argued that regional aid to Progroup will seriously distort competition in a sector that suffers from structural overcapacity. The situation would be similar to the one in the period 2001-2006 when CCM capacity, largely driven by regional State aid, increased in particular in Germany (aided projects by Leipa, Hamburger, Adolf Jass).

(110) Due to the absence of adequate demand growth, the capacity increase has caused capacity utilisation rates to drop, which has led to falling prices of CCM, reaching its lowest point at the end of 2005. In the meantime, the costs of input (raw materials, energy, recovered paper) increased, resulting in a drop in the net margins. In light of the serious economic difficulties, various companies had to close previously profitable CCM-machines at great financial costs and in terms of job losses in order to remain competitive and to prevent a further drop in prices. As a result of capacity reductions in 2004, 2005 and 2006, CCM prices recovered in 2006.

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[20] Registered under State aid CP 365/2007.

[21] Registered under State aid CP 3/2008.

[22] Registered under State aid CP 47/2008.

(111) The anticipated investment subsidies to Progroup for the Eisenhüttenstadt project are expected to exacerbate the existing sectoral problems by artificially creating new capacity that will replace the capacity of production mills that were de-installed in an attempt of industry players to restore competitive balance in the CCM market. The subsidised producer will unfairly benefit from these closures while other participants will again have to close down CCM production machines at high financial and social costs.

(112) Moreover, the complainants claim that the continuous support by Germany for this sector is also changing trade patterns. Out of the 15 production machines/mills that have been built or expanded between 2000 and 2006, eight were located in Germany with at least four benefiting from State aid. During the same period, approx. 31 CCM machines/mills were closed, out of which only five were located in Germany. As a result, Germany became a net exporter of CCM since 2002 after having been a net importer in previous years.

(113) In light of the above, the complainants consider that the Commission should open the formal investigation and prohibit the proposed measure. They refer to recital 5 of the RAG according to which the advantages of the aid in terms of the development of a less-favoured region must outweigh the resulting distortions of competition. They also refer to case law according to which the Commission should ensure that aid measures do not create a sectoral problem at Community level which is more serious than the initial regional problem[23]. Moreover, they claim that the Guidelines must be interpreted in the light of Article 87 EC Treaty and the principle set out therein, namely the incompatibility of public aid where it distorts competition in the common market[24].

3.6. Assessment of the arguments put forward in the complaints

Capacity increase on the open market

(114) As stated in paragraphs 53 and 92 above, paragraph 68 of the RAG provides that capacity increase is expressed in proportion of the size of the market using apparent consumption data of the product concerned. According to footnote 62 of the RAG, apparent consumption is measured as production plus imports minus exports and thus does not allow a subdivision into open market and captive sales. It merely determines the amount of the product that is actually consumed in the relevant geographic area.

(115) As set out in paragraphs 98 to 101 above, for the sake of completeness, the Commission also examined the increase of capacity relative to the size of the open market. The Commission considers that the correct approach to do this is to take only the part of capacities created which will be used to produce for third party sales, since only this part will directly affect the open market. This capacity has to be measured against the size of the open market. When doing so, it should be taken into account that since part of Progroup's new CCM capacities will be used to produce for intra-group consumption, the size of the open market shrinks as demand by Propapier for CCM which without the investment would appear on

[23] Joined cases T-126/96 and T 127/96 BFM & EFIM v. Commission ECR [1997], II-3437, para 101.

[24] T-27/02, Kronofrance SA v Commission, 1 December 2004, ECR []2004], II-4177.

the open market is eliminated. Therefore the 'captive' part of the capacity to be created has to be deducted from the size of the open market. Calculated this way, capacity increase remains well below the 5% threshold.

Situation of the sector concerned

(116) It appears indeed that the CCM market have been characterised over the past years by falling prices and a number of plant/machine closures. The causality of capacity reduction and state aid funded capacity increases is however not straightforward.

(117) In Germany's view, CCM machine closures were due to a natural trend to phase out outdated capacities, which is substantiated by the fact that the average age of the closed machines amounted to 51 years. These old paper machines did not comply with the requirements of changed demand patterns, in particular as regards increased demand for light paper up to 100 g/m^2 and a standardised trim width of 2.5 metres. Moreover, paper machines are subject to substantial economies of scale, which leads to older and smaller machines being replaced with bigger ones, as shown by the fact that the average capacity of machines closed between 2000 and 2007 was only 43 000 tonnes as opposed to the average capacity of newly installed machines of 369 000 tonnes.

(118) Germany also submitted Pöyry data showing that in the period until 2016 a high capacity utilisation rate between 92 and 96% is anticipated on the European CCM market.

(119) In any event, according to paragraph 68 of the RAG, the Commission has limited its discretionary power to undertake a detailed verification that the benefits of the aid outweigh the distortions of competition to a situation where one of the thresholds in paragraph 68(a) or (b) of the RAG is exceeded. The Commission is bound by the content of its guidelines[25].

(120) Moreover, the Commission considers that when applying the criteria of paragraph 68 of the RAG, it is not in contradiction with Article 87(3)(a) of the EC Treaty. The respect of the thresholds for market share and capacity increase as well as the scaling down of the maximum aid intensity ensure that the potential distortion of competition through the aid remains proportionate to the objective of regional development. At the same time, the requirements of the RAG also make sure that the contribution of the aid to regional development is secured.

3.7. Conclusion

(121) The notified aid is in line with the RAG. Consequently, the aid measure is compatible with Article 87(3)(a) of the EC Treaty.

[25] T-27/02 – Kronofrance, 1.12.2004

4. DECISION

(122) The Commission has decided, on the basis of the foregoing assessment, that the regional aid in favour of Propapier PM 2 is compatible with the EC Treaty.

(123) The Commission reminds the German authorities of their commitment to submit to the Commission a copy of the aid contract, intermediary reports as well as a final report concerning the measure in question.

(124) If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://ec.europa.eu/community_law/state_aids/index.htm. Your request should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
B-1049 Brussels
Fax No: 32 2 296 12 42

Yours faithfully,
For the Commission

Neelie KROES
Member of the Commission