EUROPEAN COMMISSION

Brussels, 19.11.2009
C(2009)

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** **This document is made available for information purposes only.**

Subject: State aid C 34/2009 (ex N 588/2008) – PT- LIP – PETROGAL, S.A.

Sir,

1. PROCEDURE

– On 17 November 2008, registered on the same date, the Portuguese authorities notified regional investment aid in favour of an integrated investment project by Petroleos de Portugal, Petrogal S.A. (hereafter referred to as "Petrogal") concerning its refinery activities in Sines and Matosinhos, situated in two areas eligible for regional aid pursuant to Article 87(3)(a) EC.

– The Commission requested additional information by letter dated 17 December 2008. On 30 January 2009 the Portuguese authorities asked for an extension of the deadline until 20 February 2009. The Portuguese authorities provided additional information on 13 February 2009.

– At the same time, the Portuguese authorities requested a meeting with the Commission, which took place on 12 March 2009. On 20 March 2009, the Commission sent a second information request, which was followed by a letter of 16 April 2009, in which a detailed description of the issues discussed during the meeting was attached. The Portuguese authorities requested an extension of the deadline until 2 June 2009, date when the reply from the Portuguese authorities was submitted.

– On 31 July 2009, the Commission transmitted a third request for information. The Portuguese authorities requested an extension of the deadline until 15 September 2009. The information was submitted on 16 September 2009.

2. DESCRIPTION OF THE AID MEASURE

– The Portuguese authorities intend to provide regional investment aid in form of corporate tax allowance to Petrogal to modernise and expand the existing refinery units in Sines and Matosinhos, the only two existing refineries in Portugal. Besides, the project aims at improving the integration of and realising synergy effects between these two refineries.

2.1 The beneficiary

– The beneficiary of the aid will be Petrogal, a subsidiary company wholly owned by Galp Energia, SGPS, S.A. (hereinafter "Galp Energia"). Galp Energia is the holding company of the Galp Energia Group ("GALP"), a group with a presence in the petroleum product market (which includes refining and marketing activities, such as non-retail and retail sales) as well as in the gas market.

– The company was set up on 22 April 1999 under the name of GALP - Petroleos e Gas de Portugal SGPS, S.A., mainly for the purpose of trading in oil and natural gas, bringing together two pre-existing Portuguese government owned companies which were placed under GALP´s control, i.e. Petrogal, focusing on petroleum products, and GDP - Gas de Portugal, SGPS, S.A., focusing on natural gas[1].

– GALP's business includes as well retail and wholesale marketing of refined petroleum products in the Iberian Peninsula. It is the market leader in Portugal[2], and has a growing presence in Spain.

– Petrogal owns the sole two refineries in Portugal. The refining business comprises all refining, supply and logistics activities. Petrogal is the largest marketer of petroleum products in Portugal, as well as one of the largest in the Iberian Peninsula. It effectively manages all the crude oil and part of the refined products imports to Portugal; it manages as well 80% of the storage capacity of crude oil and refined products[3] and has an important position in Portugal’s logistics infrastructure for oil products.

– Petrogal has an extensive product range that includes gasoline, diesel fuel, jet fuel, fuel oil, naphtha, LPG, bitumen and several aromatic products. The refining business is responsible for the supply of oil products to their retail, wholesale and LPG marketing divisions, competitors and foreign customers,

---

1 As from GALP's website: http://www.galpenergia.com

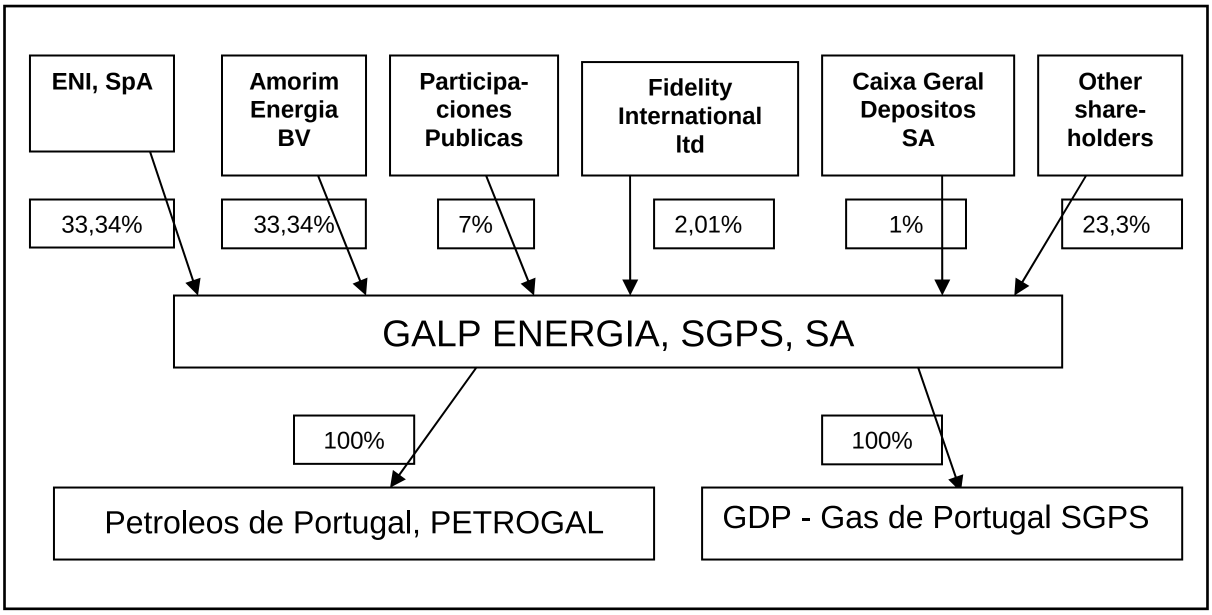
2 According to the above mentioned beneficiary's website, in 2005, through its network of service stations (837 in Portugal and 223 in Spain), the company had a 37% retail market share, based on sales volumes, in Portugal and a 9% retail market share in the Iberian Peninsula. In the wholesale market, it supplied more than 4,300 industrial and commercial users with an aggregate of 5.5 million tonnes of refined petroleum products, representing a 51% market share in Portugal and 11% in the Iberian Peninsula.

3 Data included in the Report by the Portuguese Competition Authority on the Fuel Market in Portugal, 2 June 2008, p. 9 - as published on the website: http://www.concorrencia.pt/Publicacoes/Autoridade.asp

as well as for the operation of their refining and logistics assets. They store and transport their products using either their wholly-owned storage assets or affiliated logistics companies.

– Petrogal is a 100% subsidiary of Galp Energia. The main Galp Energia shareholders are: ENI S.p.A[4] (33.34%), Amorim Energia BV[5] (33.34%), Parpública Participacoes Publicas (SGPS)[6] (7%), Fidelity International limited (2.01%), Caixa Geral de Depósitos S.A.[7] (1%), others (23.31%).

– The figure below reflects Petrogal´s ownership and controlling rights.



4 ENI S.p.A. ("ENI") is the leading Italian-based energy company, listed on the Milan and New York (NYSE) stock exchanges. Its operations in Exploration & Production, Gas & Power, Refining & Marketing of oil products, Petrochemicals and Engineering, Construction and Drilling services span over 70 countries. ENI´s refining capability is extended to Italy, Germany and Czech Republic. In Italy, it is composed of five wholly 100 per cent owned refineries and a 50% interest in the Milazzo refinery in Sicily. As for refineries outside Italy, these are limited to participations in Germany and in the Czech Republic. In Germany ENI holds an 8.3% interest in the German SCHWEDT refinery and a 20% interest in BAYERNOIL, an integrated pole that includes the Ingolstadt, Vohburg and Neustadt refineries. ENI's refining capacity in Germany amounts to approximately 70 kbbl/d mainly used to supply ENI's distribution network in Bavaria and Eastern Germany. As for the activity in the Czech Republic, ENI has an overall stake of 32.4% in Česka Rafinerska, which includes two refineries, Kralupy and Litvinov. ENI's share of refining capacity amounts to 53 kbbl/d. In 2007, refining throughputs on ENI's own account in Italy and outside Italy were 37.15 mmtonnes.

5 Amorim Energia, BV ("Amorim Energia"), based in the Netherlands. Its main shareholders are Esperanza Holding B.V. (45%), Power, Oil & Gas Investments B.V. (30%), Amorim Investimentos Energéticos, SGPS, S.A. (20%) and Oil Investments B.V. (5%). Portuguese investor Américo Amorim controls, directly or indirectly, 55% in Amorim Energia, the other 45% being owned by Sonangol, through its control of Esperanza Holding B.V. Sonangol is Angola's state oil company.

6 Participaciones Publicas (Parpública), the holding company for the Portuguese state's equity stakes in several companies.

7 Caixa Geral de Depósitos, S.A. ("CGD") (owning 1%) is a financial institution which is wholly-owned by the Portuguese state.

Share transferability

– Shares in Galp Energia are freely transferable according to the law, and to the company´s articles of association. Under the shareholders' Agreement between Amorim Energia, CGD, and ENI, the parties have committed to holding their equity stakes in Galp Energia until 31 December 2010, except in the extraordinary cases referred below. In the shareholders' Agreement, ENI and Amorim Energia also undertook not to increase, in the so-called lock-in period, their respective holdings in Galp Energia beyond 33.34%, except for the situations referred to below. In these cases, if Amorim Energia is the selling party, CGD has the right, before the other parties, either to buy the holding offered for sale or to appoint as purchaser a third party meeting the requirements set out in the Shareholder Agreement

The shareholders Agreement

– The Shareholder Agreement was signed on 29 December 2005 between Amorim Energia, ENI and REN (Rede Eléctrica Nacional de Portugal), with CGD joining the agreement on 28 March 2006. The agreement entered into force on 29 March 2006 and shall remain valid for a period of eight years. Under article 20, first paragraph c) of the Portuguese Securities Code, voting rights arising from the shares owned in Galp Energia by each party to the agreement are reciprocally assigned to the other parties. Consequently, according to the Portuguese law, Galp Energia is considered to be jointly controlled by the shareholders that are parties to the Shareholder Agreement.

– According to Portuguese authorities, it derives from the Agreement that shareholders, and in the specific case the ENI Group, cannot control and solely define strategies between their refining activities and the refining activities of Petrogal.

2.2 The investment project

– The project aims at modernising (including environmental aspects) and extending the two existing refinery units in Sines and Matosinhos. It also aims at improving the integration and complementarities of these two refineries. It aims mainly at increasing the production of diesel to the detriment of fuel oil production. The increased use of heavy crude oil, which is available on the market at a lower price, will reduce raw materials cost and will lend flexibility to the origin of crude oils to be processed.

– The project for the conversion of the Matosinhos refinery consists more precisely in the construction of a new vacuum distillation unit for obtaining vacuum gasoil (VGO) and a visco-reduction unit for the soft thermal cracking of the resulting vacuum residue.

– The project for conversion of the Sines refinery aims at the construction of a new hydrocracker, i.e. a unit for hydrocracking heavy gasoil, for the production of diesel and jet fuel. The hydrocracking unit will use as feedstock vacuum gas oil and heavy gas oil derived from visbreaking produced at the Matosinhos and Sines refineries, thereby making full use of the processing capacity of the national refining equipment. It will have a treatment capacity of around […] barrels per day, using around […] kt/annum of atmospheric residue as primary feedstock.

– The products obtained by hydrocraking (LPG, naphtha and diesel) are […] hydrogenated, which gives them a superior quality. The project will only increase the production of diesel and naphtha.

– The naphtha[8] produced in the Sines refinery will be shipped to Matosinhos as raw material for the aromatics plant, which will be a further step to increased integration of the two units. The increase in the production of naphtha is an inevitable technical consequence of the conversion project in Sines.

– The works on the investment started in 2007 and will continue until 31 December 2010. Full production capacity will be reached by 2011.

2.3 Single investment project

– The Portuguese authorities indicate that despite the geographic distance between the two refineries (some 450 km to be covered by sea transport), the investment project has to be considered as a single investment project in the meaning of the point 60 of the guidelines on national regional aid for 2007-2013[9] (hereinafter RAG). The Portuguese authorities confirm that Petrogal has not received State aid in the three years previous to the start of the notified investment project.

2.4 Costs of the investment project

– The investment in Sines represents investment costs of EUR […] million (nominal value) and is to receive an aid of EUR […] million (nominal value), resulting in an aid intensity of 16%. The project in Matosinhos amounts to an investment volume of EUR […] million (nominal value) and is to benefit of aid of EUR […] million (nominal value), corresponding to an aid intensity of 13%. The notification includes information on *de minimis* aid for studies related to the project.

– Total costs of the project amount to EUR 1 059.3 million in nominal value. All these costs are considered eligible for regional aid. A breakdown of the eligible costs is presented in the table below.

Eligible costs (in million EUR)	**2007**	**2008**	**2009**	**2010**	**Total**
Tangible fixed assets	[…]	[…]	[…]	[…]	[…]
Studies (under *de minimis* aid)	[…]	[…]	[…]	[…]	[…]
Total	[…]	[…]	[…]	[…]	**1,059,334,023**

[8] A light fraction of refined crude oil between gases and petroleum. It is used as feedstock by the petrochemical industry as its cracking supplies several products and it can also be used as a component for gasoline (light naphtha) or to produce reformate (heavy naphtha).

[9] OJ C54 of 4.3.2006, p. 13.

2.5 Financing of the project

– Petrogal plans to finance the project using its own resources, in addition to the aid applied for. There are no other sources of public financing foreseen.

2.6 Regional aid ceiling

– Sines and Matosinhos are both situated in assisted regions pursuant to Article 87(3)(a) EC treaty, with a standard regional aid intensity ceiling for large enterprises of 40% (for Sines, in the region Alentejo) and 30% (for Matosinhos, in the region Norte), gross grant equivalent (GGE), according to the Portuguese regional aid map[10].

2.7 Contribution to regional development

– In the notification, the Portuguese authorities declared that the project involves the creation of approximately 150 direct jobs and of 450 indirect jobs in the two regions. Moreover, according to the information submitted, approximately 3 000 temporary jobs will be created during the construction period.

2.8 Form of aid

– The aid will have the form of tax benefit. The tax benefit is granted in the form of a tax credit to be deducted from future payments of corporate income tax. The amount of this credit will be calculated by the Portuguese authorities as a percentage of the eligible investment. The tax credit can only be used for taxes generated by the project.

2.9 Applied aid schemes

– The Portuguese authorities implemented, based on the scheme N97/1999 approved by the Commission, a system of tax incentives established by Decree law No 409/99 of 15 October 1999, by which a special temporary tax concession could be granted under a contractual regime and limited to the investment made (hereinafter, "the fiscal scheme").

– Based on this fiscal scheme, two contracts were signed on 10 March 2008, between, on the one hand, the Portuguese government, and on the other hand Petrogal and Galp Energia SGPS, for the purpose of granting aid. The two contracts are: "contract for the granting of tax benefits" and the "investment contract".

– The signed contracts foresaw the concession of the tax credit linked to an investment. The fiscal contract allows to deduction, from the amount established under the Portuguese tax Code (Article 83(1)(a)) on corporate income tax (hereinafter CIT), of the amount arising from the application of the maximum aid intensity percentage to the value of the investment made each financial year until 31 December 2016.

---

10 The Portuguese regional aid map was approved by the Commission by decision of 7 February 2007, case N 727/2006 (JOCE C 68, 24.03.2007 p. 26)

– This tax deduction shall be made available to the beneficiary upon payment of the CIT relating to the financial period in which the deduction relevant to the tax incentive were made, or in the event that the relevant amount cannot be fully deducted, any pending amount can still be deducted, under the same conditions, upon settlement for the following financial periods until the expiration of the contract, i.e. 31 December 2016.

– As regards the aid planned to be granted for studies, the Portuguese authorities have referred to the Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of the article 87 and 88 of the Treaty to *de minimis* aid.

2.10 Aid amount

– The Portuguese authorities intend to grant regional aid amounting to EUR 160.484.006 in nominal value which is to be paid out as from 2009 until 2011 included. Besides, EUR 60 602, for the financing of the studies, will be granted under de minimis aid rules. This aid is (planned to be) paid out as follows. The table below, provided by the Portuguese authorities, details the schedule of the payment of the aid:

Year	estimated taxable Income	Taxes	Utilisation of the tax credit*	Discounted value of the tax credit**
2008				
2009				
2010				
2011	[…]	[…]		
2012	[…]	[…]	[…]	[…]
2013	[…]	[…]	[…]	[…]
2014	[…]	[…]	[…]	[…]
2015	[…]	[…]	[…]	[…]
2016	[…]	[…]		
			160,544,609	117,067,833

* Income generated in a given year will be taxed in the following year, and in this way the utilisation of the tax credit only takes effect in this year.

** Using the applicable tax rate in Portugal (5.19%), and discounting the incentive for the initial investment.

*** *De minimis* aid, applicable to studies only

– The Portuguese authorities confirmed that the aid for the project will not be cumulated with aid received for the same eligible costs from other local, regional, national or Community sources.

- In addition, the aid is granted under the condition that the beneficiary will maintain the investments in the assisted region for a minimum period of five years after completion of the investment project.
- The Portuguese authorities confirmed that the granting of the aid is subject to the Commission's clearance. They further informed that the final aid contract for the direct grant will only be issued after approval of the aid measure by the Commission.
- The works on the investment started in 2007 and will continue until 31 December 2010. The beneficiary applied for the aid in 2006, and on 23 January 2007 the Portuguese authorities confirmed in writing to Petrogal that, subject to detailed verification, the project met the conditions of eligibility laid down in the "fiscal scheme" before the start of work on the project.
- The Portuguese authorities committed that the maximum aid amount and the maximum aid intensity approved in this decision will not be exceeded, even in the case of lower or increased eligible costs.

2.11 General provisions

- The Portuguese 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.
  - the Portuguese authorities not taken any other commitment in terms of granting aid towards GALP/Petrogal, neither is the Commission aware of any further related investment to be made by the Group.

3. ASSESSMENT OF THE AID MEASURE AND COMPATIBILITY

3.1 Existence of aid

- The financial support to Petrogal will be given by the Portuguese authorities in the form of a tax credit. 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.
- As the financial support is granted to a single company, Petrogal, the measure is selective.
- The financial support given to Petrogal will relieve the company from costs which it normally would have had to bear itself and therefore the company benefits from an economic advantage.

– The fact of favouring of Petrogal and its production by the Portuguese authorities over its competitors means that competition is distorted or threatened to be distorted.

– The financial support from the Portuguese authorities will be given for investments resulting in the increased production of diesel and naphtha. Since these products are subject to trade between Member States, the support given is likely to affect such trade.

– Consequently, the Commission considers that the notified measure constitutes State aid to Petrogal within the meaning of Article 87(1) of the EC Treaty.

3.2 Legality and compatibility of the aid measure

– Portugal intended to grant the aid on the basis of the regional aid scheme N97/1999 (*Regime de auxilios fiscais ao investimento*) approved by the Commission on 6 October 1999, initially valid until the end of 2010. Following the adoption of the RAG for the period 2007-2013, the Commission proposed to all Member States appropriate measures to limit the application in time of all existing regional aid schemes for aid to be granted on or before 31 December 2006. The Portuguese authorities accepted unconditionally the above mentioned appropriate measures. In line with Art. 19(1) of the Procedural Regulation, the Portuguese authorities are bound by their commitment and as from 1.1.2007, the scheme N 97/1999 ceased to constitute existing aid in the meaning of Art. 1(b) of this Regulation.

– The Commission is not aware of any measure adopted by the Portuguese authorities to phase out this aid scheme. In absence of its prolongation in line with the regional aid rules, and in particular the regional aid map, applicable from 1 January 2007, the continued application of the regional scheme N97/1999 after 2006 is illegal. As a consequence of the State aid approval status of the underlying national measure, the notified aid to Petrogal, which was initially notified as individually notifiable aid under an existing aid scheme, has to be assessed as ad hoc aid, and the Portuguese authorities have amended the notification in this sense.

– Having established that the measure involves State aid within the meaning of Article 87(1) of the EC Treaty, it is necessary to consider whether the above mentioned measure can be found compatible with the common market. As the measure relates to a regional investment aid and was notified in 2008, the Commission assessed it on the basis of the RAG 2007, and more specifically, the provisions of section 4.3 of the RAG relating to large investment projects.

3.3 Compatibility with the general provisions of the RAG

– An initial investment is defined under point 34 of the RAG as investment in material and immaterial assets relating to: the setting up of a new establishment; the extension of an existing establishment; the diversification of the output of an establishment into new, additional products; a fundamental change in the overall production process of an existing establishment. Replacement investment is explicitly excluded from the scope of the definition of initial investment.

– The investment project aims at modernising and better integrating the two refineries. It will in particular increase the production of diesel (and collaterally naphtha), while at the same time reducing the production of fuel oil.

– In the Commission's opinion, the investment project does not fall clearly into the standard categories of initial investment within the meaning of point 34 of the RAG, and there are doubts to what extent it could be considered as a replacement investment. The project does not constitute an investment into a new establishment, nor a diversification of the output of an existing establishment into new, additional products. It may include, however, certain "extension" and "fundamental change of the production process" aspects. The new vacuum distillation unit in Mathosinhos and the new hydrocracker in Sines could represent extension investment of the existing refineries, and would lead through a fundamental change in the production process to an increased output of diesel. On the other hand, the output of the refineries would not change in terms of final products, but only in terms of quantity.

– The costs eligible for investment aid are defined in line with point 50 of the RAG, and the rules on cumulation are respected (cf. points 71-75 of the RAG).

– The beneficiary provides a financial contribution of at least 25% of the eligible costs in a form which is free of any public support (cf. point 39 of the RAG).

– Furthermore, the beneficiary has also the obligation to maintain the investment in the region for a minimum of five years after completion of the project (cf. point 40 of the RAG).

– The beneficiary is not a firm in difficulty in the meaning of the Rescue and Restructuring Guidelines. Therefore the company is not excluded, pursuant to point 9 of the RAG, from the scope of application of the RAG.

– However, there are doubts regarding the contribution of the investment to regional development. As the measure has to be assessed as ad hoc aid, the Portuguese authorities need to demonstrate, according to point 10 of the RAG, that the project contributes towards a coherent regional development strategy and that, having regard to the nature and size of the project, it will not result in unacceptable distortions of competition. In particular, the Commission expresses doubts whether the expected contribution to regional development really outbalances the sectoral effects resulting from the aid (EUR 160.49 million in aid, creating 150 direct jobs only).

– In this context, there are grounds to doubt the necessity of the aid since, as from the information included in Petrogal's 2008 financial accounts, the investment project appears to be part of the industrial strategy of the company owner of the two sole refineries in Portugal, and is likely to have been carried out also in a counter-factual scenario analysis without aid. In fact, it appears unlikely that the aid is necessary for the implementation of the investment (for which works started in 2007), and that Petrogal could have considered other locations for the investment. An unnecessary aid is unlikely to contribute to regional development and might result in unacceptable distortions of competition.

– Moreover, the Commission raises doubts on whether the formal incentive effect requirements laid down in point 38 of the RAG are met. The beneficiary applied for the aid on the basis of an expired scheme. The aid will therefore be granted as ad hoc aid. The fact that in January 2007 the Portuguese authorities confirmed in writing to Petrogal that, subject to detailed verification, the project met the conditions of eligibility laid down in the scheme before the start of works, is irrelevant in this context since this condition applies to existing, lawful schemes. For ad hoc aid, however, the competent authority should have issued a letter of intent, conditional on Commission approval, to award aid before works start on the project. At this stage, there are doubts whether the eligibility letter issued by the Portuguese authorities could be considered as a letter of intent in the meaning of point 38 of the RAG.

3.4 Compatibility with the provisions for aid to large investment projects

3.4.1 Single investment project (point 60 of the RAG)

– The Portuguese authorities have informed of an earlier investment in these refineries, but have confirmed that the investment did not receive any State aid during the three years period before the start of the works of the notified investment.

– Besides, the Portuguese authorities consider the notified investment, which takes place in both refineries, as a Single Investment Project (SIP). According to point 60 of the RAG, an initial investment is deemed to be a SIP when is it economically indivisible, taking into account the technical, functional and strategic links and the immediate geographical proximity. In this case, despite the fact of the physical distance between the two refineries (some 450 km, to be covered by sea transport) the Portuguese authorities have confirmed that the investment project is a SIP. This would imply that the investment is subject to an adjusted regional ceiling, on the basis of a down scaling percentage as from point 67 of the RAG.

3.4.2 Aid intensity (point 67 of the RAG)

– As notified by the Portuguese authorities, the total planned eligible costs for the project amount to EUR 1 058 934 146 ([…]) in nominal value.

– The calculation of the aid intensity under point 67 of the RAG depends on whether the notified investment project is to be considered a SIP, or rather two separate investment projects. In the latter case, if the investments in the two locations are taken separately, then the calculation of the aid intensity would take into account the two different standard regional aid ceilings applicable for Sines (40%) and for Matosinhos (30%).

– The net present value of the investment in Sines amounts to EUR […] for a planned aid amount of EUR […] in net present value, corresponding to an aid intensity for this refinery of 13.12% gross grant equivalent (GGE), which is below the adjusted maximum aid intensity of 15.94%.

– The net present value of the investment in Matosinhos amounts to EUR […] for a planned aid amount of EUR […] in net present value, corresponding to an aid intensity for this refinery of 10.66%, gross grant equivalent (GGE), which is below the adjusted maximum aid intensity of 14.68%.

– On the other hand, if the investment is considered a SIP, then the Commission would need to check the correct application of the scaling down rule under point 67 of the RAG. Since the aid intensity in the two regions is different (40% in Sines, 30% in Matosinhos), the Commission proposes to recalculate the maximum aid intensity by weighing the aid intensities taking proportionally into account the investment (in net present value) in the corresponding region over the total investment. The result would be an aid intensity of 37.18%, corresponding to an adjusted maximum aid intensity of 14.21%.

– The net present value of the total investment costs amounts to EUR 974 064 894, and the total planned aid amounts to EUR 121 091 314 in net present value, corresponding to an aid intensity of 12.43% GGE, which is below the previously calculated adjusted maximum aid intensity of 14.21%.

– As in both cases the aid intensity in GGE would result below the adjusted maximum aid intensity considering the scaling down rules, the Commission considers that the proposed aid intensity for the project complies with point 67 of the RAG.

3.4.3 Compatibility with the rules under point 68 (a) and (b) of the RAG

– The Commission's decision to allow regional aid to large investment projects falling under point 68 of the RAG depends on the market shares of the beneficiary before and after the investment and on the capacity created by the investment. To carry out the relevant tests under point 68 (a) and (b) of the RAG, the Commission has first to establish appropriate product and geographic market definitions

Product concerned

– Point 69 of the RAG stipulates that the product concerned is normally the product covered by the investment. When the project concerns an intermediate product and a significant part of the output is not sold on the market, the product concerned may be the downstream product.

– The products concerned by the investment project to be made by Petrogal are, in principle, the different products that these refineries can produce by refining crude oil.

– According to the notification form, the products involved by the investment fall under the following product codes: Diesel (Prodcom 23200.15.50.000); Gasoline: (Prodcom 23200.11.50.000), LPG: (Prodcom 23200.21.20.104 (propane for sale)) and no. 23200.21.0.204 (butane for sale); fuel oil: (Prodcom 23200.17.70.004); Jet fuel: (Prodcom 23200.14.00.000) and naphtha (Prodcom 23200.16.50.000). The refined products are normally classified in three categories: i) light distillates (LGP, gasoline, and naphtha), ii) middle distillates (diesel, jet fuel) and iii) heavy products (fuel oil and bitumen).

– The investment aims at the installation of conversion units designed to produce diesel from heavier fractions of crude oil which have only been used until now to produce industrial fuel oil. Therefore, there will be a shift in the production from fuel oil to diesel. The production of diesel will be increased after the investment by additional [1-4] million tonnes/annum (from [3-6] million tonnes/annum before the project till [6-9] million tonnes after the project).

– According to the Portuguese authorities, the project does not seek the replacement or introduction of a new product. It will only affect the quantities of the products that are currently produced in these two refineries, increasing exclusively the production of diesel (in detriment of fuel oil) and naphtha. Thus, the investments will not lead to an increase of production of other products produced by the refineries. Moreover, according to the Portuguese authorities, the increase of the production of naphtha is an inevitable, technically caused side effect of the conversion project.

– The following table provided by the Portuguese authorities gives a breakdown of the product mix before and after the investment. As shown in this table, there will be no material increase in productions in the remaining products:

	Raw Material and Final Product Variation			
	Now	**After Project**	**Var. (Kton/yeas)**	**Var (%)**
Crude	[…]	[…]	[…]	[8-11]**%**
	Final Products			
Naphtha	[…]	[…]	[…]	[35-50]**%**
Gasoline	[…]	[…]	[…]	[0-2]**%**
Jet Fuel	[…]	[…]	[…]	[(-2)-1]**%**
Diesel	[…]	[…]	[…]	[35-60]**%**
Fuel Oil	[…]	[…]	[…]	[(-20)-(-2)]**%**

– The Portuguese authorities highlight that the horizontally related products (paraffin waxes, sulphur, bitumen, etc) are not affected as well by the project. These are products that present no changes in their productive output or that actually decrease the total amount produced and that, therefore, should not qualify as products concerned by the investment project.

– According to the Portuguese authorities, diesel is a final product, whereas naphtha is an intermediary product which is used in its totality by Petrogal for its own production of petrochemical products and as a mixture component of gasoline. The production capacity of naphtha will increase as from [400-500] kton/year before the project up to [500-600] kton/year after the investment project will be completed.

– Naphtha can be used as feedstock by the petrochemical industry, and it can also be used as component for the gasoline (light naphtha) or to produce reformate (heavy naphtha). If case that the naphtha output will be exclusively used as an intermediate product by Petrogal, the Commission would need to assess the downstream product (according to point 69 of the RAG), but the Portuguese authorities have not submitted information on all the final product(s) for which naphtha is used.

– Following the above, the Commission considers that it can be accepted that the further compatibility assessment of this measure concerns the direct production of (1) diesel, of (2) final products derived from naphtha and possibly (3) naphtha, in case it appears that Petrogal is active also on the market with sales of naphtha to third parties.

Relevant product market

– Point 69 of the RAG stipulates that the relevant 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).

Diesel

– For diesel, the Portuguese authorities claim that from a producer point of view, this new processing units will lend flexibility in terms of choice of crude oils to be processed, and will fill the deficit in the production of diesel for the Portuguese refining system, precluding the need to import these products. Shift in the production cannot be automatically achieved. On the other hand, from the supply/producer side the Commission has considered in a previous merger decision[11] that there is a considerable degree of substitutability between refined products, since refineries can react, as to certain extent, to changes in the demand of certain types of product. Since these two opinions appear to be contradictory, the Commission has doubts on the substitutability of refinery products from the supply side, since it may appear possible to change the refinery's configuration.

– In the same merger decision, the Commission has considered that "on the demand side there is much less substitutability" as "both fuels and lubricants are manufactured for specific uses and are not substitutable for the vast majority of applications". Therefore it can be concluded that it can be established that there are no substitutes for diesel from the consumer side.

– Given the doubts on the supply side substitutability, the Commission can not conclude at this stage on the diesel market as the relevant product market.

[11] Merger decision COMP/M.727 BP/Mobil of 7.8.1996

Naphtha and final products derived from naphtha

– As for naphtha, the other product considered by the Portuguese authorities as relevant for the notified investment project, the Commission is unable to determine at this stage its degree of substitutability. This is due to the fact that the Portuguese authorities have not provided further information on this product.

– Moreover, the Commission is unable to identify the product markets for final products derived from naphtha, since the final products have not yet been fully identified.

Definition of the relevant market in terms of ex-refinery, non-retail and retail sales

– The Portuguese authorities consider that the only relevant market for assessment of this investment are the **ex-refinery sales of diesel and naphtha**, while the wholesale or retail levels should not be taken into account[12].

– The Portuguese authorities refer to a recently published In-depth Report on Fuels drafted by the Portuguese Competition Authority ("PCA")[13]. In a thorough analysis of the prevailing market conditions in Portugal, this report specifically mentioned that the activities of refining and importing are in the same first level of distribution of liquid fuels, i.e., sales at ex-refinery level.

– Sales at ex-refinery level are different from sales at the non-retail level, thereby constituting separate product markets. The Portuguese authorities claim that the production of refined products falls immediately in this level of the production chain: the ex-refinery sales. Therefore, any material change in the refining activity impacts directly that level of production.

– Recent merger decisions[14] consider that the relevant product market is that of downstream oil activities. Downstream oil activities include crude oil refining, as well as the marketing and distribution, at ex-refinery/cargo, non-retail and retail levels, of refined products to customers. The Commission has found in

---

12 In previous merger decisions "the Commission stated that motor fuels can be sold directly from the refinery to third parties in cargo (ex-refinery sales) and they can be resold to retailers and other large industrial customers (non-retail sales). (…) The Commission found that ex-refinery sales and non retail sales constitute two separate product markets". At a further downstream level, the production of diesel could concern also the retail sales of motor fuels (diesel, as well as gasoline and automotive LPG), that "include sales made to motorists from branded and unbranded service stations". See merger decision COMP/M.5005 GALP Energia / Exxonmobil Iberia, referring to COMP/M.4588 Petroplus/Coryton Refinery Business.

13 This report on the sector in Portugal includes the conclusions of a year's long in depth investigation work by the PCA: Autoridade da Concorrência, *Relatório Final sobre os Sectores dos Combustíveis Líquidos e do Gás Engarrafado em Portugal*, Lisbon, 31 March 2009 - published on the website the Portuguese Competition Authority: http://www.concorrencia.pt/Publicacoes/Autoridade.asp.

14 COMP/M.1383 - Exxon/Mobil, COMP/M.4348 - PKN/Mazeikiu

merger cases that both at the ex-refinery and non-retail levels is not possible to aggregate the different types of fuels into one category.

– The Commission has identified in previous merger decisions the differences between (i) ex-refinery sales and (ii) wholesales of fuels. Ex-refinery sales consist of sales made in large lots on a spot basis by refiners to other oil companies, traders, resellers and large industrial customers. These transactions typically involve single deliveries/purchases of lots, and are priced on the basis of market quotations. The delivery location is ex refinery.

– In the decision Galp Energia/Exxonmobil Iberia[15], the Commission found that ex-refinery sales and non-retail sales constitute two separate product markets. At ex-refinery level, GALP is active in the supply of refined oil products on the ex-refinery/cargo market with the two only refineries situated in Portugal. At the downstream level of refined product, the same decision considered the following markets: (i) retail and (ii) non-retail sales of motor fuels, (iii) LPG, (iv) lubricants, (v) bitumen and (vi) aviation fuel.

– It derives that in addition to the previously mentioned doubts on the relevant product market(s), the Commission could not conclude in the case of diesel if the relevant product market is the ex-refinery/cargo level only, or if the wholesale (non-retail) and retail sales should also be taken into account. Similarly, it is not clear whether the relevant product market resulting from the increased capacity for naphtha is the ex-refinery market for naphtha or rather the downstream market for the final products of naphtha. The Commission invites third parties to submit comments in this respect.

Relevant geographic market

– Point 68 of the RAG indicates that the relevant geographic market should normally be the EEA.

Diesel

– The Portuguese authorities suggested in the notification that the relevant geographical market for diesel **at ex-refinery level** would be at least regional (Iberian) or EEA-wide, and support their position referring to two decisions[16].

– To support their position, the Portuguese authorities also argue that prices at ex-refinery level are set according to international product price quotations ("Rotterdam Commodity Exchanges").

---

15 COMP/M.5005 - Galp Energia/Exxonmobil Iberia

16 In merger decision COMP/M.727 (BP/Mobil) of 1996 concerning fuels, the Commission concluded in particular, for diesel that, "*the relevant geographical market for ex-refinery sales appears to be EU or Western European wide. Refined products are traded ex-refinery in Western Europe at competitive prices which are freely available*". In merger decision COMP/M.3291 (Preem/Skandinaviska Raffinaderi), "on the basis of the significant imports and exports between the Scandinavian countries and the high level of overall imports" the Commission decided in 2003 that "it is reasonable to conclude that the relevant geographic market is at least Scandinavian (meaning here Finland, Norway, Sweden and Denmark)", given that the case did not raise competition concerns. Nonetheless, these merger decisions refer to regions in Europe other than Portugal and the Iberian Peninsula, and therefore they do not allow to define the geographic market for the purpose of the present decision

– As from the comprehensive analysis of the refinery sector in Portugal contained in the final report[17] of the Portuguese Competition Authority it results that, in absence of trade barriers on the import of refined products, the ex-refinery prices do not depend directly on the price for crude oil and its refining costs, but they are rather equal to the international reference prices – in the case of Portugal, the so-called *Platts* (*Rotterdam*) prices for the north-western European region (NWE).

– The report confirms that in Portugal in 2007-2008 the price for liquid fuels – ex-refinery – corresponded to the international reference price (*Platts* NWE) plus relevant spreads (transport, freight, insurance, losses, and others). This is also due to the fact that the two Portuguese refineries can process heavy crude oils, which are used as reference on the international market.

– Customers on the ex-refinery market can import fuels, in case the ex-refinery prices charged by GALP would be higher than *Platts* prices plus spreads.

– Moreover, refining net margins depend rather on market dynamics than on operation costs which are relatively stable. The Portuguese Competition Authority concludes that profit margins are determined by the international market, being therefore exogenous to the players.

– The differences in ex-refinery prices are only affected by the cost of transportation and/or mark-ups. The transportation costs are low and amount to about 3% of the product price on the Portuguese market.

– This result is reflected also in the analysis of the profit margin of the refinery sector in Portugal. The profit margin of refineries is determined in different stages. Gross profit margin can be calculated by subtracting the *Brent* crude oil price from ex-refinery prices. To calculate the net profit margin, on the other hand, the Commission would have to take into account many other variables (as the utilization rate of installed capacity in refineries, the composition of the final products, etc.).

– As for the profit margins for every single final refinery product, it can be very different, depending on the regional ex-refinery prices for these products. These margins have to be differentiated depending on the technical features of the refineries (presenting each a different production mix). In the specific case, the refining net margin for the refinery in Sines compares to the *Rotterdam cracking* margin, while for the refinery in Matosinhos it compares to the *Rotterdam hydroskiming* margin.

– In the above mentioned final report of the Portuguese Competition Authority, point 746 reads "it should be noted that the refining net margins tend to be cyclic. Normally, they decrease with the accentuated increase of the oil price and they increase in the opposite scenario, since most of the other costs present a relevant fix component". Refining net margins depend rather on market dynamics than on operation costs which are relatively stable. The Portuguese Competition Authority concludes that these margins determined by the international market, being therefore exogenous to the players. In the

[17] Autoridade da Concorrência, *Relatório Final sobre os Sectores dos Combustíveis Líquidos e do Gás Engarrafado em Portugal*, Lisbon, 31 March 2009 - mentioned above.

specific case of Petrogal, ex-refinery prices are established with reference to *Platts Rotterdam* prices.

- The refining capacity of Petrogal's two refineries represents 19.6% of the whole refining capacity of the Iberian Peninsula, the rest in Spain being controlled by Repsol (47%), Cepsa/Total (27%) and BP (6%)[18]. Nonetheless, the ex-refinery sales market takes into account both the refining capacity as well as the sales of imports (limited by the storing capacity of the undertakings). The sales market share for each competitor is covered both by production and imported products.
- The Commission considers that the price element would justify a relevant geographic market wider than the national (Portuguese) or Iberian ex-refinery market. On the other hand, this 3% gap in terms of product price could confer to GALP a commercial advantage which may have an impact on competition.
- It also appears that previous merger decisions do not apply to define the geographic market for sales at ex-refinery level for the purpose of the present decision, either because they refer to regions in Europe different than Portugal and the Iberian Peninsula, or because sales at the ex-refinery level have not been taken into account.
- On the other hand, in case the **non-retail (wholesale) and retail markets** are to be taken into account, in a more recent merger decision[19] concerning the aid beneficiary the Commission analysed the market position of GALP for refinery products (gasoline, diesel, motor fuels, LPG, industrial lubricants, bitumen and aviation fuels) and under point 43, it is mentioned that "a number of respondents expressed concerns about a further reinforcement of GALP" resulting from the proposed merger. In the current case, doubts are raised by the reinforcement of GALP's position that could derive from the investment project supported with State aid. In this merger decision, the Commission had not to define the market at ex-refinery level since this was not the object of the merger. For the non retail market of gasoline and diesel, the Commission considered as appropriate the national perspective (i.e. Portugal) since the market investigation pointed to technical and administrative barriers between Portugal and Spain[20].
- Consequently doubts remain as to whether the relevant geographic markets for diesel should be defined as EEA-wide, or rather on national or regional (Iberian) level.

Naphtha and final products derived from naphtha

- As for the relevant geographic market for naphtha, in absence of a clear view of the relevant product market, and despite the assumption of the Portuguese authorities that the relevant geographic market ought to be considered the EEA or the world market, doubts remain as to whether the relevant geographic

---

[18] Report by the competition Authority on fuel market in Portugal, Lisbon, 2 June 2008, published on the website the Portuguese competition Authority: http://www.concorrencia.pt/Publicacoes/Autoridade.asp

[19] Merger decision COMP/M.5005 GALP/Exxonmobil of 31.10.2008

[20] Merger decision COMP/M.5005 GALP/Exxonmobil of 31.10.2008, §23.

markets for this product should be defined as EEA-wide, or rather on national or regional (Iberian) level. The Commission invites third parties to submit comments in this respect.

Market shares

– In accordance with point 68(a) of the RAG, the Commission must verify if the aid beneficiary accounts for more than 25% of the sales of the products concerned on the markets concerned before the investment or if it will account for more than 25% after the investment. Apart from the geographic market, it needs to be decided which is the group level (Petrogal/GALP or ENI Group) that has to be assessed. Indeed, Galp Energia is considered to be jointly controlled by the shareholders that are parties to the Shareholder Agreement (Amorim Energia, CGD and ENI). Therefore, according to Portuguese authorities, in the particular case of ENI, it cannot control and solely define strategies between its refining activities and the refining activities of Petrogal. However, ENI has a blocking position, and it may have to be considered that ENI has a dominant influence on Galp Energia[21].

– The Commission has requested the Portuguese authorities to submit data on the market shares for Iberia and EEA also at the group level (ENI). The Portuguese authorities have refused to provide this data, considering that "(i) is not necessary for a competitive assessment of the impact of the project, on the other hand, (ii) is the concept of the undertaking concerned dictates that the assessment should be confined to GALP and, finally, (iii) is that GALP should not be required, due to the inherent confidentiality of the information, to deliver information concerning other companies and, in particular, any competitors".

– In order to establish the market shares of the aid beneficiary (GALP) on all the potentially relevant product and geographic markets concerned by the investment project, the Portuguese authorities submitted during the notification phase the following table:

Product Concerned	**Market Level**	**Market Share**					
		Portugal		**Iberia**		**EEA**	
		2007	**2012**	**2007**	**2012**	**2007**	**2012**
Diesel	Ex-Refinery	[70-100] %	[70-100] %	[15-20] %	[15-20] %	[1-3] %	[1-3] %
	Non Retail	[30-50] %	[25-45] %	[5-15] %	[5-15] %	n.a.	n.a.

21 Recent controversy took place concerning Amorim's notion to acquire ENI's stake in GALP. According to own publications, ENI has no incentives to adhere to its participation in the long-run. Conflicts of interest can occur, with a continuing participation of ENI in GALP. The relation between Amorim and ENI is strained, as Amorim is expecting conflicts of interest due to representatives of ENI, serving as directors on GALP's board.

Gasoline	Ex-Refinery	[90-100] %	[80-100] %	[15-30] %	[15-30] %	[0-3] %	[0-3] %
	Non Retail	[25-30] %	[20-30] %	[10-20] %	[10-20] %	n.a.	n.a.
Motor Fuels	Retail	[30-45] %	[25-40] %	[5-15] %	[5-15] %	n.a.	n.a.
LPG	Ex-Refinery	[45-65] %	[35-50] %	[15-25] %	[15-25] %	[0-3] %	[0-3] %
	Non Retail	[35-45] %	[35-45] %	[10-15] %	[10-15] %	[0-3] %	[0-3] %
Automotive Lubricants		[25-35] %	[25-35] %	[4-10] %	[4-10] %	[0-1] %	[0-1] %
Industrial Lubricants		[15-30] %	[20-35] %	[1-10] %	[1-10] %	[0-1] %	[0-1] %
Naphtha		[55-70] %	[55-70] %	[15-25] %	[15-25] %	[0-3] %	[0-3] %
Paraffin Wax **		[25-35] %	n.a.	n.a.	n.a.	n.a.	n.a.
White Spirit **		[15-25] %	n.a.	n.a.	n.a.	n.a.	n.a.

* *n.a. – data not available*

** *These are by-products to GALP and so there is no economic drive for their production. Therefore Galp is not aware of market evolution on these by products which are traded when there is a need in the market or a request from a buyer.*

– This table is based on assumptions on market evolution as presented by the aid beneficiary (Petrogal/GALP). Moreover, for the previously mentioned reasoning, the estimate provided by the Portuguese authorities does not take into account the market shares at group level (ENI).

– The Commission raises the doubt that the relevant geographic markets for diesel and naphtha is the national (Portuguese) or possibly the regional (Iberian) market, rather than EEA as considered under point 68(a) of the RAG. Thus, in case the Commission would consider the national (Portuguese) market as the relevant geographic market for diesel and naphtha at ex-refinery (and for diesel also at non-retail level), then the market share of the beneficiary (GALP) would be clearly above the threshold (25%), also according to data provided by the Portuguese authorities and by the beneficiary.

– The Commission notes that the market share data provided by the Portuguese authorities during the notification phase are not consistent from one table to another, and it is not clear whether they refer to Petrogal's refining capacity only, to sales of Petrogal's own production or to GALP's sales in general (production plus imports). The Portuguese authorities have been unable, during the notification phase, to provide the Commission with a clear overview of GALP's market position, especially on the regional (Iberian) and EEA markets. On the other hand, the same authorities consider that these should be the relevant geographic markets. Moreover, the market shares estimated by the Portuguese authorities (percentages based on data in tables provided by Galp Energia) are calculated on market growth assumptions estimated by the aid beneficiary and not on data contained in independent studies.

– In addition, as the Commission cannot define the relevant products, product markets and geographical markets in a definite manner at this stage, it would be difficult to make any meaningful analysis of market shares. However, it is worth noting that on at least some of the plausibly relevant market, the market share would be superior to 25%. For example, from the table above appears that in 2007 GALP's market share for diesel at ex-refinery level in Portugal was 87%. Similarly, for naphtha GALP's markets share at ex-refinery level was 63% at national level.

– The Commission concludes that test under point 68(a) does not allow at this stage to exclude without doubts that Petrogal, and respectively the GALP/ENI group(s) to which Petrogal belongs, has a market share below 25% on the relevant market(s). On the basis of information at its disposal the Commission has difficulties, at this stage, to establish the appropriate market definitions, and to establish the facts it would need to carry out market share tests for all plausible market delineations. For these reasons the Commission has doubts as to the conformity of the notified measure with the test under point 68(a) of the RAG.

Production capacity

– In accordance with point 68 (b) of the RAG, the Commission must verify if the capacity generated by the project exceeds 5% of the market measured using apparent consumption, unless the average annual growth rate of the apparent consumption of the products concerned over the last five years is above the average annual growth rate of the EEA’s GDP.

– The Compound Annual Growth Rate (CAGR) of the apparent consumption of diesel in the EEA for the year 2001 to 2006 is around 2.12% in volume terms, or 15.38% in value terms. As for the market for naphtha, the Compound Annual Growth Rate (CAGR) of the apparent consumption of naphtha in the EEA for the year 2001 to 2006 is around 2.13% in volume terms, or 15.34% in value terms. The corresponding Compound Annual Growth Rate (CAGR) of the European Economic Area's GDP for the years 2001 to 2006 reached 2.06% in real terms (to be equated to volume terms), and 4.12% in nominal terms (to be equated to value terms).

– It results that the markets for diesel and naphtha shall not be considered underperforming if the Commission considers the CAGR, both in volume and in value terms, compared respectively to the GDP growth rate in nominal and real terms. Therefore it is not necessary to check whether the capacity generated by the project is more than 5% of the market concerned.

– Nevertheless the Commission may need to verify this condition for other potential products concerned.

3.5 *Doubts and grounds for opening*

– For the reasons set out above, the Commission, after a preliminary assessment of the measure, has doubts as to whether the notified aid can be considered compatible with several points of the RAG.

– In this respect, the Commission recalls the doubts it has expressed in the present decision as to whether:

  - the investment project falls into the standard categories of initial investment project within the meaning of point 34 of the RAG,
  - the investment project contributes towards a coherent regional development strategy within the meaning of point 10 of the RAG,
  - the State aid is necessary to the implementation of the investment,
  - the incentive effect requirements laid down in point 38 of the RAG are met,
  - this large investment project is a single investment project within the meaning of point 60 of the RAG,
  - the relevant products concerned are exclusively diesel and naphtha, as claimed by the Portuguese authorities, or also other products from the refining activity, given the potential substitutability of refinery products from the supply side and the fact that naphtha may be considered an intermediate product within the meaning of point 69 of the RAG;
  - the relevant product market is to be considered being at ex-refinery level for both diesel and naphtha, as claimed by the Portuguese authorities,
  - the relevant geographic markets for the products concerned shall be defined at national, regional (Iberian peninsula) or EEA level,
  - the beneficiary Petrogal, and respectively the GALP/ENI group(s) to which Petrogal belongs, have a market share below 25% of the relevant market (point 68 (a) of the RAG),
  - for all the products concerned, in the option the production capacity created by the project is more than 5 % of each market measured using apparent consumption data, the average annual growth rate of its apparent consumption over the last five years is above the average annual growth rate of the European Economic Area's GDP.

– Therefore, given the mentioned doubts on the conformity of the measure with the RAG and as provided for in point 68 of the RAG, the Commission will approve regional aid only after a detailed a 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 and effect on trade between Member States.

– Consequently, the Commission is under duty to carry out all the required consultations and, therefore, to initiate the procedure under Article 88(2) of the EC Treaty, if the initial investigation does not enable the Commission to establish that the measure is in line the RAG. This would give the opportunity to third parties whose interest may be affected by the granting of the aid to comment on the measure. In the light of both the information notified by the Member State concerned and that provided by any third parties, the Commission will assess the measure and will take its final decision.

– The Commission also has to investigate whether 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 and effect on trade between Member States[22].

– In footnote 63 of the RAG, the Commission announced its intention to "draw up further guidance on the criteria it will take into account during this assessment". This announcement has been implemented by the adoption of the Commission Communication on Criteria for an In-Depth Assessment of Regional Aid to Large Investment Projects[23] which will serve as the basis of the in-depth assessment. In particular, the following criteria will be considered: objective of the aid, appropriateness of the aid instrument, incentive effect, proportionality of the aid, crowding out of private investment and effects on trade. At this stage, it appears that competition could be distorted especially where market shares of the beneficiary exceed 25 % of the sales of the products concerned on the markets concerned.

– In view of this in-depth assessment, interested parties are invited in particular to provide all information necessary to establish the economic incentive effect of the aid, i.e. whether the aid gives an incentive to adopt a positive investment decision because an investment that would otherwise not be profitable for the company at any location can take place in the assisted regions. Under this scenario it would be necessary to consider the counterfactual situation (i.e. what would happen in the absence of aid) and thus the possible distortion of competition and trade caused by the aid.

– The Commission therefore requests the Member State and third parties to provide any available evidence which would allow the Commission to substantiate its assessment of the measure. In particular, the Commission seeks input from the Member State and from third parties on the following issues:

  i. Initial investment project

  Given the project does not constitute an aid into a new establishment; the Commission seeks evidence on the initial investment nature of the

---

22 This may include, among others, effects on the location of the investment with regards to the incentive effect.

23 Communication from the Commission concerning the criteria for an in-depth assessment of regional aid to large investment projects, OJ C 223, 16.09.2009, p. 3.

investment project in question within the meaning of point 34 of the RAG.

ii. Single investment project

Given the distance between the two sites, the Commission seeks evidence on the single investment nature of the investment project in question within the meaning of point 60 of the RAG.

iii. Objective of the aid

The Commission seeks evidence on how the project would significantly contribute to the development of the concerned regions. Besides the cohesion objective inherent to any regional aid intervention, evidence on potential market failures addressed by the measure such as imperfect information, coordination failures, public goods, externalities will contribute to substantiate the positive effect of the measure such as spill-over effects.

iv. Appropriateness of the aid instrument

The Commission seeks clarification from the Member State of why regional aid to the undertaking in question constitutes an appropriate instrument to achieve the cohesion objective.

v. Incentive effect and proportionality of the aid

The Commission seeks evidence on what the undertaking in question does differently as a consequence of the aid. The Member State could provide company documents (e.g. business plans, risk assessments, financial reports, expert opinions) as well as other documents (containing information on demand forecasts, cost forecasts, financial forecasts) that show that the investment would not have been profitable without the aid and that no other location than the assisted region concerned could be envisaged. The Commission asks the Member State to explain the methodology used to evaluate the level of profitability of the investment project, in order to verify whether the return on investment is in line with the normal rate of return applied by the beneficiary in other investment projects.

vi. Necessary information to conclude on conditions required by points 68 and 69 of the RAG

At this stage, the Commission is not in position to conclude on relevant products, on the relevant product market(s), the relevant geographic market(s) and on market share issues on the basis of the notified information. The Member State is requested to provide the Commission with the necessary information at both GALP and ENI group level.

More specifically, the Commission asks the Member State to provide all information in order to be able to define the relevant market(s), as well as to produce clear and consistent data tables for all relevant product market(s), all relevant geographic market(s) and for the beneficiary's market shares.

The Commission also asks the Member State to provide independent studies to confirm the information contained in these data tables, especially with data confirming the forecasts produced by the Member State in the notification.

The Commission invites also third parties to submit comments in this respect.

vii. Effect on trade and competition

The Commission seeks evidence concerning any potential effect on competition on the relevant markets and indications as to which the project leads to reinforcing the existing situation of the beneficiary and its potential impact on production or investment in other regions of the Community, in the market concerned (including loss of positive externalities such as clustering effect, knowledge spill-overs, education and training, etc.).

– On the basis of the evidence submitted concerning the above mentioned issues, the Commission will perform a balancing exercise of the positive and the negative effects of the aid, conducting an overall assessment of the impact of the aid in each of the markets concerned, in such a way as to allow the Commission to close the formal investigation procedure.

4. DECISION

In light of the foregoing considerations, the Commission, acting under the procedure laid down in Article 88(2) of the EC Treaty, requests Portugal to submit its comments and to provide all such information as may help to assess the aid measure, within one month of the date of receipt of this letter. It requests your authorities to forward a copy of this letter to the potential recipient of the aid immediately.

The Commission wishes to remind Portugal that Article 88(3) of the EC Treaty has suspensory effect, and would draw your attention to Article 14 of Council Regulation (EC) No 659/1999, which provides that all unlawful aid may be recovered from the recipient.

The Commission warns Portugal that it will inform interested parties by publishing this letter and a meaningful summary of it in the Official Journal of the European Union. It will also inform interested parties in the EFTA countries which are signatories to the EEA Agreement, by publication of a notice in the EEA Supplement to the Official Journal of the European Union and will inform the EFTA Surveillance Authority by sending a copy of this letter. All such interested parties will be invited to submit their comments within one month of the date of such publication.

If this letter contains confidential information which should not be published, 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 publication of the full text of this letter. Your request specifying the relevant information should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition

State Aid Register
B-1049 Brussels
Fax (32-2) 296 12 42

Yours faithfully,
For the Commission
Neelie KROES
Member of the Commission