Conditional decisions and EC State aid law: The MobilCom case

Sabine CROME, unit H-1, and Annette SÖLTER, unit H-2, Directorate-General Competition

I. Introduction

In July 2004 the Commission approved aid granted to MobilCom AG to help it with its restructuring in 2002/2003. The approval of the aid was however linked to conditions. To offset the distortions of competition caused by the aid, MobilCom and its affiliates must halt their online direct sales of MobilCom mobile telephony contracts for seven months.

The possibility to attach conditions to a positive decision is stipulated in Article 7(4) of the Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 (now 88) of the EC Treaty (‘Council Regulation (EC) No 659/1999’) (1).

This possibility plays an important role in particular in major restructuring aid cases. The Commission made for example its final positive decision in the case Bankgesellschaft Berlin (2) subject to a number of conditions concerning compensatory measures necessary to offset competitive distortions caused by the aid.

In this respect the MobilCom decision contains two interesting aspects which should be looked at in more detail in this article. The first aspect is the kind of compensatory measure which was made a condition subject to which the aid can be considered compatible with the common market. Whereas in the majority of the restructuring aid cases, in which conditions concerning compensatory measures have been included for the approval of the aid, these conditions were primarily of a structural nature, like for example the liquidation or the sale of parts of the company, the compensatory measure in the MobilCom case consists exclusively in a behavioural measure.

The second aspect concerns the way the condition and the compensatory measures were integrated in the decision and the legal basis for such a conditional decision. Whereas in most of the cases including the mentioned Bankgesellschaft Berlin case, the conditions contained in a final conditional decision were agreed by the Member State, in the MobilCom case they were not previously accepted by the Member State.

Before looking into these issues, a short overview of the case shall be presented.

II. The restructuring of MobilCom

MobilCom is a mobile phone service provider. Before the restructuring MobilCom had also been active in the field of UMTS and landline/Internet. The company is located in Büdelsdorf, Schleswig-Holstein, Germany.

MobilCom ran into difficulties in 2002 when its main shareholder, France Télécom, announced its withdrawal from the UMTS business, and stopped all payments for the purpose of financing the UMTS business. At this time MobilCom had a significant amount of debts plus large current financing requirements to cover further network investments, ordinary organisational expenditure and interest. Since France Télécom had for months been MobilCom’s sole remaining source of financing and there were no alternative financing options, MobilCom was directly threatened with insolvency.

Against this background Germany granted a first deficiency guarantee for a loan of EUR 50 million in September 2002 to provide immediate liquidity to the company. This aid was approved by the Commission as rescue aid in January 2003 (3) and was not part of the final conditional decision adopted in July 2004.

In order to ensure further funding, which was needed to finance the requisite reorganisation measures of the company, Germany and the Land of Schleswig-Holstein granted another 80% deficiency guarantee for a loan amounting to EUR 112 million in November 2002. The Commission considered that this measure constituted restructuring aid, which was however disputed by Germany and the company. This aid measure was approved subject to conditions in July 2004.

(2) Commission decision of 18 February 2004 (not yet published in the OJ).
(3) OJ C 80, 3.4.2003, p. 5.
MobilCom implemented a restructuring plan. The basis of the strategy for restoring the firm's profitability was to concentrate strictly on the original core business as a service provider in the mobile telephony sector. The unprofitable UMTS business was completely discontinued. The restructuring plan also provided that MobilCom would withdraw from the Internet/landline sector. To this end, the landline division was integrated into Freenet.de AG, the internet daughter of MobilCom, and the stake in Freenet was partly sold later. The key components of the reorganisation strategy for the loss making mobile telephony/service provider sector were to cut 850 full time jobs, concentrate sales and customer services activities, which had previously been scattered over several sites, at the Büdelsdorf group headquarters and Erfurt, reduce customer acquisition costs (among other things by closing shops) and streamline customer portfolios. Overall, the emphasis would be on consolidation at smaller but more profitable customer and turnover levels.

In the meantime the restructuring of the MobilCom group has been completed, the company returned to profit and seems to have restored long-term viability. In September 2003 MobilCom reimbursed the two credit lines, for which the State guarantees were granted, and the State guarantees were given back.

III. Assessment of the restructuring aid: finding a compensatory measure

The Community Guidelines for rescuing and restructuring firms in difficulty (‘R&R Guidelines’) (1) lay down that restructuring aid can only be approved if undue distortions of competition are avoided. Therefore measures must be taken to mitigate as far as possible any adverse effect of the aid on competitors. This condition usually takes the form of a limitation on the presence which the company can enjoy on its markets after the end of the restructuring period.

The Commission held that competition was unfairly distorted by the granting of the restructuring aid primarily because MobilCom used the aid not only to restructure the company physically but also to reorient its marketing strategy and to focus on more profitable customer segments in its core business area as a mobile telephony service provider. The aid thus had a particularly damaging effect on competitors as they too have to target their business strategies at more profitable customer groups because the German mobile telephony market is reaching a saturation level.

On top of that, in the years leading up to the crisis MobilCom had been focusing on the UMTS sector, using aggressive pricing to pursue an expansion strategy aimed solely at boosting its market share. In the end this strategy failed, forcing MobilCom to withdraw from the UMTS sector. However, the aid granted meant that MobilCom did not have to bear alone the negative consequences of the risky strategy it had pursued, while at the same time being able to benefit from the positive effects, such as the fact that, when slimming down its customer portfolio, it could count on a larger customer base. This meant that the aid gave MobilCom a substantial advantage over its competitors.

Although the position of MobilCom in the relevant market for mobile telephony may seem limited (MobilCom has an estimated market share of around 6% after restructuring), for the above reasons the Commission considered that the aid caused undue distortions of competition and that these distortions had not been sufficiently compensated by the measure to reduce market presence, in particular the company's withdrawal from the UMTS business and the reduction of jobs, which had been put forward by Germany.

Once it had been established that the aid led to undue distortions of competition which required further compensatory measures, an adequate compensatory measure had to be found. Normally, a compensatory measure should be integrated in the restructuring plan. However, as the restructuring of MobilCom was already terminated and the measures foreseen in the restructuring plan were not considered to be sufficient, a further measure had to be found.

The Commission finally opted for a behavioural measure, which constituted in the halting of the online direct sales of MobilCom telephony contracts. The Commission took the view that imposing a ban on direct online sales of MobilCom telephony contract for seven months should offset the competitive distortions created. For the company, direct online marketing represents an increasingly important channel for selling mobile telephony contract. Halting such marketing for a while will offer competitors a chance that customers will go to their websites and sign up for contracts.

All conceivable structural measures in order to further reduce the market presence of the MobilCom group as such appeared either inappropriate to the Commission to offset the competitive distortions or disproportionate to the effects of the aid. Moreover, pure service providers like MobilCom do not own and operate the infrastructure to set up mobile services but simply resell capacities of the network operators. The Commission therefore deemed in this particular case the found behavioural measure which aims at a compensation in the field where the aid produced its undue effects, namely in the field of the market-ability of services, as the most suitable measure to counterbalance the distortions of competition.

IV. Legal basis of a conditional decision

The legal basis for a conditional decision as adopted in the MobilCom case is Article 7(4) of the Council Regulation (EC) No 659/1999 which lays down that the Commission may attach to a positive decision conditions subject to which an aid may be considered compatible with the common market and may lay down obligations to enable compliance with the decision to be monitored.

As has already been pointed out above this possibility is regularly used particularly in major restructuring cases to compensate for the distortions of competition caused by the aid. Normally, discussion with the Member State take place and an agreement can be found on suitable compensatory measures which will be included as a condition in the approval decision. The Member State submits a preceded commitment to ensure the implementation of the compensatory measures.

When assessing the MobilCom case the Commission intended to pursue the same way. The Commission entered into discussion with Germany to see whether an agreement could be found on suitable compensatory measures which would allow the approval of the restructuring aid. Despite intensive discussions on a compensatory measure no agreement could be reached between the Commission and Germany.

The Commission nevertheless considered that attaching a condition to a further compensatory measure to a positive decision was the most appropriate way to deal with the MobilCom case. The Commission took the view that Article 7(4) of the Council Regulation (EC) No 659/1999 does not require the agreement of the Member State for attaching a condition to the decision subject to which the aid can be considered compatible with the common market. The Commission therefore decided to attach a condition to its authorisation of the aid although no agreement had been reached with Germany.

In its decision the Commission thus stated that it finds that the restructuring aid is compatible with the common market pursuant to Article 87(3)(c) of the EC Treaty if Germany fully implements the condition which was described in detail to close down the direct on-line distribution of MobilCom mobile telephony contracts.

Article 1(g) of the Council Regulation (EC) No 659/1999 states that any contravention of a conditional decision constitutes a misuse of aid. This means that in case of non-fulfilment of the condition the Commission can reopen the investigation procedure and potentially take a negative decision ordering recovery of the aid as laid down in Article 16 of the Council Regulation (EC) No 659/1999.

Furthermore Article 23 of the Council Regulation (EC) No 659/1999 lays down that where the Member State concerned does not comply with a conditional decision, the Commission may refer the matter to the Court of Justice of the European Communities direct in accordance with Article 93(2) (now 88(2)) of the Treaty.

In the MobilCom case the Commission thus reserved the right to make use of the competences assigned to the Commission by articles 16 and 23 of the Council Regulation (EC) No 659/1999 in case the conditions attached to the decision will not be fulfilled.

V. Conclusion

In the MobilCom case the approval of the restructuring aid was made subject to a condition that constituted a behavioural measure. This is different from other major restructuring aid cases in which conditions primarily in form of structural measures were attached to the final approval.

Also the decision to approve the restructuring aid to MobilCom subject to the condition that MobilCom and its affiliates must halt their online direct sales of MobilCom mobile telephony contracts for seven months introduces a novelty in so far as for the first time the Commission made the approval of a restructuring aid subject to a condition for which it had no preceded commitment of the Member State concerned that it will ensure the implementation.