Subject: State Aid SA.38145 (2014/FC) – Latvia
Alleged illegal State aid to Ryanair

Sir,

1. **PROCEDURE**

   (1) On 10 January 2014, the state-owned joint stock company operating the airport of Riga¹, Riga International Airport (‘RIX’), lodged a complaint with the Commission alleging that Ryanair Limited (‘Ryanair’) had been granted unlawful State aid though a contract concluded between RIX and Ryanair in 2004. The complaint was registered under case number SA.38145 (2014/FC).

   (2) The Commission requested additional information from RIX on 20 March 2014 but received no reply. On 3 June 2014, RIX submitted a revised version of the complaint containing additional information. By letter of 9 July 2014, the Commission forwarded the complaint to the Latvian authorities who responded on 16 September 2014.

¹ Latvian: Starptautiskā lidosta "Rīga".

By letter of 3 February 2017, the Commission informed the complainant that according to Article 24(2) of the Procedural Regulation, it had failed to submit sufficient information to show that illegal aid had been granted to Ryanair. RIX replied by letter of 2 March 2017.

On 27 October 2017, the Commission sent a second letter pursuant to Article 24(2) of the Procedural Regulation, informing RIX that the submitted information was insufficient. RIX responded on 12 February 2018 and 15 February 2018.

A third letter under Article 24(2) of the Procedural Regulation was sent on 10 April 2018 and a telephone conference took place on 24 July 2018. RIX submitted additional information on 10 May 2018 and 17 September 2018.

2. DETAILED DESCRIPTION OF THE MEASURE

2.1. Airport facts and passenger development

The airport of Riga, the capital of Latvia, is the largest airport in the Baltic States with direct flights to 100 destinations provided by 19 different carriers. The airport was built in 1973 and has grown significantly. Today, it serves as a hub for airBaltic and SmartLynx Airlines, and is one of the base airports for Wizz Air. The Latvian national carrier airBaltic operates the highest share of the traffic at the airport, followed by Ryanair, which currently has a market share of 17.1% in terms of passenger numbers.

The airport is located in the Mārupe Municipality west of Riga. It is operated by the state-owned joint-stock company RIX, with the owner of all shares being the government of Latvia. The holder of the Latvian State’s shares is Latvia's Ministry of Transport.

The accession of Latvia to the EU on 1 May 2004 led to an expansion of the airport, which was trying to develop further routes into central Europe by attracting new airlines, in particular low cost carriers such as Ryanair. Ryanair started its operations at the airport of Riga on 1 November 2004. The airport was able to win further important airlines for the EU market in 2004, such as easyJet and KLM.

To accommodate the expected additional traffic, the airport decided in 2003 to extend the existing terminal infrastructure, which was limited to 1.5 million passengers at the time. The new building, which was connected with the existing terminal at the North facade, opened in 2007.

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(11) Passenger traffic at the airport, which had increased significantly after Latvia’s accession to the EU from 711 753 passengers in 2003 to 1 878 035 passengers in 2005, reached a new peak in 2018 with 7 056 089 passengers (see Table 1 below).

Table 1: Passenger numbers at Riga airport (2003-2018)

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of passengers</th>
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<tbody>
<tr>
<td>2003</td>
<td>711 753</td>
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<td>2004</td>
<td>1 060 426</td>
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<tr>
<td>2005</td>
<td>1 878 035</td>
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<td>2006</td>
<td>2 495 020</td>
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<td>2007</td>
<td>3 160 945</td>
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<td>2008</td>
<td>3 690 549</td>
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<td>2009</td>
<td>4 066 854</td>
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<tr>
<td>2010</td>
<td>4 663 647</td>
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<tr>
<td>2011</td>
<td>5 106 926</td>
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<td>2012</td>
<td>4 767 764</td>
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<td>2013</td>
<td>4 793 045</td>
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<tr>
<td>2014</td>
<td>4 813 959</td>
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<tr>
<td>2015</td>
<td>5 162 149</td>
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<tr>
<td>2016</td>
<td>5 401 243</td>
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<tr>
<td>2017</td>
<td>6 097 434</td>
</tr>
<tr>
<td>2018</td>
<td>7 056 089</td>
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</tbody>
</table>


2.2. The agreements with Ryanair signed in 2004

(12) RIX signed two agreements with Ryanair on 23 July 2004: an air services agreement (‘the 2004 Agreement’), and a side letter (‘the Side Letter’) amending the former with regard to the fee payable per turnaround.

(13) The 2004 Agreement specified the airport charges payable by Ryanair and the services to be provided by RIX. It was scheduled to start on 1 November 2004 and to continue until 31 March 2015. The agreement provided for an all-inclusive fee per departing passenger to be paid by Ryanair as set out in Table 2 below. The fee included all existing or future government and airport taxes, fees and charges relating to Ryanair’s operation at the airport. The 2004 Agreement specifies that “[...]

Table 2: Passenger fee as defined in the 2004 Agreement with Ryanair

<table>
<thead>
<tr>
<th>Number of departing passengers per year</th>
<th>Fee per departing passenger (EUR)</th>
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<tr>
<td>&lt; 50,000</td>
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<td>&gt; 50,000</td>
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<td>&gt; 100,000</td>
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<td>&gt; 150,000</td>
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<td>&gt; 200,000</td>
<td>[...]</td>
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<tr>
<td>&gt; 250,000</td>
<td>[...]</td>
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</table>

(14) Furthermore, the 2004 Agreement stipulated that departing passengers carried between 1 November 2004 and 1 April 2005 could qualify for a lower fee of EUR
[...] per passenger if Ryanair carried no less than [...] departing passengers from Riga airport between 1 November 2004 and 31 March 2006.

(15) In addition to the passenger fee, the 2004 Agreement provided for a fee per turnaround of EUR [...] in respect of ground handling services to be provided by the airport as set out in Annex I and Annex II of the agreement. However, on the same day that the 2004 Agreement was entered into, namely on 23 July 2004, RIX and Ryanair signed a separate agreement. The Side Letter changed the above mentioned ground handling fee under clause 2(c) of the 2004 Agreement from EUR [...] to EUR [...] per turnaround.

3. ASSESSMENT OF THE MEASURE

(16) Article 107(1) of the Treaty on the Functioning of the European Union (‘TFEU’) provides that any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favoring 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.

(17) The criteria laid down in Article 107(1) TFEU are cumulative. Therefore, in order to determine whether a measure constitutes State aid, the following conditions have to be fulfilled:

– the beneficiary is an undertaking;
– the measure confers an advantage;
– the advantage is granted through State resources;
– the advantage is selective; and
– the measure distorts or threatens to distort competition and is liable to affect trade between Member States.

3.1. Economic activity and notion of an undertaking

(18) The concept of an undertaking covers any entity engaged in an economic activity, regardless of its legal status and the way in which it is financed. Any activity consisting in offering goods or services on a given market is an economic activity.

(19) Ryanair is an airline and provides scheduled air services against remuneration, in competition with other airlines. It is therefore an undertaking that is engaged in an economic activity within the meaning of Article 107(1) TFEU.

3.2. Economic advantage

(20) An advantage within the meaning of Article 107(1) TFEU is any economic benefit, which an undertaking could not have obtained under normal market conditions, that is to say in the absence of State intervention.

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4 See for example Judgment of the Court of Justice of 11 July 1996, Syndicat français de l'Express international (SFEI) and Others v La Poste and Others, C-39/94, ECLI:EU:C:1996:285, paragraph 60.
Where an airport has public resources at its disposal, aid to an airline can in principle be excluded where the relationship between the airport and the airline is carried out in line with normal market conditions. This so-called Market Economy Operator test (‘MEO test’) follows the basic concept that the behaviour of public authorities should be compared to that of similar private economic operators under normal market conditions to determine whether an agreement grants an advantage to its counterpart.

3.2.1. Preliminary remarks with regard to the MEO test

As set out in point 53 of the 2014 Aviation Guidelines, two approaches can be followed in order to determine whether an agreement between an airport and an airline satisfies the MEO test.

First, the existence of aid to an airline using a particular airport can, in principle, be excluded if the price charged for the airport services corresponds to the market price (‘first approach’ – comparison with the market price).

Second, the existence of aid to an airline using a particular airport can, in principle, be excluded if it can be demonstrated that the measure will lead to a positive incremental profit contribution for the airport and is part of an overall strategy leading to profitability, at least in the long term. This is done through an ex ante analysis – that is, an analysis founded on information available when the agreement was concluded and on developments foreseeable at the time – (‘second approach’ – ex ante profitability analysis).

As regards the first approach, the Commission does not consider that, at the present time, an appropriate benchmark can be identified to establish a true market price for services provided by airports.

It should also be noted that, in general, the application of the MEO test based on an average price on other similar markets may prove helpful if such a price can be reasonably identified or deduced from other market indicators. However, this method is of limited relevance for airport services, as the structure of costs and revenues tends to differ greatly from one airport to another. This is because costs and revenues depend on how developed an airport is, the number of airlines which use the airport, its capacity in terms of passenger traffic, the state of the infrastructure and related investments, the regulatory framework which can vary from one Member State to another, and any debts or obligations entered into by the airport in the past.

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5 Ibid.
7 See point 53 of the 2014 Aviation Guidelines.
8 See points 54 to 60 of the 2014 Aviation Guidelines.
Moreover, the liberalisation of the air transport market complicates any purely comparative analysis. As can be seen in this case, commercial practices between airports and airlines are not always based exclusively on a published schedule of charges. Rather, these commercial relations vary largely. They include sharing risks with regard to passenger traffic and any related commercial and financial liability, standard incentive schemes and changing the spread of risks over the term of agreements. Consequently, one transaction cannot really be compared with another based on a turnaround price or price per passenger.

In addition, benchmarking is not an appropriate method to establish market prices if the available benchmarks have not been defined with regard to market considerations or the existing prices are significantly distorted by public interventions. Such distortions appear to be present in the aviation industry, for the reasons explained in points 57 to 59 of the 2014 Aviation Guidelines.

Moreover, as the Union courts have recalled, benchmarking by reference to the sector concerned is merely one analytical tool amongst others to determine if a beneficiary has received an economic advantage, which it would not have obtained in normal market conditions. As such, while the Commission may use that approach, it is not obliged to do so where, as in this case, it would be inappropriate.

The General Court confirmed similar findings of the Commission in its judgments of 13 December 2018 concerning the airports of Angoulême, Nîmes, Pau and Altenburg-Nobitz.

Moreover, as the Union courts have recalled, benchmarking by reference to the sector concerned is merely one analytical tool amongst others to determine if a beneficiary has received an economic advantage, which it would not have obtained in normal market conditions. As such, while the Commission may use that approach, it is not obliged to do so where, as in this case, it would be inappropriate.

In the light of those considerations, the Commission takes the view that the approach generally recommended in the 2014 Aviation Guidelines for applying the MEO test to relationships between airports and airlines, namely the ex ante incremental profitability analysis, must be applied to this case.

3.2.2. Time frame of the assessment

The Commission considers that the appropriate timeframe for assessing the profitability of arrangements between airports and airlines is typically the time horizon of the agreement itself. As airlines are able to adapt their operations in a short timeframe and as the specific contents of possible future agreements usually
cannot be predicted, a private airport operator would usually not assume that the specific terms of an agreement will continue beyond its agreed duration.\footnote{See for example Commission Decision (EU) 2015/1226 of 23 July 2014 on State aid SA.33963 (2012/C) implemented by France in favour of the Chamber of Commerce and Industry of Angoulême, SNC-Lavalin, Ryanair, and Airport Marketing Services (OJ L 201, 30.7.2015, p. 48); Judgment of the General Court of 18 December 2018, Ryanair and Airport Marketing Services v Commission (Angoulême airport), T-111/15, EU:T:2018:954, paragraphs 296 to 309.}

Thus, in this case the profitability of the agreement needs to be assessed in relation to the time period from 1 November 2004 to 31 March 2015.\footnote{Judgment of the Court of Justice of 16 May 2002, France v Commission (‘Stardust Marine’), C-482/99, ECLI:EU:C:2002:294, paragraph 71.}

The Court of Justice has ruled in the Stardust Marine judgment that, ‘[…] in order to examine whether or not the State has adopted the conduct of a prudent investor operating in a market economy, it is necessary to place oneself in the context of the period during which the financial support measures were taken in order to assess the economic rationality of the State’s conduct, and thus to refrain from any assessment based on a later situation’.\footnote{Judgment of the Court of Justice of 16 May 2002, France v Commission (‘Stardust Marine’), C-482/99, ECLI:EU:C:2002:294, paragraph 71.}

For the purpose of assessing the agreement in question, both the existence and the amount of possible aid in the agreement therefore have to be assessed in the light of the situation prevailing at the time they were signed and, more specifically, in the light of the information available and developments foreseeable at the time.

In its reconstructed analysis of the ex ante profitability of the agreements in question (see recital (46) below), RIX uses the reference date of 1 June 2004 for the application of the relevant exchange rates. Furthermore, RIX takes into account the expected incremental traffic, costs and revenues from 1 November 2004 until 31 March 2015, i.e. the end and start dates of the agreement. The Commission finds this approach to be sound for the reasons set out above.

3.2.3. Joint assessment of the 2004 Agreement and the Side Letter of 23 July 2004

The Commission considers that in applying the MEO test, the 2004 Agreement and the Side Letter described in section 2.2 above must be evaluated together as one single measure since they were entered into within the framework of a single transaction.

Indeed, the only purpose of the Side Letter was to insert an amendment with respect to the ground handling charges into the 2004 Agreement. According to the Side Letter, ‘[…]’, hereby referring to a change in a clause in the 2004 Agreement. This demonstrates that both agreements are inseparably linked.

Moreover, both agreements were concluded at the same point in time, as they were both signed on 23 July 2004.

In its profitability analysis, RIX assessed both agreements together. For the reasons set out above, the Commission finds this approach to be sound.
3.2.4. MEO assessment

(41) When assessing the measure in question, the Commission has to take into account all its relevant features and its context. It needs to be established whether, when setting up an arrangement with an airline, the airport is capable of covering all the costs stemming from the arrangement, over the duration of the arrangement, with a reasonable profit margin on the basis of sound medium-term prospects\(^\text{14}\). This is to be measured by the difference between the incremental revenues expected to be generated by the agreement and the incremental costs expected to be incurred as a result of the agreement, the resulting cash flows being discounted with an appropriate discount rate\(^\text{15}\).

(42) This approach is justified by the fact that an airport operator may have an objective interest in concluding a transaction with an airline, regardless of any comparison with the conditions offered to airlines by other airport operators, or even with the conditions offered by the same airport operator to other airlines.

(43) The Commission also notes in this context that price differentiation is a standard business practice. Such differentiated pricing policies should, however, be commercially justified.

(44) In addition, it is also necessary to take into account the extent to which the arrangement under consideration can be considered part of the implementation of an overall strategy of the airport expected to lead to profitability at least in the long term\(^\text{16}\).

(45) In the present case, neither RIX nor the Latvian authorities provided a business plan preceding the conclusion of the 2004 Agreement and the Side Letter. The Commission therefore invited the Latvian authorities to reconstruct the profitability analysis that a MEO would have carried out before signing the agreements in question.

(46) Upon the Commission’s request, the Latvian authorities presented a table prepared by RIX containing an overview of the incremental costs and revenues that could have been expected at the time the agreements were concluded, as summarised in Table 3 below.

(47) Table 3 shows that RIX expected the costs stemming from the agreements to exceed the revenues, leading to a negative net present value (‘NPV’) of the incremental cash flows of EUR – 1.9 million over the duration of the agreement.


\(^{15}\) See point 64 of the 2014 Aviation Guidelines.

\(^{16}\) See point 66 of the 2014 Aviation Guidelines.
Table 3: RIX’s ex-ante analysis of the agreements concluded with Ryanair. All amounts are expressed in EUR.

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<td>Departing movements (Ryanair)</td>
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<td>Departing passengers of diverted traffic (British Airways)</td>
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<td>Departing movements of diverted traffic (British Airways)</td>
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<td><strong>EXPECTED REVENUES</strong></td>
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<td>Aviation revenues (Ryanair)</td>
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<td>Non-aviation revenues (Ryanair)</td>
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<td>Forgone aviation revenues (British Airways)</td>
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<td>Forgone non-aviation revenues (British Airways)</td>
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<tr>
<td>Total expected revenues</td>
<td>124,686</td>
<td>1,335,499</td>
<td>1,921,381</td>
<td>1,854,947</td>
<td>1,916,726</td>
<td>1,952,885</td>
<td>1,988,792</td>
<td>2,030,139</td>
<td>2,071,079</td>
<td>2,111,768</td>
<td>575,685</td>
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<td><strong>EXPECTED COSTS</strong></td>
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<td>Ground handling</td>
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<td>Total operating and maintenance costs</td>
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<td>Terminal (extension of the Northern part)</td>
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<td>Total expected costs</td>
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<td>1,762,064</td>
<td>1,811,841</td>
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<td>541,880</td>
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<td><strong>NET CASH FLOW</strong></td>
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<td>1,390,578</td>
<td>256,629</td>
<td>141,870</td>
<td>123,882</td>
<td>104,885</td>
<td>90,476</td>
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<td>48,375</td>
<td>28,365</td>
<td>7,216</td>
<td>33,805</td>
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<td>1,299,606</td>
<td>225,113</td>
<td>117,248</td>
<td>96,033</td>
<td>76,004</td>
<td>61,548</td>
<td>-458,652</td>
<td>28,967</td>
<td>15,936</td>
<td>3,798</td>
<td>16,653</td>
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<td>Discount rate (%)</td>
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<td>NPV (2004-2015, the entire duration of the Agreement), EUR</td>
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In the following recitals, the Commission will verify the underlying assumptions of RIX with respect to (i) the expected traffic generated by Ryanair; (ii) the expected incremental revenues; (iii) the foregone revenues related to British Airways; and (iv) the expected incremental costs, in accordance with the MEO test.

3.2.4.1. Traffic projections

The 2004 Agreement does not stipulate the lines or the frequencies Ryanair would be operating from Riga airport, nor does it contain any obligations regarding passenger targets or a minimum number of passengers to be reached by Ryanair. However, the 2004 Agreement links the passenger fee to be paid by Ryanair to the number of departing passengers achieved during each year (see Table 2 and recital (13) above). For the period 1 November 2004 until 1 April 2005, the agreement stipulates that a reduced airport fee will apply [...]. On this basis, RIX argues that it can be concluded from the agreement that Ryanair planned to carry at least [...] departing passengers during the first 17 months of the agreement, which equals to [...] departing passengers per month or [...] departing passengers per year. For the period after 2005, RIX assumes that, in view of the minimum number of annually departing passengers of 250 000 needed in order to obtain a passenger fee of EUR [...], it could have expected Ryanair to achieve at least this number until the end of the agreement in 2015. RIX therefore used an estimate of [...] departing passengers per year as of the year 2006.

The Commission observes that as the 2004 Agreement does not contain any specific passenger obligations from which the expected number of Ryanair passengers could be easily projected, it can be reasonably assumed that a private operator in its planning would expect an airline to at least try to meet the minimum thresholds under the agreement in order to achieve the lowest possible passenger fee. In light of the development plans of the airport and the economic growth expected after Latvia’s accession to the EU (see recitals (9) to (11) above), the Commission accepts that it was reasonable to assume that Ryanair would achieve annually departing passenger numbers of roughly [...] in 2004, [...] in 2005 and [...] in 2006.

On the contrary, the assumption that traffic would remain constant at [...] departing passengers per year during the whole period of the agreement cannot be assumed realistic from an ex ante point of view. In particular, the airport registered a growth rate of 4.8% in the period 1999 until 2003, i.e. the years before the conclusion of the agreement with Ryanair, and could expect an even higher increase in traffic due to the planned general expansion of the airport after the accession of Latvia to the EU. This is confirmed by different strategic documents submitted by RIX from the year 2004. Merely applying the same

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18 CAGR - Compound Annual Growth Rate based on information provided by RIX.

19 See for example State public limited company ‘Riga International Airport’, Proposal by the Executive Board on rapidly increasing passenger numbers in 2005-2009, March 2004. […]
annual growth rate of 4.8% to future traffic generated by Ryanair would lead to an average number of [...] Ryanair departing passengers over the period 2005 to 2014. This is still far below the actually achieved number of [...] Ryanair departing passengers per year on average over the period 2005 to 2014 (based on ex post data provided by RIX).

(52) On this basis, the Commission finds the passenger numbers provided by RIX, in particular for the period after 2006, to be too low. A higher estimate should have been used for the profitability analysis considering at least an increase of Ryanair departing passengers similar to the historical growth rate observed at RIX of 4.8%. A corresponding adjustment of the traffic assumptions, without challenging any of RIX’s other assumptions about costs and revenues, would make the agreement between RIX and Ryanair profitable over its entire duration. Using a presumed annual growth rate of 4.8%, the NPV of the agreement becomes EUR +500 000 instead of EUR -1.9 million.

(53) The Commission furthermore performed a sensitivity analysis based on the adjusted traffic using a more pessimistic assumption about the growth rate of traffic. The conclusion of such analysis showed that even in a more negative scenario, that is by reducing the traffic growth rate by one percentage point (to 3.8% instead of 4.8%), the agreement would still be incrementally profitable.20

(54) Therefore the Commission concludes that RIX’s assumptions regarding traffic projections suffer from flaws and need to be corrected for the purposes of the ex ante analysis.

3.2.4.2. Incremental revenues

(55) In order to assess whether an arrangement concluded by an airport with an airline satisfies the MEO test, expected non-aeronautical revenues stemming from the airline's activities must be taken into consideration together with airport charges, net of any rebates, marketing support or incentive schemes (‘single-till approach’).21 Therefore, incremental revenues that a private MEO would reasonably expect from the agreements include:

– aeronautical revenues from passengers and landing charges paid by Ryanair; and

– non-aeronautical revenues from, for example, car parking, franchise shops, or directly operated shops.

20 A slightly positive NPV of about EUR 1 500 would still be achieved.

21 See point 64 of the 2014 Aviation Guidelines.
Aeronautical revenues

(56) In line with Commission practice, RIX takes into account the aeronautical revenues per departing passenger and the revenues per turnaround and multiplies them with the expected departing passenger and turnaround numbers.\(^{22}\)

(57) Regarding the passenger fee, the 2004 Agreement stipulates an all-inclusive fee per departing passenger, the amount of which depends on the number of passengers achieved during a particular year (see recital (13) above).

(58) In its calculation, RIX assumes a fee of EUR [...] throughout the agreement. This is based on the assumption that Ryanair would make an effort to reach at least the minimum of [...] departing passengers between 1 November 2004 and 31 March 2006, and [...] departing passengers as from 2005, in order to be able to benefit from the lowest possible passenger charge, i.e. EUR [...]. As stated above, the Commission agrees that a private market operator would have expected Ryanair to achieve at least the minimum threshold of departing passengers set out in the agreement and therefore finds this approach to be reasonable.

(59) However, the provided calculation is inconsistent to the extent that with regard to the passenger threshold of [...] to be reached between 1 November 2004 and 31 March 2006, the 2004 Agreement only provides for a fee of EUR [...] for the passengers carried prior to 1 April 2005 (see recital (49) above). After this point of time the conditions set out in Table 2 above apply, which means that the minimum threshold of 250 000 departing passengers per annum (calculated between 1\(^{st}\) of April and 31\(^{st}\) of March, cf. recital (13)) applies. In its calculations RIX assumes for the first 17 months of the agreement on average [...] departing passengers per month, which equals [...] departing passengers per year (recital (49)). This means that, according to the 2004 Agreement, the passenger fee would have amounted to EUR [...] per departing passenger, not EUR [...] as assumed by RIX, as of 1 April 2005 until 31 March 2006. As a result, the ex ante expected aeronautical revenue from the passenger fee needs to be adapted, leading to an increase in overall revenues for RIX.

(60) Apart from the passenger fee, RIX takes into account the ground handling fee of [...] EUR per turnaround stipulated in the Side Letter. The ex ante estimate of the number of turnarounds is derived from the ex ante estimated number of passengers, assuming a load factor of 80% and taking into account that Ryanair operates Boeing 737-800 aircraft (as stipulated in the 2004 Agreement) with 179 seats. The Commission finds this approach to be sound.

RIX submitted that under the agreement, the airport could have expected aeronautical revenues related to Ryanair of EUR [...]}. The Commission believes that these revenues are underestimated given the inconsistencies with regard to the traffic assumptions (see recital (52) above) and the wrong application of the passenger fee for the period from 1 April 2005 until 31 March 2006 (see recital (59) above).

Based on the above, the Commission considers that the aeronautical revenues need to be corrected, leading to higher expected aeronautical revenues related to Ryanair of EUR [...].

Non-aeronautical revenues

Regarding non-aeronautical revenues, RIX includes revenues from shops, restaurants, and parking, based on historical data, namely the average non-aeronautical revenues per passenger in 2003, which amount to EUR [...]23. This amount is then multiplied by the expected total number of Ryanair passengers.

Non-aeronautical revenues are essentially proportional to the number of passengers. In fact, the activity of car parks, restaurants and other businesses situated at the airport depend on the number of passengers. The same is therefore true for the revenues received by the airport operator from these activities. The most reasonable approach for determining the projected incremental non-aeronautical revenues involves therefore determining an amount of revenue per passenger, multiplied by the projected incremental traffic. The Commission considers it likely that a MEO would have considered the airport’s total non-aeronautical revenues per passenger over a certain period in the past immediately preceding the signature of the agreement in question to be representative to establish the projected non-aeronautical revenues under the contract. Although RIX based its calculations of the non-aeronautical revenues per passenger exclusively on 2003 historical data (not considering an average over a longer period in the past), the Commission finds the approach taken by RIX to be sound, since the data immediately precedes the signature of the agreements in 2004.

RIX assumes that the annual growth rate for non-aeronautical revenues is 5%. This is higher than the expected inflation rate for Latvia of 3%. In light of the expansion plans of the airport (hereby likely increasing also the number of shops, restaurants and other businesses at the airport), the Commission considers this growth rate to be a conservative, yet reasonable, ex ante estimate.

RIX estimates that the revenues from non-aeronautical activities amount to EUR [...]}. However, the Commission considers that there should be corrections regarding the traffic projections. Namely, when correcting for the higher ex ante traffic forecast (see recital (52) above), the Commission finds that the non-aeronautical revenues could have been expected to be higher, namely EUR [...].

3.2.4.3. Foregone revenues

23 LVL [...] or EUR [...] per passenger according to data provided by RIX.
While the methodology followed by RIX to calculate the ex ante incremental aeronautical and non-aeronautical revenues is sound in principle, the Commission rejects the argument by RIX that the loss in revenues due to the traffic diverted from British Airways to Ryanair should be considered as negative foregone revenues (both affecting aeronautical and non-aeronautical revenues).

The Commission notes that when listing the relevant operating costs of an airport in the 2014 Aviation Guidelines, foregone revenues are not mentioned in the Guidelines as a potential category of operating costs, since new airlines starting operations and existing airlines leaving the airport can be considered as part of the normal business operations of an airport. While it cannot be fully excluded that an arrangement with an airline entails incremental costs in the form of foregone revenues resulting from reduced activities of other airlines, convincing evidence has to be provided to show that a market economy operator in the position of the airport would have taken such foregone revenues into account.

RIX argues that “the entry of low cost airlines has an unpredictable and most likely negative impact on the business of full service carriers like British Airways, Lufthansa, KLM and others”. Given that British Airways was paying a higher fee compared to Ryanair under its agreement, RIX argues that there is a loss in revenues by the loss in British Airways passengers, which needs to be taken into account in the assessment of the Ryanair contract. It therefore assumes in the ex ante analysis that the presence of Ryanair would divert 50% of the British Airways traffic.

The effect of the diverted British Airways traffic is assumed to be zero passengers in 2004, [...] passengers in 2005, [...] passengers in 2006, [...] passengers in each of the years during the period 2007-2014 and [...] passengers in 2015, leading to negative foregone revenues of EUR [...]. For this assumption, RIX provides the following arguments:

- First, RIX sees the fact that British Airways left the Latvian aviation market in March 2007 as evidence of the traffic cannibalisation effect of Ryanair’s presence at the airport.

- Second, RIX also refers to press articles of 2009, which would provide evidence that the application of reduced tariffs to Ryanair caused the withdrawal of British Airways from the airport.

- Third, RIX argues that the fact that British Airways had to change its departure schedule for its flights to London after the arrival of Ryanair (giving up the peak time departure hour of 11:00-11:59) is evidence that British Airways left the airport because of the arrival of Ryanair.

Having analysed the information provided by Latvia and RIX, the Commission finds that the arguments are not sufficient. RIX failed to provide evidence showing that the substitutability of Ryanair and British Airways services was considered at the time of signing the agreement or that ex ante, it had been considered that Ryanair’s presence would have an effect on future revenues obtained from British Airways.

Since there was no indication in the 2004 Agreement about which routes Ryanair would operate (see recital (49) above), it would have been hard to project ex ante
which airlines and which routes could possibly be affected by the presence of Ryanair. It therefore remains unclear why in particular the London route and the future flights by British Airways would be affected by Ryanair’s presence.

(73) It should also be noted that the services and business models of Ryanair and British Airways differ considerably. Ryanair is a low cost carrier that offers no frills services and operates according to a point-to-point business model, whereas British Airways is a full service carrier that operates a hub and spoke model, using short haul flights to European destinations to support the long haul flights departing from its hub in London. Under these circumstances, there is no indication that a market economy operator in the position of RIX would have expected British Airways to divert traffic as a result of the agreements.

(74) The arguments provided by Latvia and RIX are purely ex post. RIX’s whole line of argument is in fact based on press articles and circumstances stemming from the period after the signature of the agreements (see e.g. 2009 press articles). Even those ex post arguments however fail to show an immediate link between the future number of passengers for Ryanair and the future number of passengers for British Airways. Contrary to what is alleged by RIX, the data provided by RIX itself clearly shows that British Airways did not lose passengers on the London route. The total number of passenger flying with British Airways on the London route increased in 2005 and 2006 (see Table 4 below) and data provided by RIX showed that British Airways was successful during the new departure time schedule of 15:00-16:59 (see recital (70)). Moreover, as shown in Table 4 below, the airline AirBaltic increased the number of passengers flying to London after Ryanair started its operations. All those elements confirm that following Ryanair’s arrival at the airport the market and the demand for flights to London has grown and that Ryanair did not simply took over traffic from existing airlines.

Table 4: Number of passengers of airlines on the route Riga-London over the period 2004-2008

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<td>Ryanair</td>
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Source: RIX’s submission of 10 May 2018

(75) For the reasons stated above, the negative foregone revenues related to diverted traffic of British Airways need to be excluded from the ex ante assessment of the agreements.

3.2.4.4. Incremental costs

(76) Regarding the calculation of incremental costs, according to Commission practice, all costs incurred by the airport in relation to the airline’s activities at the airport have to be taken into account. Such incremental costs may encompass all categories of expenses, such as marketing costs and incremental personnel and
equipment costs induced by the presence of the airline at the airport\textsuperscript{24}. All costs which the airport would have to incur anyway, independently from the arrangement with the airline, are not being taken into account in the MEO test\textsuperscript{25}.

\textit{Operating costs}

(77) In absence of a business plan, the incremental operating costs that were foreseeable when the agreements were signed are difficult to determine\textsuperscript{26}. In particular, the approach used for the non-aeronautical revenues, which involved using the airport’s total non-aeronautical revenues to determine the incremental non-aeronautical revenue per passenger, cannot be used for the operating costs. Such an approach would involve considering the airport’s total operating costs, reduced to the number of passengers, as incremental costs. However, a significant proportion of an airport’s operating costs is fixed, which means that the total operating costs per passenger are likely to be markedly higher than the incremental costs associated with the signature of a new agreement generating additional traffic.

(78) For its calculation of the incremental operating costs, RIX takes into account the airport’s total costs from certain cost categories called airside operating and maintenance, landside operating and maintenance, ground handling operating and maintenance costs and terminal navigation charges.

(79) The airside operating and maintenance costs are described by RIX as the costs related to the runway, apron, aircraft stands, and lighting system. RIX includes the total costs related to the following cost centres: “[…]”, “[…]”, “[…]”, “[…]”, “[…]”, and “[…]”. The yearly costs are based on the cost increase in these cost categories observed between 2003 and 2006, and allocated to Ryanair according to its market share at the airport (based on the number of Ryanair movements in total movements at Riga airport). Since in RIX’ ex ante estimation the evolution of traffic is constant from 2006 until the end of the agreement, the airside operating and maintenance costs are only adjusted for inflation after 2006. This calculation methodology leads to a total of airside operating and maintenance costs over the duration of the agreement of EUR […]).

(80) The landside operating and maintenance costs are described by RIX as the costs related to Ryanair’s share in the use of the extended passenger terminal and infrastructure. According to RIX, the landside costs are based on historical data of

\textsuperscript{24} See point 64 of the 2014 Aviation Guidelines.


2003 and include the cost centres relevant to the passenger terminal infrastructure. RIX comes to an estimate of LVL/m² [...] (or EUR/m² [...]) per month, by including the total costs related to the following cost centres: “[…]”, “[…]”, “[…]”, “[…]”. RIX assigns […]% of the terminal surface use to Ryanair based on its share of departing passengers using the extended terminal (which has a surface of 6,523 m²). Ryanair’s share of […]% (i.e. […]m²) is calculated based on the assumption that half of its departing passengers (i.e. […] departing passengers per year as of 2006) will use the new (non-Schengen) terminal, having a capacity of 750 000 departing passengers. Since the extended terminal became operational in 2006, landside operating and maintenance costs are only included as of the year 2006. For the years after 2006, the estimated cost of terminal use per m² is adjusted for inflation. RIX estimates the total incremental landside operating and maintenance costs over the duration of the agreement to amount to EUR [...].

(81) Point 11 of Annex II of the 2004 Agreement includes an obligation for RIX to provide sufficient infrastructure and operational resources so that Ryanair could maintain a 25 minutes turnaround time. According to RIX, there was not sufficient ground handling staff available at the airport in 2003 and 2004 in order to be able to service six additional movements per day to accommodate the increase in traffic generated by Ryanair. According to RIX’ estimates, the incremental number of staff to deal with the ground handling of Ryanair is […] full time equivalent employees (‘FTEs’), working in three shifts (including shift supervisors, (senior) passenger handling agents, ticketing service (senior) agents, etc.). RIX therefore includes ground handling costs, estimated over the duration of the agreement at EUR […] in its calculation. The ground handling costs mainly consist of the salaries of the additional FTEs to cover the additional movements per day.

(82) The last category of operating costs included are the terminal navigation charges which RIX was obliged to pay to the State joint-stock company Latvijas Gaisa Satiksme (‘LGS’) under national law based on the number of turnarounds. Since the 2004 Agreement with Ryanair included an all-inclusive fee, which meant that RIX could not recover the terminal navigation charge from Ryanair, RIX included it in the calculation as part of the operating costs. The charge per turnaround is adjusted for inflation and yearly adjusted for the expected number of flights executed by Ryanair. The total amount of terminal navigation charges over the period of the agreement is estimated by RIX at EUR [...].

(83) Considering the four operating cost categories explained above, RIX estimated the total incremental operating costs over the entire duration of the agreement to amount to EUR [...].

(84) Having reviewed the submitted information, the Commission is not convinced as regards the incremental nature of a large part of the included operating costs, in particular regarding the cost categories “airside operating and maintenance” and “landside operating and maintenance”. Whilst RIX has provided some general explanation as regards the mentioned cost categories, it has failed to provide sufficiently granular data to allow the Commission to assess whether these costs are in fact incremental costs or whether the airport would have incurred them also absent Ryanair’s operations.
Indeed, based on the available information, the mentioned cost categories seem to include several cost items not related to Ryanair’s presence at the airport, but which are likely to resemble fixed overhead costs (such as costs related to airfield maintenance equipment, the firefighter and crisis management unit, or costs related to the maintenance of the terminal). RIX appears to be using an average cost approach, taking into account the total costs of the airport, thereby inflating the operating costs assigned to the individual agreements.

As regards the amount for ground handling services, the Commission finds it reasonable to calculate the incremental costs based on the estimated number of additional staff needed to service the incremental Ryanair turnarounds. However, the number of FTEs included in RIX’ assessment appears to be very high and the Commission is not convinced that they constitute a reasonable ex ante estimate

Regarding the terminal navigation charges, the Commission agrees that the charges should be taken into account as incremental costs since RIX was obliged to pay them to the responsible national authority based on the number of turnarounds at the airport.

In summary, it is not clear whether all fixed, non-incremental costs have been taken out of RIX’s calculations. From the submitted information, it seems likely that the operating costs included by RIX in its reconstructed ex ante assessment are inflated and should have been lower.

From the submitted information it remains unclear whether the ex ante expected incremental operating costs provided by RIX were calculated per passenger. However, if the costs were indeed calculated per passenger, the same correction with regard to the expected passenger numbers as for the revenues (see recitals (51), (52), (61) and (62) above) would have to be applied to the operating costs, leading to a higher total cost estimate. By assuming a pro rata increase in the operating costs in line with the revised passenger numbers, this would lead to total operating costs over the duration of the agreement of EUR […] instead of EUR […], which does however have no effect on the overall result (see calculation performed by the Commission in table 5 below).

As the submitted information on the operating costs are not granular enough to enable the Commission to correct the calculation of the incremental operating costs, the Commission is not making any changes to these costs reported by RIX in its own analysis in Table 5 below.

Marketing costs

Since the 2004 Agreement and the Side Letter do not include specific marketing services to be provided by Ryanair or its subsidiaries, no marketing costs have been considered in the ex ante incremental profitability analysis.

The Commission finds it reasonable to assume that RIX would for instance need extra baggage handling agents and aircraft cleaners for the extra turnarounds generated by Ryanair flights. However, the Commission considers it unreasonable to assume that for each turnaround, the airport needs for example […] extra senior passenger handling agents on top of […] extra (normal) passenger handling agents as well as […] extra assistant passenger handling agents.
**Investment costs**

(92) Besides the operating costs, RIX claims that there are investment costs related to the agreement and includes in its calculation part of the costs related to the extension of the terminal building (see recital (10) above), as well as costs for the purchase of ground handling equipment.

(93) While the Commission considers that in principle investment costs can be taken into account in the ex ante incremental profitability assessment of an agreement, the link between the investment costs and the agreement has to be clearly demonstrated: objective evidence has to be provided that shows a clear correlation between the investment and the agreement in question. For instance, if the airport needs to expand or build a new terminal or other facility mainly to accommodate the needs of a specific airlines, such costs can be taken into account when calculating the incremental costs. In contrast, costs which the airport would have to incur anyway independently from the arrangement with a specific airline, should not be taken into account under the MEO test.\(^{28}\)

(94) Regarding the ground handling equipment, RIX states that it needed to purchase a total of […] new units including for example a pushback tractor, an aircraft starting unit, passenger stairs, and a ground power unit, to handle the expected additional traffic by Ryanair, amounting to EUR […] As Annex I of the 2004 Agreement contains a detailed list of equipment to be provided by the airport, the Commission finds it reasonable to include at least part of the acquisition costs for this equipment in the calculation. However, as the equipment in question is not specific to any type of aircraft operated by Ryanair it seems realistic to assume that part of the equipment would also have been used for the other airlines, the Commission is not convinced that the full acquisition costs can be considered incremental costs to the Ryanair agreements. However, since there is no detailed evidence in the file which would enable the Commission to calculate the correct incremental investment costs of the ground handling equipment, the Commission is not making any changes to these investment costs reported by RIX in its own analysis in Table 5 below.

(95) Regarding the terminal building, RIX allocates […] % of the investment amount in the extension of the terminal to Ryanair based on its proportional use of floor space, amounting to EUR […]. As only the first two floors of the terminal building are being used for handling passengers, only the space of these floors is included in the calculation.

(96) As part of its argument, RIX points to point 3(b) of the 2004 Agreement, which stipulates that “[…]” Point 8 of Annex II of the agreement goes on saying “[…]” Based on these provisions, RIX argues that it was obliged to extend the terminal building in order to be able to provide the necessary infrastructure for Schengen and non-Schengen passengers as the existing infrastructure was insufficient. Therefore, a proportion of the investment costs should be assigned to Ryanair.

(97) Having analysed the information provided by Latvia and RIX, the Commission finds that the provided arguments are insufficient and that RIX has failed to

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provide evidence showing a clear correlation between the operations of Ryanair and the building of the terminal extension.

(98) On the contrary, the data provided by RIX itself clearly shows that the decision to extend the terminal was already taken in 2003 in view of the accession of Latvia to the EU and the plans to increase the number of flights towards the major EU cities. The decision to extend the airport infrastructure was therefore not directly related to the signature of the agreements with Ryanair.

(99) An internal document of March 2004, containing a proposal by RIX on increasing passenger numbers in the period from 2004 to 2009 further supports the assumption that RIX was planning to attract several new EU airlines, amongst others low cost carriers, in order to expand its air traffic volume. Regarding the existing infrastructure the document states that “[…]” The document goes on by referring specifically to investments in “[…]”.

(100) Therefore, the Commission notes that investments related to the expansion of the terminal were not specific to Ryanair but were meant to be exploited by other airlines as well. At the time of the conclusion of the agreement, there would have been no reason to suspect that the created capacity would remain unused in the absence of Ryanair, in particular in view of the fact that RIX was successful in its attempts to attract new airlines and signed further contracts with easyJet and KLM in 2004.

(101) Moreover, the Commission notes that contrary to RIX’s opinion, the 2004 Agreement, in particular point 3(b) and point 8 of Annex II, did not require RIX to make investments in the terminal. RIX could have fulfilled its obligations under the contract without investing in an expansion of the airport. The investments became necessary in view of the general expansion plans of the airport, which went far beyond the additional passengers brought in by Ryanair. This is supported by the fact that Ryanair started its operations in 2004, the new terminal building however only opened in 2007. The mere fact that the airport signed an agreement with Ryanair, which included routes to central Europe and therefore the handling of Schengen and non-Schengen passengers, is not sufficient to assign the investment costs for the terminal to this specific agreement.

(102) For the reasons stated above, the Commission concludes that the attributed investment costs related to the extension of the terminal building would need to be deducted from the incremental costs analysis.

3.2.4.5. Discount factor

(103) For its calculations, RIX used a discount rate of 6.64%, which corresponds to the Commission reference rates and recovery rates for the 25 EU Member States (for

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29 State public limited company ‘Riga International Airport’ (RIX), Proposal by the Executive Board on rapidly increasing passenger numbers in 2005-2009, March 2004.


31 See judgment of the General Court, Germanwings v Commission, paragraph 74.
the period 1 May 2004 until 31 December 2006). The Commission therefore finds it to be reasonable.

3.2.4.6. Profitability analysis as corrected by the Commission

(104) Due to the inconsistent and partially incomplete information provided by the Latvian authorities, resulting in uncertainty, the Commission has performed its own incremental profitability analysis of the agreements in question, correcting the assumptions made by RIX as indicated above. The result is summarised in Table 5 below.

(105) In its calculation, the Commission has corrected the main flaws of the assessment by adjusting the traffic forecast, the aeronautical revenues from the passenger fee, and by removing the foregone revenues and investment costs related to the extension of the terminal building, from the calculation.

(106) The calculation shows that when correcting these parameters, thereby accepting all other assumptions made by RIX, the NPV of the agreements is clearly positive at about EUR + 4.9 million.

(107) The result remains positive at EUR + 2.3 million when adapting the operating costs for the expected passenger numbers as described in recital (89) above.

(108) Since the traffic assumptions were not easily predictable, as explained in recital (50) above, the Commission has furthermore performed a sensitivity analysis taking the traffic figures provided by RIX as a given. Even with this lower traffic forecast, the NPV of the agreements remains positive at about EUR + 2.4 million, which is a similar result as when adjusting the traffic projections and operating costs.

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Table 5: Commission’s assessment of the ex-ante profitability of the agreements. All amounts are expressed in EUR.

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<td>Landside (terminal extension less security)</td>
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<td>Terminal navigation charges</td>
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<td>Discounted net cash flow (discount factor of 6.64%)</td>
<td>-746.648</td>
<td>600.949</td>
<td>702.843</td>
<td>566.146</td>
<td>653.576</td>
<td>747.839</td>
<td>856.375</td>
<td>178.178</td>
<td>1.090.794</td>
<td>1.226.357</td>
<td>1.372.470</td>
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<td>Net present value</td>
<td>4.897.952</td>
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3.2.4.7.  Overall strategy to lead to profitability in the long term

(109) The agreements were part of the general expansion strategy of the airport, having the objective to open the way to new markets in Europe and to improve the profitability of the airport. Therefore, the Commission considers that the 2004 Agreement can be considered to be part of the implementation of an overall strategy to lead to profitability in the long term.

3.2.5.  Conclusion on economic advantage

(110) After the assessment of the submitted information, the Commission takes the view that, for the reasons presented above, the analysis provided by RIX is only partially reasonable and that the methodology used is only partially sound.

(111) As described in detail above, the Commission has found flaws in RIX’s ex ante analysis, namely (i) unrealistically low traffic projections; (ii) underestimated incremental revenues; (iii) the wrongful inclusion of the foregone revenues related to British Airways; and (iv) inflated incremental costs.

(112) On the basis of its own incremental profitability analysis, and the correction of some the above-mentioned flaws (see recitals (104) to (106) above), the Commission comes to the conclusion that the agreements were likely to be profitable for RIX from an ex ante perspective. It also concludes that the agreements were part of the implementation of an overall strategy to lead to profitability in the long term. Consequently, Latvia did not grant an advantage to Ryanair that it would not have obtained under normal market conditions.
4. CONCLUSION

(113) The Commission concludes that based on the foregoing assessment, the 2004 Agreement, as modified by the Side Letter, does not constitute State aid within the meaning of Article 107(1) TFEU since it does not confer an economic advantage to Ryanair.

If this letter contains confidential information, which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://ec.europa.eu/competition/elojade/isef/.

Your request should be sent electronically to the following address:

European Commission,
Directorate-General Competition
State Aid Greffe
B-1049 Brussels
Stateaidgreffe@ec.europa.eu

Yours faithfully
For the Commission

Margrethe VESTAGER
Member of the Commission