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<p>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 [...].</p>	<p style="text-align: center;">PUBLIC VERSION</p> <p>This document is made available for information purposes only.</p>
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### ***COMP Operations***

**Subject: State aid SA.35956 (2013/C) (ex 2013/NN) (ex 2012/N) – Estonia**  
***Rescue aid to Estonian Air***

Sir,

The Commission wishes to inform Estonia that, having examined the information supplied by your authorities on the measures referred to above, it has decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union.

#### **1. PROCEDURE**

- (1) On 3 December 2012, in the context of pre-notification contacts, Estonia submitted to the Commission information on its plans to provide rescue aid in favour of AS Estonian Air (hereinafter "Estonian Air" or "the airline") as well as

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on several capital injections carried out in the past. A meeting with representatives of the Estonian authorities took place on 4 December 2012.

- (2) Following these pre-notification contacts, by SANI notification number 7853 of 20 December 2012, Estonia notified to the Commission the planned provision of rescue aid to the airline in the form of a loan amounting to EUR 8.3 million.
- (3) On the basis of the information provided by the Estonian authorities, it appeared that the first tranche of the rescue loan was disbursed to Estonian Air on 20 December 2012. For this reason, the Commission registered the case as non-notified aid (2013/NN) and informed Estonia by letter of 10 January 2013.
- (4) The Commission requested additional information by letter of 10 January 2013, to which the Estonian authorities replied by letter of 21 January 2013.

## **2. THE BENEFICIARY**

- (5) Estonian Air, a stock company under Estonian law, is the flag carrier airline of Estonia, based in Tallinn Airport. Currently, the airline has more than 300 employees and operates a fleet of 10 aircraft.
- (6) Estonian Air has a 100%-owned subsidiary, AS Estonian Air Regional, which operates commercial flights to neighbouring destinations in cooperation with Estonian Air. It also participates in two joint companies: Eesti Aviokütuse Teenuste AS (51% share), which provides refuelling service to aircrafts at Tallinn Airport, and AS Amadeus Eesti (60% share), which provides Estonian travel agencies with booking systems and support.<sup>1</sup>
- (7) Estonian Air was formed as a state-owned company after the independence of Estonia in 1991 from a division of the Russian airline Aeroflot. Tallinn Airport and the airline were a single company until 1993, when the airline became an independent entity. In 1996, the State privatised 66% of the shares of the company. After privatisation, the shares were held as follows: 49% by Maersk Air, 34% by the Ministry of Economic Affairs and Communications of Estonia, and 17% by Cresco Investment Bank, a local investment bank. In 2003, SAS Group (hereinafter "SAS") bought in block the 49% stake of Maersk Air, while the other shareholdings remained the same.
- (8) At the end of 2010, Estonia decided to take majority ownership of the airline. With an injection of EUR 17.9 million by the State and EUR 2 million by SAS in September 2010, Estonia became majority owner of the airline with 90% of the shares, while SAS was diluted to 10%. Cresco Investment Bank ceased to be a shareholder at this point in time.
- (9) In November 2011, Estonia decided to invest EUR 30 million in Estonian Air, which was done in two equal segments: EUR 15 million in December 2011 and EUR 15 million in March 2012. As a result, Estonia increased its shareholding in the airline to 97.34%, while SAS was further diluted to 2.66%. Since then, the shareholding structure of Estonian Air has not changed.

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<sup>1</sup> See <http://estonian-air.com/en/about-us/>.

\* Covered by the obligation of professional secrecy.

### **3. DESCRIPTION OF THE MEASURES**

#### **3.1. The 2009 capital increase (measure 1)**

- (10) According to the information provided by the Estonian authorities, two issues caused the airline to seek new capital from its shareholders in 2009. [...] Second, the business model did not work under the stress of the financial crisis, and the airline faced liquidity problems at the end of the year.
- (11) As a result, in February 2009 all the shareholders increased proportionally the airline's capital by EUR 7.3 million. Thus, the State provided EUR 2.48 million of capital but the shareholding structure of Estonian Air did not change (recital (7) above).

#### **3.2. The sale of the groundhandling section in 2009 (measure 2)**

- (12) In 2009, Estonian Air sold its groundhandling business to the State-owned Tallinn Airport at a price of EUR 2.3 million. At the time of the sale, Tallinn Airport was 100% owned by Estonia.
- (13) The Estonian authorities have explained that an open, transparent and unconditional tender did not take place. Also, the sale price was not based on an expert opinion but it was based on the book value of the assets for sale. Depreciated assets were taken into account by adding value. According to the Estonian authorities, the price was established during negotiations between Tallinn Airport and the airline.

#### **3.3. The 2010 capital injection (measure 3)**

- (14) As explained in recital (8) above, at the end of 2010, Estonia decided to take majority ownership of the airline. With an injection of EUR 17.9 million by the Estonian State and of EUR 2 million by SAS in September 2010, Estonia became majority owner of 90% of the shares, while SAS was diluted to 10%. It appears that the participation of SAS to the 2010 capital injection was carried out through a loan-to-equity conversion.
- (15) The decision was taken as the Estonian Government wanted to ensure long-term flight connections to the most important business destinations and saw gaining control of the airline through a capital injection as the best way to reach this objective. The decision to acquire majority ownership of the airline was based on a business plan (hereinafter "the 2010 business plan") which presented an opportunity to invest into a growing and profitable company.
- (16) The capital was allegedly used for [...].
- (17) Cresco Investment Bank, which had held 17% of the shares of Estonian Air since the company's 1996 privatization, [...] refused injecting more money in the airline and rather decided to cease to be a shareholder.<sup>2</sup>

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<sup>2</sup> See Baltic Reports of 7.6.2010, *Government sets bailout deal for Estonian Air*, <http://balticreports.com/?p=19116>.

### **3.4. The 2011/2012 capital increase (measure 4)**

- (18) In 2011/2012, Estonia injected EUR 30 million in capital and increased its stake to 97.34% (recital (9) above). The capital injection was carried out in two tranches of EUR 15 million each, one in December 2011 and the other in March 2012. SAS did not participate to this capital injection and its shareholding was diluted from 10% to 2.66%.
- (19) The capital injection was carried out on the basis of a business plan presented by the CEO of Estonian Air in 2011 (hereinafter "the 2011 business plan"). The 2011 business plan was based on the assumption that a bigger network and more frequencies would improve the airline's competitiveness. It was considered that a good hub structure (hub-and-spoke network) would attract passengers and allow flexibility to reallocate traffic through hubs to counter seasonality or sudden changes in demand. In addition, the hub volumes were considered to allow the lowering of seat cost by utilising bigger aircraft. The regional network model was considered to allow the airline to grow in size and reduce risks. The business plan also implied an increase of connections to and from Estonia, of the fleet and consequently an increase of staff to handle more round trips. The 2011 business plan promised good returns and an opportunity to ensure Estonian Air's long term viability.
- (20) The capital injection by Estonia was apparently planned alongside a loan from the private bank [...]. Although the Estonian branch of the bank allegedly approved the loan through its credit committee, the loan was in the end refused by the highest credit committee [...].

### **3.5. The notified rescue loan (measure 5)**

- (21) In view of the bad mid-2012 results of Estonian Air (losses of EUR 14.9 million)<sup>3</sup>, it became clear to the management of the airline that the strategy of the 2011 business plan had not succeeded. Therefore, Estonia decided to grant additional measures to the airline, this time in the form of rescue aid.
- (22) The notified rescue measure consists of a loan amounting to EUR 8.3 million provided by the Ministry of Finance of Estonia. The loan will be disbursed in four instalments. The Commission notes that the first instalment of EUR 793,000 has already been disbursed on 20 December 2012 and the second instalment of EUR 2,938,000 in January 2013<sup>4</sup>. The loan has to be reimbursed until 20 June 2013. An annual interest of 15% will be charged for the loan.
- (23) Estonia committed to communicate to the Commission a restructuring plan or a liquidation plan or proof that the loan has been reimbursed in full not later than six months after the first implementation of the rescue aid measure.

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<sup>3</sup> See Estonian Air's review of performance for the first half of 2012, available at [http://estonian-air.com/public/Annual\\_Reports/EA\\_Review\\_1stHalf2012.pdf](http://estonian-air.com/public/Annual_Reports/EA_Review_1stHalf2012.pdf).

<sup>4</sup> See also <http://www.e24.ee/1106240/estonian-airile-makstakse-valja-kolm-miljonit-eurot/>.

#### 4. COMMENTS OF THE ESTONIAN AUTHORITIES

- (24) The Estonian authorities underline the importance of Estonian Air for the national economy. [...]
- (25) As to the 2009, 2010 and 2011/2012 capital injections, the Estonian authorities argue that the measures were provided in accordance with the market economy investor principle (MEIP) since a normal private investor would have entered into the transactions in question on similar terms, taking into account the promised returns and the situation on the aviation market.
- (26) In relation to the 2010 capital increase, the Estonian authorities argue that it was rational for Estonia to invest in the airline at the time, given that the assumed return on this investment was considered to be higher than the cost of the capital increase. This would especially be so when the benefits of having a local airline were looked at from a macro-economic viewpoint.
- (27) Concerning the 2011/2012 capital injection of EUR 30 million, the Estonian authorities pointed to the fact that [...], as a private investor, was supposed to invest in Estonian Air the same amount on almost the same terms as the Estonian State. The Estonian branch of [...] had approved the loan in the beginning, although it was later rejected by the Head Office. Estonia argues that the rejection should be seen in the context of the relationship between the bank and the other shareholder of Estonia Air, i.e. SAS. [...].
- (28) Furthermore, the Estonian Government decided to inject money to Estonian Air mainly because in 2011, the 2011 business plan fed into the Government Action Plan for 2011-2015 to develop direct air links to all major European business centres and to turn Tallinn Airport into a hub for Asia-Europe flights. What was also kept in mind at that time was the fact that the Estonian market with its population and size of economy is too small to attract any other carrier to establish a base in a peripheral country like Estonia. Dependence on low-cost carriers was not considered ideal as they operate the market only as long as they are incentivised and can easily threaten to pull out.
- (29) Finally, Estonia considers that Estonian Air is to be considered a firm in difficulty in the sense of the Community guidelines on state aid for rescuing and restructuring firms in difficulty<sup>5</sup> (hereinafter "the R&R Guidelines") since June/July 2012, once the half-year results for 2012 made clear that the airline was not in a sustainable position. Thus, in the opinion of the Estonian authorities, Estonian Air would be a firm in difficulty only at the time of the notified rescue aid (measure 5).

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<sup>5</sup> OJ C 244, 1.10.2004, p. 2. The validity of the R&R Guidelines was initially set until 9 October 2009. However, the Commission decided to extend their validity first until 9 October 2012 (Commission Communication concerning the prolongation of the Community Guidelines on State aid for Rescuing and Restructuring Firms in Difficulty, OJ C 156, 9.7.2009, p. 3) and then, in the context of the state aid modernisation (SAM) initiative, until such time as the R&R Guidelines are replaced by new rules on state aid for rescuing and restructuring firms in difficulty (Commission communication concerning the prolongation of the application of the Community guidelines on State aid for rescuing and restructuring firms in difficulty of 1 October 2004, OJ C 296, 2.10.2012, p. 3).

## 5. ASSESSMENT

- (30) By virtue of Article 107(1) TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market. The concept of state aid thus applies to any advantage granted directly or indirectly, financed out of State resources, granted by the State itself or by any intermediary body acting by virtue of powers conferred on it.
- (31) To be state aid, a measure must stem from State resources and be imputable to the State. In principle, State resources are the resources of a Member State and of its public authorities as well as the resources of public undertakings on which the public authorities can exercise, directly or indirectly, a controlling influence.
- (32) In order to determine whether an economic advantage in favour of Estonian Air was present in the different measures under assessment and therefore whether these measures involve state aid, the Commission will assess whether the airline received an economic advantage which it would not have obtained under normal market conditions. To examine this question the Commission applies the so-called market economy investor principle (MEIP) test. In principle, a contribution from public funds does not involve state aid if it takes place at the same time as a significant capital contribution on the part of a private investor made in comparable circumstances and on comparable terms (*pari passu*).
- (33) According to the MEIP test, no state aid would be involved where, in similar circumstances, a private investor of a comparable size to that of the bodies concerned in the public sector, operating in normal market conditions in a market economy, could have been prompted to provide to the beneficiary the measures in question. The Commission therefore has to assess whether a private investor would have entered into the transactions under assessment on the same terms. The attitude of the hypothetical private investor is that of a prudent investor whose goal of profit maximisation is tempered with caution about the level of risk acceptable for a given rate of return.
- (34) Finally, the measures in question must distort or threaten to distort competition and be liable to affect trade between Member States.
- (35) Inasmuch as the measures under assessment entail state aid within the meaning of Article 107(1) TFEU, their compatibility must be assessed in the light of the exceptions laid down in paragraphs 2 and 3 of that Article. According to the case-law of the Court of Justice, it is up to the Member State to invoke possible grounds of compatibility and to demonstrate that the conditions for such compatibility are met.<sup>6</sup>

### 5.1. Difficulties of Estonian Air

- (36) As stated in recital (29) above, Estonia considers that Estonian Air would qualify as a firm in difficulty since June/July 2012, i.e. at the time of granting measure 5. However, in view of the fact that the Estonian authorities argue that

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<sup>6</sup> Case C-364/90 *Italy v Commission*, [1993] ECR I-2097, at para 20.

the capital injections provided to the airline in the past were in line with the MEIP (recital (25) above) and that the present decision covers several measures granted since 2009, the Commission considers it necessary to examine whether Estonian Air would qualify as a firm in difficulty at the time when the measures identified above were taken.

- (37) Recital 9 of the R&R Guidelines states that the Commission regards a firm as being in difficulty when it is unable, whether through its own resources or with the funds it is able to obtain from its owners/shareholders or creditors, to stem losses which without outside intervention by the public authorities, will almost certainly condemn it to going out of business in the short or medium term.
- (38) Recital 10 of the R&R Guidelines clarifies that a limited liability company is regarded as being in difficulty where more than half of its registered capital has disappeared and more than one quarter of that capital has been lost over the preceding 12 months, or where it fulfils the criteria under its domestic law for being the subject of collective insolvency proceedings.
- (39) Recital 11 of the R&R Guidelines adds that, even if the conditions in recital 10 are not satisfied, a firm may be considered to be in difficulty in particular where the usual signs of a firm being in difficulty are present, such as increasing losses, diminishing turnover, growing stock inventories, excess capacity, declining cash flow, mounting debt, rising interest charges and falling or nil net asset value.
- (40) The Commission first notes that Estonian Air has continuously registered significant losses since 2006 (table 1 below):

**Table 1: Net results of Estonian Air since 2006 (in EUR thousands)<sup>7</sup>**

2006	- 3 767
2007	- 3 324
2008	- 10 895
2009	- 4 744
2010	- 3 856
2011	- 17 120
30 September 2012	- 20 200

- (41) The significant losses of Estonian Air constitute a first indication of the difficulties of the airline. In addition, it appears that some of the usual signs of a firm being in difficulty (recital (39) above) were also present. For instance, it

<sup>7</sup> Source: annual reports of Estonian Air, available at <http://estonian-air.com/en/about-us/about-company/annual-reports/>. From 2006 to 2010 the annual reports of Estonian Air are expressed in Estonian kroon (EEK). The conversion rate used is EEK 1 = EUR 0.06391.

appears that Estonian Air's interest expenses have been constantly increasing since 2008, as showed in table 2 below:

**Table 2: Interest expenses of Estonian Air since 2006 (in EUR)<sup>8</sup>**

2006	- 94 523
2007	- 99 764
2008	- 94 842
2009	- 212 309
2010	- 337 325
2011	- 2 010 000
30 September 2012	Not available

- (42) Estonian Air's return on assets and return on equity have consistently been negative since 2006, while the debt-to-equity ratio constantly increased between 2006 and 2008, when it reached 83.8%. The reason why this ratio went down in 2009 and 2010 is due to the capital increases that took place in those years (measures 1 and 3) and not because Estonian Air's debt was reduced. In addition, between 2010 and 2011, the net debt of Estonian Air exploded, passing from EUR 3.469 million to EUR 47.568 million. The data for the first half of 2012 confirm this tendency.
- (43) In addition to the above, the Estonian authorities have explained that at the end of November 2011, the airline had only EUR [2-5] million in cash, and was [...], meaning the airline would have been in default of its loans to [...]. Also, Estonian Air stopped paying some major suppliers in November 2011 and by the end of that month the working capital was not in balance: the accounts receivable were EUR [4-6] million, while the accounts payable were EUR [8-12] million. Without the capital increase in December 2011, the airline would have been in default of its loans to [...]. Default of payment is a typical sign for a firm in difficulty.
- (44) The Commission also notes that more than half of the airline's equity disappeared between 2010 and 2011. In this period, the airline lost more than one quarter of its capital. Therefore, the criterion of recital 10(a) of the R&R Guidelines also seems to be fulfilled.
- (45) Despite the capital injections in December 2011 and March 2012, the airline's financial situation deteriorated in 2012. In May 2012, when calculating the financial results for April, a monthly loss of EUR 3.7 million was found, above the budgeted loss of EUR 0.9 million. In June 2012, Estonian Air revised its forecast for 2012 and forecasted EUR 25 million in operational losses for the year (the original budget, finalised in January 2012, forecasted an annual loss of

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<sup>8</sup> See footnote 6 above.



EUR 8.8 million). By the end of July 2012, Estonian Air had reached a state of technical bankruptcy under Estonian law. Therefore, as from this point in time, Estonian Air could also be considered a firm in difficulty on the basis of recital 10(c) of the R&R Guidelines.

- (46) On the basis of the above, the Commission is at this stage of the view that Estonian Air would qualify as a firm in difficulty on the basis of recital 11 of the R&R Guidelines at the time when the measures identified above were provided, this is, between 2009 and 2012. In addition, Estonian Air would also fulfil the requirements of recitals 10(a) and 10(c) of the R&R Guidelines at later points in time.

## **5.2. The 2009 capital increase (measure 1)**

### *Presence of state aid*

- (47) The Commission has first assessed the presence of state aid in respect of the 2009 capital injection (measure 1). As explained in recital (32) above, it is considered that a contribution from public funds does not involve state aid if it is carried out in *pari passu* terms. In this respect, the Commission notes that measure 1 was carried out by Estonian Air's shareholders in proportion to their stakes, i.e. 34% by Estonia (EUR 2.48 million), 49% by SAS (EUR 3.57 million) and 17% by the local investment bank Cresco (EUR 1.24 million).
- (48) Therefore, on the basis of the limited information available at this stage, it would preliminarily appear that the 2009 capital injection was carried out by the three shareholders at the time in *pari passu* terms. However, a concomitant and significant participation of private investors is just an indication of the absence of aid. In order to take a view on the presence of state aid, the Commission has to take into account all the factual and legal elements of the transaction that appear relevant.
- (49) In this connection, the Commission observes that from the 2009 annual accounts of Estonian Air it appears that the new shares were paid for through monetary contributions and through conversion of loans given to the airline, without providing details on what shareholder injected fresh money and who did a loan-to-equity conversion.<sup>9</sup> The different nature of the contributions (fresh money increase v. conversion of debt) appears sufficient to create reasonable doubts about whether the 2009 capital injection was indeed *pari passu*, in particular bearing in mind the difficulties of Estonian Air at the time (section 5.1 above). Therefore, the presence of an undue advantage to Estonian Air cannot be automatically excluded in relation to the State's participation to the 2009 capital injection.
- (50) In addition, for a measure to constitute state aid, it must stem from State resources and be imputable to the State. This criterion is not disputed in relation to the 2009 capital injection, given that it was the Ministry of Economic Affairs

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<sup>9</sup> It appears from the press that Estonia would have injected EUR 2.48 million in cash, whereas SAS would have contributed EUR 1.21 million in cash and EUR 2.36 million by converting loans. On the other hand, Cresco would have apparently injected EUR 1.23 million in cash. See <http://travelmoments.ca/2009/03/01/estonia-saves-ov/>. This information will need to be confirmed by Estonia.

and Communication of Estonia, as shareholder of the airline, who injected the capital.

- (51) Finally, the Commission observes that the measure affects trade and threatens to distort competition between Member States as Estonian Air is in competition with other airlines of the European Union, in particular since the entry into force of the third stage of liberalisation of air transport ("third package") on 1 January 1993.<sup>10</sup> The measure in question thus enabled Estonian Air to continue operating so that it would not have to face, as other competitors, the consequences normally deriving from its poor financial results.
- (52) Therefore, at this stage, the Commission has doubts whether measure 1 involved state aid in favour of Estonian Air.

*Compatibility with the internal market*

- (53) The Estonian authorities consider that measure 1 does not constitute state aid and have not provided any possible grounds for compatibility.
- (54) The Commission nonetheless considers at this stage that the exceptions laid down in Article 107(2) TFEU are not applicable and have not been invoked by the Estonian authorities. The same conclusion would apply to the exceptions foreseen in Article 107(3), points (d) and (e), TFEU.
- (55) In view of the fact that Estonian Air can be considered a firm in difficulty in 2009 when measure 1 was provided (section 5.1 above), it does not appear at this stage that the exception relating to the development of certain areas or of certain sectors laid down in Article 107(3)(a) TFEU could be applicable, despite the fact that Estonian Air is located in an assisted area under Article 107(3)(a) TFEU and could be eligible for regional aid. Also, as regards the crisis rules enshrined in the Temporary Framework<sup>11</sup>, the Commission notes that measure 1 does not appear to fulfil the conditions for its applicability.
- (56) Therefore, it appears that the compatibility of the 2009 capital injection can only be assessed under Article 107(3)(c) TFEU, and in particular in the light of the R&R Guidelines and the 1994 Aviation guidelines.<sup>12</sup> At this stage the Commission however doubts that measure 1 could be declared compatible with the R&R Guidelines, because it seems that several of the conditions and principles of the latter would not be met.
- (57) The Commission first notes that the conditions for rescue aid laid down in section 3.1 of the R&R Guidelines do not seem to be met: measure 1 is a capital

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<sup>10</sup> The "third package" included three legislative measures: (i) Council Regulation (EEC) No 2407/92 of 23 July 1992 on licensing of air carriers (OJ L 240, 24.8.1992, p. 1); (ii) Council Regulation (EEC) No 2408/92 of 23 July 1992 on access for Community air carriers to intra-Community air routes (OJ L 240, 24.8.1992, p. 8); and (iii) Council Regulation (EEC) No 2409/92 of 23 July 1992 on fares and rates for air services (OJ L 240, 24.8.1992, p. 15).

<sup>11</sup> Temporary Framework for state aid measures to support access to finance in the current financial and economic crisis, OJ C 16 of 22.1.2009, p. 1, as modified by the Communication from the Commission amending the Temporary Community Framework for state aid measures to support access to finance in the current financial and economic crisis, OJ C 303, 15.12.2009, p. 6. The Temporary Framework expired in December 2011.

<sup>12</sup> Guidelines on the application of Articles 92 and 93 of the EC Treaty and Article 61 of the EEA Agreement to State aids in the aviation sector, OJ C 350, 10.12.1994, p. 5.

injection and therefore does not consist of liquidity support in the form of loan guarantees or loans, it does not seem to have been provided on the grounds of serious social difficulties, it was not accompanied by an undertaking given by Estonia to communicate to the Commission a restructuring plan or a liquidation plan, etc.

- (58) The criteria for restructuring aid do not seem to be met either. Paragraph 34 of the R&R Guidelines requires that grant of the aid is conditional on implementation of a restructuring plan, which must be endorsed by the Commission in all cases of individual aid. If measure 1 was to be considered state aid, it would have been granted before notification to the Commission and in the absence of a credible restructuring plan satisfying the conditions laid down in the R&R Guidelines. This circumstance would in itself be sufficient to exclude its compatibility with the internal market.<sup>13</sup>
- (59) Also, at this stage the Estonian authorities have not put forward any possible compensatory measures and own contribution of Estonian Air, which constitute essential elements for finding a measure compatible with under the R&R Guidelines as restructuring aid.
- (60) Therefore, the Commission is at this stage of the view that measure 1 would constitute incompatible state aid.

### **5.3. The sale of the groundhandling section in 2009 (measure 2)**

#### *Presence of state aid*

- (61) The Commission has assessed the presence of state aid in respect of the sale of the airline's groundhandling section to Tallinn Airport in 2009 for a price of EUR 2.3 million. At the time of the sale, Tallinn Airport was 100% owned by Estonia.
- (62) The Commission first notes that the sale of assets to State-owned companies might involve state aid unless it can be demonstrated that the price actually paid constitutes the market price for the assets in question. Usually, state aid is excluded by an open, transparent and unconditional tender. In the absence of such a tender, a direct sale can be accepted if the price is based on the values established by independent valuers.
- (63) In the present case, Estonia has confirmed that neither an open tender was carried nor was the price established on the basis of an independent evaluation. The sale price was only established on the basis of the asset's book value. The Commission notes that it is cannot be excluded that the book value does not reflect the actual market price of the groundhandling section. The Commission also considers that adding value for those assets that were fully depreciated could also entail elements of state aid. The presence of an advantage to Estonian Air through the sale of its groundhandling section cannot thus be excluded.
- (64) In order to assess whether State resources are present, the Commission first notes that Tallinn Airport was 100%-owned by Estonia at the time of the sale. In

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<sup>13</sup> See in this sense the judgment of the EFTA Court in joined cases E-10/11 and E-11/11 *Hurtigruten ASA, Norway v EFTA Surveillance Authority*, not yet published, at paras 228 and 234-240.

addition, the annual report of Tallinn Airport for 2009 clearly indicates that the airport "*lies within the jurisdiction of the Ministry of Economic Affairs and Communications of the Republic of Estonia*" and that "*the exerciser of the shareholder's right [is] the Ministry of Economic Affairs and Communications, which is represented, on the General Shareholders' Meeting, by the Minister of Economic Affairs and Communications*". On this basis, the Commission is at this stage of the view that the decision to purchase the groundhandling section from Estonian Air in 2009 can be considered imputable to the State.

- (65) For the same reasons as those stated in recital (51) above, measure 2 affects trade and threatens to distort competition between Member States.
- (66) Therefore, at this stage, the Commission has doubts whether measure 2 involves state aid. The Estonian authorities are invited to provide sufficient information which enables the Commission to assess whether the sale price actually paid was market conform.

#### *Compatibility with the internal market*

- (67) At this stage, the Commission finds no grounds that could be used as a basis for finding measure 2 – were it to constitute state aid – compatible with the internal market. The arguments presented in recitals (54) to (59) above apply *mutatis mutandis*.
- (68) In addition, the Commission has doubts about the compliance with the 'one time, last time' principle of points 25(e) and 72 of the R&R Guidelines. Point 72 of the R&R Guidelines provides that a company that has received rescue and restructuring aid in the past ten years is not eligible for rescue aid.
- (69) Given that the Commission cannot exclude at this stage that the 2009 capital injection (measure 1) constitutes unlawful and incompatible rescue and/or restructuring aid, at this stage it cannot be excluded that by providing state aid to Estonian Air through measure 2, Estonia would have breached the legal requirement of the 'one time, last time' principle.

### **5.4. The 2010 capital injection (measure 3)**

#### *Presence of state aid*

- (70) The Commission has assessed the presence of state aid in respect of the 2010 capital injection (measure 3) by applying the MEIP test (recital (33) above).
- (71) The Commission notes that this injection was not carried out on *pari passu* terms. In fact, through this capital injection, Estonia became a majority owner of Estonian Air and gained 90% of the shares, while SAS was diluted to 10%. Cresco Investment Bank decided not to participate and ceased to be a shareholder. Therefore, the assumption that the MEIP is complied with based on a concomitant behaviour of both public and private shareholders cannot be considered.
- (72) In addition, the Commission notes that SAS apparently injected the capital through a loan-to equity conversion (recital (14) above). For the same reasons stated in recital (49) above, the different nature of the contributions (fresh money increase from the State v. conversion of debt from SAS) would appear

sufficient to create reasonable doubts about whether the 2010 capital injection was *pari passu*.

- (73) The Estonian authorities moreover argue that the 2010 business plan presented an opportunity to invest into a growing and profitable company. Against the background of the deteriorated financial situation of Estonian Air at the time – especially the fact that the financial results of the airline constantly show losses since 2006 (section 5.1 above) – the Commission doubts whether the 2010 business plan's conclusion can be regarded as sufficiently sound to conclude that a prudent private investor would have entered into the transaction in question on the same terms. It appears thus necessary to collect comments by interested parties during a formal investigation procedure.
- (74) Moreover, the fact that Cresco Investment Bank [...] refused to inject additional money in the airline – and rather preferred to cease to be a shareholder – is an indication that no prudent private investor would have entered into a the capital increase on terms similar to the EUR 17.9 million capital injection carried out by the Estonian Government at that time. On the other hand, the participation of SAS to this capital injection with EUR 2 million cannot be considered significant and thus cannot be compared to the State's intervention.
- (75) Furthermore, the Commission notes that the Estonian authorities explicitly state that the decision to increase capital in 2010 was taken in order to ensure the long-term flight connections to the most important business destinations and to gain control of the company. These are macroeconomic considerations which no private investor would have taken into account.
- (76) The Commission thus considers at this stage that the 2010 capital increase entailed a selective advantage to Estonian Air.
- (77) The capital increase clearly involves State resources. For the same reasons stated in recital (51) above, measure 3 affects trade and threatens to distort competition between Member States.
- (78) Therefore, on the basis of the above, the Commission cannot exclude at this stage that measure 3 involves state aid within the meaning of Article 107(1) TFEU.

#### *Compatibility with the internal market*

- (79) At this stage, the Commission finds no grounds that could be used as a basis for finding measure 3 – were it to constitute state aid – compatible with the internal market.
- (80) In particular, the Commission notes that on the basis of the information available, it cannot be excluded that Estonian Air was a firm in difficulty in 2010 (section 5.1 above), in particular since more than half of the airline's equity disappeared between 2010 and 2011 and since it had lost more than one quarter of its capital during this time (recital (44) above). The Commission therefore preliminary considers that Estonian Air would be a firm in difficulty at the time of measure 3.
- (81) Bearing the above in mind, in order to consider the 2010 capital increase as compatible aid, it would need to comply with the legal requirements of the R&R

Guidelines. However, for the same reasons presented in recitals (54) to (59) above, the Commission considers at this stage that measure 3 would constitute incompatible state aid. This is moreover reinforced by the fact that the Commission cannot exclude at this stage that the 2009 and 2010 capital injections (measures 1 and 2) constitute unlawful and incompatible rescue and/or restructuring aid and would have been provided in breach of the 'one time, last time' (recitals (68) and (68) above).

#### **5.5. The 2011/2012 capital injection (measure 4)**

##### *Presence of state aid*

- (82) The Commission has assessed the presence of state aid in respect of the 2011/2012 capital injection (measure 4) by applying the MEIP.
- (83) The Commission recalls that, as described above, the financial situation of Estonian Air was already extremely deteriorated at the end of 2011, when measure 4 was decided (section 5.1 above).
- (84) The Commission doubts whether the strategy of the 2011 business plan was reliable and whether it was realistic to consider that only a bigger network and more frequencies, implying a relevant capacity increase in terms of connections, fleet and staff, would improve the airline's competitiveness.
- (85) The Commission recalls that according to the December 2011 financial forecast of IATA,<sup>14</sup> profit margins in the airline industry in 2011 were squeezed as oil and fuel prices surged. For 2012, IATA forecasted that the European airline industry would face pressure due to the economic turmoil that would result from a failure of governments to resolve the Eurozone sovereign debt crisis. Considering that the European airlines were likely to be hit badly by recession in their home markets, IATA's 2012 forecast for European airlines was an EBIT margin of 0.3%, with net losses after tax of USD 0.6 billion (i.e. EUR 0.46 billion).
- (86) Against the background of this uncertain development of the European air transport market, the forecast growth prospect of the 2011 business plan seems overoptimistic and the proposed strategy appears extremely risky.
- (87) This assessment is supported by the fact that neither the remaining private shareholder (SAS) nor any private investor ([...]) was willing to participate in the transaction. [...]s alleged approach to participate in the capital injection at the beginning cannot be considered as sufficient to justify concomitant behaviour since this approach was refused by the highest credit committee [...] in the end after having carried out a comprehensive risk assessment. The Commission does not exclude that the refusals of both SAS and [...] were driven by the estimation that the presented business plan is not reliable and the proposed strategy is too risky.
- (88) Therefore, at this stage, the Commission considers that a prudent investor, whose goal of profit maximisation is tempered with caution about the level of

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<sup>14</sup> <http://www.iata.org/whatwedo/Documents/economics/Industry-Outlook-December2011.pdf>.

risk acceptable for a given rate of return, would not have entered into the capital increase on the basis of the 2011 business plan and the proposed strategy.

- (89) Furthermore, the Estonian authorities state that the proposed strategy fed into the Government Action Plan for 2011 – 2015 to develop direct air links to all major European business centres and to turn Tallinn Airport into a hub for Asia-Europe flights. The Commission notes that these are political considerations which no private investor would have taken into account.
- (90) The Commission thus considers at this stage that the 2011/2012 capital increase entailed a selective advantage in favour of Estonian Air.
- (91) Given that the 2011 capital increase involves State resources and that the measure affects trade between Member States and threatens to distort competition – for the same reasons stated in recital (51) above –, the Commission cannot exclude at this stage that measure 4 involves state aid within the meaning of Article 107(1) TFEU.

#### *Compatibility with the internal market*

- (92) Based on the information available, it appears that Estonian Air was a firm in difficulties under the R&R Guidelines at the time of the capital increase at the end of 2011 (section 5.1 above). As a result, aid for rescue or restructuring appears as the only possible justification as regards compatibility with the internal market.
- (93) However, the measure does not seem to meet the criteria set out for rescue or restructuring aid under the R&R Guidelines. The arguments presented in recitals (54) to (59) above apply *mutatis mutandis*, as well as the conclusions on the potential breach of the 'one time, last time' principle laid down in recitals (68) and (68) above.
- (94) In addition, the Commission observes that in accordance with point 38 of the R&R Guidelines, compatible restructuring aid requires compensatory measures in order to ensure that the adverse effects on trading conditions are minimised as much as possible. These measures may comprise divestment of assets, reductions in capacity or market presence and reduction of entry barriers on the markets concerned (point 39 of the R&R Guidelines).
- (95) The Commission notes in this respect that the strategy of the 2011 business plan implied a bigger network, including an increase in terms of connections from and to Estonia as well as of fleet and staff. The strategy was implemented in 2012, when Estonian Air increased its fleet from eight to eleven aircraft, added nine new destinations to its network and increased its staff by 66 employees to handle more round trips. This constitutes a significant increase of capacity which contravenes the legal requirements of the R&R Guidelines.
- (96) The Commission therefore doubts whether the capital injection in 2011/2012 of EUR 30 million (measure 4) constitutes incompatible state aid.

### **5.6. The notified rescue loan (measure 5)**

#### *Presence of state aid*

(97) The rescue loan of EUR 8.3 million which was notified on 20 December 2012 (measure 5) is to be considered state aid within the meaning of Article 107(1) TFEU since the loan, stemming from State resources, entails a selective advantage for Estonian Air which affects trade between the Member States and threatens to distort competition (recital (51) above).

(98) The Estonian authorities themselves regard this measure as state aid.

*Compatibility with the internal market*

(99) Based on the information available, Estonian Air was a firm in difficulties under the R&R Guidelines at the time of granting the rescue loan in December 2012.

(100) The Estonian authorities themselves state that the airline showed the usual signs of a firm being in difficulty such as declining cash flow at least as of June 2012 and therefore met the criteria of point 11 of the R&R Guidelines. They also consider that Estonian Air fulfilled the criteria of point 10(a) and 10(c) of the R&R Guidelines by having lost half of the registered capital and having reached a state of technical bankruptcy under the Estonian law at least since July 2012.

(101) Therefore, the rescue loan must be assessed in the light of the R&R Guidelines and the 1994 Aviation Guidelines, in order to establish whether it may be compatible with the internal market pursuant to Article 107(3) TFEU.

(102) It appears that the notified rescue aid fulfils most of the criteria in section 3.1 of the R&R Guidelines concerning rescue aid:

(a) The aid takes the form of a loan which is granted at an interest rate (15%) at least comparable to those observed for loans to healthy firms, and in particular the reference rates adopted by the Commission.<sup>15</sup> Moreover, Estonia confirmed that the loan will come to an end within a period of not more than six months after the disbursement of the first instalment (point 25(a) of the R&R Guidelines).

(b) The aid seems to be warranted on the grounds of serious social difficulties and have no unduly adverse spill-over effects on other Member States (point 25(b) of the R&R Guidelines).

(c) Furthermore, Estonia undertook to communicate to the Commission a restructuring plan or a liquidation plan or proof that the loan has been reimbursed in full not later than six months after first implementation of the rescue aid measure (point 25(c) of the R&R Guidelines).

(d) Also, the Estonian authorities demonstrated that the aid amount restricted to the amount needed to keep the firm in business for six months by calculating the amount along the formula set out in the Annex of the R&R Guidelines (point 25(d) of the R&R Guidelines).

(103) However, the Commission has doubts whether the so called 'one time, last time' principle is met in relation to this measure. As explained above, the

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<sup>15</sup> According to the Communication from the Commission on the revision of the method for setting the reference and discount rates (OJ C 14, 19.1.2008, p. 6), for rescue aid cases, the 1-year IBOR increased with at least 100 basis points shall be applied. For the present case, the applicable interest rate would be 2.11%.



Commission cannot exclude at this stage that the measures granted to Estonian Air between 2009 and 2012 constitute unlawful and incompatible rescue and/or restructuring aid. Therefore, it cannot be excluded that the notified rescue aid breaches the legal requirement of the 'one time, last time' principle.

- (104) The Estonian authorities did not provide any justification which allows an exception to that rule as stated in point 73 of the R&R Guidelines. The Commission notes that Estonia's concern on the impact of the closure of Estonian Air on the national economy as described in recital (24) above, as well as other general considerations such as the lack of connectivity due to Estonia's peripheral geographical situation, are in principle not apt to constitute an exceptional circumstance in order to derogate from the 'one time, last time' principle. The Commission notes that such a derogation has never been accepted in past.
- (105) Therefore, the Commission has significant doubts whether the notified rescue aid can be regarded as compatible with the internal market.

### **5.7. Unlawful aid**

- (106) The Commission notes that, if the measures identified were to constitute state aid, they would have been granted in breach of the notification and stand-still obligations laid down in Article 108(3) TFEU. Thus, the Commission considers at this stage that the measures granted to Estonian Air appear to constitute unlawful state aid.
- (107) In particular, in relation to the notified rescue loan (measure 5), the Commission notes that Estonia has disbursed the first two tranches of the rescue loan before waiting for approval by a Commission decision. Since the rescue aid constitutes state aid, it has been granted in breach of the stand-still obligation established in Article 108(3) TFEU. Thus, the Commission considers at this stage that the rescue loan granted to Estonian Air qualifies as unlawful state aid.

## **6. CONCLUSION**

- (108) In the view of the above, the Commission has doubts on the presence of state aid as well as on the compatibility with the internal market with respect to the 2009 capital increase (measure 1), the sale of Estonian Air's groundhandling section to Tallinn Airport in 2009 (measure 2), the 2010 capital injection (measure 3), the 2011/2012 capital injection (measure 4) and the notified rescue loan (measure 5).

## **7. DECISION**

In the light of the foregoing considerations, the Commission, acting under the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union, requests Estonia to submit its comments and to provide all such information as may help to assess the measures, 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 Estonia that Article 108(3) of the Treaty on the Functioning of the European Union 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 Estonia 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 Greffe  
1049 Brussels  
Belgium

Fax No: +32-2-296-1242

Yours faithfully,  
For the Commission

Joaquín ALMUNIA  
Vice-president of the Commission